

Entrepreneurship

Peggy A. Lambing Charles R. Kuehl
Fourth Edition



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\$ *What is the geographic location and number of customers?* If the customers are located throughout the country, direct sales would be more complex than if they are in a small geographic area. Although direct sales would be possible, it would take more time and money to develop the network.

\$ *What are the product characteristics?* Perishable products must move quickly through channels. Complex, high-technology items are often sold through person-to-person sales.

\$ *What are the entrepreneur's resources?* If the entrepreneur has the financial resources to have a sales force or to market the product directly to the final consumer, this may be an alternative. However, because of limited resources, many small businesses use intermediaries who have financial resources and a marketing network that is far more efficient than the small business's own system.

\$ *How do competitors sell their products? Will the marketing intermediaries adequately promote the new product?* Entrepreneurs must consider how their competitors sell products and whether the marketing intermediaries will promote the new product if it decreases sales of competing products. If the intermediaries will not promote the product adequately, the entrepreneur may decide on a different approach.³⁷

Obstacles to Securing Distribution Channels

Although many distribution channels are available, entrepreneurs often find it difficult to get their product to market. For example, many who go directly to wholesalers or retailers with new products find that the intermediaries are not interested in taking on a new product. Entrepreneurs must realize that large retailers such as Wal-Mart, Target, and others are constantly bombarded with new products, and they do not want to stock and display a product if it will not sell. Many want proof of a demand for the product—a successful market test—before they carry the item. It is often difficult to persuade someone to carry it even for a market test.

Many entrepreneurs with new product ideas are also surprised to find that direct marketing channels, such as catalogs or home shopping services, require a minimum inventory level before they will market the product. One entrepreneur who developed a new baking device was told that she could not advertise her product in a home shopping service unless she could prove she had an inventory of at least 10,000 units. (The home shopping service did not want customers to order the product and then be told it was not in stock.) Because the entrepreneur did not have the financial resources to produce 10,000 units without a guarantee of sales, she could not use this marketing channel.

Some retailers will not accept a new product unless the entrepreneur can guarantee a minimum level of advertising to create demand among customers. Often this minimum is far in excess of the financial resources of the small firm.

Finally, because of the large number of new products, limited retail space, and the cost of inventorying new items, many retailers charge fees for carrying new products. Called *slotting fees*, they can range into tens of thousands of dollars. Other fees may be charged if a new item does not meet sales projections. These additional fees are based on the costs of removing items from inventory and the lost revenue from the item. Retailers may also ask for an annual renewal fee to continue carrying an item, as well as trade allowances or other discounts.³⁸ Obviously, for a new small business, these fees may be prohibitive. Many entrepreneurs find that these fees make it impossible to get their items on store shelves.

Slotting fees – charges by retailers for carrying a new product.

LICENSING

If an entrepreneur develops a new product but does not have the time or funds to manufacture and distribute it, a licensing arrangement may be the answer. The entrepreneur licenses another company to manufacture and sell the product in exchange for a fee.

Licensing is common in many industries, including the toy industry. The Toy Manufacturers of America estimates that 40 percent of all toys sold are licensed products.³⁹ However, that does not mean that it is easy to get a new toy licensed and distributed. Many of the licensed toys are based on well-known characters such as Barney, Batman, or the *Star Wars* characters. It is much more difficult for an inventor to get a company interested in a licensed product. Don Debelak, author of *Bringing Your Product to Market*, estimates that only 300 to 500 people per year are successful in licensing a product. Debelak states, “Companies that know how to market products usually have plenty of their own product ideas to introduce and will take on only truly novel, innovative products.”⁴⁰

LEGAL PROTECTION OF NEW PRODUCTS AND SERVICES

Nondisclosure document
– contract stating that the signator will not discuss the idea with anyone else or use it for personal gain.

Patent – the grant of a property right to the inventor(s) issued by the U.S. Patent and Trademark Office.

If an entrepreneur develops a new product or service, a major concern is that others will try to develop similar items. This comes about quickly when the entrepreneur needs advice and/or expertise during the research and development phase and when a prototype (the original model) is developed. Even discussing the idea with others may result in the concept being stolen.

A simple form known as a *nondisclosure document* is often used in the early stages of development. Anyone who must be made aware of the idea is asked to sign the nondisclosure document, which states that the signator will not discuss the idea with anyone else, nor use the idea for personal gain.

