The year 2008 has been very productive for the University of Colorado Denver’s (UCD) Institute for International Business (IIB) in regard to its international business outreach efforts. Anchoring these accomplishments are contributions made by the IIB’s Global Advisory Board, a dynamic board of international business leaders and entrepreneurs. Board members have played an active role in leading or participating in internationalization programs of the IIB.

This Global Forum Report highlights the recent contributions of board members.

**Partnering with KPMG**

A founding global advisory board member, KPMG LLP is a strong supporter of the IIB. **Rick Connor**, former managing partner of KPMG’s Denver office, has served on the board since 1997 and is currently co-chair of the IIB’s Global Advisory Board.

Last year the IIB established a partnership with KPMG’s Global Enterprise Institute, spearheaded by IIB board member **Mike Bearup**, partner in charge of KPMG’s Boulder office. The Global Enterprise Institute provides a forum for business leaders of mid-market and entrepreneurial firms to access thought-leadership on important issues facing their companies and to discuss emerging trends in international business. This focus is particularly important given the makeup of Colorado firms engaged in – or who could potentially participate in – international business.

- The May meeting focused on the opportunities and risks of global expansion for mid-market and entrepreneurial firms.
- The September meeting addressed how best to navigate the FCPA and legal risks in international deal-making.
- The November meeting discussed recent developments in the European Union and their implications for US companies. Moreover, the November meeting shed light on the global financial crisis and its impact on mid-market and entrepreneurial firms.

**Board member presentations**

Four board members served as keynote speakers or presenters in several IIB-sponsored programs. In November, **Peter Widmer**, financial advisor and former Member of the Executive Board of Julius Baer Holding Ltd. Zurich and a long-standing IIB board member, traveled to the US in order to participate in several programs sponsored by the IIB. In addition to serving as the featured speaker for the Global Enterprise Institute, Mr. Widmer keynoted the Rocky Mountain CIBER conference in Logan, Utah. This was followed by lectures on the European Union to UCD students, faculty, and staff, and a presentation to Global Advisory Board members.

**Dennis Leonard**, senior vice president of Global Human Resources Operations, Western Union Company, gave a presentation on international compensation in an international executive roundtable. **Henry Tsuei**, retired senior vice president of Western Union Company, served as a panelist on the Global Enterprise Institute’s conference on the FCPA in September.

The IIB held the second faculty development program in international entrepreneurship in June 2008. Most notable of the presentations was the keynote case on the internationalization of the National Basketball Association by **Eric Drummond**, head of International Human Resources for the NBA. The case set the stage for the discussion of international entrepreneurship issues covered during the faculty development program.

**Future Plans**

Several initiatives have already been planned for 2009, including a board member’s keynote address in the China FDIB (January 2009) and the development of a new faculty development program on the Gulf Cooperation Council Countries (UAE, Bahrain, Kuwait, Oman, Qatar, Saudi Arabia) in January 2010. Global competitiveness issues, such as the impact of the global financial crisis on US companies, will be addressed in future IIB programs. The next Global Forum Reports will continue to highlight these programs and the contributions of the IIB Global Advisory Board.

**Manuel G. Serapio, PhD**

IIB/CIBER Faculty Director

The Global Forum Report is a publication of the Center for International Business Education and Research (CIBER) at the Institute for International Business, University of Colorado Denver. Phone 303-315-3707; Fax 303-573-3945; Web http://www.cudenver.edu/international/CIBER/
Global Enterprise Institute focuses on mid-market companies

MICHAEL BEARUP is the partner in charge of KPMG’s Boulder office. He has more than 22 years of experience providing audit and business advisory services to the technology, software, medical device, manufacturing, distribution, and venture capital industries. His background includes initial public offerings, ongoing periodic reporting for publicly traded companies, and mergers and acquisitions as well as international operations of US-based technology and software companies. Bearup is an honors graduate of Washington & Lee University with a bachelor of science in accounting. He serves on the Institute for International Business (IIB) CIBER Advisory Council.

Responding to needs of the business community, KPMG LLP and the University of Colorado Denver (UCD) CIBER have taken their 20-year partnership to the next level as cosponsors of the Global Enterprise Institute (GEI), a forum where business practitioners share expertise, gain insights, and access thought leadership around key middle market issues and emerging international business trends.

“Middle market companies are increasing in importance as drivers of US economic growth,” said Bearup. “The mission of the Global Enterprise Institute is to help these mid-market companies identify the risks and opportunities associated with overseas expansion.”

Four annual GEI conferences are planned along with joint research on mid-market and entrepreneurial firms in Colorado to study and facilitate international business activities. Past and upcoming conferences:

- 12/18/07 - Going Global: Inaugural Forum 5/1/08 - Responding to a slowing US economy: Opportunities/Risks of global expansion
- 9/17/08 - Foreign Corrupt Practices Act: Implications for Colorado’s global companies
- 11/18/08 - Evolution of the European Union: Impacts and opportunities for US companies
- 2/2009 - The battle for China and India: Implications for mid-market US firms

Sessions from the second GEI conference “Responding to a Slowing US Economy” are summarized in this Global Forum Report.

Business survey

In November 2007, KPMG sponsored a survey of Colorado companies. The objective was to gauge the overall business climate in the region and to better understand the effects of globalization at a local and mid-market level. Michael Bearup presented the findings at the first GEI conference last December.

“One of the things that came out of our survey was that Colorado-based companies are considering overseas expansion in response to a slowing US economy,” said Bearup. Following are some of the key findings from the 103 respondents who participated in the survey.

- 43% rate their global expansion efforts as successful; 23% rate their efforts as having little to no success.
- The majority plan to increase global presence over the next 5 years.
- The majority say global expansion is not impacting their US employee base. 33% say their US employee base has expanded.
- Economic factors in the US and abroad have the most impact on global expansion decisions.
- Language, culture, and developing new customers are key challenges.
- The right people, communication, and knowledge of the market are key to successful global expansion.
- Technology support and human resource issues are aspects of global expansion which pose the biggest risks, but no one risk presents an insurmountable barrier.
- The keys to successfully managing non-US operations and maneuvering non-US markets include knowledge of the culture, the market and the people with whom you are doing business.
- Respondent company annual revenue: 82% less than $500 million; 11% $500 million-$999 million; 4% $1 billion-$1.5 billion.

Colorado businesses beneficiary of partnership

KPMG has been a crucial supporter of the Institute for International Business (IIB) from its inception. In 1989, just after the University of Colorado Regents approved establishing the IIIB, KPMG partners became a founding entity with a $50,000 commitment. Their support for international business initiatives at the University of Colorado Denver (UCD) was matched by the Peat Marwick Main Foundation.

Since that time, a member of KPMG has continuously served on the Institute’s Global Advisory Board, working to make the Institute a viable force in Colorado’s international business arena. Richard Connor, managing partner of the Denver Office of KPMG, has been on the Institute’s Board since 1997. The Global Enterprise Institute is the most recent example of KPMG’s support for UCD and Colorado’s business community.

Both Mike Bearup and Manuel Serapio, faculty director of the UCD CIBER, agree that their partnership brings together the best of two worlds: business and academia.

KPMG International. A global network of over 123,000 professionals in 145 countries, KPMG provides audit, tax and advisory services and industry insights to help organizations negotiate risks and perform in the dynamic and challenging environments in which they do business. KPMG LLP is the US member firm of KPMG International.

- Denver Office of KPMG LLP. The Denver Office, which includes Boulder, has served Colorado’s businesses since 1930. The two locations house over 400 employees including 350 professionals and 38 partners and principals.
- UCD CIBER. The Center for International Business Education and Research (CIBER) is part of the IIB at UCD, one of 31 universities in the US recognized by the US Department of Education as centers of excellence in international business education. The CIBER mission is to increase the business expertise and competitiveness of American businesses in the global marketplace.
Century old company a big fish in small pond

Knowing where to cut costs vital to global growth

ROBERT E. JOYCE has been president/CEO of the Wheelabrator Group since 2003. Prior to that he was executive vice president of operations for United States Filter Corp. Joyce’s career includes positions at Black & Decker Corp., Deloitte & Touche, Merck & Co. and the US Marine Corps. He currently serves on the advisory boards of CIBER and The Business School at the University of Colorado Denver. Previously he served on the boards of Axxiom Manufacturing and Ultrex, Inc. He holds an MBA from The Wharton School and a BS in Aerospace Engineering from the University of Michigan.

Despite being 100 years old, Wheelabrator is not a household name, nor does it make the products that most households buy. But the company plays an important role in the manufacture of products that directly or indirectly benefit households worldwide. Wheelabrator is “the world’s largest provider of metallic surface preparation equipment,” said Robert E. Joyce, Jr., speaking at the KPMG-University of Colorado Denver Global Enterprise Institute.

