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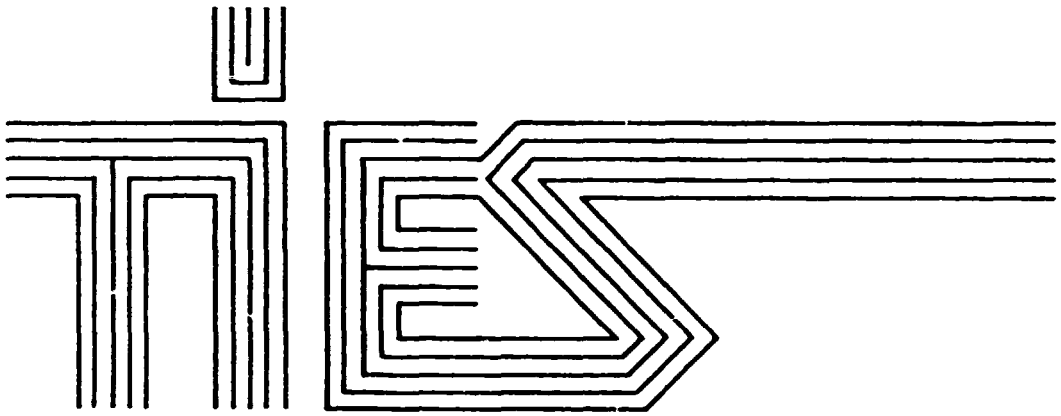

NEWSLETTER

Technological Information Exchange System

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Compiled by the Industrial Technology Promotion Division, Department for Industrial Promotion, Consultations and Technology, UNIDO, P.O. Box 300, A-1400 Vienna, Austria.

Dear Reader,

With this issue, the *TIES Newsletter* enters the second decade of its existence.

Our readers may have missed the Newsletter for some time. This was the result of a period of re-organization of our services. The activities of the Technological Information Exchange System (TIES) have also been subjected to revision and a redirecting of activities towards a new dimension, as appropriate to the changing international environment.

As a result of a thorough consideration, TIES has been given a new orientation for the years ahead, yet still keeping its identity as an instrument for the developing countries to co-operate more freely towards an increased and more effective technology flow.

TIES has matured in the last ten years and its membership is expanding, with the participating countries being fully engaged in strengthening their co-operation activities – so important to developing countries when acquiring a better knowledge of the technology market forces and gaining more equitable conditions for the acquisition of technology.

The *TIES Newsletter* is intended to be instrumental in this process. It will convey updates on TIES activities, information on developments in legislation and regulations concerned with the transfer of technology and articles of direct interest for technology negotiators.

Above all, the *TIES Newsletter* aims to increase the professional knowledge of those who are interested in international technology transfer. Our readers are cordially invited to assist us in this endeavour by giving us their comments, suggestions and contributions which may help us to better serve their interests and meet their expectations.

Technology Policy, Acquisition and Negotiation Unit
Industrial Technology Promotion Division

TIES NEWS

THE FACE OF TIES IN THE '90s

TIES, the Technological Information Exchange System, refers to a co-operative network of information and data exchange among developing countries on subjects relating to technology transfer and ranging from topics such as characteristics and conditions of the technology market and trends in technology flows, to the broader issues of technology policy, acquisition and negotiation.

Following the deliberations of, and the views expressed at the TIES meeting held in Lima, Peru in July 1989 and the Vienna Expert Group Meeting held in December 1989, UNIDO has attempted to formulate a framework for TIES in the present decade. The main elements of this concept are as follows:

1. TIES, as one of the key elements of UNIDO's Transfer of Technology programme, shall refer to the co-operative network of information and data exchange among developing countries.

2. As a result of these efforts on the part of the TIES participating countries and the UNIDO Secretariat, TIES will have the following types of data and information which will be available on a reciprocal basis under a membership-type of arrangement:

(a) Information on international technology market characteristics and trends in international technology flows as reflected in contractual terms and conditions. These are primarily statistical data that could assist developing countries in defining evaluation standards, enhance leverage during the negotiation process and improve the quality and substance of contracts being negotiated. Such information may also serve as a basis for country studies and inter-country comparisons.

(b) Information on domestic country policies and structures on technology acquisition and foreign investment; regulation; negotiation and monitoring; specific laws, rules and regulations; evaluation and monitoring policies; and institutional arrangements. This information could provide a valuable insight to particular country approaches and experiences, at the same time permitting an assessment of trends in the flow of technology in the light of such transfer of technology policies and regulations.

(c) Information on trends and developments in technology transfer and related topics which address issues of a worldwide nature, such as the General Agreement on Tariffs and Trade (GATT) negotiations affecting technology transfer to developing countries.

(d) Information on trends and developments in developed countries' legislations which may influence technology transfer and foreign investment to developing countries.

(e) Information on sample agreements or model forms of contracts. Sample agreements would correspond to practical situations and provide illustrative cases of the outcome of technology negotiations for specific sectors.

(f) Information on specific experiences on a company level in a given sector as reflected in case studies, as well as specialized information on legal, economic, financial and technical issues related to technology transfer compiled from research studies, *ad hoc* data collection and surveys.

3. It has been established that access to, and exchange of information on statistical country data under 2(a) shall be on a reciprocal basis under a membership type of arrangement. As for the other types of information, access shall be made possible through the following means:

(a) Publication of the *TIES Newsletter* on a quarterly basis. The *TIES Newsletter* will be circulated on as wide a basis as possible and is intended to become a high-profile publication devoted to technology transfer, acquisition and negotiation issues, including case studies and country reviews.

(b) Launching and circulation of the *TIES-Watch Information Notes* which will be another means of keeping TIES members, as well as potential members, abreast of current developments, trends and news on technology transfer.

(c) Preparation and launching of a series of country studies on jurisprudence and practices related to technology transfer. The first of this series will be ready before the end of 1990.

CORIS – A SPECIAL TIES COMPUTER PROGRAM

The Computerized Registry Information System, better known as CORIS, was developed by TIES. It is a software program created to enable an efficient handling, processing and retrieval of information related to technology transfer agreements negotiated by national technology transfer offices. Its purpose is to ease participation in TIES data exchange and assist in policy-making, routine evaluation and monitoring of agreements and critical planning.

CORIS has been installed and is operational in Ghana, Greece, Indonesia, Malaysia, Nigeria, the Philippines and Thailand. At the demonstration stage, it has been installed in transfer of technology registries in Brazil, China, Ethiopia, Mexico, Peru and Tunisia.

TAS PROGRAMME – TECHNOLOGY ADVISORY SERVICES

When technology negotiators require assistance in any aspect of acquiring technology they can approach UNIDO for help and guidance under the Technology Advisory Services (TAS).

This service provides fast assistance to governments and entrepreneurs in the form of impartial advice on all aspects of the technology acquisition process, starting from the selection of the most appropriate form of technology, through the preparation of tender documents, evaluation of proposals and selection of suppliers, right through to reviewing and drafting of agreements. It provides a guiding hand through the entire process, gives advice during negotiations and resolves any problems that may arise along the way.

How does TAS operate?

The service operates in two ways – one being a desk service from the UNIDO Secretariat in Vienna (Austria) from where advice can be provided based on the Organization's experience and comprehensive stock of information which may be supplemented by contributions

from outside specialists and institutions – and the other via field missions undertaken by UNIDO's staff and/or consultants, for example, in the case of large and complex industrial projects.

Some illustrative examples of TAS

1. Advisory services provided via field missions

Assistance to Rwanda in the acquisition of technology for the rehabilitation of a banana processing plant:

Upon the request for assistance from the company, UNIDO's specialized consultant undertook five missions to Rwanda between February 1988 and April 1990. The assistance was provided with the financial support of the United Nations Development Programme (UNDP). During the first mission, the consultant was able to assess the requirements of the company, send out requests for quotations from suppliers, formulate plans and complete an estimated costing.

The second and third missions provided the consultant with an opportunity to analyse the suppliers' quotations and identify the most suitable one for the task, with whom a contractual arrangement was made. A training programme was then drawn up and the actual product formulated in accordance with international specification standards. A request for bids from local contractors was then sent out for the actual transformation of the factory.

The fourth and fifth missions saw the installation of equipment and the completion of the plant, which went into production in April 1990.

2. Advisory services provided from the UNIDO Secretariat (desk service)

(a) Assistance to a Nigerian enterprise in the assessment of a licensing and joint-venture agreement proposed by a foreign partner:

Via the UNDP office in Lagos (Nigeria), UNIDO was requested by a Nigerian enterprise to assess a licensing and joint-venture agreement that had been proposed by a prospective foreign partner.

Using the expertise available within the Technology Promotion, Acquisition and Promotion Unit (with additional help from a specialized consultant), a comprehensive assessment was provided within two weeks which enabled the company to go ahead with its project in confidence and meet the required deadline.

(b) Advice to a Turkish firm on the interpretation of specific legal issues in a technology transfer contract in the light of European Community (EC) regulations:

A Turkish company requested UNIDO for advice on the interpretation of legal issues in a know-how licensing agreement in view of EC regulations on technology transfer, whereupon UNIDO called upon the services of one of its specialized consultants and was able to provide a definite clarification of the points queried by the company.

In principle, the desk services are free of charge, but UNIDO must be reimbursed for the costs incurred by field missions. In a limited number of circumstances UNIDO may, under certain circumstances, decide to use its own sources of funds for all or part of the expenses.

