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LEGAL ASPECTS OF DOING BUSINESS IN THE UNITED STATES

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I. INTRODUCTION.

While the U.S. is the largest and perhaps the most attractive market in the world, proper planning and structuring of an investment is critical to long term profitability. These materials are intended to highlight some of the major business and legal considerations which must be addressed when contemplating an investment in the U.S.

The preliminary considerations to be discussed are market research, preparation of marketing strategy, obtaining appropriate governmental approval of products and protection of proprietary information. The six (6) basic methods of product introduction in the U.S. will be addressed. They are:

1. Independent sales agency;

2. Distributorship;

3. Patent or know-how manufacturing license;

4. Joint venture;

5. Acquisition; and

6. Creation of wholly owned subsidiary.

Negotiating techniques in the context of significant cultural distinctions between Europeans and Americans will be covered.

A brief list of legal issues which should be negotiated with your U.S. business partner will be given. Also discussed will be immigration, product liability, antitrust, taxation and secured transactions law. Finally, a brief outline is provided of some of the author's eighteen years of experience in assisting European companies doing business in the U.S. concerning key characteristics of successful entries on the U.S. market.

II. PRELIMINARY CONSIDERATIONS.

There are three (3) major reasons why foreign corporations fail in being successful in the U.S. Although they have little to do with law, they merit mentioning here because of their repeated occurrence.

First, the foreign company is not aware of the size, structure and other aspects of the U.S. market. Channels of distribution may be very different in the U.S. than in Europe. Indeed, sixty percent (60%) of the time, the path that a product takes from manufacturer to the end user differs in the U.S. from Europe. Without thoroughly researching the structure of U.S. market for the specific product in question, and its distribution, including the potential for one's products, doing business in the U.S. will be a gamble. Don't sign up with the first company that comes along and offers its assistance. Be reluctant to provide exclusive deals that cover large geographic and customer territories. Indeed, avoid, if possible, granting exclusive rights at all. Please make sure that your potential partner actually can do what it says it can.

Second, foreign companies often fail to adapt their product to the U.S. market. Differences abound in technology, particularly in the electronics, construction and

consumer markets. The U.S. continues to cling to the foot and pound sterling system of weights and measures. Appropriate adaptation includes using American specialists to prepare brochures and other promotional materials, instructions and warning labels. Keep in mind that direct translators of a foreign language into English rarely is effective.

Third, if the foreign company decides to set up its own operations, it often does not have the financial capability or patience to wait two or more years to begin making money in the U.S. To be successful, one must be prepared to invest substantial sums on advertising, marketing, instruction and consulting services, all of which may be insignificant expenses in the already developed home market.

A. Market Research

Prior to investing in the United States it is essential to obtain a correct assessment of the U.S. market for one's products.

Understanding the vastness of the U.S. by the use of demographics is essential. Among other demographics, one should consider number, geographical dispersion and actual (as well as potential) purchasing volume of customers - be they businesses or consumers. Cultural differences abound as well throughout the land. Over twenty-five million Americans speak Spanish as their first language. The country is often divided into seven, twelve, twenty or even fifty different geographical territories alone.

Information concerning competitors which will be invaluable in selecting a marketing strategy will be:

1. A profile of each competitor;
    a. size, financial strength;
    b. affiliations with other companies
2. Market shares of each competitor; study recent trends;
3. Methods of marketing, including channels of distribution;
4. Technology of competitive products; and
5. Consumer perceptions of competitors.

Just because the U.S. market is the largest in the world does not mean that selling products will be easy.

1. Many European companies fail, having mistakenly assumed that their superior technology products will sell themselves.
    a. Some products may be near the end of their life-cycle in the U.S. and, therefore, not have much market potential.
    b. Similarly, the market for a product may be saturated and market entry extremely difficult and time consuming.

c. Americans are extremely price sensitive. Consequently, a product that is superior technically, with advanced features and lasting longer, may nonetheless be successful if priced significantly higher than competitors.

2. The largest market means the fiercest competition.

The Poste d'Expansion Economique in the United States, with a major presence in Chicago, is ideally suited to assist in market research studies.

1. Specialized marketing managers focus on one (1) industry to provide exceptional service to clients.

2. The marketing managers, being of European extraction, understand the European style of doing business and can highlight differences in approaches.

3. The Poste d'Expansion Economique is substantially less expensive than other competitive marketing research services.

U.S. Embassies in Europe also possess a wealth of information concerning demographics, business trends and can assist in making valuable contacts.

B. <u>Preparation of Marketing Strategy.</u>

Too many European companies have a preconceived idea concerning how to approach the U.S. market. Successful marketing in Europe does not necessarily mean that the same approach will be successful in the United States. Generally, consumer loyalty is not as great in the United States as in Europe. Consumers are price sensitive and extremely receptive to advertising.

Prior to selling in the United States you must determine:

1. Whether to start out on a regional basis (many successful European companies started by building beachheads in the Midwest), or go nationwide from the outset;

2. A pricing policy, whether to obtain market share via low prices or attempt to be profitable from the start; and

3. The method of marketing the products, whether by wholly owned subsidiary, independent sales agent, distributor, joint venture, patent, know-how or trade secret license, or acquisition (discussed below).

The Poste d'Expansion Economique can be of assistance in devising marketing strategy in the United States. Additionally, it can assist in making contacts with prospective U.S. business partners and set up participation in U.S. trade shows.

C. <u>Government and Other Approvals.</u>

1. Food and Drug Administration (FDA).

a. Any product that will be consumed by individuals must be reviewed in the context of the requirements of the Food and Drug Administration approval. As this is quite complex, it falls beyond the scope of this outline. Please contact the author for further information.

2. Underwriter's Laboratories (U.L.).

a. U.L. approval is not a legal requirement for selling products with electrical components unless the products are for sale to the U.S. government. However, it is a marketing necessity. U.S. consumers view U.L. approval as an assurance that the product performs as designed, despite the fact that it is solely an assurance of safety.

b. U.L. approval takes several months to obtain.

3. ISO 9000 Approval.

a. Although not a legal requirement, ISO certification is rapidly becoming a marketing necessity, particularly in major industries, such as the automotive and electrical industries.

D. <u>Intellectual Property Rights</u>.

Intellectual Property, or IP, is most often a company's primary asset. Unfortunately, we have found many clients totally unsophisticated in what steps can and need to be taken to protect this most vulnerable property. Software developers mistakenly sell programs instead of licensing them. Machinery and equipment manufacturers sell equipment with sophisticated components on software without specifically licensing that which is their IP. The sale of technology carries with it all the rights of ownership, including, in some instances, the right to copy and resell.

IP law is also evolving very rapidly in the U.S., resulting in greater protections being available to sellers, even for their unique designs, called trade dress, discussed briefly below.

