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## **A Legal Due Diligence Framework for Inbound Transfers of Foreign Technology Rights\*\***

The ability of any commercial enterprise to achieve its economic objectives, in the form of a fair return to all of its stakeholders on their invested capital and other dedicated resources, is a function of a number of variables. For many years, capital, in the form of machinery, land, buildings, and other tangible assets, and labor, in the form of human resources measured on both a quantitative and qualitative basis, were perceived to be the most important factors of production in any economic analysis of a specific business enterprise. However, particularly in light of the globalization of business activity in the last quarter century, it is now clear that knowledge, creativity, and innovation have moved to the forefront of business strategy for both large and small enterprises around the world.<sup>1</sup>

At the outset, let us refer to this third production factor as “technology” or “proprietary information” that has competitive significance. The use of each of these terms connotes tangible and identifiable assets that can be used by their owner and, like any other assets, are susceptible to obsolescence, misappropriation, and duplication. However, the legal framework that has been built to contain, define, and allocate ownership and control of this type of information,

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1. On this subject, see G.V. SMITH & R.L. PARR, VALUATION OF INTELLECTUAL PROPERTY AND INTANGIBLE ASSETS preface (1989), where the authors assert:

Intellectual property is fast becoming the most important asset possessed by corporations. Various forms of intellectual property are the foundation of market dominance and continuing profitability for many companies. . . . Companies are licensing, selling, joint venturing, and trading intellectual property around the world. Our global economy is based, in many ways, upon this commerce in intellectual property.

in the form of patents, trademarks, copyrights, and trade secrets, provides an owner with something far different from a set of property rights. Instead, these technology and information rights provide a tool that *may* allow the owner, which we assume to be a domestic or foreign business enterprise,<sup>2</sup> to forge and maintain an overall competitive advantage based, in part, on its ability to use, and prevent others from using, ideas and innovations meeting the requirements of specified laws throughout the world.

For the international law practitioner who is active in areas other than the specialized practice of filing for, and prosecuting and enforcing, patent, trademark, and copyright claims in foreign jurisdictions, issues relating to technology and proprietary information can arise in a number of different situations. For example, transactions involving foreign distribution and sales rights relating to domestic products are a common part of the day-to-day practice of counsel involved with clients engaged in the multinational business arena. Many of these transactions involve a contractual agreement in the form of a license, which is intended to transfer to the licensee the technology and related information, *and the legal rights associated therewith*, necessary to complete successfully the objective of the transaction: distribution and sale of the domestic products at satisfactory levels in the foreign market.

Without question, a license granted in the course of a distribution relationship involves a significant transfer of knowledge from the licensor to the licensee. A license, however, also conveys a number of significant legal rights that complement and facilitate the use of the transferred knowledge. Thus, technology transfers of this type are really better understood as the conveyance of two related, yet distinguishable, components: the relatively tangible technology and confidential information on the one hand, and the somewhat intangible legal rights associated therewith on the other hand. Thus, this article refers throughout to the business asset as technology rights and to any transaction that effects a transfer or sharing of those rights as a technology rights transfer.

Historically, issues regarding technology transfers in the international sphere arose principally in the context of limited outbound transfers from business entities in comparatively more developed countries, such as the United States, to licensees or other transferees in less developed foreign jurisdictions. Even in those cases where a direct investment was made by a U.S. entity in a foreign jurisdiction, the investment tended to be made for reasons, such as lower manufacturing costs or focused distribution efforts for the transferor, which rarely had anything to do with the desire of the U.S. entity to obtain access to particular technology rights developed overseas.

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2. As noted below, technology rights typically vest in the inventor, who may be an individual involved in noncommercial activities. For purposes of this article, however, we will assume that the ownership of the rights has vested, by contract or by operation of law, in a business enterprise.

However, the massive trade imbalances of recent years, as well as the growing number of patent applications in the United States by foreign inventors, make it clear that the United States no longer has a monopoly on the production of innovation. Any number of foreign entities, supported by governmental funding of research and development and beneficiaries of experience gained through over three decades of technology transfers from developed nations, are now in a position to assume leadership roles in the area of technology.<sup>3</sup> Accordingly, counsel must now be cognizant of the issues that arise with respect to inbound transfers of technology rights: any transaction by a domestic firm calculated to effect the acquisition of, or the right to lawfully use, technology rights developed by or owned by a foreign innovator.<sup>4</sup>

Properly structured, inbound transfers may fit quite well into a domestic client's overall program for developing or otherwise acquiring new and innovative technology and related rights. For example, the client may wish to expand its existing product line, spread overhead, make use of unused plant capacity, or diversify its resources into new markets and industries. Although the client may have the financial resources to undertake its own research and engineering program, it may prefer to reduce the time required to enter the projected market by entering into an appropriate arrangement with a third party. While in the past this usually meant turning to a domestic partner, it is now more likely than not that domestic firms seeking to develop new and innovative

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3. As is the case with domestic firms, the importance of technology to a foreign business enterprise may vary depending upon its purpose, mode of operation, and the environment and markets in which it competes. For example, the growth and development of a high technology firm clearly depends upon its ability to build and maintain a strong portfolio of technology assets in the form of patents, trade secrets, trademarks, and copyrights. On the other hand, the strength of other firms may lie not in technology or research, but in their skills in production, marketing, and distribution. Even in those cases, technical assets such as production know-how, trade secrets (e.g., customer lists and informational data bases), and trademarks may play an important role in the success of the firm. In examining the technology position of a potential acquisition candidate, licensor, or strategic alliance partner in either the domestic or foreign context, counsel should carefully understand the role that the technology rights play in the competitive environment of the target firm.

4. This article focuses upon any transaction that has as its primary purpose the objective of acquiring significant technology rights owned or controlled by a foreign inventor. These transactions can include a licensing arrangement, a technical assistance agreement, a supply arrangement, and at a more complex level, a joint venture or development arrangement or outright acquisition of the foreign entity. However, there are any number of other transactions to which the issues raised in this article are of some concern. For example, many believe that a Japanese mergers and acquisitions market is emerging that will facilitate direct investment in Japanese firms by investor groups in the United States. These transactions may take the form of full-scale strategic partnerships, with cross-shareholdings that will allow both parties to take advantage of the respective strengths of the combined entities in production, marketing, and technology. Also, institutional and pension fund investors may wish to make an investment in foreign firms as overseas securities markets begin to develop. In those cases the ability of the investor to assess and value the technology rights of any prospective portfolio firm will become relevant. A similar valuation exercise will be required as a condition of any venture capital-type investment or a corporate investment in a technology-driven overseas firm.

technology will expand from a domestic to an international search for the proper opportunity.

Certainly, whether the choice is made to acquire the new technology from a domestic or foreign firm, the client's immediate objective is to acquire a package of technology rights that includes all of the components that are believed necessary for the client to commence rapidly the manufacture and sale of the desired product. While the end result is easy enough to articulate, the route that must be taken, particularly when the technology rights are being transferred from overseas, is fraught with hazards. These hazards are created, in many instances, by the failure of the client and its counsel to carefully understand the assets that are being transferred and the unwillingness of the client and its counsel to take the time to consider how that understanding can help in properly structuring the technology transfer in order to ensure that the client receives the best value for its efforts.

The issues surrounding international technology transfers are complex, and depending upon the structure of the relationship, can involve a myriad of considerations relating not only to the technology rights themselves, but also to the corporate, tax, labor, and antitrust issues raised by regulators on both sides of the transactional border. Clearly, each of these substantive areas needs to be addressed in the course of any transaction. This article focuses, however, only upon some of the issues raised in connection with technology rights, and only then in the most general manner. The intent is to sensitize counsel to the fact that any inbound transfer of technology rights involves a significant acquisition of assets and creates an obligation to conduct the same type of due diligence investigation with respect thereto as would be done when the subject matter of the acquisition is of a more familiar nature.

The discussion in this article posits the situation where a domestic client approaches counsel regarding a possible inbound technology transfer from a firm in a foreign country. After advising the client as to the various substantive legal concerns that may arise in connection with such a transaction, counsel must then begin the process designed to ensure that the following questions regarding the technology rights associated with the transaction are addressed:

(1) What *types of technology rights* exist in the transferor's country, and how do those rights differ from rights that may exist in the United States and in other jurisdictions where the client may wish to utilize the rights obtained from the transferor? What other legal restrictions may be imposed by the transferor's country that might affect the value of the proposed technology transfer to the client?

(2) What *degree of due diligence investigation* is necessary in order to identify and assess the technology rights to be transferred from the transferor to the client?

(3) Based on the due diligence investigation, what *form of technology transfer* will best accomplish the client's objectives?

(4) What *representations and warranties* should be provided by the transferor to the client with respect to the technology rights and the technology transfer itself?

(5) What *ongoing covenants and agreements* with respect to the technology rights should be obtained from the transferor, assuming that the technology transfer has not taken the form of outright acquisition of the transferor (or the technology rights) by the client?

Certainly, none of the foregoing questions can be answered in isolation. For example, representations and warranties must be tailored to the specific transaction and must take into account the intended use of the technology rights by the client. In turn, the intended use of the technology rights tends to dictate how the technology transfer itself is to be structured. Accordingly, counsel should not lose sight of the complex relationships among each of the various major issues. The balance of this article sets forth a basic framework that is designed to ensure that a thorough and thoughtful analysis occurs at each stage of the process.

## I. The Technology Rights Framework

Once the client approaches counsel for assistance in structuring an inbound technology transfer, the first task is to identify the subject matter of the transaction: the actual and potential technology rights of the transferor. This process involves at least two important steps. First, counsel must understand the statutory and nonstatutory rights relating to the protection and transfer of technology and proprietary information that exist in the country *from which* the transfer is to occur. Second, counsel must work with the client to develop an effective yet efficient due diligence procedure, a technology rights investigation, and to analyze and assess the business and legal risks associated with the acquisition of the technology rights.