What does surface preparation mean? “We clean, strengthen or polish metallic surfaces,” said Joyce. Customers come from a wide range of industries: aerospace, automotive, construction, electronics, foundry, medical, power, railroad, recreation. “Think landing gear on aircraft, jet engines, engine blocks on autos, carburetor springs, and springs that go into shock absorbers. Anything that’s metal we touch.”

That sounds like a gigantic market but Joyce said the surface preparation industry is actually very small, about $1.5 billion globally. Wheelabrator’s share of this market is 22 percent, which translates to 50,000 customers – predominantly Fortune 1000 companies spread out over 101 countries.

Established in Pittsburgh in 1908 to serve the local foundry industry, the company today has 1300 employees working in 19 countries. Capital structure and market forces drive expansion strategy.

- Capital structure. The company has had various corporate owners in its 100-year history but since 2003 has been privately funded. “Private equity investors have very specific time frames for a return on investment: five-seven years and they’re gone. Our strategy has to accommodate investor needs in the short term. Yet, as the CEO I need to have an infinite horizon in terms of setting strategy.

- Market forces. “We split out thinking down the middle between mature markets and developing markets. We do not believe that one strategy works the same for everybody. We do not believe that equipment strategy is the same in the United States as it is in China,” said Joyce.

“The United States, Canada, Japan and countries in South America, are mature markets. No one is investing in these regions of the world in our industry or in our customers’ industries.” Nevertheless, these regions are important because of the cash they generate from aftermarket sales and service on the installed equipment base. The strategy, therefore, is to “keep those customers happy because if we lose that cash in the mature regions, there’s no hope of investing in emerging regions.” Company sales and service people help maintain customer relationships.

In the developing markets, an opposite strategy is employed. “We don’t have an installed base so we’re investing in equipment-sales people to generate revenue and satiate the primary demand,” said Joyce. The BRIC regions (Brazil, Russia, India, China) are where primary demand is growing and where many of Wheelabrator’s customers have set up operations. In order to be close to durable goods shipments and local industrial production, “we follow our customers into those markets where they are investing their dollars,” said Joyce.

For better or worse, Wheelabrator’s fortunes are closely tied to its customers. “In the 1996 time frame, there was a slowdown in the auto industry and the heavy industries that we serve cut costs in all the growth regions.” Wheelabrator’s then-management also made cuts and shut down the office in Mexico. They did not foresee that NAFTA was about to be signed and new opportunities would open. “The timing was terrible. We missed the boat,” said Joyce.

Key lesson: “You have to invest in down times. If you’re going to cut costs, don’t cut costs where the growth is; cut costs where the mature market is.”

Joint ventures risky

Global expansion strategies may look good on paper but turn out differently on the ground. Challenges can arise in developing nations where the rule of law is weak or the Western legal framework non-existent. “We can’t expose the entire enterprise to one bad transaction in a rogue nation, so we spend a lot of time educating our salespeople and our sales channels about what they can and cannot do.”

Frustrations are often built into the learning curve when operating in different countries, different cultures. “We tried in China to do joint ventures and were not successful. We got out of them primarily because of fraud and concerns about the possibility of government privatization,” said Joyce, adding, “We’ve learned that you cannot assume everyone is trustworthy.”

Show me the money

When Wheelabrator’s shareholders were unwilling to make investments in Poland and China, Joyce asked the board’s permission to find an investor who would support the company’s strategy.

“Our private equity investor now is an Eastern European fund based in Warsaw (also Budapest and London). Why? Poland is where I needed to make an investment in a manufacturing plant,” said Joyce. Wheelabrator is building a plant in Poland to be more competitive in the global market.

“Five years from now I’ll probably try to find an Indian private equity fund or go public in Bombay to raise money to invest in that region of the world. It’s important to understand where your equipment is being exported to and where your customers are going if you really want to be a global company and finance the enterprise.”

This is especially so in the world of private equity, where “you have to match the capital structure to your growth and vision.” Toward that end, Joyce advises shareholders, “Support my strategy for the duration of your involvement and give me permission to go find the next investor who’s going to help us grow into the BRIC regions.

“That’s our approach to global expansion going forward,” said Joyce.
HOV Services: Results, not labor arbitrage, key to offshoring success

SCOTT M. SHAFER is the executive vice president of Sales and Business Development with HOV Services (HOVS), a leading global business process outsourcing (BPO) and knowledge process outsourcing (KPO) provider with more than 12,500 employees and operations in the US, India, Canada, China and Mexico. Shafer began his career with Electronic Data Systems (EDS), followed by five years in a key technology leadership role at Fiserv during its formative growth years. He came to Colorado in 1993 after being recruited back to EDS as a division vice president. Seeing the trends in globalization, Shafer launched Sherpa Business Solutions, a global BPO company in 2002. Sherpa grew to more than 1500 employees and was acquired by Firstsource Solutions Limited in March 2005.

For small to mid-sized US companies, the decision to offshore usually does not come easily especially given the pros and cons that have to be weighed and the likely need for a global partner. Scott Shafer framed some of the considerations for businesspeople and faculty attending the KPMG-University of Colorado Denver Global Enterprise Institute “Opportunities and Risks of Global Expansion.”

Business Process Outsourcing (BPO) is an umbrella term used in this article to describe business process functions such as call centers, voice/non-voice processes, IT enabled services, transaction services, collections research and other back office functions.

Choosing a global partner

“The right global strategy and partner can create opportunities to foster innovation and better differentiate your products and services by providing additional value to your customer base and potentially opening new markets,” said Shafer.

However, there are considerations that must be weighed when moving forward with a BPO partnership, he said. “Think through the value gained by implementing your global strategy and its objectives. Really know your global partner and fully understand the nature of your business that will be conducted offshore. Look for reputable suppliers who bring innovation and value versus those solely peddling low-cost services, and absolutely focus first on providing value to your customers.”

When labor arbitrage is the primary reason for the selection of a call center partner, “the per-person cost of the call may be less but if it takes three times as long to do a call, you’ve lost any economic advantage let alone the cost of unsatisfied customers due to poor accent utilization and the scripting and mapping of the calls.”

“One of the cornerstones of how HOV Services creates competitive advantages for clients is through process excellence (PE) practices, which are deeply embedded in our corporate culture. HOV Services has a dedicated process excellence team that uses Six Sigma, a measure for continuous improvements in operations that deliver cost, performance and/or service benefits and new ideas with every engagement,” said Shafer. “These initiatives help differentiate our business while helping clients differentiate their offerings.”

HOV Services’ client list is comprised of many small- to mid-size companies in addition to a sizeable FORTUNE 500 account base. “More than 85 percent of our revenues come from existing clients,” said Shafer. The company’s business model accounts for this success. “The better job we do for clients, the more work they give to us.”

The way that “better job” unfolds for healthcare clients, for example, is to focus on completing the entire lifecycle of a claims transaction using Six Sigma quality methodology from the time the claim is received in the mailroom in a US location to the time it is adjudicated either in the US or globally, depending on the client’s requirements.

With its emphasis on providing value rather than on pursuing labor arbitrage, HOV Services continuously tracks feedback from clients and end-user customers to ensure world class delivery and client satisfaction.

Location, location, location

There are two factors to consider when deciding where to locate an offshore operation. The first is the country, the second is the city. “In India, Western companies tend to favor Tier 1 cities like Bangalore, Delhi and Mumbai. These cities have international airports, Western hotels and great infrastructure; you live in somewhat of a ‘Western bubble’ when you’re there.”

There is a more challenging side, however. “In those cities the war for talent can be vicious with extremely high attrition rates and salaries growing well into double digits every year,” said Shafer. “If you establish an operation in a major city, the cost containment and continuity of talent issues can be difficult to address.”

HOV Services mitigates this problem by locating in Tier 2 cities. “Although they are less modern and most likely do not have an international airport, these cities have substantive infrastructure and less intense competition for talent while providing reasonable wages,” said Shafer.

“India is still a very robust area for call center business and for collections. For certain segments of our collections business, our performance in India is significantly better than the United States. India tends to do well in collecting low balance, early stage of delinquent debt where willingness to pay is higher. Conversely, later stages of collections in the US with higher balances are serviced more efficiently in the US. By right shoring collections between India and U.S based on type of debt, we are able to deliver significant value for our clients.”

The falling dollar

According to Shafer, “The impact of the falling dollar is huge, contributing to less attractive economics in countries such as Canada and Ireland, which were once hot destinations for US companies. How does this alter the picture for HOVS’ global operations in the long term?”

