

AN INTRODUCTION TO METHODS OF OPERATION IN THE COMMON MARKET

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New Trade Frontiers lie beyond our Borders to be explored and developed by energetic and resourceful American businessmen. New markets for our goods are emerging in the developing areas which are now joining the world community of free nations. . . . I call on American businessmen to follow their heritage and to recapture the spirit and vitality of American traders of old.¹

It was in the above terms that the late President John F. Kennedy expressed himself concerning the need for American businessmen to explore and expand all avenues of American foreign commerce. Such expressions, so often echoed by the United States Commerce Department, have produced an upsurge in foreign business activities, the magnitude of which might alone justify the existence of this symposium, whose purpose it is to focus upon only some of the myriad of legal and economic factors which bear upon American economic penetration of foreign markets.

This introductory article will mention, but remain uncomplicated by, detailed consideration of such matters as financing, tax planning and possible antitrust implications. Although these are obviously important matters, and will weigh heavily in the choice of one or another method of conducting foreign business, they are considered elsewhere in this symposium. Simply stated, it is the purpose of this article to present a general consideration of the primary "methods of doing business abroad," with special emphasis on the Common Market.

INTRODUCTION

The first conceptual image that one has in treating the subject of methods of doing business abroad is an American product in the hands of a foreign user. The unanswered question is the channel through which the product may have coursed in arriving there. It might have taken the route of a direct export sale by a United States

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¹ Kennedy, Forward to U.S. Dep't of Commerce Handbook at iv (1962).

manufacturing company, or been the product of a third party abroad under a license or sub-contract manufacturing arrangement; or the item might have been manufactured abroad by a foreign branch, subsidiary or partially-owned foreign joint venture.

To be truly primary (since some American companies have made little, if any, logical and systematic penetration of foreign markets), this article will first discuss export sales and the function that they serve.

UNITED STATES EXPORTS

It goes without saying that export sales are indispensable to our national economy and international well-being. The present decade has brought to the United States the very real problem of correcting its balance of payments deficit. Naturally, increased exports is one of the means of doing so. By way of definition, Walter Surrey,² quoting Kindelberger,³ states that "the balance of payments of a country is a systematic record of all economic transactions between the residents of the reporting country and residents of foreign countries during a given period of time." An understanding of this is important.

For the first quarter of 1964, United States exports to Britain and the Common Market increased over the previous period by 25 percent and are expected to have reached \$8.5 billion for the entire year, a new record high. It was reported recently that the balance of payments deficit for the first half of 1964 was reduced to \$800 million, a 50 percent reduction over previous years. Although it looked as though the balance of payments deficit for 1964 would be improved substantially, it was down only slightly from 1963 for the whole year, because of the dollar outflow for the last quarter of 1964. Consequently, the balance of payments situation in 1965 has become an even more difficult problem. On February 18th, at a White House meeting, President Johnson and other top Administration officials met with some 350 corporate and financial leaders to request that they take specific voluntary measures to assist the government in the adverse balance of payments situation. Among other requests, it was specifically urged that American companies attempt to step up exports. The week before, on February 10th, President Johnson had said, ". . . I am calling for a redoubling of our efforts to promote exports." These expressions illustrate most effectively the tremendously important part that increased export trade plays in our national economy. It is probably correct to state that this increase is due in great part to the growing and revitalized demand abroad for the "Made in U.S.A." label and, particularly, to the present European prosperity, which produces a strong wave of desire for all consumer, as well as capital, goods. It

² Surrey, *Law Governing International Transactions* 121 (1962).

³ Kindelberger, *International Economics* 18 (1958).

has even been noted that trade between the United States and other industrial countries has been expanding faster than American domestic production.⁴

In discussing export sales, our primary inquiry should be how best to put the product into the foreign customers' hands. Development of the market is, of course, the most important objective, but also important to the person or company not experienced in foreign trade will be a review of the tools available to assist him in his task.