Patents

A U.S. *patent* for an invention is the grant of a property right to the inventor(s), issued by the U.S. Patent and Trademark Office. The patent excludes others from “making, using, offering for sale, selling,” or “importing” the invention in the United States. *Utility patents* are granted for any new useful process, machine, article of manufacture, or useful improvements. *Design patents* are granted for new, original, and ornamental designs of manufactured articles. Finally, horticultural *plant patents* may be granted for new varieties of plants.⁴¹

In order for an invention to be patentable, it must be new as defined by patent law. If the invention has been described in a printed publication anywhere in the world, or if it has been in public use or on sale in this country before the date that the applicant made the invention, or more than one year before the patent is applied for, a patent cannot be obtained. Thus if the inventor describes the invention in a printed publication, uses the invention publicly, or places it on sale, he or she must apply for a patent before one year has gone by; otherwise any right to a patent will be lost.⁴² Only the inventor may apply for a patent, with certain exceptions. A person who makes a financial

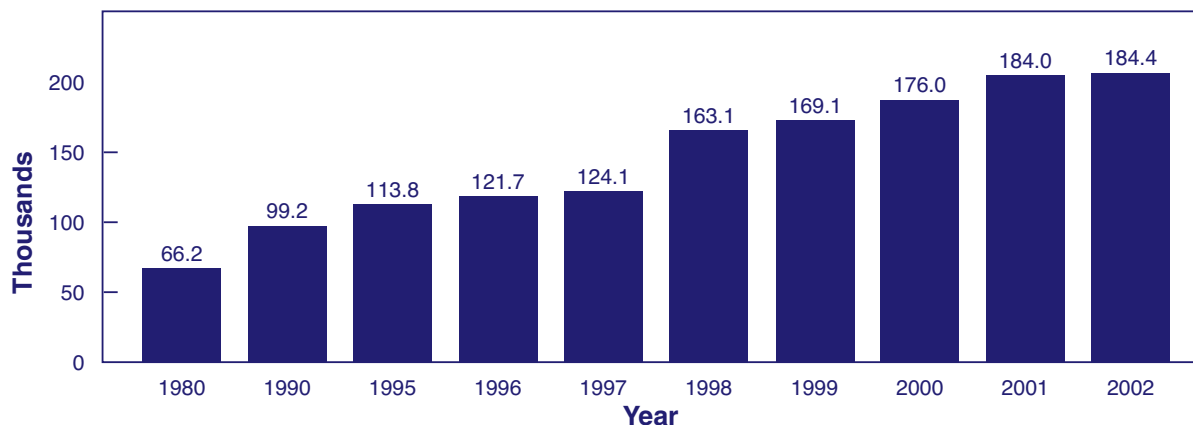
contribution is not a joint inventor and cannot be named in the application as an inventor.⁴³

As shown in Figure 2, the number of patents issued since 1980 has risen steadily.

Problems with patents Patents often do not provide as much protection as the inventor originally believes. Unfortunately, competitors can sometimes circumvent patents by making minor changes in the design of new products and then selling them as different from the patented products. And, since ideas are not patentable, an idea for a new business such as selling balloon bouquets instead of flowers is easily copied once the first person starts operating. Even if a patent is obtained, this only gives the patent holder the right to a court fight. Obtaining patents and fighting infringement are often a costly process. Also, a patent does not protect the inventor from claims that his or her product infringes on an existing patent. Although patent searches can be completed before applying, such a search will not identify patents that are pending. Therefore, it is not an absolute guarantee that the product is unique. Finally, a U.S. patent does not provide protection in foreign countries. In some countries, it is possible to obtain a *patent of importation*, which provides temporary protection. However, a permanent patent must be obtained in every country in which protection is desired.

Patent of importation – provides temporary patent protection in a foreign country.

Patent searches on the Internet One of the first steps required is to complete a search of existing patents to determine if one exists on a similar product. Prior to the invention of the Internet, this could only be done in libraries or by hiring a search firm. With the development of the Internet, a substantial amount of patent information is available free of charge. The U.S. Patent and Trademark Office (<http://www.uspto.gov>) has full texts of patents on its Web site. The European Patent Office (EPO) also offers the full text of patents for free on its Web site at <http://www.european-patent-office.org>.⁴⁴



Source: U.S. Census Bureau, *Statistical Abstract of the United States: 2003*, <http://www.census.gov/prod/2004/pubs/03statab/business.pdf>.

FIGURE 2 U.S. Patents issued, selected years 1980 to 2002.

Copyright – protection provided by federal laws for intellectual works.

Copyrights

A *copyright* is a form of protection provided by the laws of the United States to the authors of “original works of authorship,” including literary, dramatic, musical, artistic, and certain other intellectual works such as software. In addition, copyrights may be obtained on pantomines and choreographic creations, pictorial, graphic, and sculptural works; motion pictures and other audiovisual works; and architectural accomplishments. A copyright gives the owner of the copyright the exclusive rights to reproduce the work and to prepare any other material derived from the work. For any works created after January 1, 1978, the work is automatically protected for the life of the author plus 70 years. In some cases, such as an anonymous work where the author is not known, the copyright will extend for a longer period (95 or 120 years) but the term will be based on the date of the publication or creation since the author’s birth date is not known.⁴⁵

Copyrights may not be obtained on information that is common property and that does not contain original authorship. Therefore, items such as calendars, height and weight charts, and rulers may not be copyrighted.⁴⁶

A copyright is secured automatically when the work is created, and a work is created when it is fixed in written copy, videotape, microfilm, cassette tapes, or other tangible form. No publication or registration in the copyright office is required to secure a copyright. A copyright registration made with the Register of Copyrights in Washington, D.C., is a legal formality to make a public record of the copyright. However, before an infringement suit may be filed in court, registration is necessary for works of U.S. origin.⁴⁷ More information is available at <http://www.copyright.gov>.