“HOV Services continues to very selectively look for companies that add value to the company in strengthening its global model,” said Shafer. “Our company has experienced robust growth over the years and the trends in offshore outsourcing appear to remain strong for the future.”
Measuring and managing foreign currency exposures: History and markets can guide you

**LAURENCE HAYWARD** is senior foreign exchange advisor for Silicon Valley Bank. He has 33 years of experience in the foreign exchange and interest rate markets as a banker, broker, trader and marketer/advisor. He has worked in the major cities of the world including London, Singapore, Hong Kong, New York and Denver for Barclays International, First National Bank of Boston, Tillet and Tokyo Forex International, Gulf International Bank, and Silicon Valley Bank among others. He has been published in The Wall Street Journal, The New York Times and Consumer Reports and many periodicals.

"Quantum shakeup" is how Laurence Hayward described what has been happening in the global financial markets in the last 18 months. Addressing the conference co-sponsored by KPMG and the University of Colorado Denver CIBER, Hayward said, "It's possible to be 100 percent hedged against any foreign currency risk 100 percent of the time provided you do it right."

What does it take to do it right? "It's all a matter of timing and understanding some of the things that drive currencies," Hayward said. "The amount of time you spend on foreign exchange matters should be proportionate to the company's exposure compared to earnings and the maximum loss that could be caused by that exposure."

Hayward acknowledged that the subject of foreign currency exposures is complex and outside the comfort zone of most executives who are not directly involved in finance. "I don't think it's reasonable for me to expect people to do something they don't feel comfortable with. So I take the education approach — educating people who want to learn before they leap."

**Defining currency risk**

In broad terms, risk is exposure to anything with the potential to produce negative numbers on your company's financial statement. In international business, companies face the risk of one currency changing in price against another. Consequently, the need to make an investment that will reduce or hedge the risk. A perfect hedge reduces the risk to nothing except for the cost of the hedge. "Risk should always be negated," said Hayward.

Interest rate differentials need to be taken into account when choosing a hedge. "When you're dealing in foreign currencies you've got different interest rates for each one. And those interest rate differentials have an effect on what you do when you are hedging. Interest rates in the US are now about 2 percent below the euro; just nine months ago we were 1 percent higher than euro rates (figures are as of May 1, 2008)."

"The only thing that creates risk on an exposure is leaving time between when the exposure is known and when the hedge is put in place. Many people fail to manage their currency exposures because they don't understand what they should do," said Hayward.

"It helps for the company to define whether the currencies it is exposed to are high or low risk and whether or not they are fixed to the dollar. After that, company strategy should define which hedging instruments can and cannot be used."

**How the market moves**

Markets are fickle, the psychology fragile, the eccentricities many. "Markets trade and react on the difference between expectations and what the reality turns out to be. The combination of chart points, data releases, news, expectations and which way the market leans in favor of one or more of these components will dictate how it moves," said Hayward.

"Sometimes market participants try to be too clever and trade against expectations. If the expectations are wrong they quickly make adjustments, short covering or liquidating their positions."

That said, there are ways to sort through fast-changing data and determine if market bias trends toward the bulls or the bears. "Listen to the markets," said Hayward. "They will tell you things you can use and learn from."

Sophisticated traders study history along with financial data and current events to forecast trends and make judgments.

**Noticing:** Information contained in this article is of a general nature and should not be construed as advice.

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**MOST COMPANIES IN THE UNITED STATES DO NOT SPEND TIME ON FOREIGN CURRENCY EXPOSURES PROPORTIONATE TO THEIR IMPORTANCE.**

"Looking at history and how recent history has changed can guide you as to where your investment is going and help you guess tomorrow's best-case exchange rate."

Also, Hayward said, be especially observant of geopolitical risk because political changes can signal instability in a country which in turn could drag down investment returns.

"A lot of equity flows and investments have been going into China and India. Their currencies haven't been active in the way conventional currencies have been," said Hayward.

"The Chinese yuan is state controlled and the Indian market is a very young market. You might think that the Indian rupee would be strong because it is convertible, unlike the yuan. But the highly volatile mentality of the domestic Indian investor has a huge impact on their market, and that makes me wary of the currency."

As interest rates in the US have come down, "there has been a gradual slowdown in the amount of incoming cash flows which have helped to fund the deficit here. This has some huge economic implications," said Hayward, adding, "the funding of the US deficit is about foreign central banks like those of China and Japan buying US Treasuries."

For more information on US-cross border financial transactions and other trade data, Hayward recommended the Treasury International Capital system (TIC) website: www.ustreas.gov/tic.

To further your education about foreign exchange, go to the website of the Federal Reserve Bank of New York: www.frb.org/markets/foreignex.html and click on Federal Education.

To read some of Laurence Hayward's articles, go to the Silicon Valley Bank website: www.svb.com. •
Tax planning, lower costs draw companies offshore

Done right, going global can generate a windfall

DARICE HENRITZE is an international tax partner in KPMG’s Denver practice. She has more than 18 years of experience advising manufacturing, high technology, data/telecommunications, media and mining clients on all aspects of domestic and international tax issues, mergers and acquisitions, US federal tax issues and financial management. Henritze holds a BA in accounting from Colorado State University. She is a member of the American Institute of Certified Public Accountants, the Colorado Society of Certified Public Accountants, and the International Fiscal Association.

Going global requires an appreciation of the risks involved, said Darice Henritze, discussing tax issues at the KPMG-UCD Global Enterprise Institute conference.

“You need to understand the risks of operating abroad from the beginning if your business is to thrive,” said Henritze. “That means understanding the political environment and complying with the rules and regulations of the foreign jurisdiction.” Failure to go global without preparation “could be a death knell for your company.”

At the same time, no matter where in the world you are doing business, the United States maintains an interest in how you are operating and whether or not you are in compliance with a multitude of US laws and regulations. These usually involve taxes but can also be about legal issues such as the Foreign Corrupt Practices Act which makes it a criminal offense to participate in a bribe even though it may be an accepted practice in some countries.

“And you have to understand the real tax risks of what you are getting into.” The risks should not deter anyone from branching out, because “with the right planning, going global can generate a windfall for your company.”

Can a company that’s merely selling globally be considered a global organization?

“You’re global the second you access a customer in a foreign jurisdiction,” said Henritze. “And that jurisdiction is going to have taxes and rules intended to draw some of your revenues into their country.”

**Tax liabilities**

There are many methods for selling your product abroad, each with its own set of risks that can be mitigated with knowledge and planning beforehand. Henritze described the seven-level distribution hierarchy, starting at the top:

- Local to local
- Buy-sell (full-function) distributor
- Limited risk distributor
- Commissionaire (civil law agent)
- Agent
- Marketing representative
- Direct sale

There are tax risks at each level, even at the bottom—direct sale—where there is usually no face-to-face contact. The order is received on the company’s website and shipped direct to the customer in some far-off country from the United States.

Is there a tax on that order?

“If you are a software company and your customer is a resident of the European Union, that order is subject to a value added tax (VAT) of 17 to 24 percent depending on the country.”

Companies that are not aware of this and do not pay the tax run the risk of being assessed 20 percent of their software sales going back to the first sale. This can become a costly problem when ascending to higher levels of the distribution hierarchy and compliance regulations expose the oversight.

“I’ve seen numerous startup software organizations go global with direct sales via their website. Because they did not have a presence in the destination country, they did not realize sales were subject to VAT until they got ready to climb to the second level (marketing representative),” said Henritze. “In one such case, the VAT people suddenly appeared and claimed the company sold $2 million worth of software in the country for which VAT was not collected. Consequently, the company owed 20 percent of the $2 million or $400,000.”

Henritze explained a concept called “permanent establishment” that in the distribution hierarchy affects marketing representative, agent and commissionaire. “The rule says that if you have an independent rep completely unrelated to the company but with the authority to negotiate and sign contracts that bind you or to negotiate pricing terms, you are subject to tax on the income from those orders in both the United States and the foreign jurisdiction.

**Zero tax rate**

Countries that want your business often lay out the welcome mat in the form of tax incentives. “They will give you a zero tax rate for 10 years or they’ll give you a 7 percent tax rate forever,” said Henritze. “By moving operations into these foreign jurisdictions you might get your effective tax rate down to 22-23 percent whereas if you just did business in the United States, your effective tax rate might be 45-55 percent.”

But to reap this benefit, “you have to be able to tell the IRS that you intend to keep that money offshore and not bring it back to the US.”

Not a problem unless you have debt or other costs that have to be paid in the US. “You could get yourself in trouble because your cash cow is in another country and if you try to bring the cash back to the US it’s going to cause your effective tax rate to jump up to that 45-55 percent bracket.”

 NOTICE: The information in this article is not intended to address the circumstances of any particular individual or entity, nor can there be a guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act on such information without appropriate professional advice after a thorough examination of the particular situation.
Tax planning is not the only reason companies go offshore, said Henritze. “It’s also to lower costs. In a place like China you can manufacture for 20 percent of what it would cost to manufacture in the US.”

Henritze pointed out that over the last 10 years, hundreds of US companies set up manufacturing operations in China. “They received tremendous incentives in the form of long term reduced taxes, exemptions from export taxes and custom duties, and other benefits.”