1. Patent rights

Patents provide monopoly rights for inventions of all kinds, including ornamental designs. The United States Patent and Trademark Office (USPTO) handles all patent applications in the U.S.

a. Utility patents valid for twenty years initially; design patents, fourteen years.

b. Available to first to invent, not first to file patent application.

c. The USPTO offers reduced application related fees for small business entities.

d. An applicant may file a provisional application prior to filing an application for patent. The advantages of filing a provisional application include:

i. No requirement to submit claims

ii. The filing date of an application (including a PCT or foreign application) will be accorded the filing date of the provisional application if filed not later than twelve (12) months of the filing date of the provisional application.

iii. Applicant has twelve (12) months to submit a standard application containing claims.

iv. The priority date based on a provisional application will not be counted as part of the twenty (20) year patent term.

e. If an applicant has filed a patent application in a foreign country, the applicant has up to one year to file a U.S. application (Patent Act § 102(d)) to prevent a possible statutory bar.

f. International patent applications submitted through the Patent Cooperation Treaty designating the United States will be treated the same as a U.S. national application.

g. Courts provide significant protection against infringement.

i. Infringement may occur even if the infringing product is not identical but performs substantially the same function as the patented product.

ii. Infringing products offered for sale or imported into the U.S. are also be considered infringing activities.

2. Copyrights

Monopoly rights granted to original writings, and other artistic creations, including music, advertising, labels and computer software.

a. Must be independently created.

b. Copyright does not protect ideas. It only protects the expression of those ideas. Moreover, it does not protect facts.

c. The duration of copyright protection for works created after 1977 is the life of the author plus fifty years. Copyrighted works created and published prior to 1978 are valid for seventy-five years from the date of publication provided that the works were timely renewed. Works created but not published before 1978 remain copyrighted at least until the year 2002.

d. Proper copyright notice includes "©" [name of author] [year of first publication].

i. Registration is now permissive and provides for depositing copies of the work with the U.S. Patent and Trademark Office (USPTO) plus a $20 fee.

ii. Registration is a pre-requisite for a lawsuit for infringement in the U.S. and a pre-requisite to suing for statutory damages and attorney's fees.

3. Trade secrets

A trade secret is information that is not generally known and is used by a company in business to obtain an advantage over competitors who do not have it, and is subject to the reasonable efforts by its owner to maintain the secrecy of the information.

a. Can include customer lists, formulas, know-how, computer programs, etc.

b. Trade secrets can exist for an unlimited time.

i. Caveat: if no longer a secret, it's lost.

ii. Owner or holder of trade secret must exercise sufficient precautions to secure the trade secret.

c. Trade secrets are only protected against unlawful use by others. There is no protection against independent discovery or reverse engineering.

4. Trademarks/trade dress

Trademarks and trade names play an important role in marketing in the United States.

Trademark and trade name protection exists the moment the product is introduced into U.S. commerce. Registration is simple and inexpensive and establishes a priority date to protect the owner of the name or mark from unlawful use by others. This is particularly important when contemplating the licensing of rights to sell, distribute or manufacture the product.

Trademark and trade name protection can now even be obtained prior to a product being sold in the U.S. if the foreign company plans to commence selling in the U.S. within one (1) year of filing.

An application for trademark or trade name registration takes approximately one (1) year for processing, yet as of the date of filing an application, one manifests an interest in the name or mark.

a. Trademarks identify the source of products or services.

i. Trade names and service marks are also covered by trademark law.

ii. Trade dress, a non-registered trademark, covers packaging, containers, labels, some product configurations, the "look and feel" of products, size, shape, color, texture, graphics, etc.

b. Advantage: a trademark or trade dress is protectable for an unlimited time, unlike patents and copyrights.

E. Protection and Exploitation of Intellectual Property Rights

Proper use and exploitation is the best way to protect of intellectual property rights in the U.S. Thorelli & Associates recommends starting up internal intellectual property audits to determine current status of intellectual property, its creation, protection and status of exploitation and possible infringement.

1. Declaration and registration

a. Patents

If there is a possibility that the patented item will be marketed in the United States, a patent application should be filed in the United States as soon as possible after filing in Europe. Specialized patent attorneys should be retained to assist.

i. Registration with USPTO

ii. First to invent

iii. Declaration on products, brochures

2. Copyrights

a. Use of “©" [name of author] [year of first publication] is strongly recommended although not required.

3. Trade secrets

a. Use of confidentiality agreements.

b. Maintaining strict confidentiality in-house.

c. Stamping all secret information as "confidential".

i. Implement corporate policy on intellectual property

ii. Informing staff of confidentiality requirements

4. Trademarks/trade dress

a. Use of "TM11 to establish common-law rights and intent to protect trademark.

b. Use 0 for registered marks.

c. Advertising and promotion of the name in association with a product for service (creation of "secondary meaning").

d. Pursue infringers of mark.

5. Trademark registration

a. Trademark search - Thomson & Thomson a good choice.

b. Plain lettering - broadest protection.

c. Intent to use registration.

d. Use of foreign registration.

e. Creating best trademarks

i. Corned words - word without dictionary meaning (e.g., Pepsi®), Acura®, Volvo®), Xerox®).

ii. Arbitrary marks - word commonly known but used for a product with no relationship to its common meaning (e.g., Apple® for computers, Banana Boat® for clothes).

iii. Suggestion marks - generally suggests or leads reader in a direction but does not describe the product.

iv. Avoid descriptive marks

- UNINTELLIGIBLE
- Beware of translations

♦ Electrolux
♦ ICA
♦ Tabort

f. Impact of registration:

i. Incontestability after five years

ii. Can seek treble damages in infringement suit as well as attorney's fees

7. Internal policy

In order to enforce one's rights with third parties, one must implement appropriate measures within one's own organization to protect the rights.

a. In-house confidentiality obligations.

b. Work for hire.

c. Creation of intellectual property outside of work by employers, agents or contractors.

d. Maintaining trade secrets.

e. Ownership of intellectual property issues.

f. Thorelli & Associates prepares such internal policies.

8. Proper use and protection of trademarks

a. Use trademark as adjective, not noun or verb (risk of becoming generic).

b. Use trademark designations Tm and 0.

c. Use trademarks consistently - otherwise they are different marks.

d. Use trademarks distinctively.

F. <u>Enforcement of Intellectual Property Rights</u>

1. Regular trademark searches.

2. Cease and desist letters.

3. License negotiation as an alternative.

4. Litigation.

G. <u>Recent Developments and Evolution of Intellectual Property in the United States</u>

1. Former policies

a. Limited to patents and some copyrights.

b. Ambivalence toward trademark registration, although trademark law (Lanham Act) is fifty years old.

i. Impact: many trademarks became generic names due to lack of proper protection. Examples include kleenex, escalator, cellophane, aspirin, etc.

ii. New policy: everything is protectable and has value.

2. Trade dress

In the past trade dress referred only to packaging or displays of goods. Trade dress relates to today, courts have extended this to include some product configurations, namely the design and appearance of the product itself, including the form, color and shape of a product. This is the most rapidly evolving area of intellectual property law. It extends the protection of intellectual property beyond what traditionally has been protectable in the U.S. It now provides immediate protection for the unique shape, color and/or form of a product. Although the full extent of these developments are unclear today, we believe that clients' products that nonetheless is not protectable through patents or copyrights, may still be protected through trade dress. For example, even though a company's break bleeder, or lifting pump, is not protectable under patent law, these products can still be protected against direct copying through trade dress principles. This can effectively prevent competitors from making direct copies of your products!