Requests for TAS should be sent to UNIDO at the following address through the official channels, preferably by the relevant government agency through the local UNDP office:

Technology Policy, Acquisition and Negotiation Unit
Industrial Technology Promotion Division
United Nations Industrial Development Organization
P.O. Box 300
A-1400 Vienna, Austria

WORKSHOP ON TECHNOLOGY NEGOTIATION IN CAPE VERDE

From 23 to 27 April 1990, UNIDO held a workshop on the acquisition and negotiation of technology in Praia (Cape Verde). The workshop was combined with a parallel programme of advisory services through which UNIDO staff and experts were able to assist Government officials and entrepreneurs in solving problems related to on-going and prospective negotiations. The workshop itself included lectures and discussions on the following topics:

- The role of transfer of technology in the development process
- Success factors in the transfer of technology
- Methods of technology transfer and different types of contracts
- Pre-contractual arrangements and post-contractual arrangements
- Technology market characteristics
- Methods and evaluation of technology payments
- Negotiation strategies
- Information sources for technology transfer

The provision of advisory services in conjunction with the workshop proved to be very useful and paved the way for future assistance to be provided on a regular basis. Cape Verde is a small country making valiant efforts to create basic industries and attract foreign investors, but the local promoters lack exposure to the intricacies of international negotiations and therefore need more information on current practices in technology acquisition on equitable terms. The advisory services were particularly appreciated in such areas as the evaluation of contractual conditions and advice on subsequent steps to be taken in negotiations; in the drafting of joint-venture and distribution agreements, as well as advice on negotiating strategies in specific sectors, such as the hotel industry. Through this experience, we discovered that this kind of advisory programme ought to be repeated in future, not only to solve specific problems, but also to permit the building up of local competence and future self-sufficiency.

TIES AND TECHNOLOGY TRANSFER REGULATIONS IN MEXICO

The acquisition of technology by Mexican companies has been subject to legal control by the Government for many years under the provisions of the Regulation of the Law on the Control and Registrations of Transfer of Technology and the Use of and Exploitation of Patents and Trademarks.

The Mexican Law contains very detailed provisions on the restrictive conditions that should be avoided by Mexican firms when dealing with foreign technology suppliers and specifies the situations that may lead to the non-approval of the contracts by the competent authority,

presently the Ministry of Commerce and Industrial Development.

Through the 70's and 80's, the above mentioned law on transfer of technology inspired the regulatory functions implemented by other developing countries regarding technology imports. On 10 January 1990, the Mexican Government published a Regulation of the Law on the Control and Registration of Transfer of Technology and the Use and Exploitation of Patents and Trademarks. The present regulation, while keeping the regulatory function as an instrument for a better selection, acquisition, adaptation and development of technology, takes into account the present trends of the technology market, the rules of reason and the legitimate interests of the suppliers.

There is a general perception that these new regulations represent a significant liberalization of the strict controls and supervision that the Mexican Government has been applying since the early 70's on contracting parties to agreements for technology or trademark rights.

The Mexican counterpart of the UNIDO TIES network is the Ministry of Commerce and Industrial Development. It will be the potential Mexican beneficiary of a regional project aimed at modernizing the technology transfer registries in Latin America and improving the exchange mechanisms for information on transfer of technology agreements within TIES.

VISIT OF A HIGH LEVEL DELEGATION OF LES TO UNIDO

The Licensing Executives Society (LES) has for many years had an excellent reciprocal relationship with UNIDO in the field of technology transfer and is currently co-operating with the Organization in many programmes, predominantly related to technology licensing and negotiation. A UNIDO/LES meeting held in Lima (Peru) in July 1989 in conjunction with the TIES Meeting showed that the dialogue between technology suppliers and recipients which had been jointly promoted by UNIDO and LES, has given rise to a significant improvement in the conditions for international technology flows.

On 25 January 1990, the President of the Licensing Executives Society (International), Mr. Ken Payne and Mr. Vance Smith, Chairman of LES International Agency Committee (LESIAC) paid a visit to UNIDO in Vienna, and held discussions with Mr. Alberto Araoz, Deputy Director General of the Department for Investment Promotion, Consultations and Technology, as well as other staff members. The discussions reviewed the ongoing work of UNIDO and LES, assessed the positive results achieved and explored areas where further joint work could be intensified in the future. The main ponts of discussion were as follows:

(a) Monograph series on jurisprudence and practices of developing countries related to the acquisition of technology

This series was launched by the Technology Promotion and Negotiation Unit as a sales publication intended to provide guidance to prospective technology suppliers and investors on practical conditions of doing business in those countries covered by the series. So far such monographs are under preparation for India, Peru, the Philippines and Nigeria.

(b) Training Manual on Technology Transfer Negotiations

LES representatives were briefed on the progress of preparations for the Manual, which is intended to become a didactic tool for organizing regular training courses for negotiators. Six chapters of the Manual are ready with another four almost finalized, out of a total of about thirty. Before continuing the work, it is intended to organize an expert group meeting with participants selected from the different types of possible utilizers in order to assess the material so far prepared and make recommendations for a future course of action.

(c) Guidelines on technology transfer in new fields

Both UNIDO and LES representatives reflected on the fact that the internationaal environment has undergone substantial changes in the past few years, and these circumstances combined with the emergence of new technologies, have given rise to innovative practices regarding transfer of technology, industrial property protection and business in general. It is commonly felt that on the one hand such practices are not yet sufficiently known by developing countries, and on the other that they may require further development to suit the interests and expectations of suppliers as well as recipients. Since UNIDO and LES are well aware of the views, needs and expectations of recipients and suppliers, there was a consensus on the interest of joint work in these areas, not only to disseminate information on the most recent trends, but also to develop guidelines that could suitably meet the interests of both suppliers and recipients.

Technology Aquisition

PROTECTION OF LOGOS

Many organizations now have logos, which when appearing on letterheads, posters, publications, etc., can come to symbolize the organization to the general public. The ACCIS Secretariat has obtained the following information from the World Intellectual Property Organization (WIPO), on how to protect logos, etc., from being used by other entities without the owner's permission.

The protection of a logo against unauthorized use requires that it be recognized as a trademark or as a service mark. This question depends on the law of each country in which such exclusive rights are to be established.

It should be noted that in the United States of America and the Philippines only trademarks and service marks which are already in use can be registered, whereas in other countries protection may be based on use or registration. Such countries include Australia, Canada, Cyprus, Czechoslovakia, Denmark, Egypt, Finland, Israel, Italy, Mexico, Monaco, Morocco, New Zealand, Norway, South Africa, Sweden, Tunisia, the United Kingdom and Yugoslavia. However, in some other countries, rights to a trade mark or service mark can only be acquired through registration. Such countries include: Algeria, Argentina, Austria, Belgium, Bolivia, Brazil, Bulgaria, Chile, Colom-

bia, Ecuador, Federal Republic of Germany, France, Guatemala, Hungary, Luxembourg, the Netherlands, Nicaragua, Paraguay, Peru, Portugal, Republic of Korea, Romania, Spain, Uruguay, the USSR and Venezuela.

With a view to registering logos as trademarks or service marks, in a number of countries it can be useful to first consult a trademark lawyer or agent. WIPO administers the Madrid Agreement Concerning the International Registration of Marks, to which 27 countries are party. Under that agreement, the applicant may choose the countries in which the international registration of a trademark or service mark is to have effect. International registration through the Madrid Agreement can only take place, however, after the applicant has obtained the registration of the mark in the country in which it has a real and effective commercial establishment. *(ACCIS Newsletter Vol.6, No.1, May 1988)*

AN INTRODUCTION TO THE USE OF WARRANTIES AND GUARANTIES

Following the first article written by Prof. G. Markos, Hungary, on the subject of warranties and guaranties, which appeared in the previous *Newsletter*, we are reprinting three further articles of his on the same subject. These cover warranty in the most important laws; what should be warranteed and what should be guaranteed in a contract; and preparation for negotiating warranty/guaranty conditions. As we mentioned before, the complete paper by Prof. Markos will serve as an instruction manual during training workshops on contract and licensing procedures.

Warranty in the most important laws

As already indicated in the previous article *(TIES Newsletter No.40)*, warranty – or guaranty – is a promise by the supplier that the commodity supplied under the contract will be as represented, i.e. will be free of defects and that should defects be detected, the supplier will fix (make good, correct) them.

It is obvious that any purchaser will be interested in the real meaning of such a promise, in other words:

- What defects are covered by such a warranty or guaranty; and
- What are the rights of the purchaser and the obligations of the supplier if defects occur.

In order to be able to deal with the warranty/guaranty provisions in the types of contracts usually involved in the transfer of technology transactions, we first have to briefly see what laws in general say about the subject.

The purpose and scope of this review is to review the basics of these two most important aspects.

Warranties may be implied or expressed

Implied warranties mean that a law contains obligations that are deemed to be in force in any contract subject to the provisions of that law, even if they are not explicitly stipulated in the contract.

Provisions for warranties laid down by a law may be binding or non-binding.

A binding provision of the law cannot be validly excluded or derogated by a contractual stipulation, whilst a non-binding provision can be derogated or even excluded by the provision of the contract, in which case the contractual stipulation will be valid.

Warranty or guaranty?

The statement that:

It will work and if it doesn't, I will fix it (make it good, correct it)

is a warranty. It is an expressed or contractual warranty, because it is spelled out.

Nothing is said here, however, as to how the supplier will fix it. In this respect the applicable law will govern as the above warranty is only implied.

The statement:

It will work and will produce X metric tons per hour of product with a specific power consumption of Y Kwh/ton and will have a purity of Z per cent minimum, and if it doesn't, I will make it good (fix it, correct it)

is an expressed or contractual warranty also including a promise of performance values. As to how defects will be corrected, again the applicable law will govern.