The subject matter of any technology transfer consists of a body of knowledge and experience, often without clearly defined boundaries, which has been developed or acquired by the transferor relating to the creative process of conceiving, designing, engineering, manufacturing, marketing, selling, and otherwise supporting a unique product or service. In most countries of the world, this knowledge can be loosely segregated into statutory elements (such as patents, trademarks, or copyrights) and nonstatutory rights relating to what have come to be referred to as trade secrets. However, any similarities among international technology regimes are quickly consumed by the various historical, cultural, economic, and political considerations that influence policies in a given country with respect to the acquisition and use of these significant tools for economic development.<sup>5</sup>

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5. A detailed description of the various statutory and nonstatutory technology rights referred to in the text is beyond the scope of this article. In addition to taking advantage of the specialized skills of experts in each of these areas, counsel may also wish to consult one or more of the treatises that

## A. PATENTS

In most nations around the world, patents are a creation of statutory law and generally grant protection to an invention<sup>6</sup> that meets specified standards of utility, novelty, and originality,<sup>7</sup> provided that the practice of the invention is fully described in an application filed with, and reviewed and approved by, the appropriate governmental agency. If a patent is granted in a given nation, it generally provides the owner with the right, for a limited period of time, to prevent or exclude others from making, using, or selling the invention in that nation. However, a patent does not itself confer on its owner the right or ability to make, use, or sell the invention.<sup>8</sup> As such, a patent is really a legal right that complements and enhances the technology embodied in the protected invention.

A patent owner has several strategic options with regard to the use and control of the patent rights. First of all, the patent rights can be used as a means of preventing others from exploiting the invention, even when the owner does not have the financing or production capabilities to use the invention itself. Second, the exclusionary screen provided by the patent can be complemented by the owner's own production and development efforts, in effect a use of the invention. Finally, the owner can license the patent rights to others, a form of exception to the monopoly rights, in return for royalty income, or in some cases, as a valuable contribution of capital to a new business enterprise.<sup>9</sup>

Counsel must understand and appreciate that patents, as well as the various trademarks and copyrights described below, are a creation of the statutory law of the nation in which an application therefor is made. As such, a valid statutory patent right in one nation does not provide similar protection outside of its borders.<sup>10</sup> The foregoing may be true not only because an application for protection has not been made, but it may also be the case that the idea and subject

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have been written in each of the substantive areas, including M. NIMMER, *NIMMER ON COPYRIGHT* (1984); D. CHISUM, *PATENTS* (1984); J. MCCARTHY, *TRADEMARKS AND UNFAIR COMPETITION* (2d ed. 1984); J. GILSON, *TRADEMARK PROTECTION AND PRACTICE* (1984); and R. MILGRIM, *MILGRIM ON TRADE SECRETS* (1984). All of the foregoing contain annotations to information on foreign technology regimes.

6. Not every invention may receive patent protection. For example, to be patented in the United States, an invention must fall into one of the following categories: processes; machines; manufacturers; composition of matter; or processes involving new uses of known processes, machines, manufacturers or compositions of matter, or improvements in any of the above. Foreign jurisdictions also have their own definition of the classes or categories of patentable inventions in that jurisdiction.

7. An idea is not patentable; only the embodiment of the idea, in the form of an invention, is patentable. In the United States, see 35 U.S.C. §§ 101–103 (1988). In determining whether an invention is original or nonobvious, reference will usually be made to the prior art of the technical knowledge embodied in the invention.

8. In the United States, see 35 U.S.C. §§ 154, 271, 281 & 284 (1988).

9. Patent rights may be contributed to the capital of a new foreign joint venture, subject to any local regulations governing technology transfers and permissible forms of foreign investment.

10. While a patent granted in Country A cannot be enforced in Country B, importation of goods from Country B that infringe a Country A patent may be stopped, and the infringer may be sued in Country A.

matter of the application would not otherwise be eligible for patent protection<sup>11</sup> or would conflict with preexisting rights granted to an earlier applicant in that country. Moreover, the scope of inventions that qualify for patent protection,<sup>12</sup> the class of persons who may apply for a patent, the type of patent application and publication and review procedures,<sup>13</sup> the legal significance of the patent grant<sup>14</sup> and related enforcement procedures,<sup>15</sup> the duration of the patent, and any

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11. The fact that technical information is not eligible for the grant of a patent does not mean that such information would not qualify for trade secret protection in a given jurisdiction.

12. The strength and breadth of patent coverage may vary substantially, even among developed nations. For example, the scope of patent coverage in the United States reflects a result-oriented review, while a problem-solution framework exists in Europe and Japan since protection in Europe and Japan appears to be more limited to specific industrial and commercial applications of the patented process or innovation. Therefore, the breadth of patent coverage tends to be greater in the United States than in Europe and Japan since production in Europe and Japan appears to be more limited to specific industrial and commercial applications of the patent process or innovation. Moreover, patent coverage in Europe tends to be further diluted by the multijurisdictional enforcement approach that exists in the European Community (EC). The Japanese system has also failed to provide patent coverage on a timely basis or in a manner which meets the expectations of foreign inventors.

13. For example, counsel should understand whether the nation grants patent protection to the inventor who is the first to invent the idea embodied in the invention, as is the case in the United States, or to the person who is the first to file an application covering the invention, as is the case in Europe and Japan. Once a patent application is filed, search and examination is automatic in the United States; search is automatic in Europe, but examination must be requested; and in Japan, an applicant may defer search and examination for up to seven years after filing. A nation may require publication of the application prior to the grant of a patent. For example, in Japan publication is required eighteen months after the filing of the original application. However, the patent review process remains quite lengthy in Japan, meaning that information in published patent applications can be effectively copied and used for commercial purposes far in advance of the actual patent grant. Applications are also published in Europe prior to grant, but are not published in the United States. Patent rights generally vest at first publication in Europe and Japan, although such rights will not be enforceable until grant. In the United States patent rights vest at the time the patent is granted.

14. Not only do procedural differences abound, but counsel should also recognize that the actual patent rights granted to the owner may be quite different from those that exist in the United States. For example, in a developing nation such as Thailand, products or designs covered by a certain patent may be imported *until* the patent is worked (i.e., used by its owner for commercial purposes) or the process or design is used in Thailand; no infringement action may be contemplated against production or sale of a patented article or design that was begun in good faith prior to the date of publication of the patent application; compulsory licensing may be applied for by third parties upon certain conditions; if a patent is not worked or used without justifiable reasons after six years from the date of grant, it may be cancelled; and one patent holder may be allowed to infringe another patent, without compensation, if such infringement is believed to be in the public interest.

15. Not only are there significant deficiencies in patent enforcement procedures in nondeveloped nations, but patent enforcement procedures also differ among the United States, Europe, and Japan. For example, in Europe and Japan the validity of patent claims is usually decided at the opposition stage, after the patent application is published and prior to the patent grant, rather than at the enforcement stage (after the patent is granted), as is the case in the United States. *See also* PRACTISING LAW INSTITUTE, FOREIGN PATENT LITIGATION 18-27 (1983), where several factors regarding foreign patent litigation are mentioned, including: the time limits for bringing an infringement action; how far back the patent owner can go in collecting past damages; whether or not injunctive relief is available; whether a bond must be posted by the plaintiff; the use of discovery proceedings; the



other rights that might flow from the grant of a patent will vary throughout the world.<sup>16</sup> For example, in many countries it is necessary that the patent be worked or used<sup>17</sup> within a specified period of time or the protection will be lost, and compulsory licenses to the patented technology will be granted by governmental action.

In the United States patents are issued by the Patent and Trademark Office and may either be utility patents or design patents. A utility patent protects the utilitarian features of an object and has a life of seventeen years. A design patent protects only the appearance of the object and typically has a life of fourteen years. Initial ownership of patents belongs to the inventor, who must be one or more natural persons. In most instances, however, an employer has the right to have the patent on an invention of an employee assigned to it.<sup>18</sup> During the last decade, a decided trend has developed in the United States to strengthen the enforceability of patents and patent protection.<sup>19</sup>

In considering international patent programs it is important to remember the effect of international treaties. The International Convention for the Protection of Industrial Property,<sup>20</sup> the so-called Paris Convention, was originally signed in 1833 and provides that all nations that are parties to the Convention must grant to nationals of other member nations the same rights to patent protection as they grant to their own nationals. Specifically, the Paris Convention provides that any patent application in a member nation may be filed in any other member nation

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duration of a patent infringement suit; and the attitude of courts toward patentees. Local patent counsel clearly should be consulted in assessing the strength of any potential patent infringement remedy in a foreign jurisdiction, since even in Europe the procedures vary significantly from country to country.

16. The state of technological development in Japan makes it one of the most desirable nations for considering some form of technology acquisition. A good, brief introduction to the Japanese system of technology rights, although written from the perspective of an American firm licensing technology into Japan, can be found in Cunard, *Protecting American Technology Transferred to Japan, Including Patent, Trademark and Licensing Issues*, in JAPAN-UNITED STATES TRADE AND INVESTMENT: STRATEGIES FOR THE 1990'S, at 93-121 (ABA National Institute Materials, Nov. 1989).

17. Among the developed nations, Japan and Europe have such work and compulsory license provisions.

18. In the United States an employer generally has the right to have the patent on an invention of an employee assigned to it if the employee was hired to invent. In other cases, unless a written assignment of inventions agreement has been signed, the employer has only a shop right, or royalty-free license to use the invention, but does not have a right to the patent. Accordingly, written assignment of inventions agreements has become quite customary in the United States, although their contents are often the subject of state statute. *See e.g.*, CAL. FORMS: LEGAL AND BUSINESS §§ 27:191-193 (1990). However, in Japan and many other Asian nations, the right of an employer to employee inventions is far less clear, as is the utility of any assignment of inventions agreement.

19. The federal district courts have original jurisdiction of patent infringement suits in the United States, and all appeals are heard by the Federal Court of Appeals for the Federal Circuit, which has exclusive appellate jurisdiction over patent appeals.