The legal basis for these developments is the Supreme Court's recent decision in the Two Pesos, Inc. v. Taco Cabana, Inc., 112 S. Ct. 2753 (1992) case. In an effort to protect consumers from unnecessary confusion, the Supreme Court upheld the rights of a restaurant owner in the design of his restaurant from being identically copied by a competitor. Similarly, if a cheap copy of a product is introduced into commerce, customers, expecting to buy the product that they always have, end up buying an inferior quality product that does not function as effectively. The Supreme Court reasoned that such confusion could not serve the end user's interests, and consequently ruled that direct copies were a violation of the originator's trade dress rights.

As you can imagine, the far reaching ramifications of the Two Pesos case can change the shape of intellectual property law. Designers of furniture and other consumer products can be protected against "knock offs". Manufacturers of tools and equipment can be protected against direct copies.

Thorelli & Associates is following the developments of trade dress law closely, and is currently engaged in several lawsuits protecting the rights of original designers and developers of products that have been unfairly copied.

a. Examples include the "look and feel" of products (series of greeting cards) the design of restaurants (Mexican restaurant).

b. Almost anything may be a trademark if it is capable of human perception and serves to identify the source of a product or service and carries the producer's good will.

2. Trade dress need not be registered as a trademark to be protected. Section 43(a) of the Lanham Act protects unregistered marks.

3. Supreme Court case Two Pesos, Inc. v. Taco Cabana, Inc., 112 S. Ct. 2753 (1992).

a. Breakthrough trade dress case. Trade dress is immediately protectable under Section 43(a) of the Lanham Act without any showing that it has acquired secondary meaning, if the trade dress is inherently distinctive.

4. Product packaging vs. product configuration

a. Product packaging.

More traditional trademark issues because the packaging is not the product itself, and serves to identify the seller/manufacturer.

b. Product configuration

Not a symbol of the manufacturer, but the product itself. As a result, product configuration cannot be suggestive, or descriptive of the product, nor arbitrary or fanciful in relation to it.

Product configuration inherently distinctive if it

i. is unusual and memorable;

ii. is conceptually separable from the product;

iii. is likely to serve primarily as a designator or origin of the product

5. Court interpretations of recent trademark cases

Supreme Court has not ruled on product configuration per se. District Courts are split on product configuration as trademarks

6. Functional vs. non-functional aspects

a. Advice: create own "inherently distinctive" look for product, and promote the particular appearance of your product separately from your other identifiers (trademarks and other source identifiers).

7. Implications of trade dress law developments: trade dress, like other trademarks, protects the distinctive appearance of a product for unlimited duration, unlike patent or copyright protection, which is limited in duration.

8. It also expands the protection against pure counterfeiters, or people trading on the goodwill of the originator of the mark.

a. Examples

H. Legal Aspects of Licensing and Exploiting Intellectual Property

1. Most important: define the intellectual property to be licensed.

a. Specify patents, areas of technical know-how and trade secrets, trademarks, copyrights, etc. (intellectual property audit, intellectual property protection).

b. Limit to current, known technology. Do not license later developed or after acquired intellectual property.

2. Limit areas of use

a. by industry, by product, by consumer (end user, integrator, etc.)

b. customer restriction

c. geographic limitation

i. anti-trust aspects

3. Exclusive vs. non-exclusive license

a. Up front payments for exclusives

4. Sublicensing rights

5. Payments

a. Royalty calculations, preferably by percent of either value of product produced or sales.

i. If fixed price per unit, include inflation adjustment.

b. Minimum annual royalties to retain rights.

6. Protection of intellectual property

a. Ownership, patent and trademark filing fees and registration responsibility should be with licensor to ensure proper handling.

b. Who prosecutes infringers?

c. Who defends attacks against the intellectual property?

7. Confidentiality-critical for post termination use of proprietary information

8. Development of new technologies during term of license agreement

a. by licensor-should be eliminated from the license agreement.

b. by licensee, should call for cross license and provision preventing licensee from "blocking" licensor's intellectual property.

i. Antitrust aspects

9. Product liability considerations

10. Termination provision

11. Covenant not to compete

12. Governing law

III. METHODS OF PRODUCT INTRODUCTION.

As stated earlier, the basic methods of introducing a product in the U.S. are via independent sales agent, independent distributor, patent, trade secret or technology licensee, joint venture, acquisition, or wholly-owned subsidiary. The best method depends on a myriad of factors including the commitment made to the U.S. by the foreign company; the marketing strategy chosen; the size and strength of the foreign company; the structure of the U.S. market; the availability of raw materials and/or appropriate partners; and competitive factors.

If you desire to increase the use of existing capacity of your plant or wish to approach the U.S. market conservatively at the outset, engagement of a sales agent or independent distributor may be the best approach. If you desire to take advantage of lower raw materials, labor or production costs or you are faced with excessive transportation costs or customs duties, perhaps licensing your technology, entering a joint venture, acquiring a company or setting up your own operations is desirable.

In assessing the proper method of introducing your products in the U.S., please bear in mind the vastness of the country. The U.S. is over five (5) times the size of Europe and has four (4) times the population. You cannot reach the entire U.S. from one location. A distribution network must be part of the long term marketing scheme.

Below is a brief description of the salient characteristics of the six (6) methods of product introduction along with a summary of advantages and disadvantages of each.

A. Independent Sales Representative.

An independent sales representative is a sales agent selling products in the name of the foreign principal. Generally, the independent sales representative:

1. Solicits orders from customers in exchange for commissions;

2. Never takes title or possession of products;

3. Provides no after-sales service to customers;

4. Has no responsibility for shipment or delivery of products to customers (drop shipment by the foreign company); and

5. Assumes no responsibility for billing and collection of fees (this is the responsibility of the foreign company).

Advantages.

1. Small commitment to agent. Relationships normally terminable on thirty (30) days' notice.

2. Inexpensive as initial U.S. investment.

3. Manufacturer is responsible for shipping, billing and collection which gives the manufacturer control over customer relationship.

4. Conservative initial investment in the U.S.

Disadvantages.

1. Little control generally over agent.

   a. Agent may not properly market products and even damage goodwill.

   b. Agent may send bogus orders to Europe.

   c. Agent may sell competitive products also and not promote the European company's products properly.

2. The European company must pay high commissions to obtain cooperation (decreases profitability).

3. All responsibility for shipping, service, repairs, collection, etc., rests with the European company.

   a. Agent often does not investigate credit worthiness of customers. This should be part of the negotiations.

4. Difficult to generate enthusiasm within European company's organization.

5. The European is company responsible for patent, trade name and other proprietary information protection.

6. If the relationship terminates, the European company will have difficulty in servicing accounts.

7. The European company will often get incomplete feedback about customer perceptions and complaints, and about competitors' strategies.

8. Product liability responsibility rests almost exclusively with the manufacturer.

B. <u>Independent Distributor.</u>

An independent distributor purchases products from the European company and warehouses them. Thereafter, it sells the products for its own account.

Independent distributors provide after sales service to customers yet product liability responsibility usually rests with the European company, as does patent and trademark protection.

Profits to the European company come in the form of sales to the independent distributor.

Advantages.

1. Substantial commitment by distributor through the purchase and warehousing of product.

2. All risks in sales are distributor's except for perhaps product liability and patent protection.

3. The European company benefits from pre-existing goodwill of distributor.

4. Independent distributors can provide entry into a large distribution network, a key factor in the huge U.S. geographical market.