If nothing is said in the contract, the purchaser has the rights provided by the applicable law. This is a warranty by law or an implied warranty.

The promise or warranty for capacity, specific consumption and purity as indicated above is a **value warranty or warranty for performance or efficiency. The obligation under the value warranty** expires the moment it has been proved or can be deemed that the object supplied actually has the properties or **values** promised at the time of supply and no defects have been detected in this respect, or it can be deemed free of such defects (e.g. in a successful Performance Guaranty Test).

It is the obligation of the purchaser to check and test the goods on arrival and see whether they are or are not defective.

If a defect under a warranty has been detected, the supplier has to make it good only if he has been notified within a certain period from the time it was detected or could have been detected. Such time limit is indicated in a general way in the applicable law (implied) or is stated in the contract (expressed). The warranty will still remain valid for so called **hidden defects** that cannot be detected by means of conventional methods.

A claim for correction under the warranty obligation can be enforced in court only within a time limit defined in the applicable law (statutory limitations).

The statement:

I undertake to fix (make good, correct) any defect in my supplies that have not originated after I have supplied such goods, but have been detected after my obligation for value warranties is over (expired), within a period of 18 (or 24) months from my demonstration of the warranted technical values

is an expressed or contractual warranty limited to the period stated.

The statement:

In addition to the warranty (implied or expressed), I undertake to fix (make good, correct) such and such defects in my supplies which did not originate after I supplied such goods, but were detected after my obligation for value warranties was over (expired), within a

period of 18 (or 24) months from my demonstration of the warranted technical values

is a guaranty (or guarantee).

Remarks

- In some continental laws both the words warranty and guaranty mean undertakings against the defect, the cause of which was present in the goods at the time of supply, with the **guaranty** expressing a more specified, broader and stronger liability.
- In the strict legal meaning of the word, a **guaranty** is a promise by a party to make good **a wrong** committed by someone else (e.g. a bank guaranty).
- Experience has also shown that in Anglo-American contractual usage and practice, the two words are used interchangeably, or mixed, i.e. both words appear in the same contract text, with many companies offering guaranties (or guarantees) for their products in the same way that European companies do.
- It should also be considered that it is rather the content of the provisions and the consequences attached thereto than the word or name appearing above them that is more important. Any name can be used such as **defects liability clause** or **defects correcting clause** but if the clause promises that the goods will be free from defects and promises (expressly or implicitly) correction or compensation, then it is a warranty clause.

The reverse is also true. If the clause is called a warranty, but contains other promises or provisions, e.g. the maintenance of some equipment or machine, then it is either not a warranty clause at all, or it is a warranty plus something else.

As can be seen, the responsibilities of the supplier under the warranty and under the guaranty – as used here – may overlap and run parallel to one another.

What should be warranteed and what should be guaranteed in the contract?

In general, we should say that the fitness for the very purpose of the contract should be warranteed.

In a transfer of technology or licence agreement, the economic aim or purpose of the licensee or recipient of the technology is to obtain a technology and rights thereon or thereto which enable him to economically produce a product at a grade or quality that would be competitive in the markets considered.

What are the factors that are required to arrive at this aim?

- That the process can be realized and is appropriate for the production of the product at the quality required;
- That the technical means or equipment suggested by the licensor for the realization of the process will be suitable for this realization and thereby for the production of the product;
- That the production will be economic;
- That the price obtained when marketing the product will be as expected;
- That consequently the economy of the project will be as expected; and
- That the rights granted, the technology transferred, the equipment supplied can be used and the product sold undisturbed without infringing the rights of others.

Does the licensor of the process or the transferor of the technology have to warrant that the process can be realized and is appropriate for the manufacture of the desired product?

The answer is: **YES**, he has and he should.

Does he have to warrant that the equipment suggested by him for the realization of the process will be suitable and appropriate for the said realization?

The answer is: **YES**, he has and he should.

Does he have to warrant that the production will be economic?

The answer is: **NO**, he does not and he should not, because he does not lead production and cannot be made responsible for the acts of the recipient or for the conditions prevailing in the recipient's country, i.e. for wages, prices of materials, utilities etc.

Does he have to warrant that the price realized in the market will be as expected?

The answer is: **NO**, he does not and he should not. Any commercial activity and risk will be outside the scope of the licensor's responsibility.

Does he have to warrant that the economy will be as expected?

The answer is: **NO**, he does not and he should not. All economic risk is outside the scope of his responsibility and is entirely the responsibility of the licensee or recipient of the technology.

Does he have to warrant that the recipient is not inconvenienced in his rights to use the technology, i.e. the process and equipment suggested, in marketing or use of the product?

The answer is: **YES**, he has to and should do so.

How does the scope of the licensor's obligation influence his warranty?

If it is a licence agreement involving only the granting of licence rights and the supply of process know-how, then he has to warrant that the process transferred can be realized and is appropriate for the production of the product at the quality prescribed in the contract, under the conditions as prescribed in the contract and that such rights on the technology, on the equipment suggested and on the product as prescribed in the contract can be used without restriction.

What shall he warrant for if he grants a licence on the process, supplies the process and design of the plant as well as all equipment required for the realization of the process, in other words, the complete plant?

He has to warrant that the process transferred can be realized, is appropriate for the production of the product at the quality described and under the conditions specified in the contract, that the design is correct for these purposes and all equipment supplied by him will be suitable for the realization of the process; will be fit for this realization as described in the contract; will be free from defects; that the rights granted in the contract for the use of the technology and equipment as well as the marketing and use of the product, will be free from legal defects, i.e. can be used without hindrance.

As can be seen, the licensor or transferor of the technology has to warrant for the usefulness and fitness of the technology in both of the above cases. His obligation to warrant for the equipment will be that of any other independent supplier of equipment.

As can also be seen, important factors required to achieve the economic aims and purposes of the licensee or recipient of the technology are not and will not be covered by the warranty.

It is also obvious that the licensor or transferor cannot be made responsible for the commercial or economic results of production and marketing.

What can the recipient do to improve such a situation?

He can ask the licensor or transferor of technology to also provide, in addition to the said warranties, certain value-warranties, or warranty for values in the form of guaranties for such technical parameters, which technically create the foundation for an economic production.

It should be emphasized that whilst these are generally termed **technical guaranties**, such as guaranty for capacity, quality etc., they are actually value warranties, expressed or contractual warranties and not guaranties, and such an obligation will and shall terminate and expire once the supplier has successfully demonstrated that the performance values can be attained. An exception will be the mechanical guaranty, which is indeed a guaranty. As indicated, in addition to the implied warranties, values of such parameters which would lay the foundation for the economic production and marketing shall be guaranteed for the economic aspect of the project. Such parameters are called critical parameters.

Most of these will obviously be of a technical character and as such will be value warranties or technical guaranties.

For all technical guarantees it should in general be emphasized that in order to have the real effect of good warranty clauses there are, among others, two important requirements.

The first is, that the licensor or transferor should become well acquainted with local conditions, including testing the materials to be processed in the plant and the equipment, at least at the laboratory or pilot plant scale (the latter may only be done against payment). In order to be able to inform the licensee or recipient in time of the results that can be expected from the plant and also to be able to fix the parameters to be guaranteed.

The second is that the licensee or recipient should include in his preparations for the negotiations a determination as to which of the parameters are critical for him and which of these critical parameters should have priority.

It is quite obvious that a lag of a certain percentage behind capacity value to be warranteed will not have the identical impact on the losses to be suffered by the licensee or recipient as the lag of the same percentage in the purity or grade of the product or the same percentage in the specific consumption figures.

In certain cases (e.g. specific power consumption) such a lag will lead to an increase in production costs, while in others (e.g. lower purity or grade) such a lag will lead to a reduced market price for the entire production, while in other cases again it would require new investments (e.g. above a certain level of steam consumption a new boiler must be installed to cover the excess steam consumption).

When negotiating value warranties, sometimes also called performance guaranties – we will call them **technical guaranties**–the following issues are to be faced:

- Specification of expected performance;
- Testing of such expected performance and of deficiencies therein;
- Time questions must be regulated;
- Remedies available to the recipient for defaults of the licensor or transferor and for the deficiencies detected;
- Procedure for correcting deficient performance and for discharging the transferor's obligations;
- Securities covering the liabilities of the transferor or the supplier.

Preparation for negotiating warranty/guaranty conditions

It was already mentioned in the previous article *(TIES Newsletter No. 40)* that **unpackaging** is a coin with two faces for a company in a developing country.

On the advantage side there are:

- Savings in hard currency, because certain works (e.g. detailed engineering) are carried out and certain equipment is procured in the recipient's country.
- Such indigenous work and procurement helps industrial development and builds-up experience, thus increasing self-sufficiency.

On the disadvantage side there are:

- Taking responsibility away from the transferor and offering him the means to weaken his warranty or guaranty.
- Increasing the recipient's own risks, including the possibility of losing the economy made by unpackaging.

It is a task and challenge then, to strengthen advantages and reduce disadvantages.

This can be done by good preparation, good organization and increased negotiating power.

It is obvious that the more a project of a completed plant is **sliced** into a greater number of smaller contracts, the less will be the responsibility of each supplier of limiting his own liability under the contract to a certain percentage of the total value of his contract.

This tendency, which is inherent to **unpackaging**, is clearly also the desire of some transferor companies, who according to experience, make it a policy to transform even a contract for a complete plant into a package of independent agreements or contracts, licence agreements, technical assistance agreements, design agreements, training agreements, transfer of future development results agreements and equipment supply agreements. Some transferors even go so far in such **slicing** as to even have a separate guaranty agreement, independent from all others.