In this, the basic principles come first, and these have their genesis in the United States rules applicable to foreign commerce; only with an understanding of these may the exporter proceed to the vast number of foreign rules affecting international trade. Unfortunately, space does not permit a detailed analysis of the many United States laws which bear upon foreign trade, but the exporter should be aware of their existence.⁵

For source material and assistance in connection with methods of export, the reader's attention is directed to our own governmental agencies. The United States Bureau of Foreign Commerce has for one of its main purposes the rendering of assistance to American businessmen in the conduct of international trade and endeavors to help them understand the various United States trade regulations. In this pursuit, it maintains 39 field offices across the country. Publications are constantly at hand.⁶

Turning now to market development, any form of foreign advertising is, of course, very important. Trade journals are a good

⁴ Humphrey, *The United States and the Common Market* 45 (1962).

⁵ See, e.g., Tariff Act of 1930 (Hawley-Smoot Tariff Act), 46 Stat. 763, as amended, 19 U.S.C. §§ 1001-1654 (1959), as amended, 19 U.S.C. §§ 1202-1624 (Supp. V. 1964); Trade Agreements Extension Acts, ch. 474, 48 Stat. 943 (1934) (codified in scattered sections of 19 U.S.C.); Trade Agreements Extension Act of 1945, ch. 269, 59 Stat. 410 (codified in scattered sections of 19 U.S.C.); Trade Agreements Extension Act of 1951, ch. 141, 65 Stat. 72 (codified in scattered sections of 19 U.S.C.); Trade Agreements Extension Act of 1955, ch. 169, 69 Stat. 162 (codified in scattered sections of 19 U.S.C.); Trade Agreements Extension Act of 1958, 72 Stat. 673 (codified in scattered sections of 19 U.S.C.); Trade Expansion Act of 1962, 76 Stat. 872 (codified in scattered sections of 19 U.S.C.); Antidumping Act, 1921, 42 Stat. 15, as amended, 19 U.S.C. §§ 160-71 (1958); Export Control Act of 1949, ch. 11, 63 Stat. 7, as amended, 50 U.S.C. App. §§ 2021-32 (1959), as amended, 50 U.S.C. App. §§ 2021-32 (Supp. V. 1964); Trading With the Enemy Act, 40 Stat. 411 (1917), as amended, 50 U.S.C. App. §§ 1-6, 7-39 (1959), as amended and as supplemented by the Foreign Assets Controls Regulations and the Transaction Control Regulations; General Agreement on Tariffs and Trade (GATT) Oct. 30, 1947, 61 Stat. (5) (6), T.I.A.S. No. 1700.

⁶ A good introduction to these is contained in various pamphlets and books published by the U.S. Bureau of Foreign Commerce, including such basic pamphlets as "Foreign Commerce Handbook" and "Selling around the World." Also available is an "International Business Publications Checklist" and the U.S. Department of Commerce weekly "International Commerce." Many, many others are available from the Government Printing Office in Washington.

source of new interest from foreign industrial markets. But, of course, the nature of the product has a great bearing on what will be most successful. In some cases, International Trade Conventions and Trade Fairs prove effective in introducing an American product to world markets. The United States has since 1954 set up United States exhibitions at Trade Fairs around the world. Commerce Department officials make all the arrangements for American manufacturers and in many cases provide free transportation to the fair site. United States Trade Centers are also of substantial benefit to manufacturers.⁷ Additionally, a system of foreign distribution is of the utmost importance.

DISTRIBUTION CONTRACTS

In setting up a network of distributors to handle export sales, there are several factors to keep in mind. The first of these is the form of distribution contract. Should the arrangement be formal or informal? Although there may be something to be said for maintaining loose arrangements, as in simple letter agreements, this author tends to favor formal agreements.

In these, several points, often overlooked, deserve special consideration. (i) The date and place of execution of the agreement are important when determining the validity of a contract under civil law. (ii) Specifying your own law as the one to govern interpretation of the contract will solve many problems if a dispute arises.⁸ (iii) Likewise, specifying English as the official language of the contract will be important. Never state that both languages will prevail, as I have seen in some cases. Very difficult problems of translation and interpretation can result. (iv) In distribution contracts, it is important to be certain that the parties have created a principal-to-principal relationship and not an agency. In addition to the many unknown and unwanted liabilities that could be created by an agent, there are also foreign labor laws to contend with. In some countries an agent is an employee and, as such, is entitled to labor benefits, which are not insignificant by any means. (v) Where governmental approval is required, it should be made the responsibility of the distributor to obtain it and pay any charges that may be connected therewith. (vi) Designation of the currency in which payment is to be made is also important, since convertibility may require a

⁷ They now exist in London, Frankfurt, Bangkok and Tokyo.