Disadvantages.

1. Distributor may also sell competing lines which are more profitable.

2. Profits limited due to need to give distributor high profit margin to encourage sales.

3. Customer loyalty may be with distributor rather than with the European company.

    a. The European company generally has little or no contact with the U.S. market and may, therefore, be left with nothing if the relationship is terminated. This indicates need for an attorney to negotiate favorable terms in the event of termination.

C. <u>Patent, Trade Secret or Know-How License.</u>

A patent, trade secret or know-how license is a grant of the right to use proprietary information usually in exchange for an initial down payment plus a royalty.

Generally, the licensor of the technology is expected to protect and enforce the proprietary information from infringement or misuse (differs from common European practice).

Advantages.

1. Often a substantial down payment if exclusive rights are granted, followed by royalties.

2. Spreads development costs and maximizes income from development project.

3. Makes possible the quick, competitive introduction of products in the U.S.

4. Small initial investment - no need for major capital export.

5. Possible synergism with U.S. licensee who has technology and marketing capabilities.

6. Simplicity of administration.

    a. After start-up phase where intensive technology transfer and consultation is necessary, licensor generally can shift attention to other matters and enjoy royalty payments.

7. Overcomes domestic content legislation which, in sales to government funded projects, requires at least fifty percent (50%) U.S. content. Also eliminates risk from protectionism, including customs duties and quotas.

Disadvantages.

1. Although licensor is protected by patent, licensees sometimes appropriate technology for own use.

    a. Attempt to "engineer around" licensed technology.

    b. Patent litigation is lengthy and expensive.

2. Difficult to locate trustworthy partner. Even if an agreement is carefully negotiated with assistance of an attorney, trust is key element to the relationship.

3. Difficult to control quality in manufacture which could damage goodwill.

4. Difficult, if not impossible, to reacquire all technology from licensee. You may be putting a prospective competitor in business.

    a. Underscores the need for careful negotiations of licensing agreement requiring disclosure of books and records, customer lists, price lists, etc.

D. Joint Ventures.

A joint venture is the ownership of a single enterprise by two (2) or more partners. A joint venture can be a partnership or a corporation and is generally created for a single project or series of projects. If a partnership, the European firm might lose tax treaty protection due to the existence of a permanent establishment. (See Taxation, below).

Joint ventures are most commonly used when an outstanding match between parties exists. A company with technological expertise may form a joint venture with a marketing company, for example.

Advantages.

1. Risk sharing - lower financial commitment.

2. Hopefully a synergistic effect, utilizing U.S. company's manufacturing or marketing expertise.

3. Share in profitability of company.

4. Can take advantage of pre-existing goodwill of U.S. partner.

Disadvantages.

1. Differing management styles. Trust, communication and common goals are critical ingredients.

2. Financing of cash shortfalls are difficult to agree on if no structure is set up.

3. U.S. partner may have own similar products which they will emphasize in marketing.

4. Joint ventures generally require a great deal of disclosure and information sharing between the partners.

5. Future difficult to predict. Partners often drift apart.

6. Termination generally difficult and unsatisfactory. One may put a competitor in business.

E. Acquisition

Acquisitions are achieved via the purchase of stock or assets of a U.S. company. Acquisitions usually occur when the European and American companies match exceptionally well and the European company has substantial financial resources available to acquire the company.

Advantages.

1. The European company "assumes" the position of the target company.

a. Goodwill, management team, infrastructure, distribution network, etc., can all be acquired if skillful and thorough negotiations and agreements are prepared.

b. You become a going concern immediately.

2. Gives European company complete control over introduction of own products.

Disadvantages.

1. Complex, lengthy and often expensive negotiations for acquisition.

2. Expensive initial investment in the U.S. with a large financial risk.

3. May not have proper assessment of marketing potential of product which leaves European company in a different business than initially intended.

4. Hidden liabilities of the company may arise; departure of key personnel; etc. European companies who buy U.S. companies without legal advice are looking for trouble.

F. <u>Incorporation of Subsidiary.</u>

A wholly-owned subsidiary gives the parent corporation direct and exclusive control over its involvement in the U.S. market. The subsidiary can be a sales representative, distributor, licensor, or licensee of the parent company's technology.

Incorporation requires the following simple steps:

1. Obtain clearance of corporate name with the Secretary of State in the state where you want to incorporate (to decide on a suitable state, consult your U.S. attorney);

2. Describe the purposes for which the corporation will be organized;

3. Disclose the type of stock to be issued and the number of shares to be initially issued;

4. State the consideration for the shares;

5. State the initial number of members of the Board of Directors; and

6. Appoint the Registered Agent of the company.

There is no longer any minimum initial capitalization required in most states.

Normally, in order for a direct "Greenfield" operation to be successful in the U.S., qualified American marketing specialists must be hired. It takes too long for foreign management to understand the market and how to market to it.

If a subsidiary is incorporated, you must carefully structure the relationship between the European parent and the subsidiary from the outset, on an arm's length, commercially reasonable basis. Unreasonable pricing or other concessions can lead to problems with customs duties, anti-dumping laws and general taxation.

Advantages.

1. Low cost of incorporation.

2. Complete and exclusive control.

3. Establish independent presence in the U.S.

   a. Build goodwill.

   b. Commence independent credit line.

4. Flexibility - can still negotiate previously described relationships.

5. Tax advantageous - U.S. subsidiary not subject to European taxation.

6. No need for any U.S. government approval to incorporate.

7. Often lower U.S. labor and production costs.

Disadvantages.

1. Little expertise available from within U.S. company. Europeans responsible for management and marketing in U.S. have difficulty understanding different styles.

2. Often is time consuming and expensive in the long run to build from scratch.

3. Difficult to obtain independent financing in the U.S.

4. Failure rate high.

5. Growth frequently slow. European companies often become impatient at the slow growth which usually requires at least two or more years to become profitable.

G. <u>Use of U.S. Subsidiary as Bridge.</u>

Regardless of whichever of the above investment methods is chosen, or the many hybrids thereof, use of a U.S. subsidiary is many times advisable.

1. A U.S. company is inexpensively organized and maintained. The cost of incorporating is approximately $2,000 plus filing fees.

2. A U.S. corporation is an independent taxable entity providing an opportunity for the negotiation of appropriate distribution, transfer pricing, marketing and technical support agreements.

3. By channeling product, technology, etc., through a U.S. subsidiary, the European company can build up a pool of equity in the U.S. for possible future expansion.

4. Liability for acts in U.S. can be limited through use of subsidiary. European courts generally do not make parent corporations responsible for the acts of subsidiaries. This can be very important in product liability lawsuits, by the invocation immediately of European jurisdictional protection. Consult your local counsel on this.

5. A U.S. subsidiary is good as a hedge against future tax increases or exchange controls in Europe.

6. The U.S. subsidiary establishes its own credit.

7. The U.S. company can serve as a bridge for immigration purposes (discussed below).

8. The U.S. company can serve as a guard against heightened protectionist tendencies in the U.S.

IV. NEGOTIATING A CONTRACT.

In negotiating a contract concerning any of the above methods of product introduction, you can be certain that a U.S. lawyer is involved on behalf of the U.S. company. Either he/she will be directly involved in the negotiations or will be in the background, giving advice to his/her client on an ongoing basis. You must obtain legal counsel to protect your interests at a very early stage of negotiations.