In such slicing practices, logical and lawful interests get mixed with clever strategical and tactical elements.

On the one hand, it is natural that if a third party or the recipient himself takes over part of the work, the transferor is not inclined to take responsibility for the results of this

work and it is his lawful and logical self-defence to exclude possible dangers which might affect his own liability for the entire result. On the other hand, attempts to further reduce responsibility beyond the logical limits should be counteracted.

This calls for a number of things to be done on the part of the recipient.

Prior to negotiating warranty/guaranty conditions, the recipient should:

- Fully understand the most critical factors or parameters in the technology (which he does not yet know well).
- Clarify what the minimum values of such factors or parameters that need to be guaranteed are, and which the transferor can and is willing to guarantee, in order to make the project lucrative.
- Clarify what exactly the transferor's supplies should and will include.
- Fully understand the meaning and substance of the warranties and guaranties.
- Carefully select the governing law by comparing rights and obligations under this law with his own requirements; he should select a law which is acceptable to all parties concerned and fully understand his rights and the transferor's and supplier's obligations within that particular law. In other words, what are the implied rights and obligations and what should be the expressed ones?
- Carefully consider the course of events in the realization of the entire innovation and its realization, in particular: In the designing phase; in the equipment procurement phase; in the quality control phase; in the transportation phase; in the storage phase; in the construction phase; in the erection phase; in the commissioning phase; in the commercial operation phase, including responsibilities, demands for data, time questions, potential delays and their consequences, potential risks of damage and their consequences, etc.

In short: **What might go wrong** in each phase and what the effects on the schedule of a delay or a defect could be.

Making a check-list of problems to be negotiated

When negotiating the warranty/guaranty conditions, the recipient should clarify and carry out:

- What the transferor believes to be critical parameters;
- What values he is willing to guarantee;
- What are the requirements of the transferor in order to be able and willing to guarantee and meet his guaranties as to: design; equipment specification; guaranteed equipment efficiency values; raw materials and auxiliary materials; utilities (quantity, specification); staff (number, qualification, experience, training); other conditions.
- To check how such conditions will be met or what is the minimum available which is still acceptable to the transferor;
- To make the transferor perform tests with samples of the recipient's materials and then revise his value warranties and prerequisites therefor;
- To consult with potential clients for the product(s) and collect their reactions and opinions;
- To jointly analyze the test results and client's or clients' responses and fix values, as well as permissible tolerances and consequences for not reaching them;
- What methods will be used to check warranted values, what instruments are required and available, where to measure, when to measure, how to measure, what tolerances the method and instruments will have and how evaluations should be done;
- What the various terms -- even the most commonly used ones such as capacity, purity etc. – mean exactly and how to define them in a clear and unambiguous way so as not to allow room for later interpretation disputes;
- To carry out a joint analysis with the transferor as to **What might go wrong, What if it goes wrong, Who does what** in such a case and **Who pays what;**
- The transferor's role in each phase and in particular in checking detailed engineering; in checking equipment specifications prior to procurement; in the selection of suppliers; in the wording of warranty/guaranty clauses in contracts with such suppliers; in preparing erection, commissioning schedule and plans based on the transferor's plans; in the quality control of critical equipment; in the testing of erection; in the training of staff.
- Exclusions of the transferor from warranty/guaranty;
- The interconnection of all the above with other clauses of the contract.

COMPUTER CONTRACTS

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Introduction

The computer industry is one of the rapidly growing areas of international trade. Not only is there a great deal of commerce in computers and their associated equipment, but there is also an increasing trade in the programs which are needed to run them. Further, the last few years have shown a remarkable development of small computers designed for one or two users, and a whole new market has developed for equipment and programs to link such computers into networks and transfer information between them.

Because of the development of the international market it has been necessary for lawyers and businessmen to develop appropiate legal arrangements for the international transfer of such products. Some generally accepted standards are now emerging in such legal arrangements.

Let us start by defining some of the parts of the computer market, and the terminology used in it. Computer-related products can be generally divided into hardware and software. **Hardware** includes the actual computers, as well as other pieces of equipment which attach to them, such as printers, keyboards, information storage devices and

communications devices. Software is the set of instructions (usually called **computer programs**) which are fed into the computer to adapt it to carry out a particular task. All computers, when they are acquired from the manufacturer, have some software with them. This software, called the **operating system** is necessary so that the computer can accept and act upon other computer programs with which it is to be used. Thus, any purchase of a computer will normally include transfer of the operating system software.

There is one other major type of software, besides operating systems. This is called **applications software**. Applications software causes the computer to carry out particular operations which the user desires. For example, computer programs to do business accounting, or to do engineering calculations, or to play a game, are all applications software.

In this paper, I shall discuss the legal arrangements which are used to govern the transfer of both hardware and software and set out the general items which must be covered in any computer contract, whether for the purchase of hardware or for the development of new applications software. I shall then discuss some of the special features of hardware contracts and some features of contracts to develop new software.

Basic Parts of a Computer Contract

A contract can be considered as a set of rules agreed upon by the parties in order to carry out some transaction. The drafting of these rules must be done very carefully, to ensure that one party does not obtain an advantage over the other by reason of the rules.

There are certain basic questions which should be addressed in all contracts for computer hardware or software. These are the following:

(a) What does the user get?
(b) When does the user get it?
(c) How much will it cost?
(d) What constitutes acceptance?
(e) Who owns it?
(f) What happens if it does not work?

In the discussion that follows, I shall use the term **provider** to mean the person who has the computer hardware or software and wants to enter a contract to sell, lease, or license it. I shall use the term **user** to mean the person who wishes to acquire the hardware or software.

Let us now turn to look at the particular clauses in a contract which deal with the questions posed above.

What does the user get?

Most contracts have a **whole contract** or **integration** clause. This clause says that the document includes the entire contract between the parties, and that the parties are not bound by any other oral or written statements which were made before the agreement was entered into.

This can be very critical. Often a salesman, who is trying to sell computer hardware or software, will make statements as to what the product can do. These statements should be included in the contract as a promise from the provider that the product will do these things. The legal term for such a promise is a **warranty**. Unless there is a specific warranty from the provider, the user will not be able to cancel the agreement if the equipment or software fails to do what the salesman said. Thus, if the contract only says that the provider is selling a "Model 1-2-3 Computer" the user may have to accept that computer even if it turns out that it will not do what the salesman promised.

Form the user's point of view, therefore, it is always important to include a specific statement of what the equipment or software is expected to do, and to have the provider give a warranty in the contract that it will do this.

When does the user get it?

Most contracts have a specific date by which the hardware or software must be delivered. If the hardware or software is not delivered on time, the user may suffer serious consequences. For example, his business may be dependent on the fact that a computer will be installed by a particular time or that a particular piece of software will arrive by a particular time. However, if he has to sue the provider, he may not be able to say exactly how much money he lost because the hardware or software was late.

For this reason, many computer contracts contain specific penalties if the equipment or software is delivered late. The user will be able to recover these penalties without giving specific proof of how much money he has lost. However, the penalties should not be too severe. If they are, the provider may decide that it is just as cheap for him not to deliver the product at all (and pay damages for non-performance), than to deliver it late and have to pay penalties.

How much will it cost?

There are several different types of contract which are common in the industry. For computer software which are already developed and which are sold widely, usually the contract is for a fixed price. Where the contract is for a new piece of software which must be specially written, or where it is for a new type of computer system which has to be specially developed, it is sometimes a fixed price. However an alternative would be to price new projects by a price which varies with the time and material costs of the provider. This is known as a **cost plus** or **time and materials** contract.

Even where there is a fixed price contract the parties may include a clause which states what will happen if there is a price change before delivery. Such a clause may provide that the user has the benefit of the lower price if the price drops, but also has the option of cancelling or paying the higher price if the price rises. In a clause of this nature, the provider must supply the product at the price stated in the contract. In international contracts, the parties may wish to include provisions which may modify the price, or permit one party to break the contract, if there is a major fluctuation in currency exchange rates between the time the contract is signed and the time when it will be carried out.(1)

What constitutes acceptance?

When a new piece of computer equipment is delivered, there is usually an acceptance test. If the equipment does not pass this test, then the user does not pay for it until it is repaired by the provider, so that it can pass the test. The acceptance test for a computer will test the computer's operating system software. Similarly, when complicated software is delivered, there is usually an acceptance test or a period of time during which the user can test the software before having to pay for it.

Before entering a contract, each party should think carefully about what testing should be done as part of the acceptance test. Often, the provider will give test data which can be used for the purpose of seeing whether the hardware or software works. However, if the provider is giving these data, he could of course arrange it so that it will not reveal all defects. Therefore, from the user's point of view, it is often safer if the user provides his own acceptance test data. However, this requires the user to spend time and money to develop test data, and it also requires him to have a good enough knowledge of the hardware and/or software so that he can develop test data which will reveal any flaws. Because of the expense and knowledge required, many users decide not to provide their own test data. Instead, they rely on the test data given by the provider.

Who owns it?

Although much hardware is sold, there is also a certain amount which is leased. When obtaining harware from a provider who is not the manufacturer, you should check to make sure that the provider owns the hardware. Further, you may wish to decide on the basis of financing costs whether it is cheaper for you to buy or lease. If you lease, you will of course have to give the hardware back to the provider, or pay an extra amount to purchase it once the lease is over.

Most software is not sold. Instead a license is given to use a copy of the software, often under certain restrictions. Most hardware has some software included.(2) Thus, even in the case of hardware which is purchased outright, there may well be a license for some software along with it. The license will give the right to use the software with that particular computer, but it will probably contain restrictions as to its use with other computers and the number and purpose of copies which can be made. The contract should be very clear as to whether it involves a lease, a license, or an outright sale, or a combination of these.