Naturally, if the volume of export sales is great, the U.S. manufacturing company will no doubt have its own fully-trained export department. Their tools will be such works as Ashwell, *Exporters Encyclopedia* (1963); Lewis, *International Trade Handbook* (1963) and the *Foreign Traders Encyclopedia* (1964).

⁸ Schmidt, *Licensing Know-How, Patents and Trademarks Abroad*, in *Legal Problems of International Trade* 248, 266 (Proehl ed. 1959).

license or government approval. (vii) The United States Trading with the Enemy Act and Commerce Department Regulations must be kept in mind if there is any chance that United States goods will find their way into Communist countries.

This paper will not discuss the various other provisions of the distribution agreement, since they are not unlike those contained in any domestic agreement. Nor is there any need to discuss territorial restrictions that might run afoul of the United States anti-trust laws or the anti-cartel laws of other countries, including the European Economic Community. These will be discussed later in this symposium. Suffice it to say that territorial restraints of trade are very much of interest today. Indeed, some feel that the ideal solution for greater trade on a world basis is a true multilateral policy of free trade.⁹ This leads us to a discussion of one such system, the European Economic Community, or the Common Market, as it is sometimes called.

THE COMMON MARKET

A few introductory words about the European Economic Community are appropriate here.¹⁰ First, it was formed in 1957 under the Treaty of Rome¹¹, and became effective January 1, 1958. Its name implies its commercial purpose,¹² and its members are France, Belgium, Italy, the Netherlands, Germany and Luxembourg. The Treaty of Rome provides for (a) a common tariff, (b) a customs union, (c) regulations for industry and agriculture, (d) free movement of labor and capital and (e) a European Investment Bank. Its aims are high, and the very fact that it has functioned successfully to date, although not all of its purposes are yet achieved, is remarkable in itself, particularly in view of the bitter national rivalries which had existed for centuries.

I might point out that the member nations do not treat their obligations lightly. In other words, the Common Market is here to stay. The Court of Justice of the European Economic Community at Luxembourg, on July 15, 1964, confirmed its earlier holdings to the effect that the EEC Treaty takes precedence over any national measure in conflict therewith, and that the European Economic Community is of such a special character that the Member States must be

⁹ Hauser & Hauser, *A Guide to Doing Business in the European Common Market* (1960).

¹⁰ See generally Treaty Establishing the European Economic Community and Connected Documents, The Secretariat of the Interim Committee for the Common Market and Euratom, Brussels, n.d. (Eng. ed.).

¹¹ Treaty of Rome, March 25, 1957, 298 U.N.T.S. 14, CCH Common Market Rep., ¶ 109.

¹² As contrasted with economic unity, political unity is yet to be achieved.

deemed to have limited their sovereign powers and transferred to the organs of the Community such competence as may be required to fulfill their tasks under the Treaty.¹³

Tariffs have been substantially reduced among the six members of the Common Market and are to be made uniform against the rest of the world, including the United States, Great Britain and the rest of the Outer Seven.

As a result, in order to trade effectively in Europe, it is no longer feasible simply to export and sell. One must produce in Europe, not only in a Common Market country, but also, perhaps, in one of the other European countries as well. In the opinion of this writer, an effective "Common Market" trading area in all of Europe, including Great Britain, will probably not exist for several years.¹⁴ If we assume that the tariff walls will continue as they are today, and could even grow higher, we see that they must be dealt with from within a member country. Other factors also have a bearing on this. An American company may find, for example, that it should have a foothold within the Common Market, not only because of tariffs, but also because of freight, lower labor costs or lower costs of raw materials.¹⁵ Furthermore, it has been argued that regional freetrade blocs have both positive and negative effects on the economic efficiency of the world.¹⁶ It is hoped that counter measures will offset any negative aspects which have a tendency to impede progress in the future.¹⁷

The profit motive being ever-present, we must, then, consider means of entry other than export sales; and, within the framework of the Treaty of Rome, we will discuss the manner in which a United States company may penetrate European markets with a manufacturing

