OCCASION

This publication has been made available to the public on the occasion of the 50th anniversary of the United Nations Industrial Development Organisation.

DISCLAIMER

FAIR USE POLICY

CONTACT

Please contact publications@unido.org for further information concerning UNIDO publications.

For more information about UNIDO, please visit us at www.unido.org

UNITED NATIONS INDUSTRIAL DEVELOPMENT ORGANIZATION
Vienna International Centre, P.O. Box 300, 1400 Vienna, Austria
Tel: (+43-1) 26026-0 · www.unido.org · unido@unido.org

Distr.
LIMITED

ID/WG.131/5
28 July 1972

ORIGINAL: ENGLISH

United Nations Industrial Development Organization

Expert Group Meeting on Licensing Practices
Vienna, 28 August - 1 September 1972

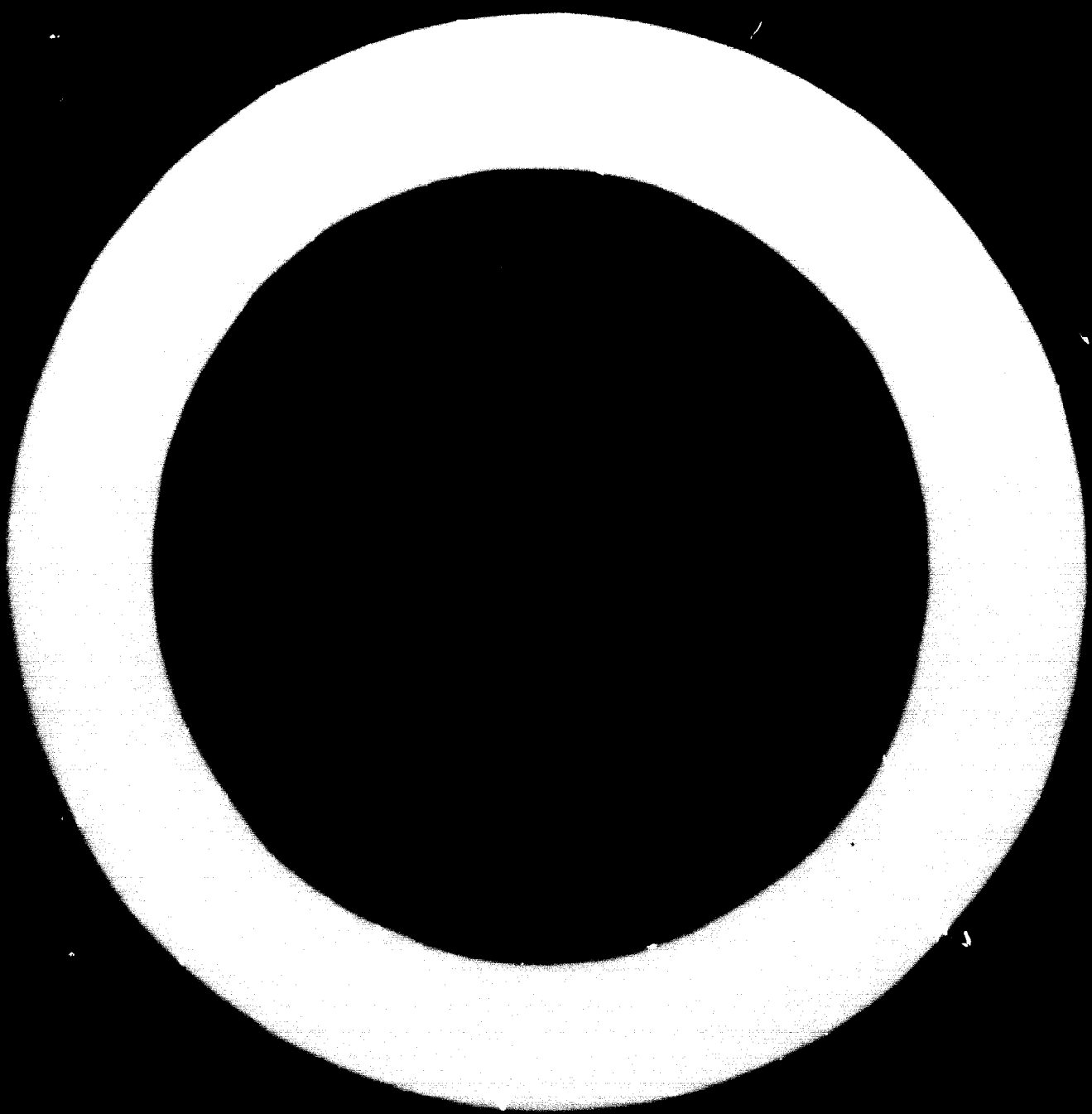
INTERNATIONAL LICENSING FROM AND TO HUNGARY 1/

by

A. Vida
Consultant to UNIDO
Hungary

1/ The views and opinions expressed in this paper are those of the author and do not necessarily reflect the views of the Secretariat of UNIDO. This document has been reproduced without formal editing.

id.72-4716



Almost all East European countries - with exception of Greece - have a socialist system, which disregarding its political features determines their economic policy.