Trademark – a word, symbol, name, or device that a business uses to identify its goods and distinguish them from others.

Trademarks

A *trademark* is a word, symbol, name, or device that a business uses to identify its goods and distinguish them from those of others. (A service mark is similar in that it is used to distinguish the services of one provider from another.) The mark is granted when the design is used; however, an application can be filed as long as there is intent to use it. As with copyrights, it is not essential to register a trademark or service mark with the Patent and Trademark Office; however, it does provide several benefits:

- \$ notice nationwide of the trademark owner’s claim
- \$ evidence of ownership of the trademark
- \$ ability to invoke jurisdiction of federal courts
- \$ ability to use registration as a basis for obtaining registration in foreign countries
- \$ ability to file registration with the U.S. Customs Service to prevent importation of infringing foreign goods⁴⁸

The designations “TM” for trademark and “SM” for service mark usually indicate that a company or individual claims rights to the mark. These designations are often used before a federal registration is issued. There are no federal regulations governing the use of these designations; however, there may be state or local laws.⁴⁹ The federal registration symbol “®” may be used once the mark is actually registered with the U.S. Patent and Trademark Office. Even if an application is pending, the symbol may not be used before the mark is officially registered.⁵⁰

In addition to the federal trademark laws, state trademark statutes exist and are not preempted by federal laws. State registrations are less expensive and easier to obtain than federal registration. It is advisable to obtain state trademark registrations in the principal states where the mark is used.⁵¹

One of the biggest problems with trademark law is that it is often vague and confusing, making it difficult to determine if trademark infringement will result. For example, when Compaq computers were developed, the inventors were told by their lawyers that the name might infringe on the trademark of a cable-switching company named Compac. The inventors decided to keep the Compaq name anyway because they believed it was a good name. No lawsuit resulted.⁵² On the other hand, Lone Star Steakhouse and Saloon has been involved in a number of lawsuits concerning the rights to use the Lone Star mark.⁵³

Trade Secrets

If a business has a process or information that cannot be patented, copyrighted, or trademarked, the entrepreneur may still wish to keep the information confidential. In this situation, a *trade secret* may be helpful. Employees are asked to sign a statement that they will not disclose the information. This becomes a legal contract and violation of that contract is illegal.

The theft of a trade secret has been and still is subject to a civil lawsuit in many states and to criminal action in some states. However, now the theft of a trade secret may also be subject to federal criminal action. With the passage by the U.S. Congress of the Economic Espionage Act of 1996, the theft of a trade secret is now a federal criminal offense. A person convicted under this law can be fined and imprisoned, and an organization can be convicted and fined.⁵⁴

In order to make a trade secret contract binding, the entrepreneur should first define what is to be protected as narrowly as possible. If common information is included in the contract, it may be declared void. Second, the number of people who are asked to sign it should be limited. If every employee is asked to sign the document, the agreement becomes less enforceable. Finally, employees should sign the agreement when they are first employed. It is better if the entrepreneur can prove that the employee received something as a condition of signing the agreement. Therefore, if the entrepreneur waits until the employee has worked for the company for many years, the contract may not be upheld. Asking the employee to sign the document as a condition of a promotion or raise, however, may be upheld.⁵⁵

Trade secret – a legal protection for information that cannot be patented, copyrighted, or trademarked.

NEW PRODUCT DEVELOPMENT AND THE BUSINESS PLAN

If the new business is dependent on a new product that has been developed or will be developed, a thorough explanation of the stage in the development process must be given in the business plan. If any copyrights, trademarks, patents, or trade secrets will be obtained, that information should be explained in the legal section of the plan.

Since new product development is a risky and time-consuming endeavor, banks will usually not be interested in reviewing business plans requesting financing for the early stages of the process. Often, a business plan based on new products must be submitted to investors, or the entrepreneur must use his or

her own funds. Banks will be more likely to provide financing once the product is developed and the entrepreneur can demonstrate that a demand for the product exists.

SUMMARY

New product development is a high-risk endeavor, since many new products and services fail. Small companies can develop products more easily than large companies can because they are less bureaucratic and can react quickly to market changes. Small businesses, though, are hindered by a lack of financial resources and obstacles such as minimum inventory levels and slotting fees. In addition, the entrepreneur may need to obtain a patent, copyright, trademark, or trade secret to provide legal protection for the new product.

DISCUSSION QUESTIONS

1. Identify two products or services that have failed (do not use the ones listed in this chapter). Why do you think they did not succeed?
2. Choose an item that is used in everyday activities (chair, desk, toaster, and so on). List all of the assumptions you can identify that are associated with this product. Then vary those assumptions to create new product ideas.
3. When cheaper, look-alike products are created to compete with original products, the look-alike items are often called *knock-offs*. Identify some products for which knock-offs have been created. Through library research, identify any legal action that was taken.
4. Many experts state that in order to be successful, a new product has to be the first of its kind on the market. Do you agree? Why or why not? Give examples to support your answer.

ENDNOTES

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