¹³ *Humble v. Government of Belgium*, Cour de Justice de la C.E.C.A., Case no. 6/60; *N.Y. Algemene Transport en Expeditie Onderneming van Gend & Loos v. Netherlands Fiscal Administration*, Cour de Justice de la C.E.C.A., Case no. 26/62, Feb. 5, 1963, 9 Rec. de la jurisprudence de la Cour 1 (CCH Common Market Rep. ¶ 8008); *Da Costa en Schaake N.V. v. Netherlands Fiscal Administration*, Cour de Justice de la C.E.C.A., Case no. 28/62, March 27, 1963, 9 Rec. de la jurisprudence de la Cour 59 (CCH Common Market Rep. ¶ 8010). See also Note, Common Market Assimilation of Laws and the Outer World, 58 Am. J. Int'l L. 724 (1964).

¹⁴ The United States and Great Britain and the other countries may, to some extent, keep pace by employing bilateral duty reductions agreed upon with individual Common Market countries, as contemplated by Article 18 of the Rome Treaty.

¹⁵ 1 American Enterprise in the European Common Market: A Legal Profile 23 (Stein & Nicholson ed. 1960).

¹⁶ Humphrey, *supra* note 4, at 6.

¹⁷ The Common Market, of course, has had a salutary effect upon the world trade of the member nations. It was recently pointed out by the Netherlands Trading Society that the shares in world trade of each of the Member States of the European Economic Community have increased and, as a result, there was a combined increase of 7.2% for the two-year period of 1960-1962 over the period 1952-1954, while for other countries, not members of the Common Market, there was a decline in the later period.

operation in a Common Market country. Some American companies, having been engaged in foreign business on an export basis as outlined above, may now desire to expand their international operations to include European manufacturing, even though they might not otherwise have done so. This expansion may be accomplished in several ways. It must be emphasized at the outset, however, that the approach which is taken by any one United States corporation must be analyzed from the point of view of that company's particular situation. The needs of one corporation in its international operations may be vastly dissimilar from those of another.

One question which often arises is whether it is more advantageous to embark on a licensing program; to manufacture directly in a foreign country; or to enter into joint ventures with local manufacturing companies. Naturally, many factors will control this determination and varying opinions are available.

LICENSE AGREEMENTS

It is sometimes said that the only manner by which an American company may utilize its technology abroad without the involvement of financial participation is the direct licensing of a foreign company. Pugh states that "the major incentive for direct licensing to independent foreign licensee companies is the desire to participate in the profit resulting from the exploitation of industrial property rights in certain foreign areas without the necessity of contributing the personnel, capital and other resources which might be required for a direct equity investment."¹⁸ In this, this author cannot fully concur. Proven technology and know-how constitute an industrial property right of the highest value, and properly handled by foreign manufacture on a contained basis it can, and often has, provided the consideration for the transfer of equity shares in the manufacturing entity.¹⁹ On the other hand, if uncontrolled, the same American technology, though developed over many years and at great expense, can be lost where no equity participation has been obtained in the foreign manufacturing company. I might add that the establishment of manufacturing operations abroad on a joint venture basis will meritoriously assist in the adverse balance of payments situation which, as indicated earlier, presently faces the United States, if the equity participation is obtained by the contribution of intangible property rights and equipment, rather than cash.

¹⁸ Pugh, *Tax Aspects of Foreign Licensing*, in 2 *Doing Business Abroad* 602 (Landau ed. 1962).

¹⁹ For a discussion of how member nations and the European Economic Community view the inherent and tangible value of know-how, see 2 Stein & Nicholson, *op. cit. supra* note 15, at 279.

Eckstrom points out that "every licensee is a potential competitor after the termination of the license" and states that "the inevitable disclosure of at least some know-how is, for practical purposes, almost impossible to retrieve in toto."²⁰

The feeling of this writer is that license agreements always have one serious defect and that is that they do not produce a permanent economic penetration by the licensor into the licensee's country, even though there is, in fact, a substantial financial outlay. Generally, the pattern of such agreements contemplates that the licensor will grant to the licensee the right to use patents and trademarks and will provide him with sufficient technical knowledge to enable him to manufacture the product in his country. This involves a substantial expenditure on the part of the licensing company in the initial stages of production and, as consideration therefor, a license fee or royalty is paid to the licensor for a stated term of years—maybe. Generally, such contracts provide that the license fees are to be paid long after the technical information and know-how have been imparted to the licensee, except, that is, when improvements are made from time to time, and except for situations where the companies have come to the parting of the ways and the licensee decides to pay the royalty no longer.