20. 25 Stat. 1372, T.S. No. 379; revised in 1990, 32 Stat. 1936, T.S. No. 411; revised in 1911, 38 Stat. 1645, T.S. No. 579; revised in 1925, 47 Stat. 1789, T.S. No. 834; revised in 1934, 53 Stat. 1748, T.S. No. 941; revised in 1958, 13 U.S.T. 1 T.I.A.S. No. 4391; revised in 1967, 212 U.S.T. 1583, T.I.A.S. No. 6923.

within twelve months of the first filing date with the same priority as if it had been filed in each member nation on its first filing date.<sup>21</sup> Several other provisions of the Paris Convention provide counsel with a sense of the differences in patent regimes which exist around the world:

(1) Some patent systems will not grant protection unless the invention meets certain standards of absolute novelty. The priority provisions prevent a prior filing in another nation from destroying the novelty of the invention that is the subject of the patent application in the second nation.

(2) As noted above, some nations require publication of a patent application before the patent issues, generally eighteen months after the priority date. The ability to withhold the filing of a patent application for a specified period of time, and thus delay publication, allows the owner to consider further whether trade secret protection is preferred in the nation requiring publication.

(3) Under the Paris Convention a nation can revoke a patent because of nonuse where a compulsory license would not be sufficient to cure the abuse. Compulsory licenses cannot, however, be imposed until after four years from the filing date, or three years from the date of the patent, whichever last expires. Counsel should be aware that in certain countries application can be made for a license upon the payment of appropriate compensation; thus, in effect, the owner is compelled to license rights under its patents, albeit for compensation or a reduction in the amount of any annual renewal fees.

(4) Counsel should be aware that pressure exists among developing nations to require an exclusive compulsory license, rather than a nonexclusive license, in the event that an invention is not worked for two years. Also, developing nations are concerned that equal treatment provisions may perpetuate what they perceive to be an existing imbalance in technology transfer.

The terms of the Paris Convention have been supplemented by the Patent Cooperative Treaty (PCT)<sup>22</sup> that came into force in 1978 among some of the members of the Paris Convention. The PCT permits an applicant to make a single filing in one nation of an international application. In this manner, the priority period is extended to twenty months, at the end of which time the applicant starts the national procedure in each of the designated national offices by paying the required filing fees. Other procedures exist for patent filings in regional areas,<sup>23</sup>

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21. This advantage may raise difficulties in the course of a due diligence investigation where the transferee wishes to seek patent protection for the technology in a first to file jurisdiction, since it requires that a search be made in a number of jurisdictions to ensure that a blocking patent application has not already been made in another jurisdiction that will have priority in the subject jurisdiction due to the application of the Paris Convention procedures.

22. The PCT was signed at a diplomatic conference in Washington, D.C. in 1970 and came into effect in 1978. See 28 U.S.T. 7645, T.I.A.S. No. 8733.

23. In Europe, for example, the Convention on the Grant of European Patents permits an inventor to obtain a bundle of national patents for European countries designated in the application after filing with, and review by, a central European Patent Office. An application under this procedure is published eighteen months after the priority date. Patents issued are subject to rights established

although procedures may differ, and an owner may still wish to make individual filings in each nation, if possible.

## B. TRADE SECRETS

Trade secrets, sometimes referred to as know-how or proprietary information, consist of information not generally known to the public that the owner uses or plans to use in its business and that gives it an advantage over actual or potential competitors.<sup>24</sup> So long as such information is not published or released without restriction into the public domain, it is protectable as a matter of statute or contract under the laws of many countries, particularly in the developed nations.<sup>25</sup> Trade secrets may even include technical information that is patentable, although a decision may be made not to seek a patent in order to avoid disclosing sensitive information in the patent application.<sup>26</sup>

In the United States the key to trade secret protection lies in the owner's determination to limit access to the information and to maintain its confidentiality by requiring all persons exposed to the secret to agree in writing to keep it confidential. Properly maintained, trade secrets may have an indefinite life, and the owner may maintain an action against those who gain knowledge of the information through improper means or in violation of a confidential relationship.

The list of possible trade secret information can extend to such things as machine drawings, process instructions, manufacturing costs, manufacturing and testing specifications, customer lists, sales records, and marketing techniques. In some cases trade secret information can also encompass technical aspects of a

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under the national laws and courts of each of the nations mentioned in the application. See 13 I.L.M. 268 (1974); Singleton, *Convention on the Grant of European Patents and Convention for the European Patent for the Common Market*, 13 INT'L LAW. 119 (1979).

24. See RESTATEMENT OF TORTS § 757 comment (b) (1939). Also, the Uniform Trade Secrets Act defines a trade secret to mean:

information, including a formula, pattern, compilation, program, device, method, technique, or process, that:

- (i) derives independent economic value, actual or potential, from not being generally known to, and not being readily ascertainable by proper means by, other persons who can obtain economic value from its disclosure or use, and
- (ii) is the subject of efforts that are reasonable under the circumstances to maintain its secrecy.

UNIFORM TRADE SECRETS ACT § 1(4), 14 U.L.A. 372 (1985 & Supp. 1989).

25. See generally A. WISE, *TRADE SECRETS AND KNOW-HOW THROUGHOUT THE WORLD* (rev. ed. 1981). Trade secret rights in the United States are generally a function of state law.

26. A patent application may be filed in one country but not in another, due to disclosure requirements. For example, a patent application in Country A may require very limited disclosure, whereas an application in another country, such as the United States, may involve such a broad degree of disclosure that the owner will prefer to maintain the information as a trade secret. Therefore, the technology package in the two nations will differ: in Country A it will consist of the patent and the trade secrets that are undisclosed in the patent; in the other country it will consist of only the trade secrets. A useful summary that compares trade secrets to patent and copyright information appears in Pooley, *Trade Secrets: Overview*, in *PROTECTING TRADE SECRETS* 1989, at 47 (Practising Law Institute 1989).

production process that do *not* work, since such knowledge would be valuable to someone seeking to develop the process independently in a timely manner. In each case the key inquiry for counsel is the availability of trade secret protection in the transferor's jurisdiction<sup>27</sup> and the maintenance of procedures by the transferor to ensure that such information is maintained in a confidential fashion.

Counsel should be aware that in some foreign jurisdictions the definition of a trade secret is quite restricted and may depend upon the status of the defendant at the time the information was disclosed. Also, governmental authorities may decree that trade secret information can only be afforded protection for a limited period of time. Finally, even when trade secrets are recognized, a company may have no effective remedy available against third parties who may have benefited from disclosure of trade secret information in violation of contractual restrictions. Indeed, many of the major trading partners of the United States have been cited for any number of shortcomings in their systems of trade secret enforcement.<sup>28</sup>

Trade secret protection can arise as a matter of statute or pursuant to contractual provisions. The manner in which these restrictions are enforced, however, varies from nation to nation depending upon, among other things, cultural attitudes and national policies relating to such disparate factors as the right of a worker to pursue employment free of restrictions imposed by virtue of prior employment. The following list is illustrative of some general concerns counsel should take into account:

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27. Counsel should ensure that the transferor's jurisdiction does not impose any limitations or restrictions upon a resident's ability to transfer trade secret information to a foreign transferee, and a representation to that effect should be sought from the transferor. Also, counsel should note that some jurisdictions refuse to include techniques of a nonindustrial nature in the definition of know-how or trade secrets and may otherwise limit the duration of trade secret protection. For example, the duration of trade secret protection in Venezuela is limited to five years. *See* Presidency of the Republic (Venezuela), Carlos Andres Perez, Decree No. 2442, Nov. 8, 1977, art. 65(e). With respect to the various practices in developing nations relating to the definition of know-how, see Correa, *Legal Nature and Contractual Conditions in Know-How Transactions*, 11 GA. J. INT'L & COMP. L. 449 (1981). For a survey of alleged deficiencies in the intellectual property protection regimes of foreign countries, see U.S. INT'L TRADE COMM'N, PUB. NO. 2065, FOREIGN PROTECTION OF INTELLECTUAL PROPERTY RIGHTS AND THE EFFECT ON U.S. INDUSTRY AND TRADE (Feb. 1988) [hereinafter PUB. NO. 2065].

28. Generally, with respect to a number of foreign jurisdictions, the United States International Trade Commission (USITC) has noted inadequate civil and/or criminal penalties, unreasonably slow, underfunded, or inexperienced enforcement processes, and political corruption and antforeign bias in the enforcement agencies. *See* PUB. NO. 2065, *supra* note 26. In light of the foregoing, the United States Trade Representative has made the development of adequate standards for trade secret protection a key objective of the United States in the Uruguay Round of the General Agreement on Tariffs and Trade, and has also indicated its intent to continue to pursue unilateral and bilateral action on the subject. The USITC's report also can provide counsel with guidance as to those countries where problems are likely to arise in the area of technology rights. Among the countries cited are Brazil, Mexico, Korea, India, Taiwan, and Japan. *See also* Cass, *Changes in Section 337 Under the 1988 Trade Act*, in *THE NEW TRADE LAW: OMNIBUS TRADE AND COMPETITIVENESS ACT OF 1988* (Practising Law Institute 1988). The 1988 Trade Act contained a number of amendments to § 337 of the Tariff Act of 1930 relating to intellectual property rights in the context of international trade, a phenomenon that is illustrative of the heated debate that surrounds many of the issues raised in this article.