The basis of the economic policy in these countries is therefore the social property of every important instrument of production, the most important part of these is State property. But regarding territory, population, economic level there are great differences among the various East European socialist countries, so we will content ourselves with preparing a paper only on licensing from and to Hungary, that will enable us in the meantime to give more details.

1. Economic Policy Regarding International License Agreements

It would be possible to furnish statistics about the increase of licensing into Hungary, but we should content ourselves only with referring to Dr. HOROOS, Minister of Metallurgy and Machine Industry, who said that in the last four years the number of licensing to Hungary was higher than in the previous 15 years. It was established that about 50 percent of licenses bought in the period 1950-1970 by Hungarian enterprises were licensed to Hungary in the last three years of the same period. [1)]

As regards licensing from Hungary, remaining henceforward in the frames of the Ministry of Metallurgy and Machine Industry, we can report on the fact that on the 15 July 1972 there were 959 inventions, know-hows, improvements that were offered for sale abroad, a number illustrating the aim of the Hungarian industry licensing its technical achievements abroad. It is quite a different question, how skillful

and successful this was turned out.

It may be clear that even when enterprises have a great independence, in a socialist country where economic policy is rather intensively directed by the State, such a favourable trend of international licensing from and to abroad would not exist if it were not favoured by the State.

And now we reached the subject of the economic policy regarding international licence agreements. We think it may be enough to give only a selection of the relating most important documents in Hungary.

The Economic Committee of the Hungarian Government adopted in 1969 a basic resolution on licensing from abroad, that says

- the concerned (ministries, enterprises) are due to study the possibility of licensing from abroad before deciding on a certain job of technical development;
- certain fiscal provisions were decided by the Government on furthering licensing from abroad;
- the task of the ministries was established to further licensing from abroad.[2)]

This basic resolution prepared the field. A year later the Parliament voted in the Act about the Fourth Five Year Plan (1970) under the heading "foreign trade" on licence agreements as follows: "Mutual advantageous relations, transmissions of licences and technologies, the various ways and means of scientific - technical, producing and marketing co-operation are to be amplified" (Section 31, item 4).[3)]

Finally let us cite a speech delivered by R. Ayers, Secretary of the Hungarian Socialist Workers' Central Committee at the 10th Party Congress in 1970: "Foreign trade with western countries continues to be of great importance, and these relations gradually expand to other ways of co-operation too: to the co-operating exploitation of natural resources, to joint scientific research, to the development of license trade ..." 4)

The quoted documents of three different types are able to give a glance into the trend of Hungary's economic policy regarding international licensing.

2. Rules of the Patent and Trademark Act on Licensing

Hungary is one of the few countries all over the world where the civil law (i.e. the Patent and the Trademark Acts) is particularly rich in provisions on licence agreements. Both acts were adopted by the Parliament in 1969 and entered in force in 1970, and both have a special chapter providing for licence agreements.

There are some common features of the two acts as regards licence agreements:

(a) The rules established by these acts are facultatives, the wording of the two acts is literally identic as they say, that "the parties, by mutual consent, may lay down terms that differ from the provisions relating to licence agreements where this is not prohibited by legislation". (Patent Act Sec. 20. it. 1.[5] Trademark Act. Sec. 11. it. 1.[6]). But such a prohibition is only established by Sec. 9. it. 3. of the Trademark Act and we shall report on it later.

(b) The subsidiary applicability of the general rules of civil law is also established by both acts as they say, that "matters relating to license agreements and not covered by this Act shall be governed by the provisions of the Civil Code". (Patent Act. Sec. 20. it. 2., Trademark Act. Sec. 11. it. 2.) There are especially the rules on the validity, contestability, cancellation of contracts, that may be applied from the Civil Code, that is why there was no reason to create special rules in the Patent or Trademark Act.

(c) Concerning the definition of a licence agreement there is also a significant similarity between the wording of the two acts. In this respect Sec. 17. it. 1 of the Patent Act says: "On the basis of an agreement granting a license under a patent the patentee grants a license for the exploitation of the invention; in exchange, the user is under obligation to pay royalties". There is only one word that varies from the same definition of the Trademark Act (Sec. 8.) where not "exploitation of the invention" but instead of it "use of the trademark" is said.