Should the latter situation occur, the licensor is left with his bare legal rights which, in a foreign jurisdiction subject to foreign courts and nationalistic tendencies, may not be of the greatest value.

Even assuming that the licensee continues to pay the royalty, however, the licensor never really has a permanent interest in the arrangement. Experience has demonstrated that the real effect of licensing is the creation of a competitor. The result is that the licensor may, perhaps, be permanently shut out of markets whose potential could be as great or greater than the domestic market. This statement becomes more meaningful when we consider that the combined population of the EEC countries is 170 million.

BRANCH OR SUBSIDIARY

A branch or wholly-owned subsidiary operation in a given EEC country is certainly the ultimate in obtaining a more permanent economic interest in the Common Market.

The formation of a subsidiary corporation in one or more of the Common Market countries is generally a simple act to accomplish. Although the corporate laws will vary from country to country, they are based upon the civil law concept and are not entirely unlike our

²⁰ Eckstrom, *Industrial Foreign Licensing Agreements*, in *A Lawyer's Guide to International Business Ventures* 105, 107 (1961) and Lovell, *Foreign Licensing Agreements* (1958).

own corporate laws. Later in this symposium, the corporate laws of the various countries are considered in greater detail.²¹

With respect to the establishment of branch operations, there are, of course, advantages and disadvantages, depending upon the laws of the host country. Generally speaking, it will be necessary to register the corporation with the proper local authorities if the branch is to have legal standing within the Community.²² It should be pointed out, however, that local opposition to branch establishments may cause severe administrative problems such as the filing of translated and certified copies, not only of the charter and by-laws of the parent company, but also of the corporate laws of the jurisdiction of the corporation of the parent company.²³ Moreover, a higher rate of tax may be imposed upon a branch of a foreign corporation in the host country than may be imposed upon a locally-incorporated subsidiary.²⁴

If either a branch operation or a wholly-owned subsidiary operation is not feasible because of the capital requirements mentioned earlier,²⁵ or for other reasons, then consideration should be given to other alternative methods of operation. As one such alternative, the joint venture company has come more and more into use.

JOINT VENTURES

Under such arrangements, the American company obtains an equity interest in the jointly-owned company; which interest may be purchased or, as is often the case, may be obtained in exchange for machinery or manufacturing know-how.

Let us consider the components of a joint venture. First, there is the preorganization agreement; sometimes this is referred to as the promotion or promoters agreement (obviously, it is also called simply the joint venture agreement).²⁶

A few observations with respect to the constitutive provisions of the joint venture agreement may be appropriate here. If, in the subscription for share capital, an exchange of stock is planned for know-how or other intangible rights, one should consider that the new company will thereafter own the property in the rights transferred, and it may be difficult to retrieve them in the event the

²¹ See articles at pp. 449, 463, 487, 501, *infra*.

See also Drachsler, *American Parent and Alien Subsidiary: International Antitrust Problems of the Multi-National Corporation*, A.B.A. Bull., Section of Int'l & Comp. L., July 1964, p. 29.

²² See Croswell, *International Business Techniques, Legal and Financial Aspects* 65 (1963).

²³ Surrey, *supra* note 2, at 21.

²⁴ Germany is an example of this.

²⁵ Pugh, *supra* note 18.

²⁶ Surrey, *supra* note 2, at 27.

company is later dissolved. An alternative approach would be to have the shares issued in exchange for the initial disclosure of the know-how and the performance of technical services, rather than to create an outright transfer of the property. A companion technical service agreement (referred to below) should then provide that the licensor retain ownership in the intangible property which will be returned upon termination of the agreement or dissolution of the jointly-owned company.

With respect to the transferability of the shares of the jointly-owned company, care should be taken to provide for a right of first refusal if either party should desire to sell its shares, and a sensible method of valuation of the shares, taking into account a factor for goodwill, should also be provided.