But what the government gives the government can take away. “About six months ago, the Chinese government said, ‘We’ve got enough manufacturing in China. We’ve decided to get rid of all of these tax incentives.’

“So all the companies that moved into China because they could get a 10-year tax holiday and relief from export taxes are all of a sudden paying a significant income tax and 100 percent export taxes. And they’re stuck there; they can’t get back out without tremendous cost.”

Henritze foresees other countries following China’s lead. “In the situation that we’re in right now, where the economy is troubled in the United States, I do believe there will be a trickle down effect around the world. More countries, especially so-troubled in the United States, I do believe following China’s lead. “In the situation that they’re going to invest in manufacturing in China because they could get a 10-year tax holiday and relief from export taxes are all of a sudden paying a significant income tax and 100 percent export taxes. And they’re stuck there; they can’t get back out without tremendous cost.”

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“So all the companies that moved into China because they could get a 10-year tax holiday and relief from export taxes are all of a sudden paying a significant income tax and 100 percent export taxes. And they’re stuck there; they can’t get back out without tremendous cost.”

Tier 1: Buy-sell manufacturer - a company that will manufacture for another company. "The company might actually own the factory and be able to push profits into a low tax jurisdiction. All the risks fall to the company including product, safety, market, credit and all other business risks.”

Tier 2: Contract manufacturer - a manufacturing services provider that has very limited inventory risk and no credit risk as it is separated from sales and marketing functions. “On the benefit side, the company contracting with the manufacturer does not have to invest in building or buying a factory. Control over the finished product is much less at this level though the company might employ an oversight person to ensure quality.”

Tier 3: Consignment manufacturer - a manufacturing services provider similar to a contract manufacturer with one major difference. “The company consigns all raw materials to the manufacturer who has no inventory, credit, warranty or other risks. Although there is less control and greater risk in all departments, benefits also are smaller.”

Tax issues generally include a combination of the following: transfer pricing, VAT, customs, currency & finance, expatriate tax issues, US Commerce Department reporting, local incentive negotiations, foreign exchange controls, withholding taxes, treaty issues, and/or local compliance and tax issues.

Then there’s Subpart F, a tax levied by the IRS on foreign-source earned income whether or not that income is remitted to the US. Subpart F is applicable at Tier 1 and 2 but not at Tier 3.

Henritze stressed the importance of understanding the complexities of manufacturing in foreign jurisdictions and how they apply to laws there and in the US.

Your money, their way

Once invested in a country, you may find that the government had less restrictions on the money you brought in than on the money you will want to take out at some point.

“Most governments that give you an incentive will require that you negotiate a minimum amount of capital infusion into their country. And once you infuse that amount they probably will not let you take it back out. You have to keep it at that level or keep it growing,” Henritze cited two countries in particular that make it difficult to repatriate profits on the investment.

“In countries like Brazil and China, you may be generating a tremendous amount of revenue but it may be trapped there. This could be a problem when you have debt that has to be serviced back in the United States.

“If you don’t understand what the restrictions are in getting your cash back into the US, you may put your company in a precarious position,” said Henritze.

A few more things to think about.

Foreign exchange controls. Companies doing business globally also have to be aware of foreign exchange controls. “As a result of what happened on 9/11, the US government is now very, very interested in where you have your money. The US Department of Commerce will impose a hefty fine — as much as $100,000 — if you fail to tell them you have control over a bank account in a foreign jurisdiction.”

Income taxes. “When you go offshore, the type of income taxes that can cause unpleasant surprises are not just on passive types of income such as interest, dividends and royalties earned by your offshore entity. Income becomes taxable when your offshore entity buys product from a contract manufacturing facility you’ve set up in China or some other country and then resells it elsewhere in the world.

“There are a set of rules that view this as shifting income because you bought from a related part of your operation and shifted income outside of that contract manufacturer’s jurisdiction. All that income will be taxed when it’s brought into the US,” said Henritze.

“These and other rules are intended to speed up the time at which you can get taxed in the US. The foreign rules are intended to shift as much income as possible into the foreign jurisdiction. So you’ve got everybody fighting for your tax dollar. You’ve got to be really careful.

“I would emphasize that it’s not income taxes but indirect taxes which tend to cost companies the most money,” said Henritze. “Because indirect taxes are taxes on gross not on net.”
FCPA - Foreign Corrupt Practices Act
Understanding compliance issues key to operating abroad

MICHAEL SCHWARTZ is a Principal in KPMG’s forensic practice in Houston, Texas. He joined KPMG in 2002 and in 2007 was named the national service line coordinator for Foreign Corrupt Practices Act-related forensic services. A former assistant US attorney in the US Attorney’s Office in Houston, Schwartz is a member of the State Bar of Texas, the Bar of the District of Columbia, the Houston Bar Assoc., and the American Bar Assoc. He is admitted to practice in the US Court of Appeals for the Fifth Circuit and the US Tax Court. He holds a B.A. in economics from Cornell University’s College of Arts and Sciences, and a juris doctor degree from Emory University School of Law.

PANELISTS:
John A. Ruhnka, Professor of International Business, University of Colorado Denver
Suzanne Schoettger, Vice President of Business Controls Compliance, Liberty Global, Inc.
Frank Schuchat, founding member law firm Schuchat, Herzog & Brennan, LLC
Henry Tsuei, (retired) Senior Vice President Western Union Co.

Global companies of every size need to understand the nuances of the Foreign Corrupt Practices Act (FCPA) and the potential civil and criminal penalties that can result from a lack of compliance with its rules and regulations, according to speakers at a meeting of the KPMG-University of Colorado Denver Global Enterprise Institute.

“Violators of the FCPA risk not just regulatory penalties but criminal charges, heavy fines and jail,” said Michael Schwartz who led a panel discussion of the 1977 statute.

Enforcement of FCPA provisions is split between the Department of Justice (DOJ) and the Security and Exchange Commission (see sidebar above). “In recent years the DOJ and the SEC have made enforcement a priority,” Schwartz said, pointing out that “between 2003 and 2007, the number of FCPA enforcement actions increased tenfold.

“And yes, the DOJ and SEC do talk to each other about cases,” said Schwartz. This may not be cause for concern – unless one or the other wants to talk to you.

Key FCPA provisions
Anti-bribery - it is illegal to directly or indirectly offer, promise, or make a corrupt payment to a foreign government official for the purpose of obtaining or retaining business. Enforcement responsibility: Department of Justice (DOJ)
Books and Records - companies are required to (1) keep accurate books and records and (2) devise and maintain an adequate system of internal accounting controls. Schwartz reminded the audience that “the FBI in the 1930s caught Al Capone not for doing something illegal but for failing to report the illegal income on his federal income taxes. So if you pay a bribe, you need to report it promptly and describe the payment for what it is” even though you are confessing to a crime.

Enforcement responsibility: Securities and Exchange Commission (SEC)
For more information log on to usdoj.gov/criminal/fraud/docs/statute.html

Affirmative defenses
There are certain affirmative defenses that can be employed if challenged. John Ruhnka noted an affirmative defense that is called ‘facilitating payments’ – a small sum given to low-level government officials to get them to do what they’re supposed to do anyway.” These officials are not in a position to award contracts or influence decisions, but they can hold up permits, licenses and generally hinder application processes and services. The FCPA allows this defense if the payment is lawful under the written laws of the foreign country.

While this is indeed an affirmative defense, “the burden of proof is on you,” said Schwartz, “and there is no country that has a written law saying it is okay to make payments to government officials to get them to do their jobs. So that affirmative defense can be difficult to argue.”

Another affirmative defense, and “one that comes up all the time,” said Schwartz, “is that the payment was made as part of product promotion activities which may or may not include bringing the government official to the home office for a product demo or to a conference and paying reasonable expenses associated with the visit. In such cases the government official can be treated in the same manner as any other customer.”

There are caveats, Schwartz said, referring to a case where a trip to Disneyland was tacked on to the home office visit and the company reimbursed the official for his expenses. “The company crossed the line from reasonable marketing and selling expenses to an illegal payment to a government official.”

Frank Schuchat said, “My rule of thumb is never put cash in the hands of the foreign official; that’s risky. Have your company pay the expenses directly.” Also, he added, document those expenses.

“In China there is a cultural norm which is very different from ours,” said Henry Tsuei. “Customers expect the vendor to pick up the tab. Be aware of that and look for expertise to help you navigate the environment.”

Schwartz pointed out that businesspeople in China may be in what appears to be a private-sector enterprise but which may in fact be owned by the government. “Know your customer and who you’re doing business with,” he said.

Not just the FCPA
When the FCPA was enacted, the statute met with derision in the rest of the world, said Ruhnka. “But gradually, that has changed. Now individual European Union countries are adopting FCPA-type guidelines.”