Specific provisions which should be negotiated in any agreement are, among others, the following:

1. Grant of a limited license;

2. Minimum sales quantities to retain exclusivity;

3. Territorial and/or customer limitations;

4. Warranties;

5. Pricing and credit terms, including security interests through collateral or liens and exchange rate risks;

6. Patent, trademark, trade name and other IP rights protection and enforcement;

7. Responsibility for product liability claims;

8. Information sharing, including disclosure of customer lists, production costs, new technology, etc.;

9. Covenant not to compete;

10. Confidentiality;

11. Specific provision concerning the term and termination of the agreement;

12. Dispute resolution provisions; and

13. Governing law.

This is not an all-inclusive list. It is intended to alert you to some of the essential elements of a contract for the marketing of products in the U.S.

A separate, detailed outline regarding contract negotiations, including specific provisions essential to a contract for sale of products in the U.S., has been prepared by the author, and is available upon request.

V. NEGOTIATING DISTINCTIONS WITH AMERICANS.

Although Americans often look like Europeans and we certainly have many cultural similarities between us, there are many major differences in how we approach negotiations that can make a big difference in how a deal works out, if at all. Some of the major cultural distinctions relating to negotiations are listed below.

A. Americans Promise Everything.

Many Americans claim to be able to do everything. "We are your sole viable source". We are the "best", "strongest", "we cover the entire U.S., etc. Our suggestion is to get proof of what Americans promise as well as references.

Europeans, on the other hand, generally are very conservative in their representations. They seldom exaggerate in business.

B. Americans Aim Higher than Europeans.

Americans will start their negotiations asking for a far better deal for themselves than what they are willing to accept.

Europeans, on the other hand, start their negotiations very close to the level at which they are prepared to proceed with a deal.

As a result, many negotiations that might have been successfully completed, either stall, or unnecessarily fail. Consequently, a shrewd European company will commence its negotiations far from its acceptable level as well.

C. Short Term vs. Long Term Orientation.

There are fewer and fewer long term associations in American business. Loyalty between supplier and customer is not great, even at the raw materials level.

Today, there is less interest among firms concerning market share, and more concern about short term profitability.

Europeans, on the other hand, are much more long-term oriented. Europeans will forego short term profits for long term stability and growth.

D. Social Aspects vs. Business.

Although Americans are interested in negotiating their deal fairly quickly, they are also outwardly friendly, often inviting their foreign visitors home for a barbecue to meet the family. This should not be misinterpreted as an attempt to deceive or fool foreigners into believing that the Americans are trustworthy, its just their way of doing business.

Europeans are more confined to the business relationship rather than the personal relationship, and would prefer remaining focused on the business aspects of the negotiation. Europeans are prepared to enter into negotiations immediately. One approach is to exhibit some additional patience.

E. Degree of Specialization of Negotiating Partner.

In America, organizations are very centralized. Few people have specific power to make decisions. However, since organizations are often large, it can be difficult to know whether one is negotiating with the proper person.

This is critical in a sensitive transaction.

European organizations are decentralized where decisions are often reached at an organizational level by groups of people. Once a decision has been reached to give an individual negotiating power, they can complete the transaction.

The suggestion is to find out early on the specific negotiating power of your partner.

F. Patriotism.

Americans talk a great deal about patriotism, but it really isn't there. Americans will happily buy foreign made products with perhaps the exception of cars, as long as they are price competitive and of decent quality.

Europeans, due to the fact that they buy almost half of their consumption from abroad, have very little patriotism when it comes to the products they purchase.

G. Job Security.

Americans do not have much job security. Consequently, when negotiating a contract, the American's job could be on the line. If he/she doesn't negotiate a

good contract, they may lose their job. Imagine the degree of preparation and zeal with Americans negotiate contracts.

A European's job security is much greater. Consequently, they are generally prepared to accept a reasonable deal.

H. Cultural Diversity.

America is the most culturally diverse country in the world. The country spans an entire continent requiring a keen understanding of the different cultural aspects and backgrounds of the individuals with whom one is negotiating.

Europe is, generally, a homogeneous society where the same values can be, by and large, expected.

I. Quality Emphasis/Price Orientation.

Americans are not quality oriented unless a higher quality can be achieved at the same or lower price. Americans are, however, extremely price conscious. Even if superior quality, reliability, durability, and longevity can be proven, if the price is more than marginally in excess of a competing product, an American won't buy it.

Europeans are quite quality conscious and are prepared to pay extra in order to achieve that quality.

J. Use of Lawyers in Negotiations.

Virtually all American businesses have lawyers. You can be certain that your prospective U.S. business partner has been in touch with its counsel prior to negotiations.

This is not the case in Europe. Many European companies will negotiate with foreign companies without the benefit of local representation. Consequently, agreements are much simpler and without fanfare. The key is confidence and trust between partners, not the degree of certainty in the agreement.

It is essential that you obtain qualified legal counsel in the U.S. and involve your lawyer in the negotiations at an early stage.

VI. STEPS TO TAKE AFTER DECISION IS MADE TO INVEST.

Once a decision has been made to commence selling in the U.S. the following steps should be taken.

A. Structuring Relationship with U.S. Partner.

It is essential that the relationship with your U.S. partner be structured, in writing, with the legal protection recommended above. Too often, we have been contacted by European companies who have failed to commemorate their agreements with their U.S. partners in writing only to be embroiled in lengthy lawsuits to disconnect themselves.

Many times, clients tell us that they have not had a written agreement in order to maintain flexibility to terminate the relationship based on the lack of a formal relationship. If an American company has devoted substantial resources to marketing a product, hired personnel to deal specifically with a foreign company's products, exhibited at trade shows, expressed interest in a long term relationship, and the like, a U.S. court of law might protect the right of the American company to continue in the relationship even without the benefit of a written agreement. Consequently, it is absolutely essential that you have written agreements.

Equally important is that you maintain power in the negotiations by preparing all drafts of the agreements. You can never obtain as good an agreement if you let your U.S. partner prepare the drafts of the agreement. You will always be negotiating from "behind" or a position of weakness. Moreover, it will cost more money to have your lawyer review another lawyer's work, provide you with comments and recommended changes, prepare insertions of sections that were omitted in the initial draft, and negotiate with the American party's lawyer.

B. Customs.

If products are to be shipped to the U.S., customs classification must be obtained as soon as possible. Customs classification can have a substantial impact on the overall profitability of your U.S. investment. In many cases specialized customs attorneys should be consulted.

1. Components are subject to a lower tariff than complete final products.
2. Transfer pricing normally serves as basis for customs assessment.

C. Immigration.

Many clients deem it necessary to have senior level management personnel from the parent corporation on location initially to supervise operations or provide technical support. Long term, however, key marketing personnel should be U.S. nationals.

To arrange for a U.S. visa, advance planning is essential. If proper steps are taken, temporary U.S. work visas should not be difficult to obtain.