What happens if it does not work?

In international agreements, it is necessary to include a clause stating which country's law will apply. The laws of different countries vary greatly, and different results may occur depending on which law is employed. It is therefore necessary that the law of one country be named specifically so that both parties will know which law governs their obligations.

It should not be a matter of national pride for each party to try to have the law of his own country included as the law of the contract. Instead, it is a good idea for the parties to agree to apply the law of a country which has specific and clear rules relating to computer contracts.(3) In this way, both parties will know exactly what their obligations are.(4)

Apart from deciding on which law should apply, the parties should also decide on who should apply it. Often, there are several possible courts in which a suit may be brought. Many contracts contain a specific provision saying which court will have jurisdiction.

In an increasing number of computer contracts, the parties provide for arbitration instead of going to court. The reason for this is that most courts do not have judges who are specialists in computer-related fields. It is not always possible to explain a complicated computer contract so that a non-expert judge can interpret it. However, if the parties choose to have arbitration they can specify that the arbitration will be carried out by people with computer expertise. They can either do this by specifying particular people as arbitrators or by specifying particular qualifications which the arbitrators must have. If this is done, the parties often get a much better interpretation of their agreement, without having the risk and uncertainty associated with going before a non-expert court. Further, arbitration is frequently faster than court proceedings.

Often, the parties do not pay enough attention to the question of choosing which court should have jurisdiction or of choosing an arbitrator. This clause can have a great effect on the outcome if there is a dispute between the parties. For example, if one of the parties is in the Republic of Korea and the other in the United States of America, the Korean will be at a great disadvantage if the arbitration or court hearing takes place in the USA. Each time there is a hearing, he will have to travel to the USA, whereas the American party will have much less travelling and hence less cost.

If arbitration is chosen, it is possible to provide in the agreement that the arbitration will take place in a neutral country to which both parties must travel. This provides a **balance of inconvenience** so that neither party will have an advantage over the other. For example, in the situation where there is a Korean and an American it may be possible to agree that the arbitration be held in Europe. This would oblige both the American and the Korean to travel, and would therefore not give anyone a major advantage in the case of arbitration.

In many developing countries, there are specific provisions in the country's technology transfer law governing the question of which court will have jurisdiction and which law will be applied. These provisions must be taken into account as they may well limit the freedom of the parties to provide for arbitration or to provide that a specific country's law will apply.

The result of a court case or arbitration is usually the award of money as compensation for the damages suffered.

In many cases, the damages will be very high if a computer or computer program does not function correctly.(5) If the provider had to pay all of the damages, he would go bankrupt. Therefore, the provider will often refuse to sign a contract which would require him to pay all damages which may arise if the system does not work. Instead, the parties may agree that the provider's liability is limited to merely fixing whatever is wrong and that he

will not have to pay any damages for losses suffered by the user. The user will then seek insurance to protect himself from damage if something goes wrong.

The provider will usually also require a provision stating that he is not obligated to fix any problem unless he is notified within a warranty period. This warranty period is frequently very short. A ninety day period used to be normal, but now many providers are offering 120 or even 180 days.

The negotiating of computer contracts

A contract for a large purchase of computer equipment or computer software may take a very long time to negotiate. One problem is that most lawyers are not very familiar with computer equipment, and initially try to draft unrealistic contract provisions.

One way to speed up the negotiating of computer contracts and to help reach an agreement which is fair to both parties, is to use standard contract clauses. Several books have been written which give such standard clauses. For example, the United Nations Industrial Developement Organization (UNIDO) has a helpful paper on the subject.(6)

In the USA, the Association of Data Processing Service Organizations (ADAPSO) has developed a number of standard contracts for different types of computer transactions.(7) In each of the ADAPSO contracts, several different versions are given for each clause, so that the parties can choose the version which is most appropiate to their needs.

There are also textbooks which give standard clauses and comment on how these have been interpreted by the courts.(8)

As the number of computer contracts increase, it can be expected that there will be more and more **standard** clauses and that the problems of negotiation will become less difficult as lawyers and businessmen become more familiar with these clauses.

Hardware contracts

In contracts for computer hardware, all six of the basic questions discussed above are very important. However, there are certain additional matters to be considered as well.

Computer hardware can be acquired in several different ways. They can be acquired from the manufacturer, or from the manufacturer's distributor. In addition, they can be acquired from distributors who purchase the computer from the manufacturer, and purchase other equipment (such as printers, memory storage and the like) from other manufacturers, and assemble these to sell as a complete system. These distributors are usually known as OEM (Original Equipment Manufacturers) even though they do not usually manufacture equipment but rather combine the equipment of other manufacturers.

Another type of distributor is known as VAR (Value Added Retailer). VAR's usually buy a computer and associated equipment, and then add the software which they have written themselves or have obtained from another source. Thus, the product which they sell is usually a computer, along with software to carry out a particular function.

There is one problem which frequently arises when a computer is acquired from one provider and the rest of the equipment which attaches to it is acquired from other providers. The computer may function perfectly when tested alone with each of the pieces of the equipment also functioning perfectly. However, when they are assembled together, they do not work properly. This may be because they simply are incompatible (i.e. they are not designed to work together) or because there is something wrong in one piece of equipment which cannot be found by using that piece of equipment's normal test procedure.

A similar problem sometimes arises when hardware and software are purchased separately. Hardware may pass its acceptance test correctly, and the software may pass its acceptance test correctly when used on another computer. However, when the two are put together, they fail to function.

If all the hardware and software are obtained from a single provider (for example a VAR), the user can then simply demand that the provider fix the problem. It is then up to the provider to determine what is defective, and to fix it. However, the situation is more complicated when the hardware and software were supplied by different providers or where different pieces of hardware were provided by different suppliers. In this situation, each provider may say that the problem does not stem from the piece of equipment or software he provided. Under such circumstances, the user must either determine what is wrong by himself or must hire a consultant to do it for him before he can effectively make use of the warranties in his possesion. For a user who does not have much technical expertise, it is sometimes better, therefore, to buy from an OEM or a VAR who can provide all of the necessary hardware and software. In this way, no problem arises in determining which provider is responsible when the overall system does not work.

Software contracts

When a computer programmer sits down to write a program, he writes it in a human, readable, form. The program is written in a standard computer **language** which other humans can read and understand. These computer languages have names such as BASIC, COBOL or PASCAL. BASIC, for example is very similar to English, but is a more rigid language, in that each word has only one meaning. A computer program written in one of the standard computer languages can easily be read by another programmer who understands that language.

The program in this form (in which it can be easily read by a human) is said to be in **source code**. A programmer needs to have the source code form of a program if he wishes to understand how the program functions, or if he wishes to correct errors in the program or modify it in any way.

The source code form of a program may be recorded on a diskette, may be written or printed in a book, or may be stored in many other ways. However, it is not the form of the program which is used to operate the computer.

The form of the program which actually operates in the computer to carry out its intended function is called **object**

code.(9) It is created from source code by treating it in a computer with another, specialized computer program. Object code is usually recorded on a diskette which can be inserted into a computer when the program is to be used, or else it can be recorded permanently on a chip which is permanently wired into the computer, or semi-permanently on a disk within the computer. If a printout is made on paper of object code, all that is seen is a series of 0's and 1's.

Although a highly skilled computer programmer can understand what is represented by object code, it is very difficult and time consuming to read. Since most computer programs have thousands (or even hundreds of thousands) of instructions, it is not practical for a computer programmer to read a program in object code and make corrections or changes to it. Thus, if any corrections or changes or improvements are to be made to a program, the person who wishes to make those corrections or changes or improvements must, in practice, have access to the source code.(10)

Generally, computer programs are accompanied by human readable documentation. A computer program which is distributed to an end user for him to use usually has with it what is called **user documentation**. This is usually a booklet or manual, which explains how the program should be used, and often gives some examples or training aids to help a person learn to use it.

Another type of documentation also usually exists as well, although the person using the program seldom sees it. This is called **programming documentation**. It consists of an explanation by the person who wrote the program of how the steps in the program interact with each other. It is designed to help other programmers who need to understand the program. The programming documentation is very important to anyone who wants to change or improve the program. If he does not have it, he will have to study the source code of the whole program in great detail before he dares to make any changes. The reason for this is that changes in one part of the source code will affect other parts of the program, often in an unintended and serious manner. With the programming documentation, though, the programmer can read how the parts interact, and can proceed to make his changes accordingly.

You will see from the foregoing that there are four major aspects to a typical computer program. These are the source code, the object code, the user documentation and the programming documentation.

It is very difficult to prepare a contract for the development of a large piece of software. Unless the software is very simple to design, it is often not known at the time the contract is being negotiated exactly how long it will take to write. Further, the user may not know exactly what he wants, other than knowing that he wants the software to accomplish a particular job. It is therefore not possible to have a realistic estimate of the cost or even an exact description of what is to be prepared. The solution which is frequently used is to divide the contract into two stages. These may be called the **requirements stage** and the **software development stage**.

The requirements stage usually has a fixed price associated with it. The subject matter of the requirements stage contract is not software. Instead, what the provider agrees to give is a complete description of the data which the software is to process and a complete description of the result to be obtained by processing. Usually, this is defined in terms of what input information is required, in which format, the format of the screen displays and printouts which are to be provided as output. The description will be given to the user in the form of a **Requirements Document.** The Requirements Document, therefore, is that which is contracted for in the requirements stage. It defines the software to be written in terms of input of information and output of information.