Of importance, too, is sufficient representation in the management of the company, not only on the board of directors, but with adequate provision for representation and voting rights in shareholders' meetings on all important matters. Similarly, a dividend policy for the jointly-owned company should be promulgated at the outset. Sometimes this latter factor is not taken into account soon enough, and, especially in a 50-percent-owned situation, deadlocks can result.

The second document to be drafted is the by-laws of the jointly-owned company. They should be considered a part of the preorganization agreement. Such matters as share transfers, voting rights and the objects of the corporation are of the greatest importance.

If we assume that the object of the corporation is to manufacture and sell a U.S.-designed product in a particular country, then the next document required is one which makes available to the new company manufacturing techniques, know-how and/or patents.

In drafting this technical service agreement or patent license, the licensor should treat the jointly-owned company as if it were an unrelated third party, taking care that property rights are not unintentionally granted to the licensee, and that upon breach of any of the terms of the agreement, the licensor has preserved his remedies in full.

Where trademarks are important, they should be guarded carefully, that is, they should be made the subject of a separate agreement. Trademark laws are universally ones which are closely defined, and permissive use of marks should receive the utmost attention.

To give only one example, under Italian law and trademark practice, non-exclusive trademark grants are not permitted and, if attempted, may result in the trademark becoming public property. Trademark agreements must be registered with the Central Patent Office in Italy; hence, they will receive the closest scrutiny.

We now have three agreements to cover the manufacture and sale in a specific country of our hypothetical U.S.-designed product.

What about export sales? Should the joint venture company be allowed to sell outside the host country without restrictions of any kind? A better question would be, are there any rules which require that the manufacturing company must be allowed to sell in member nations without restrictions?

ANTITRUST IN THE EEC

The rules governing competition contained in the Treaty of Rome²⁷ prohibit any private arrangements which affect trade among the members and have as their purpose the restraint, hindrance or distortion of competition within the European Economic Community. Price fixing, production controls, division of markets, unfair discrimination between customers and tie-in agreements are prohibited. Certain exemptions, however, are provided in the case of

any approved agreements between enterprises or associations for any concerted practices which contribute to the improvement of the production or distribution of goods or to the promotion of technical or economic progress, while reserving to users an equitable share in the profit resulting therefrom, which neither impose on the enterprises concerned any restrictions not indispensable to the attainment of the above objectives nor enable such enterprises to eliminate competition in respect to any substantial proportion of the goods concerned.²⁸

As an additional means of complying with the provisions mentioned here while still maintaining some degree of influence over the export of the product, consideration should be given to distribution of the product outside of the host country by a separately controlled selling company. This may be accomplished by an exclusive export distribution agreement, so long as it violates none of the specific prohibitions mentioned above.

GENERAL OBSERVATIONS

As we have seen, "Methods of Conducting Foreign Operations" is not just a subject or single topic but, rather, a wide range of subjects, all interrelated to produce effective and dynamic foreign commerce. The laws, too, are dynamic, changing not only with the needs of a single State or nation, but of several nations. We are con-

²⁷ Treaty of Rome, March 25, 1957, arts. 85-90 (CCH Common Market Rep. ¶¶ 2001-2850).

²⁸ Croswell, *op. cit.* supra note 22, at 145.

cerned not only with domestic laws and local foreign laws, but also super laws, that is, the laws promulgated by various organizations of States which are superimposed on the already complex laws of the individual Member States. By narrowing our frame of reference to the European Common Market, we afford ourselves some relief, but the respite is, perhaps, illusory, since many of the observations made in this symposium will have equal significance in other parts of the world.²⁹

Furthermore, few of the laws of the individual member countries concerning methods of conducting business are made uniform by the Treaty of Rome. The many and diverse legal forms of business entities are left unchanged. The characteristics of the G.m.b.H., for example, are still the same in Germany and quite unlike the S.a.r.l. in France which, in turn, bears little resemblance to the Dutch N.V.

These are discussed in detail in the articles that follow, but their diversity points up the need, when establishing a trading or manufacturing facility in Europe, to consider many factors which are purely local in nature, yet which affect the entire operation.