- Trade secret statutes and common law standards<sup>29</sup> should be reviewed in order to identify the scope of protectable information,<sup>30</sup> the class of potential defendants, and the penalties and enforcement procedures available under the statutes and the common law.
- Although trade secret protection can usually be created as a matter of contract, some nations limit the duration of such restrictions; in other cases nondisclosure agreements imposed upon employees may be set aside if the effect of such an agreement is to restrict unreasonably the employee's right to choose an occupation.<sup>31</sup>
- Trade secret laws reflect cultural attitudes as well. Thus, in many instances trade secret protection is not available on the same basis as it is in the United States. Many countries provide that an employee's right to seek employment includes the right to make use of information learned from previous employers. Also, in contrast to the prevailing practice in the United States, inventions made by an employee during the course of employment in a foreign country are not always assumed to be the property of the employer.<sup>32</sup>
- Local business practices and national policies have a significant impact on the potential for wide diffusion of trade secret information. Specifically, in those economies where corporate networking exists, such as in many parts of Asia, it is common practice for members of the corporate family to share competitive information.<sup>33</sup> Also, in less developed countries government policies tend to favor distribution of technical information throughout the local business community, rather than permitting a few firms to enjoy a competitive technical advantage.

The need for counsel to understand clearly the various cultural and business practices of, and the relative availability of trade secret protection in, the home market has dual importance for the domestic client. First, the client needs to determine whether a significant risk exists that the confidential information would, by operation of local law or otherwise, be disseminated to competitors who might use it to produce identical or similar products that would diminish the

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29. Statutes and common law regarding trade secrets may have originated in the context of the regulation of unfair competition.

30. In Brazil, commercial information and manufacturing information are distinguished, and accorded different levels of trade secret protection.

31. In Japan, for example, see on this issue the Judgment of Oct. 23, 1970, *Yugen Kaisha Foreseco Japan, Ltd. v. Okuno and Diamatsu*, Nava District Court, Japan, 624 HANJII 78, where the court held that a noncompetition agreement would be against "public order and good morals," and therefore null and void, if it threatened the livelihood of an employee by unreasonably restricting the employee's right and freedom to choose an occupation.

32. See *supra* note 18.

33. For example, in Japan many of the standard business practices, including sharing of information among members of various corporate and business groups, would likely violate antitrust restrictions in the United States.

value of the transferred rights. Second, the client should be concerned as to whether disclosure of the information into the public domain in the foreign jurisdiction would impede its own ability to claim trade secret protection for the same information in the United States and other markets.

### C. TRADEMARKS

A trademark is a word, symbol, or other similar means used on an article or product to identify and distinguish its source. Trademarks do not protect the products themselves from being copied; however, they can be very valuable marketing tools in that they imply a certain level of quality and service that cannot be imputed to what might otherwise be nearly identical generic or off-brand products. Counsel should clearly understand the procedures required to protect a trademark, which typically include registration of the mark, and in some cases, a review and publication procedure prior to approval. Foreign trademark protection may differ from procedures in the United States, and many countries require repeated filings and tax payments to maintain the mark.<sup>34</sup>

### D. COPYRIGHTS

In the United States copyright law is governed by title 17 of the United States Code, and section 102(a) thereof makes copyright protection available to all "original works of authorship fixed in any tangible medium of expression, now known or later developed, from which they can be perceived, reproduced, or otherwise communicated, either directly or with the aid of a machine or device."<sup>35</sup> Section 102(b), however, goes on to make it clear that copyright protection does *not* extend to any "idea, procedure, process, system, method or operation, concept, principle or discovery." Copyright protection of some sort exists throughout the world, and the author or owner of a copyright has the right,

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34. In the United States trademark protection is provided by the Federal Trademark Act of 1946, 15 U.S.C. § 1051 (1988), as amended, commonly known as the Lanham Act. A number of significant modifications to the trademark laws were effected by the Trademark Law Revision Act of 1988, Pub. L. No. 100-667, 102 Stat. 3935 (1988) (amending 15 U.S.C. §§ 1051-1128 (1988)), including amendments that permit application for registration of a mark prior to actual use of the mark on goods in commerce, a practice that had been a long-standing feature of foreign trademark regimes. As with patents, trademarks are the subject of various international and regional treaties.

35. For those companies that are involved with the production, development, and sale of computer programs and semiconductor chips, special attention should be paid to protection made available under the copyright laws of various nations, such as those granted in the United States under the Semiconductor Chip Protection Act of 1984 dealing with mask works fixed in semiconductor chip products. See 17 U.S.C. § 901 *et seq.* (1984). In some instances the written expression of the computer program (e.g., the source and object code), encoded on magnetic media or stored electronically or optically or on paper, may be protected by copyright. The source code may also be protected as a trade secret, and patent protection may be available to protect the ideas that form the basis for a particular computer program. Finally, trademarks can be a very effective marketing tool for the distribution of computer applications programs.

for a specified period of time, to exclude others from reprinting, publishing, copying, distributing, publicly performing, or publicly displaying the work and from preparing derivative works based on the copyrighted work. However, a copyright does not prevent another from using the knowledge set forth in the work to make, use, or sell the idea or invention.

Once again, the nature of technology rights is a function of local regulations and international treaty provisions. Counsel needs to understand each relevant framework that may apply to the protection of the subject matter of the technology transfer. To this end, counsel should review, with the assistance of local counsel, the statutory and case law in the nation from which the technology rights are being transferred and each other jurisdiction where the relevant technology is being used or in which the transferee reasonably expects that an opportunity exists for exploitation. In particular, any material differences relating to the formation of technology rights that may exist between the United States and the transferor's jurisdiction should quickly be identified and explained to the client.

## II. Antitrust and Technology Transfer Policies

In addition to the specific national laws and international treaties relating to technology rights, counsel involved in an international technology transfer should also be concerned with domestic and international antitrust issues.<sup>36</sup> The sophistication and application of antitrust laws vary dramatically from nation to nation. For example, the European Economic Community concerns itself with any action calculated "to take improper advantage of a dominant position,"<sup>37</sup> where the owner of a patent monopoly uses that power to coerce a licensee into accepting contract clauses that significantly increase the economic value of the patent to the owner.<sup>38</sup> On the other hand, a nation's antitrust policy may focus upon the competitive effects of a particular transaction or agreement upon the local market and whether or not the arrangement has a substantial benefit to the public.<sup>39</sup>

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36. See G. HOLMES, *INTELLECTUAL PROPERTY AND ANTITRUST LAW* (rev. ed. 1989). Part III deals with various antitrust issues that arise in connection with the acquisition of intellectual property, and chapter 12 is devoted to "Acquiring Externally Developed Intellectual Property."

37. See the Treaty of Rome art. 86, which states that "To the extent to which trade between any Member States may be affected thereby, action by one or more enterprises to take improper advantage of a dominant position within the Common Market or within a substantial part of it shall be deemed to be incompatible with the Common Market and shall hereby be prohibited."

38. Among the contract provisions that may give rise to antitrust concerns are grant-back clauses covering the development of improvements by the licensee that must be licensed back to the licensor; field-of-use restrictions; tie-in or tie-out relationships, which require the licensee to either purchase (tie in) or refrain from purchasing (tie out) various products; package licensing; restrictions on licenses to third parties, and other, similar provisions.

39. Various countries have entered into treaties including a restrictive business practice clause that may call for consultation between the nations on such practices. Also, the United States main-

As a supplement to antitrust regulations aimed at various *competitive* effects of technology transfers, many nations have enacted specific legislation regulating the content of technology transfer agreements in order to foster the development of local technical capabilities, and in many instances, to monitor the use of foreign exchange and the amount of foreign investment and involvement in the local economy. Regulations of this type may take a variety of forms and are typically focused upon the transfer of technology *into* the nation (an inbound transfer), although a number of restrictions may also be imposed upon technology exports. One or more of the following regulations may be involved in the technology transfer:

- A technology transfer agreement, however that is defined in local regulations,<sup>40</sup> may need to be registered with, and even approved by,<sup>41</sup> local authorities, including banks. Such registration is sometimes a condition to the validity of the agreement, or at a minimum, is required in order for deductions to be taken for any royalty payments or for certain amounts to be repatriated from the country. In some countries criminal sanctions can be imposed for failure to register a technology transfer agreement.
- As noted above, many nations impose compulsory work requirements with respect to a patent. If relevant, it may be appropriate to impose an obligation upon the transferee to use its best efforts to work the technology in order to avoid a compulsory license of the information. When the client is to receive rights under a patent that is the subject of a work requirement, the transferor should provide assurances that its actions, or inactions, with respect to the patent will not result in the grant of a compulsory license to a third party that will impair the economic value of the prior technology transfer to the client.
- Royalty restrictions may be imposed as to the amount and duration of required payments. Often these restrictions arise when the amount of foreign exchange available within the nation is an issue.
- When a technology transfer occurs in the course of a distribution or sales arrangement, restrictions may be imposed on the transferor's ability to terminate the distribution arrangement. In such cases the transferor may wish to establish a set of objective performance criteria that can serve as the basis for properly terminating the relationship if expectations have not been achieved.
- Finally, local authorities may impose restrictions upon contractual provisions that are similar to those discussed above in the context of antitrust. Among such provisions are tying arrangements, restrictions on the manu-

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tains antitrust cooperation arrangements with Canada and West Germany. See USITC, PUB. NO. 935, INTERNATIONAL TECHNOLOGY TRANSFER: A REVIEW OF RELATED LEGAL ISSUES (Jan. 1979).

40. The registration requirement can apply not only to licensing agreements, but may also extend to almost any form of technical assistance and consultation agreement.

41. In some instances approval must be obtained prior to signing the agreement.



facture of competing goods, pricing restrictions, "grant-backs,"<sup>42</sup> export restrictions, restrictions on the right to sublicense, volume restrictions, and royalty payments. Some nations will limit the duration of any confidentiality provisions and may request other modifications, which may or may not be acceptable to the transferee.

While most of these restrictions apply to technology that is imported into the nation, counsel must review the laws of the exporting nation to ascertain their applicability to outbound transfers of technology. As a general matter, the issue is whether a nation has implemented any system of registration with respect to international technology transfer agreements, and if so, whether the procedures permit governmental review and approval of the content of the agreement prior to the effectiveness of all or a portion of the agreement. Registration and review procedures may be utilized for a number of purposes, including the control of the terms of any import or export of technology into the nation, antitrust review, tax review, and regulation under the nation's foreign exchange control laws. While it is far more likely that imports of technology rights will be reviewed, the scope of a nation's registration provisions may be broad enough to cover all forms of technology transfer, although the review in such cases may be limited to the effect that the technology transfer might have upon the domestic market.<sup>43</sup> As the quality of foreign innovation continues to increase and more and more nations move toward becoming net exporters of technology, it can be expected that local governments will take an interest in regulating outbound technology transfers, particularly when the transfers are made to less developed nations.