When drafting the requirements stage contract special care should be taken to specify who owns the Requirements Document. Both the user and the provider would like to own this document. The provider because he can control its use. The provider will of course be interested in being hired by the user to write the software. If he owns the Requirement Document, he can prevent it from being used by another person to assist in writing the software. As the provider can use it, this gives him a special advantage in obtaining the contract to write the software. On the other hand, if the user owns the Requirements Document, he can then use it as a basis for obtaining tenders to write the software from a number of software providers. He therefore does not necessarily have to use the same provider who gave him this document to write the software.

The second stage contract, the software development contract, is usually only entered into after the requirements stage is finished and a price for the writing of the software has been determined, based on the requirements set out in the Requirements Document.

In a software development contract, the question of acceptance testing is critical. For safety, the user will probably want to develop his own acceptance test data. Further, he will want to have a long enough warranty so that he can actually use the software for a period of time to see whether there are any problems which were not found during the acceptance testing. The period of time should be sufficient to give some experience with any special reports or summaries which the software is intended to create, but which are only infrequently produced.(11)

The question of who will own the software is also quite important. There are two ways in which this may be resolved. The user may not want the software provider to write similar programs for the user's competitors. If this is the case, the user will want to own all of the software which has been created. The provider, however, will probably charge a lower price if all the user receives is a copy of the source code, object code and documentation, together with the right to use it in his own business. Under these circumstances, the provider would keep ownership of the software and the copyright to it, but would be free to license it to others This would mean that the provider can expect to get back some of his money from other such licenses and would therefore charge less than if the user was the owner.

Depending on what the user wants, he may therefore end up either with the ownership of software, or merely with a license to use it on his premises. This should be carefully negotiated. In any event, the user will probably wish to

have the source code and the programming documentation so that he can make necessary changes later on, without having to go back to the software provider.

Footnotes

1. This is of course a protection for the user, but it may also be important to the provider if he receives sub-contracted equipment from another country.

2. For example, every computer has an operating system. Sometimes this is permanently stored on a chip or disk within the computer so that the user is not necessarily aware of its existance. At other times it is supplied separately on diskettes and the user must load it into the computer. Many personal computers are now sold with some built-in applications software, such as a word-processing program.

3. Some courts will only give effect to this sort of agreement if there is some connection between the contract and the country whose law is chosen.

4. For example, many agreements for chartering ships are under the laws of the United Kingdom, even though neither party to the charter is British. The reason for this is that the British law on chartering is very well established, so that each party knows what his obligations will be.

5. For example in my country a major company bought a new computer system to keep track of billing its customers. The computer system did not work correctly and the major company could not bill its customers for six months. It almost went bankrupt as a result.

6. *The Commercialization of Software: Main Issues and Contractual Terms and Conditions* by Carlos Correa, (UNIDO/IS.574), available from the United Nations Industrial Development Organization, P.O. Box 300, A-1400 Vienna. Austria.

7. These standard form contracts are available from the Associaticon of Data Processing Services Organizations, 1300 North 17th Street, Suite 300, Arlington, Va. 22209-3899 U.S.A. The cost of such contracts is quite high to persons who are not ADAPSO members.

8. See for example, *Computer Contracts - Negotiating, Drafting* by Robert T. Bigelow, published by Matthew Bender & Co. Inc., 11 Penn Plaza, New York, NY 10001, U.S.A., (April 1987).

9. Several intermediate versions of a program between source and object code can also exist. For simplicity, these are not discussed. The principles applying to them are the same as those applying to object code.

10. A very skilled programmer may be able to deduce the source code by reversing the process by which object code is made. However, this takes considerable time and skill and runs the risk of introducing errors.

11. For example, accounting software may have some special programs which are only used once a year, at the year's end. The acceptance period should be long enough to make sure that these are used once it is in normal use.

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Recent Legislation

Philippines

Revised Rules of Procedure of the Technology Transfer Registry of the Bureau of Patents, Trademarks and Technology Transfer (BPTTT)

Republic of the Philippines, Department of Trade and Industry, Bureau of Patents, Trademarks and Technology Transfer Makati, Metro-Manila, 15 June 1988.

Department Administrative Order No. 5 Series of 1988

SUBJECT: Revised Rules of Procedure of the Technology Transfer Registry

Pursuant to the provisions of Executive Order No. 133 reorganizing the Department of Trade and Industry and its attached Agencies and Section 79-B of the revised Administrative Code, the following revised rules and regulations are hereby promulgated.

RULE I. Definitions

Section 1. For purposes of these rules and regulations, the following terms shall be understood as follows:

(a) **Registry** shall refer to the Technology Transfer Registry within the Bureau of Patents, Trademarks and Technology Transfer of the Department of Trade and Industry.

(b) **Technology Transfer Arrangements** shall refer to contracts or agreements entered into by and between domestic companies and foreign companies and/or foreign-owned companies involving the transfer of systematic knowledge for the manufacture of a product, for the application of a process or for the rendering of a service, including the transfer, assignment or licensing of all forms of industrial property rights.

(c) **Domestic Companies** shall refer to enterprises, partnerships, corporations, branches or other forms of business organization formed, organized, chartered or existing under the laws of the Philippines.

(d) **Foreign Companies** shall refer to alien enterprises or foreign firms, associations, partnerships, corporations or other forms of business organization not organized or existing under the laws of the Philippines.

(e) **Foreign-Owned Companies** shall refer to enterprises, partnerships, corporations or other forms of business organization formed, organized, chartered or existing under the laws of the Philippines, the majority of the outstanding capital of which is owned by aliens.

(f) **Net Sales** shall refer to the invoice value based on actual sales minus:

1. Trade, quantity or cash discounts and broker's or agent's commission, if any;
2. Return credits and allowances;
3. Tax, excise or other government charges; and
4. Freight, insurance and packaging cost.

(g) **Packaging Cost** shall refer to cost of materials incurred in the process of placing the licensed product in container(s), receptacle(s) or wrapper(s) necessary for marketing and transporting products to specific areas of destination.

(h) **Net Foreign Exchange Earnings** shall refer to the FOB value of the exported licensed product(s) minus the landed cost of imported materials and components used in connection with the manufacture of the exported licensed product(s).

(i) **Imported Raw Materials and Components** shall refer to non-indigenous raw materials and semi-finished products with less than 50 per cent local content, directly or actually used as inputs in the manufacture or processing of a licensed product which is completely finished and forming part thereof.

(j) **Local Content** shall refer to the difference between the manufacturing cost (which includes the cost of raw materials, labour and factory overhead, but excludes the cost of depreciation) and the landed cost of imported raw materials and components.

(k) **Landed Cost of Imported Raw Materials and Components** shall refer to the sum of the CIF value, customs duty, tax and importation charges.

RULE II. Functions of the Registry

Section 2. General Functions. The Registry shall have the following general functions:

(a) Formulate policies that would promote the inflow of appropriate technology into the desired/preferred sectors of activity with focus on the developmental and regulatory roles of the government in the field of technology transfer;

(b) Establish general and equitable standards on which to base the relationships between/among the parties to the technology transfer arrangements, taking into consideration the special needs of the country for the fulfillment of its economic and social development objectives such as the development of indigenous technology and the conservation of foreign exchange resources from the purchase of unnecessary technology and from the excessive cost of imported technology;

(c) Encourage technology transfer arrangements under conditions where the bargaining positions of the parties to the technology transfer arrangements are balanced in such a way as to avoid abuses of a stronger position and thereby to achieve mutually satisfactory technology transfer arrangements;

(d) Measure the extent of technology absorption and adaptation under the technology transfer arrangements; and

(e) Perform such other functions as may be necessary for the accomplishment of these objectives.

Section 3. Specific Functions. The Registry shall have the following specific functions:

(a) Issue rules and regulations for the effective, efficient and economic implementation of policies and guidelines relative to technology transfer;

(b) Evaluate and register all technology transfer arrangements in accordance with the national technology transfer policies;

(c) Monitor the implementation of technology transfer arrangements;

(d) Render advisory service to the private sector on the negotiation of the terms of the technology transfer arrangements and technology sourcing;

(e) Collect and disseminate information on the technologies which could be tapped by the private sector.

RULE III. Requirements for Registration

Section 4. Filing of Technology Transfer Arrangements. All technology transfer arrangements shall be submitted to the Registry, duly notarized and/or authenticated, for approval and registration, accompanied by a duly accomplished Applications Form No. TTR-1 together with the supporting documents listed therein. Filing of agreements shall be in accordance with the following schedule:

1. New Agreements – Within thirty (30) working days from the date of execution or effectivity, whichever is earlier;

2. Renewal Agreements – Within thirty (30) working days before the expiration of the term of the existing technology transfer arrangement;

3. Amendatory Agreements other than those mentioned under Section 7 of Rule IV – Within thirty (30) working days from such amendment or modification.

Failure of the applicant to comply with any of the requirements in connection with the application for registration within a period of fifteen (15) working days from the date of notification shall be construed as an abandonment of the applicator. Upon written request by the applicant, however, the registry may extend the said period.

Section 5. Date of Official Acceptance. The date of full compliance by the applicant with all the pertinent requirements of the Registry shall be deemed as the date of official acceptance, which shall be duly recorded in the Application Entry Book. A notice of official acceptance shall be issued by the Registry in favour of the applicant firm.

RULE IV. Evaluation Procedure and Guidelines

Section 6. Scope of Evaluation. The Registry shall evaluate and register technology transfer arrangements taking into account the legal, technical and economic aspects thereof in the light of national technology transfer policies.