1. Visa Waiver Program and B-1 Visa for Temporary Business Visitors.

    a. Available for aliens visiting U.S. on business on behalf of a foreign company.

    b. Available initially for up to six (6) months and can be extended for additional periods.

    c. Salary must be paid by foreign company.

    d. Expenses can be reimbursed by U.S. company.

    e. Status can be changed to a temporary work permit while alien is in the U.S.

2. Visa Waiver Program.

   a. Available for up to 90 days, thereafter the alien must depart the U.S.

   b. No need to file or obtain documents prior to travel. Visitor need only have a valid passport and a round-trip airline ticket. Europe is part of a visa waiver program. A simple form is filled out in the flight and handed to an immigration officer at the U.S. port of arrival.

   c. Status cannot be changed without alien leaving the U.S.

3. L-1 Intra-Company Transferee Visa.

   If the European parent corporation desires to have a European national working in the U.S. for its U.S. subsidiary, a B-1 visa cannot be used. In such a case, an L-1 visa is the easiest and most advantageous to obtain.

   a. An L-1 Visa is valid for a maximum initial period of three (3) years and may be extended:

      i. up to five years for employees with special knowledge

      ii. up to seven (7) years for managers and executives

   b. In a start up situation, the initial period of stay granted is normally one (1) year.

   c. It permits the European national to be paid by local U.S. company.

   d. The qualifications for an L-1 Visa are as follows:

      i. Alien must have been employed by the parent or an affiliate abroad for at least twelve (12) months during the immediately preceding three years;

      ii. Alien must have been employed in an executive or managerial capacity or in a capacity involving specialized knowledge;

      iii. The application, to be filed by the prospective U.S. employer, must indicate that the need for the alien's service is temporary; and

      iv. The immediate family of L-1 visa holders will be admitted to the U.S. on L-2 Visas. L-2 Visa holders, however, are not permitted to work in the U.S.

4. H-1 B Visa for Aliens in the Profession Coming to Fill a Professional Position.

The H-1 B Visa is available to professional aliens, including physicians, nurses, engineers, scientists, professors, lawyers, teachers, and fashion models. Management and executives, with appropriate backgrounds, as well as computer specialists and other professionals can also obtain this visa.

a. The qualifications for an H-1 B Visa are as follows:

i. Alien generally must have at a minimum the equivalent of a U.S. Bachelor's Degree and specialized knowledge or experience in the field;

ii. The salary offered must meet or exceed the compensation offered Americans in the same type of work;

iii. The position to be filled can be permanent. However, the need for the alien's services must be temporary;

iv. The alien can be newly hired to fill the U.S. position or can be an employee of the same corporation assigned to the U.S. from abroad;

v. The visa can be valid for an initial period of three (3) years; and

vi. Extensions of up to three (3) years in total can be obtained.

b. Procedure to obtain an H-2B Visa

i. Prospective U.S. Employer must file a Labor Condition Application with the Department of Labor including attestations.

ii. Petition must be approved by the INS. A limit of 65,000 applications will be accepted each fiscal year (the limit has not been).

5. H-2B Visa for Temporary Workers.

H-2B Visas are available for aliens who are skilled or unskilled to work for U.S. companies in positions that are temporary in nature and for which no unemployed U.S. workers are available. This visa is difficult and complicated to obtain due to the high seven percent (7%) U.S. unemployment rate and the requirement of obtaining labor certification.

The qualifications for an H-2B Visa are as follows:

a. Prospective U.S. employer must file an application for temporary alien labor certification with U.S. Department of Labor; and

b. Prospective U.S. employer must show that there are not sufficient U.S. workers who are able, willing or qualified to obtain the

position and that the prospective alien worker possesses a superior knowledge or skill.

c. One must show that the position is temporary in nature, not just that the need for the alien's services is temporary.

6. H-3 Trainee Visas.

An H-3 Visa is available for aliens to obtain training in the U.S. which cannot be obtained elsewhere in the world.

a. Visa available for period of approximately one (1) year.

b. Alien may not perform valuable services to U.S. company.

c. Alien may not be paid salary by U.S. company but may have expenses reimbursed.

d. A detailed program of training and classroom work must be submitted with the Visa Petition.

7. Permanent Residence Visas.

Once the alien has been offered permanent employment in the U.S., a permanent residence visa (green card) petition can be filed.

Obtaining original transcripts, certificates and preparing innumerable forms prior to filing applications can take several months. Furthermore, depending on the preference classification of the alien, there may be a wait prior to obtaining a permanent residence visa due to the backlog of demand for visas. A detailed discussion of immigration law goes beyond the scope of this paper. Please contact the authors for more details.

D. Product Liability.

Prior to introduction of any products in the U.S., a product liability management program must be implemented. This is a program provided by Thorelli & Associates which is designed to reduce the risk of product liability to the lowest possible level, before any claims are filed. The risks of product liability in the U.S. are much higher than anywhere else.

1. The frequency of claims in the U.S. is much higher than in Europe.

2. The amount of the damage awards can be staggering and often unpredictable.

3. When lawsuits are filed, everyone in the manufacturing and distribution chain is normally included as a defendant.

4. However, only one percent (1%) of companies doing business in the U.S. are ever sued for product liability.

The following preliminary steps should be taken prior to introducing products in the U.S.:

1. Research U.S. market for similar products re:

    a. Industry safety standards, government regulations, etc.;

    b. Labeling requirements, types of instructions, etc.; and

    c. Design, quality, consumer perceptions, etc.

2. Ensure superior quality control and design at point of manufacture;

3. Provide for additional quality check prior to shipment to the U.S.:

    a. Sometimes production department in Europe ships lower grade product to U.S. due to U.S. not being a major market;

4. Draft warranties to be granted U.S. customer with utmost care including proper disclosures and disclaimers;

5. Prepare detailed instructions and warnings in both brochures and on the product:

    a. A product commonly used in Europe may be entirely new in the U.S.;

6. Have promotional material closely reviewed re possible exaggerated claims; and

7. Obtain product liability insurance with adequate cover.

8. Shift responsibility for product liability as much as possible to U.S. partner and U.S. customer through the negotiation of protective Agreements, Sales Terms, Sales Agreements, etc.

The trend in the U.S. is to limit product liability damages as much as possible to provide for a more equitable business tolerable climate.

The U.S. Congress recently passed legislation limiting the rights of plaintiffs to file product liability cases, limiting the amounts of recovery, etc. However, President Clinton, vetoed the legislation on the principle that it unfairly limited the rights of consumers. Renewed efforts are planned.

In a landmark decision in the spring of 1996, the U.S. Supreme Court handed down a decision in the BMW of North America, Inc. v. Gore, 116 S. Ct. 1589 (1996) case, whereby the Supreme Court struck down a verdict based on the exorbitant amount awarded by the jury. Never before had the

Supreme Court considered a case based on the amount of the award. The Supreme Court handed down three new tests with far reaching implications, concerning liability cases of all kinds:

1. Has there been any physical or economic harm done to the plaintiff? If there has been none, the award should so reflect in its size.

2. There must be a reasonable relationship between the amount of damages that can be proven and the amount of the award.

3. There must also be a close connection between the degree of reprehensibility and the level of punitive damages.

E. <u>Gefting Paid by U.S. Customers.</u>

1. The payment culture in the United States is normally thirty days after receipt of invoice. Payments generally lag somewhat behind that, and it is not unusual for payment to be made by customers in around fifty or sixty days.