General considerations are also important. The products themselves, literature and management's thinking will have to be adapted to local conditions. Language, metric measurements, voltages, cycles, RPM speeds, capacity ratings, lower water temperatures, are all very real changes which must be dealt with in each country.

Financing overseas operations is, likewise, a matter of increasing importance. Many forms of financial assistance are available for industrial expansion in foreign countries, among which the most often utilized are the national and international agencies headquartered in Washington.³⁰

Funds are also available from insurance companies and other sources of institutional funds, United States investment banking institutions, commercial banks and private financial institutions.

Another factor of general interest to be borne in mind in conducting one's international business through a foreign vehicle is the manpower problem. For example, if United States employees are transferred to the new entity, care should be taken to preserve the vested

²⁹ See Looper, *The Significance of Regional Market Arrangements, in Legal Problems of International Trade* 364 (Proehl ed. 1959).

³⁰ For an excellent comparison of the purpose, resources and nature of the loans extended by such financial agencies, including the Export-Import Bank, the Agency for International Development (AID); the International Monetary Fund (IMF), International Bank for Reconstruction and Development (IBRD), International Finance Corporation (IFC), International Development Association (IDA), Inter-American Development Bank (IDB) and the Inter-American Social Progress Trust Fund, see McLean, *Financing Overseas Expansion*, *Harv. Bus. Rev.*, March-April 1963, pp. 56-57.

rights of such employees in the United States company's pension or profit-sharing plan.

Prior to the 1964 Revenue Act, individuals who were employed by a foreign affiliate of an American concern could not be covered under the domestic company's pension plan if such plan were to qualify for the special tax advantages extended to such plans. The reason for this was that, under section 401, a qualified pension plan had to be for the exclusive benefit of employees, and an employee of a foreign affiliate was not, by virtue of that relationship, an employee of the domestic company. Such individuals are normally granted a leave of absence as provided in the standard plan.

In the 1964 Act, Congress made it possible for citizens employed by foreign subsidiaries (foreign corporations 20 percent of whose voting stock is owned by the domestic corporation, and also certain foreign subsidiaries of such foreign corporations) to participate under the qualified pension plan of the domestic company just as they now may participate under social security. This provision is effective for taxable years ending after 1963.

To accomplish this result, the new law provides that the citizen shall be considered an employee of the domestic parent corporation. But he will be so considered only if:

- (1) The domestic parent has entered into an agreement with the Internal Revenue Service for covering citizen-employees of the foreign subsidiary under social security pursuant to section 3121(1);
- (2) The plan of the domestic parent company provides that it will cover citizen-employees of all foreign subsidiaries in connection with which such an agreement has been made; and
- (3) The citizen-employee is not covered under a plan of deferred compensation (whether or not qualified) of any other employer.

As a result of his being treated as an employee of the domestic parent corporation, contributions made by the parent to its plan on behalf of the citizen-employee will not be currently taxed to the employee. The parent corporation itself will not be allowed a deduction for contributions made on behalf of a citizen-employee of the foreign subsidiary. However, the subsidiary will be allowed the deduction for United States tax purposes, thus reducing its earnings and profits subject to future United States taxation when remitted as dividends.

It is beyond the scope of this writing to delve into problems of American taxation relating to foreign operations. On the other hand, United States tax considerations may be indispensable to a determination of the method of foreign operation which may be more appropriate in a given situation. For instance, if the decision is made to form a

subsidiary in France or Germany, rather than to operate directly in those countries, consideration might be given to the question of whether to transfer assets, such as machinery, for the stock of the new subsidiary, instead of capitalizing for cash.

Under United States tax rules,³¹ it is provided that such a transfer may be accomplished without recognition of gain to the transferor, but this will be true only if a prior ruling is obtained to the effect that the transaction is one which does not have for its principal purpose the avoidance of the United States tax.³²

Stanley S. Surrey, Assistant Secretary of the Treasury, has recently stated that the Treasury Department's purpose is to reduce tax restrictions on the free flow of capital and goods between the developed countries and to increase United States private investment in less developed countries by modernizing international tax rules and mechanisms applicable both to taxation of income earned abroad by American taxpayers and income earned in the United States by non-American taxpayers.