### III. Due Diligence Investigation Procedures

Once counsel understands the regulatory regime that applies to technology rights in the transferor's country, he or she can then begin to assist the client in undertaking a thorough business and legal investigation. In any technology transfer the primary objective of the transferee is to ensure that it will be able to pursue freely and aggressively what it perceives to be the competitive advantage in acquiring the subject technology rights. However, the scope of the investigation and the disclosure that will be required from the transferor really depend upon the magnitude of the proposed transaction and the time and costs that the client is willing to incur. It would be foolish, though, to define the investigation simply by reference to the proposed structure of the transaction, such that a license

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42. See *supra* note 38.

43. See e.g., Japan's Foreign Exchange and Foreign Trade Control Law, Law No. 228 of 1949, arts. 29 & 30; Mexico's Law on the Registration of the Transfer of Technology and the Use and Exploitation of Patents and Trademarks; and Thailand's Patents Act B.E. 2522 and the Ministerial Regulation No. 7 (B.E. 2529) issued thereunder. With respect to the registration of international technology licenses, see Einnhorn, *Patent Licensing Transactions*, 1 PAT. L. & PRAC. § 5.05[7] (Matthew Bender 1968).

agreement is treated one way and an acquisition of the foreign company is treated another way.

For example, consider for a moment that any technology acquisition, in whatever form, constitutes a real investment and transfer of assets on the part of the transferee, since presumably it will rely on the transferred rights in developing its future product portfolio. A simple license agreement can relate to an absolutely essential technology right that the transferee believes is necessary to compete effectively in the United States and in other large markets. In that case the client will require the utmost care in the course of its investigation. On the other hand, an acquisition of the foreign company may, depending on the circumstances, not involve a material expenditure on the part of the acquiror, and thus a somewhat limited scope of review may be appropriate.

Still another important consideration in the initial definition of the scope of the due diligence investigation is the fact that it may not be possible to identify the appropriate structure for the technology transfer until the client and its counsel has had a chance to review and evaluate fully the transferor's technical portfolio. Accordingly, counsel should seek to ensure that the client insists on full and adequate disclosure by the transferor of the information necessary to effectively complete the due diligence investigation. Once the information is available, it can be analyzed from a number of important perspectives, and the client will then be in a better position to structure the technology transfer in a manner that best suits its own unique commercial requirements.<sup>44</sup>

The first part of any due diligence investigation consists of listing and inventorying the various components of technology and confidential information that are relevant to the technology transfer. As noted above, since the client is often unable to finalize the precise structure of the transaction until it has had a chance to assess the value of the transferor's technology portfolio, it is wise to seek fairly broad disclosure of information at the outset, ideally as if the transferee was going to acquire the entire business of the transferor. The legal due diligence checklist in that context is fairly straightforward and should consist of the following items:

- A list of all claimed patents, trademarks, copyrights, and copies of the relevant registrations and any pending applications.<sup>45</sup> In addition, an effort

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44. In a direct investment transaction, such as an acquisition or formation of a joint venture company, the investigation focuses on the investor's expectation that the technology rights of the foreign company to which it will have access will create significant value for the company, and accordingly, an acceptable return on its investment. However, if the client is licensing the technology rights from the foreign licensor, it will want to ensure that the particular technology rights that are the subject of the agreement will be adequate to fulfill the client's objectives as part of its own portfolio of technology assets. This investigation may be particularly important if the licensed technology is essential to the licensee's product development plans, or the license agreement is part of a broader relationship concerning the markets in which the transferor is active.

45. For a brief of due diligence procedures in the United States with respect to verifying ownership of patents, trademarks, copyrights, and trade secrets, see Engel & Radcliffe, *Financing*

should be made to obtain copies of any other materials that might qualify for statutory protection. Obviously, this information will be difficult to obtain and usually will arise out of a search of the transferor's files or, if that is inappropriate, interviews with the transferor's intellectual property counsel, general counsel, and officers and employees of the transferor.

- Since trade secrets are not registered, a description of all confidential information that the transferor treats as a trade secret, and as appropriate, a copy of any written documentation related thereto. Such information should be presented in a manner that preserves its confidential nature.
- A list and copies of all agreements to which the transferor is a party, either as a licensee or licensor, with respect to any item of technology or confidential information that it owns or has a right to use.<sup>46</sup> In addition, counsel should request a list, and brief description, of any other agreements to which the transferor is a party that involve an obligation by either party to such agreements to maintain the confidentiality of any specified information. Such agreements typically arise when technical information is being reviewed in contemplation of some future business relationship, such as a distribution or development arrangement. Finally, any documentation relating to prior assignment of technology rights to the transferor should be reviewed to ensure that it effectively conveys ownership to the transferor.
- A list of the key employees who are most active in the development of the transferor's technology rights and copies of any written agreements with those employees relating to the use or ownership of inventions developed by them during their term of employment, their use of confidential information acquired during their term of employment, or any other significant matter relating to their present and future relationship with the company.<sup>47</sup> The laws of each country will vary as to the rights and obligations existing between an employee and an employer with respect to inventions and confidential information that the employee develops, or is exposed to, while employed or engaged by an employer. Counsel should work with transferor's counsel to understand the prior employment relationships of any key

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*of High Technology Companies: Intellectual Property Assets as Collateral*, in 1987 LICENSING LAW HANDBOOK: COMPUTER SOFTWARE DISTRIBUTION AND ACQUISITION ISSUES 14-1 (1987). The points made in the article may be illustrative of procedures to be followed in foreign jurisdiction.

46. Although sometimes ignored in the domestic context, particular concerns arise in some foreign jurisdictions when research has been conducted pursuant to the terms of a governmental grant. Counsel should review closely any such grants or related agreements to see whether the government has maintained an ownership interest in the products of the funded development effort.

47. The terms of any employment agreement with key employees are relevant for a number of reasons. Counsel needs to ensure that the valuable services of a key technical employee remain available to the transferor, and therefore must review the terms of any cash or equity compensation arrangement with such employee. Also, confidentiality and noncompetition agreements may be an appropriate part of a written agreement with specified employees, although the enforceability of such provisions may vary from nation to nation.

employees to ensure that claims from prior employers will not be asserted with respect to inventions developed by that employee before or during his employment with the transferor. Also, if appropriate, counsel should ask to review copies of all prior agreements and correspondence between key employees and their prior employers relating to their terms of employment and any confidential information of the prior employer.

- A list of any actual or threatened claims by third parties, in the form of a lawsuit, administrative proceeding, or demand letter, with respect to any alleged infringement, or in the case of claims by former employers, misappropriation of confidential information by current employees. The list should be supplemented by an independent review using patent infringement, copyright, and trademark search reports for each of the material technical assets identified in the course of the investigation. Each claim should be discussed with transferor's counsel, and if necessary, appropriate consideration should be given to obtaining one or more legal opinions on such matters.

Ideally, counsel should be supplied with copies of all items identified on the list for review. Legitimate concerns do arise, however, with respect to the breadth of disclosure of potentially sensitive information, particularly when agreement has not been reached on the structure of the technology transfer and the overall business relationship. Also, cultural factors may impact the willingness of the transferor to provide certain information, or perhaps more importantly, the wisdom of such a request by the transferor. Accordingly, steps should be taken to minimize the perceived disclosure burden upon the transferor through one or more of the following means:

- As to information filed with regulatory agencies, such as the patent or copyright office, an attempt should be made to obtain copies directly from the agency. In the case of applications that are not yet published, information should be obtained pursuant to a confidentiality agreement or an independent review or opinion of counsel, as noted below.
- Contacts with, or interviews of, employees should be conducted in a manner that ensures that protection is not lost for trade secrets that might be disclosed in the context of the due diligence investigation.
- Disclosures may be expressly prohibited under the terms of any license or similar agreement between the transferor and any third party. Therefore, care must be taken that the value of the rights contained in the license or agreement is not diminished through any inadvertent or inappropriate disclosures.
- Disclosure may be made pursuant to the terms of a carefully drafted confidentiality agreement. Such an agreement should be very specific regarding the permitted uses of the information and the persons who may receive it. Correspondingly, the agreement should *not* prevent the recipient of the information from legally and independently developing technology that

contains information that is similar to, or competitive with, the information provided under the agreement during the due diligence investigation.<sup>48</sup>

- Finally, in some cases the opinion of patent counsel with respect to a pending patent application or the report of an outside expert or consultant regarding the development of the technology, its technical feasibility, and the quality of the underlying documentation may alleviate the need for direct disclosure of the information to the potential transferee. Local counsel may also be helpful in assisting in the interpretation of various rules and regulations and in locating information with respect to the technology rights.

#### IV. Qualitative Analysis of the Due Diligence Information

Once the documentary information has been collected, it is important that the principals meet to discuss and assess the transferor's existing technology rights: how they were obtained; how the technology and information is being protected; and to the extent regulatory filings have not been made, on what basis statutory protection is not being pursued. Additional concerns are how and to what extent the technology and the productive use of the information depend upon the skills of key employees or licenses obtained from third parties, what technology is being utilized by current and prospective competitors, how new and supplemental technology will be obtained and developed, and what, if any, future agreements might result in a technology transfer, by license or otherwise, to third parties.<sup>49</sup> From this, the answers to three key questions should be obtained.