2. A seller cannot retain title to products after they have been sold, even if no down payment has been made by the customer and the seller has specifically reserved title until payment is made. This is the law pursuant to the Uniform Commercial Code (UCC).

3. Banking sophistication is low.

   a. Bank guarantees and letters of credit are still not commonly used among smaller corporations.

   b. Personal and company checks are <u>not</u> as good as cash. They are merely an obligation to pay.

4. Credit background investigation services are generally unreliable. Dun & Bradstreet reports are actually based on the responses to questionnaires filed by the company in question.

5. The best strategy is normally to ensure payment in advance or by irrevocable confirmed letter of credit with a European bank, to be disbursed upon loading of goods on the carrier.

6. If credit is granted, a security interest must be created in favor of the seller in order for the seller to have a right to retake the products in the event the customer does not pay, and in order for the seller to have a priority in the event the customer goes bankrupt.

   In order to obtain an enforceable security interest in the products sold, the European company must do the following:

   a. A thorough check with the Secretary of State in the relevant jurisdiction must be made to determine whether security interests currently exist which may include, by general reference, the subject matter of the sale;

   b. A special security interest form must be filed with the relevant state and/or county authorities where the products will be used or warehoused;

i. These forms must be carefully drafted to ensure proper protection; and

c. A security agreement must be executed by both seller and purchaser and must also be filed with the relevant state and/or county authorities.

If no such filing is made, the security interest is ineffective against other creditors who may have security interests, particularly in the event of bankruptcy of the customer.

7. To collect unpaid balances you can engage collection agencies that retain between thirty and forty percent of any amounts collected, or use an attorney. Unfortunately, if the amounts due are in any way disputed, it is generally not worthwhile pursuing claims under $10,000. For further guidance concerning collection of unpaid amounts, please consult the author.

F. <u>Antitrust and Trade Regulation.</u>

U.S. antitrust laws exist to protect competition in the marketplace. As with European Union competition laws, there are very few absolute rules under U.S. antitrust laws.

1. Horizontal agreements among competitors are almost always automatically unlawful.

   a. Territory or customer allocation agreements among competitors.

   b. Price fixing or bid rigging agreements among competitors.

2. Vertical agreements, where the manufacturer attempts to control the activities of members of the distribution chain, stand a better chance of passing antitrust scrutiny today than previously.

   a. It is no longer automatically unlawful for a manufacturer to restrict customers to whom, or the territories in which, a distributor may sell. Under the current administration, these restrictions can be lawful depending on the purpose behind the restriction and its competitive impact.

In distribution and licensing arrangements, one must consider the impact of any provision which imposes restrictions on one party or the other. Ordinarily lawful limitations may, under certain circumstances, create an anti-competitive effect which can render the restriction unlawful. Tie-in arrangements where a manufacturer agrees to sell one product only if the customer also purchases another product, agreements to deal exclusively with one another, or requirements contracts, may violate the antitrust laws.

In particular, patent licensing arrangements have been utilized by the licensor to require, among other things, royalties beyond the termination of the patent; the purchase of accompanying, yet unprotected products; and requiring the licensee

to acknowledge the validity of the patent. These may all be in violation of antitrust laws.

Generally, if legal counsel is retained at an early stage, most planned business relationships can be achieved with a minimal amount of adjustment, and still comply with current U.S. antitrust laws.

G. Taxation.

The Tax Reform Act of 1986 was the most significant overhaul of the U.S. Internal Revenue (Tax) Code in a generation. The following are basic guidelines for the tax law and how it affects European investment in the U.S. The reader is cautioned not to rely on the information contained within this section without consulting his/her U.S. tax accountant or attorney.

1. Taxation of U.S. Business Entities.

   a. U.S. Branch.

      A branch in the U.S. is a non-incorporated division or office of a foreign company.

      i. All U.S. source income, and in limited circumstances, non-U.S. source income, which is effectively connected with the branch's U.S. trade or business is subject to U.S. taxation. In addition, a secondary withholding tax at a rate of five percent (5%) may apply to dividend payments by the U.S. subsidiary of a European corporation to its parent. A branch is generally not an appropriate form for the conduct of U.S. operations due to the cumbersome and potentially expensive reporting requirements placed on permanent establishments.

   b. Wholly-owned U.S. subsidiary.

      i. A U.S. subsidiary has its own existence. Therefore, it is an independent taxable entity. Taxes of a U.S. company are calculated based on its world-wide income which is taxed at normal U.S. tax rates. The tax rate for 1996 is thirty-four percent (34%).

2. Repatriation of Earnings.

   a. Branch operation.

      All after tax repatriation of funds flow back to the parent tax-free because the branch and parent are viewed as a single legal entity.

   b. U.S. subsidiary.

      i. A U.S. subsidiary is required to withhold tax at the rate of five percent (5%) on dividends paid to its one hundred percent (100%) European parent. Thus, income earned

from a U.S. subsidiary is taxed twice - once at the corporate level, and once again upon transfer to the European parent corporation.

3. Taxation of Individuals.

a. U.S. Tax Residents.

i. Non-citizen tax residents are subject to U.S. taxation on the same basis as U.S. citizens. Thus, under the new code, the maximum individual income tax rate is thirty-three percent (33%). The tax rate for net long term capital gains is twenty-eight percent (28%). In addition, to the extent that a particular item of income is taxed in both the United States and Europe, the United States provides a foreign tax credit to be applied against the taxpayer's share of U.S. tax liability. As in Europe, non-citizen tax residents would be entitled to business related expense deductions, etc.

b. Non-resident non-citizens.

i. Non-resident non-citizens are subject to U.S. taxation only based on their U.S. related income.

4. Distinction Between Resident and Non-Resident.

Any individual holding a permanent residence visa or meeting a substantial presence test is considered a resident and must pay taxes as such. In order to avoid tax resident status, a good rule of thumb is to limit one's presence in the U.S. to a maximum of one hundred twenty (120) days in a taxable year.

Regarding specific tax aspects, you are advised to consult a qualified accountant or tax attorney.

H. <u>Business Relationships, Generally.</u>

It is important to consult an attorney prior to acquiring interests in real estate, hiring employees, executing service contracts, etc.

VII. KEYS TO SUCCESS IN THE U.S.: A 17-YEAR LEGAL PERSPECTIVE.

There are many keys to success in the U.S. Much depends on the specific industry and a slew of other factors. However, there are a number of salient characteristics of companies who have been successful over the years. Some of those characteristics are listed below.

A. Successful Products.

1. Unique product with specific consumer advantage.

    a. The foreign company must sell a unique product that solves a particular consumer problem. It must provide the end user with an advantage over competitive products.

2. The product must be fully adapted to U.S. requirements, including not only weights and measures, but design, color, appropriate brochures and promotional materials, instructions, warning labels, etc.

3. Price competitiveness.

    a. The product must be competitive in terms of price and quality. Even if a product lasts five times as long as the competitive product, if it is twice as expensive, the foreign manufacturer will have great difficulty in penetrating the market.