Section 7. Decision. The Registry shall render action on applications for registration in accordance with the following schedule:

1. Within two (2) working days for the following technology transfer arrangements:

(i) agreements patterned after the ITR Model Contract on Licensing and Technical Assistance with a royalty fee not exceeding 2 per cent of the net sales;

(ii) agreements involving pure trade mark licensing;

(iii) franchise agreements with a fee not exceeding 1 per cent of net sales;

(iv) agreements which are royalty-free; and

(v) amendatory agreements to ITR registered agreements involving minor changes such as addition of new products involving the same technology under the same terms of a ITR registered agreement or change of technology supplier/technology recipient or change in corporate name of technology supplier/technology recipient;

2. Within ten (10) working days for agreements involving technology and know-how whether patented or not and trade marks with a royalty fee not exceeding 2 per cent of the net sales excluding franchise agreements;

3. Within thirty (30) working days for all other types of agreements.

The reckoning of the above evaluation period shall be from the date of official acceptance of the technology transfer arrangement as defined in **Sec. 5 of Rule III** hereof.

Upon the expiration of the periods stated above without action having been rendered, the application shall be deemed as automatically approved; provided, however, that provisions in the technology transfer arrangement which contravene **Sec. 12 of Rule IV** shall be deemed not written; provided further, that **Sec. 13 of Rule IV** shall be complied with.

Section 8. Notice of Decision. The Registry shall issue a notice of approval which shall specify the terms and conditions of registration. From the date of receipt of the said notice, the applicant shall have thirty (30) working days within which to submit its acceptance and/or the required amendment(s) or modification(s). Failure to do so within the said period may be construed as abandonment of the application.

Section 9. Draft Technology Transfer Arrangements. Applicants may, prior to the execution of technology transfer arrangements, submit drafts thereof to the Registry with the normal application, for which approval in principle may be granted, registration being withheld until the execution thereof.

Section 10. In evaluating technology transfer arrangements, the Registry shall take due consideration for agreements where:

1. The use of the technology/industrial property right(s) will lead to substantial contribution to the national development objectives and goals such as employment generation and export promotion, use of indigenous raw materials, conservation of energy, etc.

2. The use of technology/industrial property right(s) answers an immediate need, taking into account the gap between the requirement of the industry and the national technological capability.

3. The use of technology/industrial property right(s) does not result in environmental pollution and/or health hazard to employees of the technology recipient and to the community at large.

Section 11. Similarly, in assessing the reasonableness of the payment in relation to the value of the technology to the technology recipient and the national economy, the following criteria shall be taken into account: Scope, complexity and pioneering nature of the technology; importance of the technology in relation to the technology recipient's overall activity; degree of mastery of the technology by the technology supplier; stage of the licensed product in the product life cycle; use of indigenous raw materials and services; energy savings; level of priority of the licensed activity, employment generation, export earnings and its effect on the balance of payments; spill-over of technology to local industry; technology supplier's share in the technology recipient's profit; royalty approved for the industry under which the licensed product is classified.

For consistency, the royalty base shall be expressed in terms of net sales whenever applicable.

Minimum royalty shall not be allowed, unless the requested minimum royalty is proven to be much less than the royalty payments due based on historical sales and/or sales projection of the licensed product(s).

A bonus royalty of 2 per cent of net foreign exchange earnings, as herein defined, may be allowed if the technology supplier commits to an export development programme to assist a new exporter in penetrating the export market.

Royalty for the license to use trade mark(s) shall not exceed 1 per cent of net sales of the licensed product(s).

Section 12. Restrictive business clauses shall not be allowed in any technology transfer arrangement; specifically, the following clauses shall be prohibited:

1. Those which restrict directly or indirectly the export of the products manufactured by the technology recipient under the technology transfer arrangement, unless justified for the protection of legitimate interest of the technology supplier and the technology recipient, such as exports to countries where any of the party's industrial property rights will be infringed or where exclusive licenses to use the technology in these countries have already been granted;

2. Those which restrict the use of the technology supplied after expiry of the technology transfer arrangement, except in cases of early termination of the technology transfer arrangement due to reason(s) attributable to the technology recipient;

3. Those which restrict the manufacture of similar or competing product(s) after expiry of the technology transfer arrangement;

4. Those which require payments for patents and other industrial property rights after their expiration, termination or invalidation.

5. Those which provide free of charge that improvements made by the technology recipient shall be patented in the name of the technology supplier, or shall be required to be exclusively assigned to the technology supplier, or shall be required to be communicated to the technology supplier for its use;

6. Those which require that the technology recipient shall not contest the validity of any of the patents of the technology supplier;

7. Those which restrict the technology recipient in a non-exclusive technology transfer arrangement from obtaining patented or unpatented technology from other technology supplier(s) with regard to the sale or manufacture of competing products;

8. Those which require the technology recipient to purchase its raw materials, components and equipment exclusively, or a fixed percentage of the requirement, from the technology supplier or a person designated by him, unless it could be proven that:

(i) the selling price is based on international market prices or the same price is charged by the technology supplier to third parties and that there are no cheaper sources of supply; and

(ii) such requirement is necessary to maintain the quality standards prescribed by the technology supplier;

9. Those which limit the scope of production and pricing of products manufactured by the technology recipient and set a minimum volume of production, unless such a minimum volume can be proven to be reasonable, based on historical sales and/or sales projection of the licensed product(s);

10. Those which restrict the research and development activities of the technology recipient designed to absorb and adapt the transferred technology to local conditions or to initiate R&D programmes in connection with new products, processes or equipment;

11. Those which prevent the technology recipient from adapting the imported technology to local conditions, or introducing innovations to it, as long as it does not impair the quality standards prescribed by the technology supplier;

12. Those which require the technology recipient to employ personnel designated by the technology supplier, except to the extent necessary to ensure the efficient transfer of technology, or those which require the continued employment of such personnel when adequately trained personnel are available or have been trained.

13. Those which require the technology recipient to grant exclusive sales or representation rights to the technology supplier or any person designated by the technology supplier, unless the technology recipient does so on his own volition;

14. Those which require the technology recipient to keep part or all of the information received under the technology transfer arrangement confidential beyond a reasonable period, e.g. five (5) years after termination/expiration of the technology transfer arrangement;

15. Those which exempt the technology supplier from liability for non-fulfillment of his responsibilities or that which provide for a maximum amount beyond which the technology supplier shall not be liable, with regard to third party suits arising from the use of the licensed product or licensed technology.

Section 13. Requisite Provisions. The following provisions shall be required in technology transfer arrangements:

1. That the laws of the Philippines shall govern the interpretation of the same and in the event of litigation, the venue shall be the proper courts in the place where the technology recipient has his principal office.

2. A fixed term not exceeding five (5) years with no automatic renewal; however, a term longer than five (5) years may be allowed under the following conditions:

(i) licensed activity has a long gestation period, provided the royalty payment shall apply only to sales of the licensed product(s) generated for a five (5) year period; and

(ii) royalty-free agreements.

Automatic renewal provisons may be allowed in royalty-free technology transfer arrangements.

3. That the technology, if used in accordance with the specific instructions of the technology supplier, is suitable for the manufacture of the licensed product(s) or for the extension of services pursuant to the technology transfer arrangement;

4. That, on the date of the signing of the technology transfer arrangement, the technology supplier shall warrant, to the best of its knowledge, that it is not aware of third parties' valid patent rights or similar protection for inventions which would be infringed upon by the use of the technology by the technology recipient when applied in accordance with the technology transfer arrangement;

5. Continued access to improvements in techniques and processes related to the technology shall be available during the period of the technology transfer arrangement;

6. In the event the technology transfer arrangement shall provide for arbitration, the Procedure of Arbitration of the Arbitration Law of the Philippines or the internationally accepted rules of arbitration such as the Arbitration Rules of the United Nations Comission on International Trade Law (UNCITRAL) or the Rules of Conciliation and Arbitration of the International Chamber of Commerce (ICC) shall apply and the venue of arbitration shall be the Philippines;

7. That Philippine withholding taxes on all payments relating to the technology transfer arrangement shall be borne by the technology supplier;

8. That all payments relating to the technology transfer arrangement shall be remitted to the technology supplier at the prevailing exchange rate at the time of remittance.

Section 14. In the event the technology transfer arrangement shall provide for the rendering of related technical services by foreign national(s) under the registered technology transfer arrangement, the rate of fees shall be determined based on the following factors:

1. Qualifications of the technician/engineer rendering the services (background in terms of education and experience, current field of specialization, level of expertise);

2. Scope of work;

3. Amount of royalty payments or technical fees in the technology transfer arrangement;

4. Actual salary scale for a particular level of expertise in the country where the supplier of technology is based;

5. Economic benefits of the foreign technology such as increase in exports and employment generation; and

6. Time required to efficiently cover the various services to be rendered.

Section 15. Exceptional Cases. In exceptional or meritorious cases where substantial benefits will accrue to the economy, such as high technology content, increase in foreign exchange earnings, employment generation, regional dispersal of industries and/or substitution with or use of local raw materials, or in the case of BOI registered companies with pioneer status, exemption from any of the above requirements may be allowed after evaluation thereof on a case by case basis.

RULE V. Certificate of Registration

Section 16. Issuance of Certificate. Upon fulfillment of the pre-registration and registration requirements, the Certificate of Registration shall be issued.

Section 17. Certificate Registry Book. Immediately after the Certificate of Registration is issued, the title of the technology transfer arrangement and parties thereto, its registration number and date of registration shall be entered in the Certificate Registry Book.