1. *Will the transferee be free to use the acquired technology for the commercial development of products and services that can be sold and distributed in its target markets?*

Sometimes referred to as infringement analysis, the inquiry at this point assumes that the acquired technology rights cannot be improved or further developed and asks whether or not those rights will, in their present state, infringe upon the rights of third parties.<sup>50</sup> Counsel must analyze with the client the

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48. The recipient of any information under a confidentiality agreement will usually be asked to agree to return all copies of the information received from the transferor, provided that such information is clearly marked "confidential." Counsel for the investor should insist upon proper procedures to ensure that no dispute arises as to what information is intended to be covered by the agreement, including disclosures made in the course of nonwritten communications.

49. While the client's interests obviously are paramount in negotiating the terms of the technology transfer, counsel should not ignore the goals and objectives of the foreign transferor, particularly since they will influence the manner in which the foreign party may be willing to structure the transaction. Counsel should ask the client why the foreign party is willing to enter into the transaction. Among the expected responses might be such things as: the foreign party's desire to gain access to the client's technology; to penetrate the U.S. marketplace; to enhance its reputation in the industry; to gain access to the client's manufacturing capabilities or sources of supply; or simply to generate royalty or sales income that can be utilized in other parts of its business.

50. For example, in the United States employees may be subject to claims, by their prior employers, that they are utilizing trade secrets of the former employer in a manner that violates the

manner in which *each* piece of technology and confidential information was developed or acquired by the transferor in order to anticipate any future problems. Also, the client should identify any actual or known potential competitors who may have perfected rights that might create an infringement issue.

If the patent position of a competitor appears to cover the transferor's technology or other confidential information, it may be precluded from using the technology until the term of the underlying patent expires. In that situation, thought should be given to entering into a license agreement with the patent holder, even if the patent technology is not currently being used by the holder. Also, if a portion of the technology has been acquired under the terms of any license or similar agreement with third parties, a review should be made of any provisions that might restrict the use or transfer of the technology, as well as any provisions dealing with the ownership of rights to any improvements, enhancements, or modifications.

*2. Assuming that the transferee will be free to use the transferred technology without fear of adverse claims by third parties, does the transferred technology, in its current form, provide the transferee with a satisfactory level of protection from competition by third parties?*

Answering this question involves an analysis of the *quality* of the technology rights as well as the *strength* of the procedures that have been implemented to ensure that the technology and confidential information have been adequately protected by appropriate statutory filings and internal practices calculated to maintain the integrity and confidential nature of any trade secrets. Obviously, even well-protected and documented technology may be of little value if it does not provide the owner with a unique competitive advantage. Correspondingly, the most creative research and development plans may fail to bring the desired return to the owner if the technology and resultant products are not eligible for, or do not receive, adequate protection.

The *quality* of a given technology package will depend upon its composition. For example, the commercial value of a patent will depend upon the breadth of its claims and the relation of those claims to the key technical components of the subject product. Specifically, a fairly narrow or weak patent may have a high commercial value because of the particular feature the patent covers, the utility of the patent in supporting a defense against a third-party patent infringement claim or otherwise blocking a competitor's attempt to obtain a patent on its own technology, or because the patent reduces the competitiveness of the product by forcing a competitor to make costly design changes in order to avoid a claim of infringement.

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employee's obligation to maintain the confidentiality of such trade secrets. In those cases, the new employer may be subject to suit by the employee's former employer with respect to unlawful misappropriation of trade secrets, thereby creating a "cloud" over the technology that might be sought by the transferee.

If the technology rights consist mainly of trade secrets, which may be the case because the owner does not wish to disclose sensitive information in a patent application,<sup>51</sup> the analysis must take into account the fact that actions with respect to trade secrets generally only lie in the case of theft or misappropriation and that local factors may operate to further limit the degree of protection otherwise available to the owner. Thus, a real risk exists that competition may arise from third parties who independently develop similar products or acquire the information through means that are lawful within the subject nation.<sup>52</sup> In such cases great care should be given to evaluating the internal procedures that have been implemented to protect the trade secret information. It is also important to analyze whether some limited form of patent protection might actually be useful for prolonging the life of the competitive advantage and otherwise dissuading the independent development efforts of competitors.

The *strength* of the transferor's technology rights really depends upon whether or not the various components thereof have been properly maintained. An investigation should be conducted to ensure that patents remain valid. Moreover, patent, trademark, and copyright registrations should be maintained, and renewed if necessary. Contractual restrictions and covenants in third-party technology agreements, such as licenses, should be reviewed to ensure that no defaults exist,<sup>53</sup> and any prior transfer or assignment documents from third parties should be reviewed to ensure that they effectively conveyed title to the relevant technology or confidential information to the transferor. Also, if possible, an independent search should be conducted to ascertain whether any liens or mortgages have been imposed on the technology.

3. *What steps can be taken to enhance the transferor's technology rights portfolio by improvement or development of its technology or by strengthening the degree of protection for the existing technology?*

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51. Patent protection may not be pursued in instances where the technology is moving so fast that the patent claims will become outdated before the patent issues. Also, trade secret protection may be preferred if the patent that would be issued is so weak that other parties would simply invent around the claims contained therein.

52. As noted in the text, independent development operates as a defense to a claim of trade secret misappropriation. It has been suggested that trade secret protection can be circumvented by product development efforts that are done in a manner that does not infringe upon the rights of others, yet takes advantage of careful analysis of innovative techniques embodied in existing products. In this regard, see Davidson, *Reverse Engineering and the Development of Compatible and Competitive Products Under United States Law*, 5 SANTA CLARA COMPUTER & HIGH TECH. L.J. 399 (1989), which provides a useful introduction to some of the things that must be borne in mind with respect to reverse engineering activities. But see Lake, Harwood & Olson, *Tampering with Fundamentals: A Critique of Proposed Changes in EC Software Protection*, 6 COMPUTER LAW. 12:1 (Dec. 1989), in which the authors argue vigorously against any modifications to EC copyright protection that would have the effect of facilitating reverse engineering activities. The article also contains a number of annotations on the subject.

53. For example, a license agreement may contain options, reversions, durational limitations, territorial limitations, and other restrictions on the rights granted to the transferor.

Based on the business and legal analysis discussed above, counsel should have assisted the client in understanding the state of development of the transferor's technology rights, the likelihood that a patent will issue with respect to an important piece of technology, the feasibility of the technology, the availability of any competing products that may undermine the value and utility of the technology as it presently exists, and the likelihood that significant trade secret information will be lawfully disseminated into the public domain. At some point the client may decide that the technology transfer may only be justified if certain improvements are made to the technology itself or to the protection program that surrounds it.

The desire of your client to participate actively in a program dedicated to improving the subject technology really depends on an assessment of the amount and type of work that remains to be done to bring the technology to the desired level, and most importantly, whether the client believes that the completed work will create a technical position that justifies entering into a business relationship with the transferor that is far more complex than a mere licensing arrangement. In some instances the client may be best advised to rely on its ability to obtain a license to the products arising out of the transferor's own ongoing research and development activities,<sup>54</sup> rather than committing money and personnel to a joint development or other similar arrangement.

If, as a result of the due diligence investigation, a conclusion is reached that the transferor has not taken appropriate steps to effectively protect its technology rights, yet those rights do not appear to infringe upon the known rights of others, the parties may agree upon an appropriate program designed to strengthen the technology rights position. For example, a number of patent applications can be prepared and filed in multiple jurisdictions in a manner of months, with the result being that the value of the rights themselves would be significantly higher to both parties. This process may also help identify technology or other information that may be suitable for further development.

## **V. Structuring the Technology Transfer Arrangement**

Once the technology rights and related information have been appropriately defined and analyzed, the information can be used to evaluate the appropriate form or structure of the technology transfer arrangement. Any client that is assessing the merits of an inbound technology transfer does so with the intent of developing and expanding its own portfolio of products, services, and unique technical skills and ideas. Accordingly, the structure and content of the technology transfer really depend upon what the client intends to do with the technology

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54. If this is the case, the license agreement should carefully distinguish the old or current products and the expected new products that will also be subject to the terms of the license agreement.



rights, and where the rights fit into the client's overall plans with respect to the development of its own technology and acquisitions of ancillary rights from other third parties.

A technology transfer may involve one or more distinguishable arrangements, which may take the form of different contractual agreements designed to convey the appropriate rights in a specific component of the overall technology rights package. Accordingly, once the due diligence investigation is completed, counsel should consider with the client whether one or more of the following arrangements are necessary or desirable.

#### A. LICENSING AGREEMENT

The most basic form of technology transfer is the licensing agreement, which may cover patents, trade secrets, copyrights, and/or trademarks.<sup>55</sup> A patent license conveys to the licensee the right to make, use, or sell the subject matter of the licensed patent without being sued for patent infringement, although the licensee itself does not acquire the right to sue in its own name for patent infringement. In effect, the patent license is a contractual exception to the patent owner's right to prevent others from making, using, or selling the subject matter of the patent.

If a patent licensing arrangement is chosen for the technology transfer, counsel should ensure that the client understands each of the components of the transferor's current patent portfolio and the degree of protection that each patent provides for the subject technology in each jurisdiction where a patent has been obtained. Any patent license should cover all of the patents necessary for the client to manufacture, sell, and use the desired products. Also, the client may wish to ensure that it obtains a license under any further patents acquired by the licensor that cover future improvements to, or patents granted on, the transferred technology.

License agreements that include trade secrets should clearly define the confidential information to be transferred to the licensee and the permitted uses of such information. Correspondingly, the licensee may wish to ensure that the competitive advantages inherent in the trade secret information are not lost through the licensor's failure or inability to maintain the confidentiality of the information, and as discussed below, may insist upon covenants from the licen-

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55. In some instances a computer software license may also be included as part of a technology transfer. Computer software licensing raises a number of issues that are beyond the scope of this article. However, counsel should appreciate that computer software can be subject to each of the aforementioned types of technology protection. For example, the written expression of the program (e.g., the source and object code), encoded on magnetic media or stored electronically or optically or on paper, may be protected by copyright. The source code can be protected as a trade secret, and patent protection is available to protect the ideas that form the basis for the program itself. Also, trademarks can be a very effective marketing tool for various applications programs.

sor that it will institute and maintain procedures calculated to prevent unauthorized access to the trade secret information.