4. Requirement: Thorough market research.

    a. Companies that think they can be successful in the U.S. without engaging in thorough market research before entering into a relationship will be relying on luck for success rather than proper preparation.

B. Marketing.

1. Marketing materials should be prepared by Americans. Marketing materials translated from the foreign language into English almost always are full of mistakes and sometimes even include unwitting warranties which can expose the manufacturer to unnecessary product liability risks.

2. The marketing strategy must be prepared for a complicated, segmented market. The United States is full of many different markets.

3. Marketing focus on niche markets. Foreign companies who want to sell products that are already on the U.S. market, must be prepared to invest heavily in promotion. Small to medium size companies general do not have the capital resources necessary to do so. Consequently, it is essential that foreign companies define their customer market very closely and invest all of their resources in penetrating that specific market. "it is better to go after a large share of a small market, than to go after a small share of a large market."

4. You must constantly be aware of your competitors' activities. Just by being on the U.S. market can provide tremendous insight into competitive developments in an industry. Market research studies have indicated that just by being on the U.S. market positively impacts the foreign company's activities outside of the United States. This is due in large part to the intense competition here.

C. Medium To Long Range Focus.

1. It is essential to think more in the long term than in the short term. Foreign companies who believe that they can make quick profits in the United States are generally fooling themselves. It takes two to five years to establish a new company in the United States, and unless one has direct access to a broad and sophisticated distribution network, penetrating the U.S. market is a long and laborious process.

D. Legal Structure.

1. Always have written contracts. Do not fool yourself that by doing business without a written contract you can maintain better flexibility and be able to terminate an unsuccessful relationship quickly.

2. Use an American lawyer - your U.S. partner is! As stated previously, there are over ten times as many lawyers in the United States as in Europe. There is one lawyer for every two hundred and fifty people. All American business people have lawyers and are much more sophisticated in law than Europeans.

3. Control negotiations by preparing all drafts of agreements. This was discussed earlier in this memorandum and is critical to successful negotiations.

4. Negotiate with two or more parties at a time. Often, foreign companies believe that it is unethical or immoral to negotiate with more than one prospective partner at a time. It is the best way to not only achieve the best deal for you, but also to find out the level of sincerity and interest of your prospective U.S. partner.

E. Successful Negotiations.

1. Learn about your prospective U.S. partner. Do not believe everything you hear. Insist on references and contact those references. Engage in independent research concerning your prospective partner through trade associations or contact with competitors.

2. Ask for more than you can reasonably expect to obtain to allow for negotiating room.

3. Use your lawyer in negotiations. Too often, lawyers are contacted in the U.S. after all of the business terms have been ironed out. Only then do clients begin to realize that there are many other issues, including product liability, product liability insurance, intellectual property issues, and the like that should have been included.

4. Negotiate flexibility into your contract. It is better to have a contract that will permit you to easily terminate a bad relationship than it is to have a wonderful, iron clad agreement, that locks you up for an extended term.

5. Recognize key cultural distinctions between Europeans and Americans. This was addressed earlier in this memorandum.

F. <u>Product Liability Preventive Management.</u>

1. Although a significant problem, keep in mind that only 1% of companies doing business in the U.S. are ever sued for product liability. Less than half of the cases result in a verdict or judgment, and less than half of those cases result in verdicts for the plaintiff.

2. The quality of European made products is generally not a problem. The problem is improper documentation. Promotional materials, brochures, product descriptions, instructions, warning labels and the like should all be prepared by Americans, and at minimum, should be closely reviewed by an American lawyer with experience in product liability matters.

3. The reason why many product liability cases are lost, is because the defendant manufacturer does not take the case seriously and take appropriate action to defend its interests. This may be what happened in the spilled McDonald's coffee case, among others.

4. Warranties and guarantees, just like other written documentation, must be adapted to the U.S. market and appropriately limited.

5. The risks should be shifted as much as possible to U.S. distributors, licensees, partners, and of course, the end user. That can be done by providing the appropriate instructions, warnings and limiting warranties.

6. Product liability insurance can be obtained in Europe and is generally less expensive there. Have your U.S. attorney review the terms to ensure appropriate levels of protection. For example, many policies do not cover legal fees or punitive damages, often times both significant portions of product liability lawsuits.

7. Require your subcontractors in Europe and elsewhere to protect you from product liability damages in the event their components or subassemblies are ultimately to blame for the product liability problem.

8. Remember that product liability lawsuits in the United States relate only to disputes about money, not about defective products or justice. If you keep money as the focal point of your management of a product liability lawsuit, you will be able to make the appropriate decisions.

VIII. ROLE OF ATTORNEYS IN THE UNITED STATES.

There are at least twenty-five thousand (25,000) lawyers in Europe. There are more than forty thousand (40,000) attorneys in the Chicago metropolitan area alone. This indicates the much larger role attorneys play in American life.

The need for lawyers is greater in the U.S. than elsewhere due to the lack of statutes governing the relationships of parties. U.S. law relies more heavily on cases than statutes and, therefore, is constantly changing to fit the needs of society. Parties to a contract are, consequently, left to negotiate virtually all aspects of their legal relationship unlike in most of Europe when parties can consult a law book to resolve disputes and interpret the relationship.

The U.S. is a litigious society. Oftentimes, lawsuits are filed as merely a part of negotiations rather than being a true reflection of an irreconcilable difference between parties.

Two (2) ways in which lawyers are compensated in the U.S. differ from European practice. A few lawyers take cases on contingency. If the client wins, the lawyer is paid; otherwise not. Also, in over ninety percent (90%) of lawsuits, each party bears its own costs of litigation. In Europe, the loser is usually responsible for the winner's legal fees. Only if fraud or willful or outrageous conduct is proven can fees normally be recovered unless already agreed to in advance.

As specialized international attorneys are often involved in setting up operations on behalf of clients, including obtaining proper visas, locating premises, negotiating employment agreements, etc., they become intimately associated with the client's business.

Attorneys are generally in a good position to recommend outside consultants, such as accountants, bankers, marketing consultants, insurers, etc.

Often, attorneys are used as chief negotiators in complex negotiations. They are relied on as trusted business advisors and often serve on the Board of Directors of client companies.

Fees for lawyers vary a great deal, from approximately One Hundred Fifty Dollars ($150.00) per hour up to over Four Hundred Dollars ($400.00) per hour. Much depends on the lawyers age, experience, degree of sophistication and the size of the law firm.

An American attorney who has experience in representing European business interests in the U.S. and is familiar with European attitudes and ways of doing business can be of particular assistance in acclimating a European company to the U.S.

1. Comparing U.S. and European law applications to similar situations helps to clarify differences in law.

2. A lawyer who specializes in representing European business interests in the U.S. is often in Europe and can meet with clients at their headquarters.

3. Further, such a specialist can draw on his experience to highlight mistakes or experiences of other European clients.

Thorelli & Associates

Thorelli & Associates offer over 30 years of experience in the legal representation of businesses and individuals with particular emphasis in assisting European interests in the United States. The firm provides an array of services, ranging from initial consultation regarding the impact of U.S. Federal and State laws on proposed activities to the purchase or sale of entire businesses. Having assisted many companies in the initial phase of their investment, the firm is experienced in providing strategic planning for long term success.

For more information, please visit us on the web at www.thorelli.com.