Section 18. Cancellation of Registration. If, after investigation by the Registry, it can be established that the terms and conditions of the technology transfer arrangement have been amended or modified without reccurse to **Sec. 4, Rule III,** or the terms and conditions stated in the Certificate of Registration have been violated, the Registry may cancel the registration of the technology transfer

arrangement and require the surrender of the Certificate of Registration. Such action will be made only after the parties in whose names the Certificate of Registration was issued are given an opportunity to be heard, in line with the provisions of Executive Order No. 913 and its implementing rules.

Section 19. Sanctions. The Registry shall determine the appropiate sanctions to be imposed for such violation and/or shall recommend to other appropiate government agencies the imposition of such other sanctions that could properly be employed by these agencies under their respective charters.

RULE VI. Reconsideration

Section 20. Requests for reconsideration in respect of pre-registration conditions or specific terms and conditions shall be filed with the Registry within fifteen (15) working days from the date of receipt of the notice of approval. All requests shall be filed in writing stating clearly and concisely the reason(s) therefore, and shall, whenever relevant, be accompanied by supporting documents. The Registry shall render its decision within thirty (30) working days from the date of filing of the request.

RULE VII. Submission of Annual Reports

Section 21. For the purpose of monitoring the progress of projects which are being undertaken under the registered technology transfer arrangements, technology recipients shall submit to the Registry, not later than the last day of March of each year, the accomplished Annual Progress Report Form No. TTR-2.

RULE VIII. Penalties

Section 22. Technology recipients failing to register their technology transfer arrangements, as required under **Section 4, of Rule III** hereof, shall be subject to the following schedule of fines:

	Basic Fee	Daily Fine	Start of Penalty Period
(a) New transfer of technology arrangements	P250	P25	After the 30th working day from the date of execution or effectivity, whichever is earlier
(b) Renewal of transfer of technology arrangements	P500	P25	Date of effectivityof the renewal of the technology transfer arrangement
(c) Amendatory/ supplemental technology transfer arrangements	P100	P5	After the 30th working day from the date of execution

Section 23. The following schedule of fines for late or non-submission of Annual Progress Reports shall be imposed as follows:

	Basic fee	Daily fine	Start of penalty period
First violation	P25	P5	1 April of each year
Second violation	P50	P10	1 April of each year
Third violation	P100	P20	1 April of each year

Section 24. The penalty shall commence on the dates mentioned above and shall end on the date of filing of the application with the Registry.

RULE IX. Termination of Technology Transfer Arrangements

Section 25. When a technology transfer arrangement is terminated by the parties thereto prior to the expiration of its term, notice of such termination shall be filed with the Registry not later than thirty (30) working days from the date of such termination.

RULE X. Confidential Character of Certain Data

Section 26. Information and documents received by the Registry for registration of technology transfer arrangements shall be treated as confidential and shall not be divulged to any private party without the consent of the parties concerned. However, nothing herein should bar the Registry from releasing aggregative information on particular sectors of the industry based on documents submitted by applicant firms.

RULE XI. Transitory Provisions

Section 27. This Revised Rules of Procedure shall not have retroactive effect on all technology transfer arrangements existing and registered prior to the effectivity of these rules and regulations. All other technology transfer arrangements pending approval with theTechnology Transfer Board and carried over to the Registry shall be governed by the Technology Transfer Board rules and regulations.

RULE XII. Reckoning of Dates

Section 28. Whenever these rules and regulations prescribe a period within which an act shall or shall not be performed, the first day shall be excluded and the last day included in the computation thereof, unless otherwise provided.

RULE XIII. Notices

Section 29. Notices sent by the Registry shall be addressed to the party seeking the registration of the technology transfer arrangement at its principal place of business. Such notices may, with like effect, be delivered to its authorized representative(s) as appearing in the records of the Registry.

RULE XIV. Fees

Section 30. The Registry shall collect a filing fee of the amount of P1,000 for each application and an additional

P1,000 upon issuance of the Certificate of Registration for new technology transfer arrangements and P1,500 for each application and an additional P1,500 upon issuance of the Certificate of Registration for renewal of technology transfer arrangements.

RULE XV. Final Provisions

Section 31. All other rules and regulations contrary hereto are hereby repealed or modified accordingly.

Section 32. This Administrative Order shall take effect fifteen (15) working days after publication in the Official Gazette.

Approved:

(Signed) LILIA R. BAUTISTA Undersecretary of Trade and Industry

Recommended by:

(Signed) IGNACIO S. SAPALO Director, Bureau of Patents, Trademarks and Technology Transfer.

RECENT PUBLICATIONS

Table of contents of *les Nouvelles*, the journal of the Licensing Executives Society, Volume XXV, No. 1 of March 1990

Software Licensing in Latin America, by James Leavy;

Australia and Licensing in Pacific Rim, by David Walsh;

Japanese Approach to Innovation, by William R. Boulton;

Canada-U.S. Free Trade and Licensing, by Gervas V. Wall, Sheldon Hamilton and Sheldon Burshtein;

U.S.-U.S.S.R. International Arbitration, by Alex Keviczky;

Effective Licence Negotiating Techniques, by Paul D. Greeley;

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Biomedical Research as Philisophy, by Harvey Rubin, M.D.;

Section 337: Trade-based Remedy, by Kenneth R. Adamo;

LES International-LES Brazil Conference Programme.

Workshop for UNIDO/INTIB National Focal Points on Industrial Information Networking and Co-operation Moscow, USSR, 30 May-3 June 1988

ID/WG.474/1 International co-operation in the information field – some new trends and tendencies

ID/WG.474/2 UNIDO industrial and technological information programme: present status and future development

ID/WG.472/5(SPEC.) Report of the Follow-up Subregional Meeting on the Promotion of Intra-African Industrial Co-operation within the Framework of the Industrial Development Decade for Africa (IDDA). Tangier, Morocco, 30 May-3 June 1988

Regional Consultation on the Phosphatic Fertilizers and Pesticides Industry in Africa. Yamoussoukro, Cote d'-Ivoire, December 1988

ID/WG.475/1(SPEC.) Guidelines on the purchase, maintenance and operation of basic insurance coverage for processing plants in developing countries

ID/WG.475/2(SPEC.) Survey and guidelines on joint venture agreements among developing countries in the fertilizer industry

First Interregional Consultation on the Food-Processing Industry with Emphasis on Sugar-Cane Processing. Havana, Cuba, 26-30 September 1988

ID/WG.476/1 Study on the market aspects of by-products: diversification of the sugar industry

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ID/WG.476/3 Improvement of the productivity in the sugar-cane sector. Background paper for Issue II

ID/WG.476/4 Issue Paper I. Diversification of the sugar-cane industry

ID/WG.476/5 Issue Paper II. Improvement of the productivity in the sugar-cane sector

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PPD.82(SPEC.) Expert group meeting on exchange of information among developing countries on available technologies in the field of small and medium industries. Ljubljana, Yugoslavia, 12-14 April 1988. Report

PPD.83(SPEC.) Workshop on industrial co-operation among developing countries in the field of agricultural machinery and agro-industries. Novi Sad, Yugoslavia, 16-20 May 1988. Report

PPD.84 Export processing zones in transition. The case of the Republic of Korea

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ODG.3(SPEC.) International Conference on the "Human Dimension of Africa's Economic Recovery and Development". Khartoum, Sudan, 5-8 March 1988. Strengthening the scientific and technological capabilities in African countries for industrial development

ODG.4(SPEC.) International Conference on the "Human Dimension of Africa's Economic Recovery and Development". Khartoum, Sudan, 5-8 March 1988. Development of human resources for industrialization in Africa

ODG.5(SPEC) International Conference on the "Human Dimension of Africa's Economic Recovery and Development", Khartoum, Sudan, 5-8 March 1988. Accelerated development of indigenous entrepreneurial capabilities for small- and medium- scale industries in Africa

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IPCT.57(SPEC.) Discussion Meeting on Advanced Materials for Developing Countries, Vienna, 7-10 December 1987. Experts' working papers

IPCT.58(SPEC.) Expert Group Meeting for the Asian and Pacific Region, in preparation for the First Consultation on the Sugarcane Processing Industry, Guangzhou, People's Republic of China, 22-24 March 1988. Report

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IPCT.60(SPEC.) Expert Group Meeting on Small- and Medium-scale Enterprises including Co-operatives. Harare, Zimbabwe, 7-10 June 1988. The role of small- and medium-scale enterprises in the economic development process. Introductory comments.

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IPCT.62(SPEC.) Expert Group Meeting on Small- and Medium-scale Enterprises including Co-operatives. Harare, Zimbabwe, 7-10 June 1988. Guidelines and specifications for the construction of small-scale industrial estates in developing countries

IPCT.63 Software production: organization and modalities. Prepared by Hans-Jochen Schneider, UNIDO Consultant

IPCT.64(SPEC.) Expert Group Meeting on Small- and Medium-scale Enterprises including Co-operatives. Harare, Zimbabwe, 7-10 June 1988. Institutional infrastructure for the promotion/development of small- and medium-scale enterprises in Africa

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IPCT.55 Meeting of the Consulting Group on Informatics Technology for Development, Vienna, Austria, 14-16 December 1987. Report

ID/353/Corr.1 (ID/WG.468/15.Corr.1) Second Consultation on the Training of Industrial Manpower, Paris, France, 14-19 September 1987. Report. Corrigendum

ID/357 (UNIDO/IIB/SER.B.62) Industrial development abstracts (introduction) UNIDO Industrial Information System (INDIS) Nos. 15401-15700 (ISSN 0378-2654 $US22)

ID/357 (ID/WG.470/11) First Consultation on the Non-ferrous Metals Industry, Budapest, Hungary, 30 November-4 December 1987. Report

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