Whatever form the license agreement may take, the licensee is simply acquiring from the licensor the right to use various components of the licensor's technology rights for the purposes stated in the license agreement. However, in order for the technology transfer to be meaningful, it may be necessary for the parties to contract as to certain other goods and services relating to the use of the technology. Each of these agreements tends to build a greater degree of dependence between the parties, and as such, may lead to more complex concerns regarding the day-to-day operations of each company's business operations. For example, the license may cover the right of the licensee to copy and/or manufacture the licensed technology, to modify or change the technology, and to distribute the products produced as a result of the use of the technology.<sup>56</sup>

## B. SUPPLY AGREEMENTS

In addition to a license agreement, the parties may enter into one or more supply agreements concerning the sale by the transferor to the transferee of assemblies, subassemblies, components, parts and manufacturing tools, and test sets that will permit the transferee to manufacture and sell products using the licensed technology in a timely and cost-effective fashion. Alternatively, or in addition, the transferor may provide the licensee with information as to purchasing specifications and sources. Complexity arises when the transferor is the sole source of a particular component or when the component contains confidential information that is owned or controlled by a third party and that the transferor is unable to pass along freely to the transferee.

## C. TECHNICAL ASSISTANCE AND TRAINING AGREEMENTS

Again, in order to make the technology transfer more effective, it may be necessary to contract for technical<sup>57</sup> and management assistance, as well as train-

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56. When distribution rights are involved, it may be appropriate to request a trademark license as part of the technology transfer. In deciding whether or not a trademark license is necessary, a decision needs to be made as to whether it would be advantageous to identify the product made pursuant to the technology transfer agreement with any trademarks owned by the licensor. This decision will turn upon an assessment of the customer identification and quality representation inherent in the licensor's association with the product. From the licensor's perspective, it must assure itself that the licensee's products will satisfy the implied standards of quality associated with the trademark.

57. Technical assistance would include plant design, equipment procurement, machinery layout, and engineering assistance. Counsel should advise the client that many nations impose restrictions on the ability to foreigners to enter the country for any length of time to conduct some of the activities typically associated with technical assistance, and reference should be made to applicable laws on employment, entry of aliens, and work permits. In particular, attention should be paid to any specific requirements relating to the assignment of ownership rights in technology in connection with an acquisition transaction, as well as any general conditions imposed upon direct investments.

ing, from the transferor to the transferee. Assistance may be performed in the transferor's country, the transferee's country, or both. Cooperation of this type may quickly lead to a further level of involvement between the parties, particularly when the assistance relates to research, development, and engineering efforts aimed at adapting the transferred technology to the transferee's country and markets.

A transaction involving a license agreement, a supply agreement, a technical assistance and training agreement, or a combination thereof, implies a very basic relationship between the transferor and transferee. For the transferor, the relationship involves an economic decision to sell or lease a portion of its technology rights in exchange for a stream of income in the form of royalties or related fees. For the transferee, a decision has been made to make a specified investment in the acquisition of the transferor's technology rights in order to develop, manufacture, and sell products in a given market.

There will be situations, however, when a more complex relationship is appropriate, particularly if the client believes that the existing technology rights may benefit from enhancement and development efforts or if the client perceives that the transferee's home market is a desirable or advantageous locale for the formation of a more robust business relationship. This form of investment can take many forms, some of which are briefly referred to below and are subject to many of the basic concerns with respect to establishing some form of basic business presence in a foreign jurisdiction.<sup>58</sup>

#### D. JOINT DEVELOPMENT AGREEMENT

A joint development agreement, sometimes referred to as a research and development agreement, sets forth the terms upon which the transferor and the transferee will work together to make fundamental changes in, and improvements to, the technology and confidential information that is the subject of the original transfer. The following issues need to be considered in such an arrangement.

- Who will own any inventions derived from the development effort and what rights will each of the parties have with respect to such inventions?
- What will be the basis upon which each party will participate in the development effort? For example, will one of the parties simply fund the research and development efforts of the other?

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58. Without going into detail, the client should be urged to consider alternative forms of foreign presence in the market, such as sales through domestic agents or distributors, an internal program of export to the foreign market, local agents in the foreign market, or a registered presence, such as a branch office, joint venture company, or wholly owned subsidiary. The form in which the client chooses to do business in the foreign jurisdiction depends upon perceptions of such things as political risk, local control policies, discriminatory practices aimed at foreign business entities, currency considerations, export-import restrictions, the availability of skilled labor, and the competitive environment within the market. Counsel's job is to educate the client regarding potential restrictions imposed on its desired foreign presence, particularly, in the context of this article, any impediments to the desired development and protection of technology rights.

- Where will the development work be carried out, what will be the duration of the development effort, and what provisions should be made for amending or terminating the project if it proves to be unsuccessful?
- Finally, how will the inventions that arise out of the development project relate to the original licensing arrangements between the parties?

#### E. JOINT VENTURE ARRANGEMENT

The parties may choose to establish a separate commonly owned joint venture company for the purpose of exploiting the subject technology rights and manufacturing the various derivative products. Also, the joint venture company may conduct additional research and development projects. The joint venture arrangement serves a number of purposes, and obviously tends to bring the interests of the parties into much closer alignment than would be the case if the technology transfer simply consisted of a license agreement between two essentially unrelated parties.

Most of the same issues raised in the context of the joint development arrangement pertain to the joint venture arrangement. In addition, the parties must agree on the control mechanisms for the joint venture and the form of contribution that each party must make in the form of patent licenses, technical information, technical and management assistance, training, cash, capital, labor, and other similar items. Great care must be taken to comply with applicable tax and antitrust laws, as well as the particular concerns raised by governmental agencies in the country where the joint venture is to be formed. Finally, the joint venturers must achieve some consensus about the overall objectives of the joint venture and the means by which it can be terminated.

#### F. EQUITY INVESTMENT OR ACQUISITION

Generally, foreign investment can take the form of direct investment, where the investor exercises significant control over the enterprise; or portfolio investment, where the investor obtains an equity stake in the continued growth and development of the enterprise but exercises little, if any, actual management control. Foreign investment of either type may be undertaken when the investor believes that the investment will strengthen its market position in its own domestic market, the market in which the investment is made, and in any other markets where the goods and services of the foreign party can be effectively exploited.

A detailed exposition on foreign investment is not possible in the context of this article. Each nation may have detailed requirements that it imposes upon foreign investors. However, the decision to make some form of investment in the foreign party significantly broadens the type of due diligence investigation that might be required, with regard not only to technology rights, but also to any other significant assets and capabilities of the foreign party. In that situation, the

degree of emphasis upon the technology rights investigation will depend upon some of the following factors:

- The importance of the technology rights portfolio to the party to be acquired. For example, the value of a high technology company is intimately tied to the strength and utility of its patents, trade secrets, copyrights, and trademarks. As such, the bulk of due diligence in this type of transaction will focus upon the technology rights.
- The reasons for making the proposed acquisition. If the investment is to be made in order to take advantage of lower production or labor costs, or to facilitate direct marketing and sales in the country, the technology rights aspects of the transaction tend to be relatively narrow. In those cases the investor is probably more concerned about ensuring that any technology transferred to the foreign party by the investor after the acquisition is effectively protected.
- The future plans of the acquiring company in the foreign market.<sup>59</sup> For example, the acquiror may believe that a direct investment will facilitate its ability to make future penetration in the marketplace with products that have not been developed or that will be the subject of joint development efforts with employees or other parties in the foreign country.

Once again the structure of the technology transfer is really a function of a number of variables, including the goals and objectives of the transferee, and not unimportantly, the perceived value of the technology rights as evaluated through the technology rights investigation. The client will not only need to make a judgment regarding the scope and integrity and the technology rights, but also must assess the management and technical skills of the transferor and the general legal and business environment in the transferor's country.

## **VI. Representations, Warranties, and Covenants**

Representations, warranties, and covenants are of value in any commercial transaction, and inbound technology transfers are certainly no exception. Properly drafted, they can provide a basis for a common understanding between the parties as to the due diligence that has been undertaken in structuring the transaction and the ongoing expectations that have been created relating to activities following the original execution of the agreement. What must be understood, however, is that the nature of the assets in an inbound technology transfer, the technology rights originating in a jurisdiction foreign in law and culture, will require careful drafting to accommodate and record the results of the aforementioned due diligence investigation.

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59. Obviously, the factors to be considered must take into account internal commercial planning objectives, cost and distribution analysis, and a detailed economic study of the subject market.

While the exact language will be subject to some debate,<sup>60</sup> experience has shown that the transferor should make representations, warranties, and covenants relating to the following:

- (1) The transferor should certify that all material information regarding its technology rights<sup>61</sup> has been fully disclosed to the transferee, subject to any accommodations made by the transferee in order to preserve the confidential integrity of the information.
- (2) The transferor should represent that it owns each of the technology rights free and clear of any encumbrances or licenses to third parties. In those situations where the technology rights are used pursuant to a third-party license, a representation should be provided stating that the transferor possesses the right to use those rights and that the transferee will also have a similar right.<sup>62</sup>
- (3) Since in many jurisdictions it is necessary that certain actions be taken to maintain the validity of various statutory technology rights, the transferor should certify that all foreign and domestic patents, copyrights, and trademarks are valid and in full force and effect and are not subject to any current taxes, maintenance fees, or similar actions. In addition, the transferee should clearly undertake to maintain the payment of future renewal fees and taxes.
- (4) Under U.S. law there is no implied warranty that an invention has commercial utility. In other countries, however, a license implies a more

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60. The transferor may want to qualify some of the representations so that they are limited to matters within its knowledge or relate only to items that might have a material adverse effect upon the conduct of its business. For example, the transferor may represent that its technology does not, *to its knowledge*, infringe upon the rights of others or that no claim of infringement exists that will have a *material* adverse effect upon its business. Generally, from the transferee's perspective, any qualifications are inappropriate, and the transferor should bear the risk, by appropriate indemnification, of any unknown events, that in retrospect, constitute a breach of a given representation or warranty.