In February 1999 the Organization for Economic Co-operation and Development (OECD) Anti-Bribery Convention became effective and has now been ratified by 37 countries. It criminalizes in each country the same kinds of conduct that the FCPA criminalizes for US companies. Unlike the FCPA, the OECD has no enforcement authority but monitors implementation by participating countries.

“There are any number of agencies around the world that share information about bribery investigations so it’s not surprising when someone gets caught in the net,” said Schwartz.

NOTICE: Information contained in this article is of a general nature and should not be construed as advice.
Something as simple as an e-mail from any employee worded in an ambiguous way can trigger an investigation that necessitates the hiring of external attorneys, said Suzanne Schoettger. “In the end you find out nothing wrong happened, but meanwhile you were distracted from business and potentially ruined your relationships in a foreign country. This is why all employees should be given training in the corruption laws.”

Red flags

Schwartz and panelists agreed that risk assessments should start with the most obvious red flags.

- Some countries are more likely to be hotbeds of corruption than others. The Transparency International Corruption Perception Index ranks countries perceived to be high risk for this kind of activity. Companies low on the index automatically raise a red flag.
- Bonuses or payments directed to an account in the Channel Island for services provided in some other country.
- Beware the ‘politically exposed person’ which is a government official’s close family member or business associate. This might be a very innocent relationship but could be very risky under the FCPA rule.
- Joint ventures. From an FCPA perspective, this is a high risk area to the extent that you rely on third parties or agents to do business on your behalf. And if you are a minority partner you have very little ability to control the business activity of the company. This is why it’s important to know who you’re dealing with, their reputation and business practices and how they acquired their book of business. It’s a good idea to write compliance issues into contracts and it’s best to do so in the local language.
- The FCPA is about where you touch government, and there are particular industries that are problematic in distinguishing between private and state-owned entities,” said Schwartz. He cited oil and pharmaceuticals in China, telecom in Netherlands, and the health care industry in Canada.
- “Canada may be fine from a corruption perception, but the reality is you’re dealing with government officials when you’re dealing with health care in Canada.”

The future of the EU in a globalized world

PETER J. WIDMER is financial advisor to a small number of wealthy European families. He previously was Chairman of Julius Baer Investment Management Inc. New York/London, Chairman of Julius Baer Investments Ltd London and a Member of the Executive Board of Julius Baer Holding Ltd Zurich. He was responsible for all institutional asset management business of the group outside Switzerland. Prior to working for Julius Baer, Widmer was with Swiss Bank Corporation Zurich and various asset management and brokerage firms in Geneva and London. He was a member of the Swiss Financial Analysts Society and holds the Commercial Diploma of the Swiss Business Association.

In 1957, six European nations signed the Treaty of Rome to create a common market for goods and services while laying the groundwork for peace and security. “To what extent has the EU fulfilled this mission?

“What started as a loose confederation of six fiercely independent nations has changed the course of history, initiating the longest period of peace in more than 300 years,” said Peter Widmer, addressing the KPMG-University of Colorado Denver Global Enterprise Institute on the subject of the European Union.

“Today, the EU is a major world power representing 27 member countries with a combined population of 450 million,” said Widmer. These numbers make it a significant trading bloc on a level with the US, China, Russia and India.”

Furthermore, Widmer added, “By providing democracy and stability in Europe – including former Soviet Union countries in eastern Europe and western Balkans – the EU has increased the potential for trade and growth across the continent.”

The EU seeks close cooperation with NATO (North Atlantic Treaty Organization); 19 member countries of the EU are also members of NATO.

Years of negotiation

In the context of the world in the late fifties, the European Union was a visionary organization based on the idea of sovereign nations sharing a common destiny. “This is remarkable given the history of Europe,” said Widmer.

While the first condition of membership is an easy one – the applicant must be a European country – the rest of the process involves meeting requirements specified in the EU’s 35 acquis (chapters of law) relating to the stability of a prospect’s democratic, political, economic and legal institutions as well as any human rights concerns and corruption issues that may exist.

In addition, there must be a functioning market economy in the country as well as the capacity to cope with competitive pressures and market forces within the EU. Meeting these requirements can take years of negotiation. Hoping to accede to membership are Turkey, Croatia, and Serbia.

With growth has come challenges. If a sign were to be posted at the entrance of EU headquarters in Brussels, it might read: 23 official languages spoken here. While English and French are usually preferred for verbal communications, documents have to be generated in the written language of the member state to facilitate comprehension. This makes for an “unwieldy, labor-intensive organization,” and is a weakness in Widmer’s view.

The EU’s rapid expansion has led to growing pains and, in some cases, dissatisfaction with how the organization is run. According to Widmer, citizens feel left

Please see EU Page 10

FCPA jurisdiction

The FCPA has territorial jurisdiction over foreign companies and nationals. Briefly, this includes:

- Any company doing business abroad, whether foreign or domestic, that has traded on any exchange in the US;
- Any foreign or domestic company doing business in the US whether or not it’s publicly traded;
- US residents working for a foreign company. Said Schwartz, “Even if you’re working for a company that is organized and existing under the laws of France and doesn’t do business in the US or have any trades in the US, you’re still subject to the FCPA.”

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out of the democratic process and smaller members feel underrepresented. “This is what led to the rejection of the constitution in 2005 by France, Holland and Ireland.”

The Treaty of Lisbon, the successor to the rejected constitution, would improve administrative efficiency and democratic transparency and implement a host of reforms, one of which would allow majority rule in many cases rather than the unanimous decisions now required. However, the treaty has yet to be ratified by all 27 members (as of this writing).

Then there is the issue of national egos. It is hard for 27 countries to take a single position on world affairs when nationalism rears its intractable head. Small wonder “the EU rarely speaks with one voice,” said Widmer. “An exception is the recent financial crisis” in which the European Commission agreed on a bold plan to boost business and consumer confidence.

“It is a serious crisis such as this that brings out the best in the EU,” Widmer said.

The internal workings of the EU must be addressed going forward. Externally, the EU is grappling with issues exacerbated by global economic woes and tensions.

■ **Energy.** Russia is the EU’s major supplier of energy. In 2007, 38% of the EU’s gas and 33% of its oil imports came from Russia. These figures can climb to 100% for some European countries – especially former Soviet republics and satellites – which rely on Russia for virtually all their energy. “Russia is quite ready to use its energy resources as a threat to the EU,” said Widmer. In what was considered a courageous action, all 27 members of the EU held an emergency meeting on Sept. 1, and agreed to condemn Russia’s aggression in Georgia.

■ **Expansion.** “The EU has to decide on the limits of expansion in terms of geography, politics, culture.” Turkey, which has been negotiating with the EU for years, has most of its territory in Asia and is only minimally in Europe. Consequently, there is some opposition to approving membership for this large and predominately Muslim country. “EU expansion philosophy depends on the outcome of negotiations.”

■ **Globalization.** Depending on where one stands, globalization is a desirable challenge to improve competitiveness or a threat to workers at risk of having their jobs outsourced. The European Commission has made a clear choice in embracing globalization and rejecting protectionist policies.

### The euro vs. the dollar

The euro has been strengthening against the dollar as a reserve currency. Already, 25 percent of the currencies held by governments and institutions worldwide is in euros and this makes the US “financially vulnerable,” said Widmer.

Introduced in 1999, the euro is the official currency of the EU. Of the 27 member states, 15 have adopted the euro as their single currency after meeting criteria such as a budget deficit of less than 3 percent of its GDP, a debt ratio of less than 60 percent of GDP, low inflation, and interest rates close to the EU average. Slovakia has been approved to replace its national currency with the euro in 2009.

The European Central Bank (ECB) is responsible for implementation of monetary policy for the euro area. Unlike the US Federal Reserve Bank which has a larger mission relating to interest rates and the overall health of the economy, the ECB is concerned primarily with maintaining the euro’s purchasing power and price stability.

Both the European Union and the United States are in recession. “It’s the first financial crisis in a globalized and integrated world.” Widmer believes the recession will be sort-lived, but in the aftermath, “there may be serious inflation because of the enormous injections of cash into the world’s financial system.”

How are the dollar and euro faring in this downturn? “The dollar benefits initially in world crises, but it is a fundamentally weak currency whereas the euro’s fundamentals are strong.

“Despite the continuing weakness of the dollar since 1971, there has been no improvement in the US trade balance,” said Widmer. “Europe is an attractive market for US manufactured products, but much of that manufacturing has been lost to foreign producers.” The result? Reduced exports and a higher trade deficit. Meanwhile, “the US borrows from China to buy the products that China makes.” One solution, he said, may be in emulating Switzerland’s focus on high value-added and innovative businesses that can be grown at home.

“The US is in a difficult position because its competitiveness is diminishing as its dependence on foreign financing is increasing,” said Widmer, pointing out that “the US is the world’s largest debtor.