Included in the program is the formulation of income tax treaties with less developed countries and reshaping of income tax treaties with developed countries. The guidelines and procedures applied by the Internal Revenue Service in the administration of tax laws relating to foreign income are to be improved. The Treasury Department has been occupied with the task of issuing comprehensive Regulations under the Revenue Act of 1962 relating to the taxation of foreign income and is, at the same time, considering a broad revision of United States tax rules governing the taxation of foreigners who receive income from United States sources.³³ The subject of taxes, of course, will be considered in detail later in the symposium.

In conclusion, it should be apparent that, in order to produce the most effective corporate, tax and legal structure in the conduct of foreign operations, competent legal advice is of paramount importance.

Foreign lawyers are becoming increasingly aware of the need to obtain American legal training, so that they may better represent American businessmen and corporations in their respective countries. In a recent report of a special committee on relations with lawyers

³¹ Int. Rev. Code of 1954, § 351.

³² Int. Rev. Code of 1954, § 367.

³³ Canadian Tax Executive Institute, *The United States Tax System and International Tax Relationships—Perspective in 1964* (September, 1964).

From other sources, however, comes quite another reaction to the activities of the Treasury Department in 1962 through 1964. One question, often heard, is how does it all work? The Regulations to which Mr. Surrey refers are to many incomprehensible. Indeed, many feel that the net effect of the enactment of the Revenue Act of 1962 and the Internal Revenue Service handling of taxation of foreign income will, rather than reduce tax restrictions on the free flow of capital, increase such restrictions and result in a decrease of United States private investment abroad.

of other nations, the American Bar Association pointed out that, after contacting 137 law schools in the United States, 39 out of the 98 law schools which replied had one or more foreign law students and 9 had 10 or more foreign law students.³⁴

Education in international law in the United States is, likewise, of great importance today. When we speak of educational advancements in the field of international law, of course, we refer to legal matters relating to foreign trade, not public international law.³⁵ Nor do we refer to this field of law as private international law, as is sometimes done, since that term is properly confined to the field of conflict of laws.³⁶ This symposium provides ample proof of the growing desire and need on the part of American lawyers for education in the area of international trade and foreign law. Law schools all over the country are adding courses to their curricula to deal with the subject, and more and more text books are being published to accommodate them.³⁷

The role of American industry in the world of international commerce has made the United States the most prominent of international industrial nations; this must, of necessity, carry with it development of expertise, not only in foreign manufacturing and management, but also in financial and legal fields. American law firms, financial institutions, accounting and management firms now establish foreign offices on an ever-increasing scale, in order to become better trained in the local law, and thus, in turn, better able to serve their clients in all parts of the world. This symposium is aimed at assisting in such training and provides one of the very real means for developing, along with industrial expansion, legal and intellectual enlightenment in the methods of conducting foreign commerce.

³⁴ Report of the Special Committee on Relations with Lawyers of other Nations, 88 A.B.A. Rep. 671 (1963). The total number of foreign students enrolled in law schools in the United States amounted to 313, 254 of whom were studying at Harvard, Yale, Columbia, SMU, Tulane, University of Miami, University of Michigan, Northwestern University and the University of California at Berkeley.

³⁵ For many years, such advancements have been made in the public international law field. In 1914, under the auspices of the American Society of International Law, a conference was held of teachers of international law and related subjects representing 41 colleges and universities in the United States. Their recommendations for increased facilities in the study of public international law were extensive and are reported in *Resolutions and Recommendations of the Conference of International Law and Related Subjects*, 8 Am. Soc'y Int'l L. 315 (1914).

³⁶ Black, *Law Dictionary* 1358 (4th ed. 1951).

³⁷ A Lawyer's Guide to International Business Transactions (Surrey & Shaw ed. 1963); *Doing Business Abroad* (Landau ed. 1962); *Surrey, Law Governing International Transactions* (1962); *Legal Problems in International Trade and Investment* (Shaw ed. 1962); 4 *Southwestern Legal Foundation, Institute on Private Investments Abroad and Foreign Trade* (1962); *Legal Aspects of Foreign Investment* (Freedman & Pugh ed. 1959); *Legal Problems of International Trade* (Proehl ed. 1959).