61. Definitions often play an important part in properly drafting the representations and warranties. Care should be taken to define precisely such terms as "trademarks," "copyrights," and "patents." For instance, trademarks might include all trademarks, trade names, corporate names, company names, business names, trade styles, service marks, logos, and other source or business identifiers, and the goodwill associated therewith, now existing or hereafter adopted or acquired, all registrations and recordings thereof, and all applications in connection therewith. Copyrights might include all copyrights in published and *unpublished* works, now or hereafter existing, and all applications, registrations, and recordings relating thereto. Finally, the definition of patents might include all patents and all applications therefor and all reissues or extensions of such patents and all continuations, continuations-in-part, or divisions of such applications. In considering the definition of patents or patent rights, several substantive issues also arise. Specifically, the parties may agree upon a particular field of use in which the patent rights are to be granted. Also, the definition should make it clear whether the patent rights extend to patents owned and controlled by the transferor. Finally, the definition of "patent rights" should take into account all prior and future patents that the parties wish to have covered by the agreement.

62. See the discussion below at para. (6) regarding the analysis that should be undertaken to ensure that full title and right of use of technology rights are conveyed in a technology transfer.

positive obligation. For example, it may be appropriate to request a representation that an invention will perform certain functions or produce a specified result.<sup>63</sup> Also, a representation may be provided to the effect that the technology is suitable to produce a specified result or product. These representations may become important in the event that the transferee wishes to utilize the transferred technology in other jurisdictions.<sup>64</sup>

- (5) Should the parties contemplate further development or enrichment of the technology package, the transferee may require some assurance regarding the transferor's ability to achieve the transferor's objectives by obtaining a representation to the effect that the transferor owns or possesses valid licenses or other rights to use all technology rights necessary to conduct its business in the manner in which it has been, and is proposed to be, conducted. A representation of this type will force the parties to discuss the future development of their business relationship and often leads to disclosures regarding the transferor's plans to acquire needed technical employees or related lines of business.
- (6) As described above, a good deal of the due diligence investigation will focus upon the possibility that the technology and confidential information will infringe upon the rights of a third party. Accordingly, the transferor should represent that it has the right and authority to use each of the technology rights in connection with its business; that such use has not and will not conflict with, infringe upon, or violate any patent or other proprietary right of any other person; and that it has not infringed and is not now infringing any proprietary right belonging to any other person. Moreover, the transferor should make it clear that there are no pending or threatened adverse claims concerning any of the technology rights, that there is no basis for any such claim,<sup>65</sup> and that

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63. Although, in the fact situation posited in the text, the client-transferee will want to push for broad representations regarding the quality of the transferred technology, generally it is a good idea to limit such representations to a warranty that the technology transferred is current and that it is the same as that used by the transferor for a certain process or similar use. Any further warranties may be inappropriate, since the ability of the transferee to achieve a given result will depend upon the conditions of its own manufacturing and production facilities, as well as the capabilities of its labor force.

64. In the People's Republic of China, a foreign supplier of technology must guarantee that it is complete, faultless, and effective and will be able to achieve the targets specified in the contract. See article 9, Rules and Regulations for the Implementation of the Regulations on Administration of Technology Impact Contracts, effective January 20, 1988. Similarly, the Republic of Korea will not permit a general disclaimer of warranties as to the quality and fitness of licensed technology for its intended purpose.

65. The parties will need to clearly allocate responsibilities in the event that a third party infringes upon any of the technology rights. Generally, issues arise as to which party is responsible for initiating any action against the infringer, which party is responsible for expenses of the action, whether the noninitiating party can join in the litigation, which party is entitled to the benefits of any reward in the litigation, and finally, the rights of the transferee against the transferor in the event of any infringement action.

no similar claims have been received in the past.

- (7) In those cases where local government approval or review of the technology transfer is required, the transferor should represent that all necessary governmental procedures have been completed.
- (8) Given many of the uncertainties associated with international patent protection, trade secrets may become the most important part of any technology transfer. The transferor should represent that all of its trade secrets are valid and protectable, are not publicly known, and have not been used, divulged, or otherwise appropriated for the benefit of any person other than the transferor. Also, a representation should be made to the effect that all documentation with respect to each material trade secret is accurate and sufficient to permit its continued usage and development without the need to depend upon the skills and knowledge of one or more specific employees.
- (9) If appropriate, key employees should represent that they are not in breach of any agreement with a prior employer with respect to the use of inventions or trade secrets. Also, to the extent possible under local law, key employees should clearly assign to the transferor any and all rights that they might have in inventions or trade secrets that may be used by the transferor in the conduct of its business, even if such technology was independently developed prior to their employment with the transferor.
- (10) The value of the transferred technology depends upon the transferor's willingness and ability to protect and enforce its statutory and contractual rights relating thereto and the transferor's interest in preserving the economic value of the rights.<sup>66</sup> As such, appropriate covenants should be obtained as to the transferor's continued vigilance in enforcing secrecy agreements with third parties, including employees, and actively pursuing infringement actions. In particular, the transferor should make specific representations regarding the procedures that it will take to

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66. Among other things, the transferor should agree to place patent or patent-pending notices on patented products or their packaging in order to place potential infringers on notice as to patent protection, to use copyright and trademark notices, and to place appropriate notices as to confidentiality and trade secrets on written embodiments of trade secret information. On a broader basis, the transferor may be required to make specific undertakings as to compliance with any working requirements for patents and trademarks, maintenance of sufficient capital and human resources to protect the value of its technology, and forbearance from business activities that are subject to governmental controls. Another component of the value of the technology rights is the transferor's willingness and ability to maintain existing standards of quality control with respect thereto, and if desirable, the transferor's undertaking to continue production of the product lines and engage in constant advertising and marketing activities with respect thereto. Finally, the transferor should also agree to maintain detailed information as to the use of all elements of the technology rights package and should also covenant that all quality control, security, and enforcement procedures will be preserved and followed after the transaction has been completed.



maintain the confidentiality of its trade secret information,<sup>67</sup> and should agree to notify the transferee of any misappropriation of any trade secret information.

- (11) Finally, the parties should address any concerns regarding the transferor's further assignment or transfer of the technology rights, by license, operation of law, or otherwise, as well as the consequences of any termination of the business, by sale, bankruptcy, government action, or otherwise, on the transferee's rights. Agreement on these points can be reached in the context of the overall remedies for any breach of the agreement by the transferor, perhaps by a reduction in the amount of royalties to take into account any diminution in the value of the technology rights or greater risks associated with reliance on the technology due to the breach of confidentiality provisions.

The foregoing list is not intended to be exhaustive. Counsel should, however, be aware of the effects of foreign laws upon the enforceability of any representations and warranties. In this regard, local counsel should be consulted before using any of the representations and warranties, and if that is not possible, counsel should strive for representations that are commercially reasonable and for remedies that have a good chance of being enforced in the context of the legal system in which the transferor is situated.

## VII. Assignment of Technology Rights

The final major element to consider in the context of the technology transfer is the actual transfer, license, or assignment of the rights from the transferor to the transferee. While the following guidelines apply to outright transfers of ownership in technology assets, they are also useful in assessing the integrity of a license or other conveyance that does not convey ownership of the transferred rights to the transferee. In addition, the checklist provides a means of evaluating whether or not a prior technology transfer to the foreign party was effective, an important consideration when such rights are being reconveyed in the subject transaction.

- (1) The transfer of patents should include not only patents, but also patent applications, continuations, continuations-in-part, or divisional applications. Claims for past infringement should also be transferred.
- (2) Any trademark assignment must also include a transfer of the goodwill that stands behind the trademark. The trademark assignment should carefully cover all trademarks, whether or not registered, and any applica-

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67. However, the ability or willingness of the transferor to actively protect its technology rights must be taken into account. In some instances, cultural factors, or the unavailability of competent local counsel and a body of appropriate law on the subject, may make it impossible for the transferee reasonably to expect that infringement or misappropriation claims will be pursued.

tions. Copyright transfers should cover all of the rights therein owned by the transferor.

- (3) Licenses may be assigned in the same manner as any other contractual agreement, although it is quite likely that any license will contain a contractual restriction upon any transfer or assignment of the licensee's rights.
- (4) While in the United States, assignments of patents, trademarks, and copyrights are effective when made, more burdensome procedures and approvals may be imposed in foreign countries, and any assignment may not be effective until actually approved by the relevant government agency. Even in the United States, any such assignment should be recorded with the appropriate governmental filing office promptly following the assignment. A covenant with regard to such a filing should usually be inserted in the documentation relating to the transaction.
- (5) Although security interests in various components of a technology rights package are possible in the United States, such transactions are simply not recognized in most foreign jurisdictions.

### VIII. Conclusion

The lessons set forth above regarding the appropriate scope of the due diligence investigation in technology transfers are applicable to a number of different forms of transactions and potential business relationships. What this article has tried to illustrate for counsel is the fact that thorough investigation can, and should, be undertaken with respect to any inbound transfer of technology rights; that very difficult issues can arise due to the disparate laws governing those rights around the world; and that the resolution of those issues can be extremely important in structuring and documenting the transaction and assessing the value of the business relationship to the client.

There is not a good deal of lore on the subject of negotiating *inbound* technology transfers, largely for the same reasons that the domestic bar is only slowly acquiring a taste for, and understanding of, the complexities of merger and acquisition activities in the United States by foreign investors. Transactions of this type can be extremely difficult, particularly when a new, and relatively small, domestic company finds itself in the midst of negotiations with a large and well-established foreign company that has achieved leadership within its industry. In those situations, counsel should bring to the table not only the concerns raised in this article, but also a careful understanding of cultural subtleties that must be observed and respected in such a transaction.