In 2007, Europe was responsible for half the $280 billion in foreign direct investment (FDI) into the US as the economy then was considered to be productive and innovative in certain industries.” However, there are only 6 triple-A companies left in the US compared to 30 in 1980.”

With the collapse of the Soviet Union in 1991, the US became the world’s sole superpower. “But a new pattern is emerging and the trend is away from one superpower to two and three. The European Union and China have become strong contenders for this designation.”

Widmer stressed that opportunities still exist for US companies in all areas where there is technological leadership, excluding industrial products and finance.” Mid-market companies should be especially well-positioned to succeed in the downturn provided they have experienced management and sound business models.

“By 2010 we will see growth coming back. Environmental issues will create a big market and companies that are solution-oriented will do well,” advised Widmer.
DENNIS T. LEONARD is senior vice president of Global Human Resources Operations for the Western Union Company. He is responsible for the Global Total Rewards strategy including compensation, benefits, payroll and human resources information system for over 6,000 people in 50 countries. He is based in Englewood, Colorado at Western Union’s global headquarters. He holds a BS in business administration from Central Connecticut State University and an MBA in corporate finance from the University of Dallas. Leonard’s professional designations include: Senior Professional Human Resources (SPHR), Certified Employee Benefits Specialist (CEBS), Chartered Financial Consultant (ChFC) and Certified Financial Planner (CFP). He is on the global advisory board of UC Denver’s Institute for International Business.

The Internet and cheap long distance phone rates have done away with the need for telegrams but not for the need to send and receive cash. Western Union’s global money transfer business is flourishing and “the brand is the company’s most powerful asset with the exception of our employees,” said Dennis Leonard speaking at UC Denver’s International Executive Roundtable.

At 365,000 agent locations in 200 countries, the trusted Western Union brand means help is on the way for millions of migrants and nationals alike.

Leonard described Western Union as an “old new company” with roots dating back to 1851. In 1995 the company became a subsidiary of privately held First Data Corp., which spun it off in 2006. The “new” Western Union is now a Fortune 500 public company, positioned to grow its brand, offerings and partnerships on a global scale potentially more lucrative than ever before.

“At the time of the spin off, we had 5,000 employees; we now have 6,000 and annual revenue of about $5 billion. Third quarter 2008 revenue is up 10 percent over the previous quarter.”

The major revenue engine for Western Union is its consumer-to-consumer (C2C) money transfer segment. Recently, the company added a new segment to provide consumer to business (C2B) bill paying services.

Internally, divestiture created challenges as the new Western Union took off. The human resources (HR) structure that worked for First Data with 33,000 employees did not work for Western Union with its far smaller numbers. “We had different pay structures in different countries throughout the world which added a lot of overhead and costs to our organization,” said Leonard.

“We needed to create a consistent and flexible HR structure that would support our rapidly growing business and allow us to develop and deploy our people in ways that would facilitate global mobility and growth.”

Global rewards framework

According to Leonard, the revamped structure was designed to “increase world class retention through reduction in perceived inequities. It is built around a market supported approach to a global rewards framework.”

- Clear career paths. “We want our employees to stay with us as long as possible, providing they’re doing a great job,” said Leonard. “As we look at succession planning, we ask: Do we have the right people in the right jobs? Are we giving them the right opportunities globally to move up in the organization so they can then help us to expand?”

- People need to visually understand where they’re at in the organization, where they want to be and the path they need to take to get there. Opportunities need to be fair across borders and across the corporate hierarchy. We’re trying to create additional career opportunities for people by facilitating movement among and between the various levels.

- Global approach to job titles. “Multiple job codes existed for the same work depending on location and needed to be standardized.” This affected compensation as well as personal objectives. “For example, accountants in one country had different target bonus opportunities than accountants in another country although they all performed the same functions,” said Leonard. “We have now leveled and calibrated all jobs globally.”

- Standardized compensation plans.

- Consistent short-term incentive program. “If you don’t have an adequate bonus program then you see salaries start to creep up which then adds to your fixed costs vs. variable costs based on the company’s performance,” said Leonard.

- Consistent long-term incentive program. “The same equity grant guidelines now apply to all regions and are tied back into our core values from an HR standpoint. Western Union is a pay-for-performance culture where high performers are recognized and rewarded accordingly and where the work environment provides everyone with opportunities for personal growth.”

- “We believe in a common approach to structuring our jobs. How we pay people in those jobs will help strengthen our presence as an independent global leader and position us for continued growth and achievement.”

A guest asked if it were fair to use enthusiasm as a measure of an employee’s commitment. “Might that be a move toward too much measurement?” Leonard suggested that in addition to making an evaluation based on data, “use your gut reactions and trust your managers on the ground.”

As for job prospects in foreign countries, “the market has tightened considerably,” said Leonard whose company recently hired graduates from UC Denver Business School’s MS in international business program.

He added, “The job opportunities that exist are in domestic assignments that involve global projects.”

HOW WE PAY PEOPLE WILL HELP STRENGTHEN OUR PRESENCE AS AN INDEPENDENT GLOBAL LEADER AND POSITION US FOR CONTINUED GROWTH.
Faculty Development Program in International Entrepreneurship

Up until about 1993, very few people inside and outside of academia talked about entrepreneurship, said Patricia McDougall, a leading researcher and speaker at the 2008 Faculty Development in International Entrepreneurship (FDIE).

“Nori did international business (IB) faculty even acknowledge the existence of entrepreneurship.”

Technology – the Internet and before that the fax machine – enabled scholars to turn international entrepreneurship into a worldwide conversation, she said. “In the new millennium the study of international entrepreneurship took off. By 2004, all of a sudden IB scholars started getting interested in the subject.”

Walter Kuenmerle, an acknowledged expert on international entrepreneurship, noted in his address that “IB preceded discussions about entrepreneurship by about 15 years” and both fields faced the same challenges in the early stages of development: to be considered relevant and taken seriously by faculty and students.

Two disciplines

With the goal of putting both disciplines under the spotlight, the FDIE focused on the intersection between international business and entrepreneurship. Faculty members, current and prospective researchers, and directors of entrepreneurship centers were brought up to date on the latest concepts for teaching or internationalizing their programs.

Mind of the entrepreneur, role of the teacher

WALTER KUENMERLE is a researcher, lecturer and consultant for numerous business schools, companies and nongovernmental organizations worldwide. An expert on international entrepreneurship and private equity, he was a professor at Harvard Business School for more than 10 years, and in 1999 was named one of two Novartis Fellows. His research has appeared in publications such as Strategic Management Journal, Journal of International Business Studies, and Harvard Business Review among others. Kuenmerle holds a master’s degree in industrial economics from the Koblenz School of Corporate Management in Germany and a doctorate in business administration from Harvard Business School.

Are entrepreneurs people who just get lucky or do they possess certain characteristics that ensure success? Walter Kuemmerle posed, then answered, this question in his address to the FDIE. “I think there is a certain disposition toward entrepreneurship but a lot of it can be learned, especially through role models and great teaching.”

Teachers can help would-be entrepreneurs determine if they have the right stuff by asking pointed questions based on what Kuemmerle described as “the five characteristics that distinguish entrepreneurs.”

Are you comfortable stretching the rules? This does not mean doing something illegal. “Many entrepreneurial ventures have been built by people reinterpreting rules in a way that is creative but not illegal.” As an example, Kuemmerle cited Bill Gates of Microsoft. “Gates offered to potentially sell DOS to IBM when he did not own it yet. He stretched the rules. This is something that is very hard to teach and it’s a part of entrepreneurship.”

Are you prepared to make and deal with powerful enemies? “This way of thinking isn’t necessarily innate to students.”

“There is a certain aspect of entrepreneurship that a lot of people who research and teach it are not 100 percent comfortable with and it’s important to acknowledge this. The academic system is set up in a way that is not exactly friendly toward entrepreneurial ideas; there are certain things you can and cannot do. But at the individual level we are all entrepreneurs. When we get up in the morning and think about what we have to do next, that’s entrepreneurial.”

Do you have the patience to start small? “People with business degrees are often impatient types and don’t appreciate how long it took some of the most successful entrepreneurs to develop and fine-tune their product or service offering before a full-scale roll-out.”

Are you willing to shift strategies quickly? “Entrepreneurs are able to stand up in front of a group of people and declare, ‘What I said yesterday doesn’t apply today.’ I know of very few companies that had a business plan that worked out exactly as written. Sometimes they exceeded it and often they under-performed. So flexibility is important.”

Are you a closer? “This is the one characteristic that is quite difficult to teach in the business schools. It’s about salesmanship.”

On the question of whether or not entrepreneurs are risk-averse, Kuemmerle said, “I don’t know any successful entrepreneur who wakes up in the morning and says Show me the risk so I can take it. In a very smart way entrepreneurs off-load a lot of risk to others. This is something you have to acknowledge in the classroom when you talk to students about entrepreneurship.”

Students should also be asked how they feel about risk: How much loss they can tolerate and if they have a fallback option.

An early definition of entrepreneurship was focused on the individual’s attitude towards risk. Among other definitions it was later defined as “opportunity-oriented behavior – the relentless pursuit of opportunity without regard to tangible resources.”

However, Kuemmerle’s research shows that “most smart entrepreneurs know they need certain resources.” Therefore, he defines entrepreneurship as “Opportunity-driven behavior that’s cognizant of but without intense regard to the resources required to pursue the opportunity. It is the art of matching resources to opportunity and adjusting the match as the enterprise grows and changes.”

Sponsored by the U.S. Department of Education and the the Institute for International Business (IIB), University of Colorado Denver (UCD) CIBER in collaboration with CIBERs at Indiana University and Brigham Young University, the June 2-5, 2008 conference featured presentations by distinguished specialists from academia and the business community.

At the UCD CIBER, the teaching of international entrepreneurship leverages the university’s strengths and exploits Colorado’s position as one of the top entrepreneurial states in the US, according to Manuel Serapio, IIB/CIBER Faculty Director and coordinator of the 2008 FDIE.

Read highlights below and on following pages.
International entrepreneurship research

PATRICIA MCDougall is the associate
deans of faculty and research and the William L. Haerber Professor of Entrepreneurship at Indiana University’s Kelley School of Business. She helped pioneer the growing field of international entrepreneurship. The co-editor of four books, her research has been published in a variety of professional journals and business publications: Academy of Management Journal, Journal of Business Venturing, Entrepreneurship Theory and Practice, Inc. Magazine, USA Today, and The Wall Street Journal. In addition, her business cases appear in more than twenty-five books, McDougall holds a PhD in Strategy from the University of South Carolina.

It used to be that before a company ventured onto foreign shores it established a solid footing in domestic markets, said Patricia McDougall in outlining the evolution of international entrepreneurship in her presentation to the FDIE.

This is no longer the case. Thanks to the technology that has made communication instantaneous and transportation cheaper and faster, firms no longer have to develop in stages as they acquire the knowledge and capital to enter foreign markets.

“Tried and tested global marketing strategies – joint ventures, outsourcing, exporting, networks of global business associates – are enabling factors in an entrepreneurial firm’s ability to be international from the outset,” she said.

In her 1989 study that laid the groundwork for academic research on international entrepreneurship, McDougall introduced the term International New Ventures or INVs to more accurately describe a company’s business strategy.

“An INV is a business organization that, from inception, seeks to derive significant competitive advantage from the use of resources and sale of outputs in multiple countries,” said McDougall. “Internationalization is a multidimensional variable. A company’s level of internationalization is more than just their percentage of international sales. For example, a US company selling in Canada is not as international as a US company selling on multiple continents.”

INVs are also known as “born globals” and “global startups.”

So does it matter where a firm is located if it’s an INV?

“We found that geographical location does matter when you consider internationalization, but it matters up to a point,” said McDougall. That point pertains to locations in industry clusters such as biomedical in Denver or technology in California’s Silicon Valley. While clusters provide economic benefits due to concentrations of vendors and suppliers, “there is a point where too much clustering may result in resource scarcity and intense competition for what remains.”

At what age is an INV no longer considered New? “The operational definition of New tends to be six years old or less,” said McDougall. “Some scholars use up to eight years old or less and a few scholars use ten years old. I don’t think you can defend anything beyond ten.”

McDougall cited numerous research papers in her presentation and said choices for further research on international entrepreneurship were plentiful. Among the topics she suggested: “What is distinctive about IE? What are its theories? Are its boundaries too fuzzy?” And perhaps the most thought-provoking: “Is IE a field?”

Teaching IB from an entrepreneurial perspective

MANUEL SERAPIO is associate professor of international business and management at the University of Colorado Denver, director of the Master of Science in International Business program, and faculty director of the University of Colorado Denver (UCD) CIBER. He has designed and conducted dozens of international business and development programs for various universities and multinational companies. Serapio holds a PhD in international business from the University of Illinois, an MBA from the University of Hawaii, and a BA in economics from Ateneo de Manila University.

Entrepreneurship is as much about knowing how to go after low-hanging fruit as it is knowing how to optimize profits, said Manuel Serapio in his address to the FDIE. Of course, one doesn’t preclude the other, but “an entrepreneur just starting out needs to look for the low-hanging fruit and then take steps to reach for it,” said Serapio. This is a practical approach that can produce quick success and open more opportunities in the process, he said.

As an example, Serapio cited Starbucks. “Their first two stores were in Seattle; their third was in Vancouver. Why did they open a store in Vancouver and not in the US?”

True, Serapio said, “Vancouver was a good market and in close proximity to Seattle. But the major reason was that Starbucks had plans to go public and they wanted to show traders that the company’s potential was not limited to Seattle or the United States.

“That was the low-hanging fruit for Starbucks, and the market gave them a nice premium for exporting their business model across the border.”

Serapio invites international dealmakers to his class in ‘International Business - An Entrepreneurial Perspective.’ ‘They talk about the challenges they’ve faced and how they’ve dealt with them.”

It’s the “how” that Serapio emphasizes in class:

• How do you create an environment for international business opportunities and deals?
• How do you identify and select from alternative international business deals (product/service selection, country/market options)?

• How do you take an international business idea from concept to an actual business?
• How do you structure an international business deal?
• How can you best structure your mode of entry (e.g., export/import, international franchising, international alliances, offshoring) in international markets?

The objective, Serapio said, is to “connect the Why and the What to the How and help our students better understand how to put together international deals. It’s not very easy.”

Traditional international business courses emphasize the Who as in “Who is the primary actor?” Serapio’s approach is to put the spotlight on the entrepreneur – the person who is running the business or the person within a multinational corporation who happens to be an entrepreneur.

Although it is assumed there is an abundance of resources in a large company, “the corporate entrepreneur often has to fight for those resources and faces challenges similar to those of the lone entrepreneur trying to build a business,” said Serapio.
Entrepreneurship a good play for NBA in China

ERIC DRUMMOND is head of international human resources for the National Basketball Association based in New York City. He has over 20 years of Fortune 500 experience with companies such as Ingersoll-Rand, PepsiCo, and Coors Brewing. His focus has been in the area of global human resources supporting various international business units. He has lectured at several institutions including the University of Colorado Denver, University of Geneva, NYU, and Yonsei University (Seoul) among others. He has lived in Europe, Asia, and the Middle East. A native of Detroit, he earned a master’s in labor relations from Michigan State University. Drummond serves on IIB’s Global Advisory Board.

The NBA entrepreneurial? Some would say No. After all, the National Basketball Association has been around since 1946 and is a well-established brand domestically and internationally. “Many of the players on the 30 NBA teams are known worldwide,” said Eric Drummond, a featured speaker at the Faculty Development in International Entrepreneurship (FDIE) program.

Pick a country – any country – and mention names like Kobe Bryant and LeBron James and watch faces light up in recognition.

International sales of NBA business units account for about 15 percent of the league’s revenues. Furthermore, said Drummond, “The NBA recruits talent from around the world. The 2008–09 season boasts 76 players from 31 countries.”

This does not sound like your typical entrepreneurial start-up operation.

Drummond suggested otherwise, pointing out that when a domestic company recognizes an emerging opportunity in another country and seeks to breathe life into it despite obstacles, an entrepreneurial vision and strategy are essential.

Such was the case in China, which a year ago represented the “Perfect Storm,” a confluence of conditions that made the NBA’s international marketing team, led by Heidi Ueberroth, move to plant its flag on Chinese soil. The NBA already had a presence in China through various programs such as exhibition matches, touring basketball events, and televised games. The league also had offices and employees in the country. But conditions now were ripe for something on a much bigger scale.

Unlike companies that have flocked to China in the last several decades, the NBA was not looking for low cost labor. In fact, Drummond said, “Wages are rising there and are now up to 50 percent higher than just five years ago.”

So if it were not about wages, it had to be about the market. And for the NBA, the market was and is enticing.

- 1.3 billion population
- A growing middle class; 400 million people moved out of poverty in the last 20 years.
- Basketball has been in China since the late 1890s; Chinese fans are almost as fanatical as those in the US.
- In the 15-24 age group, 83 percent identify themselves as fans of the NBA, up from 75 percent the previous year.
- In November 2007, at the start of the season, 200 million Chinese turned on their TVs at 8:00 in the morning to watch a regular season NBA game. This was because Yao Ming of the Houston Rockets and Yi Jianlian of the Milwaukee Bucks now NJ Nets) played against each other for the first time.
- Oh, and let’s not forget the hugely successful Summer 08 Beijing Olympics and the new arena built to accommodate basketball and entertainment events during and after the official games.

Charting a different course

In its 62-year history, the NBA has grown by adding teams in the US and Canada, and maximizing profits through three main revenue streams:

- Sponsorships
- TV, broadcasting rights
- Merchandise sales

“But we asked ourselves if that were the best we could do to take advantage of this perfect storm,” said Drummond. “We came to the conclusion that if we concentrated on the same three revenue streams, we’d probably continue to make money but we’d miss the opportunity we saw developing in China.

“We shifted the paradigm from what we’d always done to what we’re good at: running a first class professional league and establishing the financial models to make that work.”

The international marketing team considered creating a second league which would function as a division of the NBA. But that had political ramifications “because it could be viewed by the China Basketball Association (CBA) as a rival.” The CBA has ties to the government and culturally to the people so that idea was quickly dropped.

“The choice came down to doing the same thing in the same way – exporting the NBA’s US business model intact – or figuring out a different way to make things happen in this particular market,” said Drummond. “This is where we became entrepreneurial and started thinking outside the box.”

The result was the formation of NBA China, a separate legal entity that is majority owned by the NBA but operates independently. It is headquartered in Beijing. Tim Chen was hired as CEO. Chen, most recently the head of Microsoft for China and previously the head of Motorola for China, “had the reputation that a brand like the NBA needed,” said Drummond.

The marketing team then contracted with Goldman Sachs to do valuation on the Perfect Storm. “We wanted them to put a dollar figure on what NBA China could look like five years out.” The number Goldman Sachs came back with? $2.3 billion.

Impressive, but not impressive enough to convince the NBA Board of Governors (the 30 team owners) in the US to provide the funding for a new venture. “They were focused on the States and not on making investments above and beyond what was already budgeted for China,” said Drummond.

Now what?

It was every entrepreneur’s biggest challenge: How to raise the funds to move forward. A stumbling block, yes, but the international marketing team had come
too far to turn back now. “We did what no other sports league had ever done: We made a decision to do a private placement, to sell 10 percent of NBA China to outside investors,” said Drummond.

“There are no outside investors in the NBA so this was all new, a way to raise seed capital to grow this business exponentially without straining the 30 team owners.”

But 10 percent of what? Ten percent of the new entity’s current business wouldn’t amount to much; however, 10 percent of the $2.3 billion projected for NBA China five years out would be sizable. So the Goldman Sachs figures were used to attract investors. But not just any investors, not family and friends who are the traditional targets of entrepreneurs. Wanted were investors who had connections as well as capital to offer.

“We held 14 investor meetings in October 2007 to find Chinese strategic partners. We pre-selected 38, mostly companies in banking, media, and technology. Of the 38, 21 actually received the private placement memo.” The response? “We had more interest than we wanted,” said Drummond.

Although a good problem, it was a problem nevertheless, “because we had to pick and choose and not upset people who might become sponsors if not investors.”

This past January, NBA China received the support it needed when investors snapped up the initial 10 percent. ESPN, a division of The Walt Disney Company, became the anchor investor with 5 percent; Bank of China 2 percent; Legend Holdings Ltd. (parent of Lenovo laptop computers) 2 percent; Li Ka Shing Foundation 1 percent. There was one more investor NBA China couldn’t refuse: Another 1 percent went to China Merchants Bank because of its strategic importance.

“So we actually sold 11 percent ($253 million); the NBA retained 89 percent.”

**Joint venture**

According to Drummond the National Basketball Association will eventually run NBA China League “but it will be a joint venture with the CBA,” thus eliminating any potential rivalries and bad feelings.

The NBA in the US came together bit by bit, adding elements as market opportunities grew. “In China, we’re starting with a blank sheet of paper that we can fill with franchise rights, league ownership, collective bargaining and innovative brand extension opportunities all up front.”

Drummond projects that in the next two years, the NBA will have 100 retail stores in China, some company owned, some franchiser owner. “This is nothing we’ve ever done before. In our US model we have only one store in New York City.” The biggest opportunity for brand extension is in arenas, he said (see sidebar).

There has been a paradigm shift, Drummond said. “We’re looking at using the NBA brand and NBA expertise for growth rather than relying on expansion teams. Because our best export is not a team but our knowledge. We know how to run a first class professional league and we know the financial models to make that work.”

NBA China is not just about the NBA, Drummond said. “Culturally it’s also about what we want to do for the country and for basketball.”

In addition to philanthropy, plans include a revamp of the entire provincial basketball system, a grassroots effort that consists of basketball academies and clinics “that will help manage how basketball is taught from high school to college.” If all goes according to plan, it is likely that NBA China will go public in three-five years.

And the owners? What do they think of NBA China now? “Brilliant,” they said at a recent board of governors meeting.

Despite the excitement about China in many corporate boardrooms, there is unease among some Americans who feel that the communist government could clamp down on foreign companies anytime they choose. Drummond does not share these concerns.

“I would submit there is no way the Chinese government can stop what is happening there now. They could perhaps put brakes on the economy, try to steer it, but that train has left the station.”

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### Beijing Olympic Basketball Arena

Two years ago, kicking off the Perfect Storm, the NBA started advising the Beijing Organizing Committee for the Olympic Games (BOCOG) on the design of the Beijing Olympic Basketball Arena (BOBA).

“They came to us because they knew we knew about arenas,” said Drummond. “In order to incorporate the upscale elements they wanted, we advised them to increase their budget by many millions.”

There are many “firsts” attached to development of the arena. It is the first collaboration of its kind in Asia. The goal was to develop a world-class NBA-style venue that would remain an attraction for citizens and tourists long after the closing ceremony of the 29th Olympic Games.

By all accounts, the goal has been accomplished. The arena is twice as big as current CBA stadiums, with a capacity of nearly 19,000 seats, including club seats and 48 private suites, all with excellent views of the action. Furniture, light fixtures and audio-visual systems have been custom designed. Food and beverage options from around the world will satisfy a multitude of tastes. “After the Olympics the site will host NBA games, concert tours and shows, international and regional events, even a traveling circus,” said Drummond.

The arena will be run by a partnership of the BOCOG, NBA China, and AEG, a wholly owned subsidiary of the Anschutz Company and operator of facilities such as the Staples Center in Los Angeles. For the NBA it’s another first, their first venture into facility management in China.

“We’ve learned from the States; we’re doing this is Europe and now also in China. This arena in Asia is a first of its kind,” said Drummond, looking ahead to which city will want the next one. Will it be Shanghai, Chengdu, Guangzhou? “In China, they go from primitive to state of the art like this,” he said, snapping his fingers. “There is no in between.”

And in a country where basketball is a favored sport and a new billionaire pops up on a monthly basis, there will also be no shortage of funding.
Teaching IB: The GEM factor

DONNA KELLEY is an associate professor of entrepreneurship at Babson College, Mass. She teaches entrepreneurship, corporate entrepreneurship and entrepreneurship in Asia. Her research on management practices for innovation and corporate entrepreneurship in large established organizations, and the patent, alliance and product innovation activities of technology-based startups has been published in the foremost academic journals. Kelley holds a PhD from Rensselaer Polytechnic Institute, an MBA from the University of Massachusetts Amherst, and a BA in chemistry from the Massachusetts College of Liberal Arts.

In her address to the Faculty Development in International Entrepreneurship, Donna Kelley explained the significance and goals of the Global Entrepreneurship Monitor (GEM).

According to the 2007 Executive Report, GEM is a “multinational, harmonized research program providing annual assessments of the entrepreneurial sector for a range of countries.”

In 2007, 42 countries participated in the GEM project. These include high-income countries such as France, Japan, United States; middle- and low-income countries in Europe and Asia such as China, India, Russia; and middle- and low-income countries in Latin America and the Caribbean such as Argentina, Brazil, Chile. In 2008, 45 countries are participating.

GEM measures the percentage of individuals in a country who are just starting businesses or are owner-managers of businesses up to 3.5 years old. “We measure individual participation in entrepreneurship as a percentage of the total population,” said Kelley. “We’re not focused solely on formal business registrations but can also capture those people who are engaged in informal businesses. In some economies, this number tends to be pretty high.”

In 2007, Thailand and Peru showed the highest entrepreneurial activity. Latin American countries and China also exhibited high rates of entrepreneurship. GEM also measures a number of characteristics of entrepreneurship in a country, such as perceptions about entrepreneurship, motivations for starting a business, the innovativeness of the products, and growth prospects. A global report is published every year, and there are also special reports on women-led businesses, entrepreneurial finance, and high-growth entrepreneurship.

“Our goals are to increase global awareness about entrepreneurial activity, increase academic understanding of the nature of entrepreneurship, and ultimately impact society in terms of creating policies that are supportive of new business creation,” said Kelley.

GEM was founded in 1999 by Babson College in the US, and the London Business School in the UK. •