(d) Relating to the expiration of a licence agreement there is again a literal identity, providing that "the licence agreement expires, with prospective effect, when the duration fixed in it comes to an end, or if certain specified circumstances occur". (Patent Act Sec. 19. it. 1, Trademark Act Sec. 10.) It is clear that the last words relate to the possibility of cancellation of the contract as provided in the Civil Code.

(e) In respect of the rights of licensee in the event of trademark infringement we have to underline that

these provisions being not included in the special chapters on licence agreements, are not facultative, but compulsory. The wording of Sec. 14. of the Trademark Act is as follows: "In the event of Trademark infringement, the registered user may institute proceedings in his own name, provided he has previously called upon the proprietor of the trademark to take appropriate action in order to put a stop to the infringement and the latter has failed to take action within thirty days". Sec. 27. it. 1 of the Patent Act is identically formulated with the only one difference that these rights are not limited to the registered user, but they are granted to the non registered too.

These are the common features of the Patent and the Trademark Act as regards licence agreements and now we have to report on their specific rules, that are as we have already said facultative.

The Patent Act provides for the effect of registration saying that "a licence agreement may be invoked against a third party who acquired his right in good faith and for a consideration only if it is recorded in the Patent Register". (Sec. 17. it. 2.)

A very important obligation of the patentee, that as we know does not figure in any act of other countries the warranty of title is worded as follows:

"The patentee shall guarantee, for the duration of the contract, that third parties shall have no right in the patent which would prevent or limit its exploitation. This guarantee shall be subject to the same rules as those applying to a vendor for the transfer of his right of ownership, with the difference that the licensee, instead of withdrawing, may rescind the contract with immediate effect." (Sec. 13. it. 1.)

There is no need to say that this rule protects the licensee, and may have a great importance when licensing to Hungary from abroad.

Concerning the size of the rights granted by a licence agreement the following provisions correspond to international practice: "The licence agreement shall cover all points of the patent claims and every mode of exploitation to any extent whatever, without limitation in time or space. However, a right of exploitation under a licence agreement shall be exclusive only if expressly stipulated." (Sec. 18. it. 2.)

An obligation of giving information that bounds the patentee declares as follows: "The patentee shall inform the user of any rights deriving from the patent, as well as of important circumstances. Nevertheless, he shall be obliged to transfer technical know-how for the carrying out (working) of the invention only if this has been expressly agreed ". (Sec. 18. it. 3.) This rule completely corresponds to the international practice of licence agreements.

On the assignability of the licence agreement the following rule is decisive: "The licence may be assigned by the user to a third party only with the express consent of the patentee". (Sec.18. it. 4.) I think this rule is also quite logical.

As regards the maintenance the rule is, that "the patentee shall be obliged to ensure maintenance of the patent". (Sec. 18. it. 5.) I am convinced that the same settling is general in most countries.

Lastly there is again a rather original rule on the lot of royalties if the patent is cancelled, where the acts says:

"If the patent ceases to exist with retroactiv effect to its origin, the user may claim only the portion of the royalties he paid that was not covered by the useful results derived from the exploitation of the invention" (Sec. 19. it. 2.).

There are such or similar settlings adopted by courts and literature of certain other countries too, but as we know it was only the Hungarian law-maker who introduced that rule in the same act.

As regards the Trademark Act its general provisions on the rights and obligations of the parties are worded as follows: " A licence agreement grants, for the duration of trademark protection, the right to use the trademark, without territorial limitation, for all goods enumerated on the list of goods. However, unless expressly stipulated, the user shall have no exclusive right to exploitation, and unless expressly authorized by the proprietor of the trademark, he shall not grant a further licence to a third party". (Sec. 9. it. 1.) All these rules are rather logical and corresponding to the international practice.

Concerning the control of the quality the rule established by the act is more original as it says:

"The proprietor of the trademark may stipulate in the contract that the trademark shall be used only for goods having a specific quality. In such case, he shall have the right to control the quality of the goods, even if this is not mentioned in the contract". (Sec. 9. it. 2.)

As for the method applied by this rule we may establish that it supplements the contract, as for its object it is typical for the socialist law. In most of the East European socialist countries there are such or similar provisions in the trademark acts.

The same idea, the protection of the consumers is further developed by the following rule stating the voidness of the licence agreement, that is worded as follows:

"The licence agreement is void if its existence or application is liable to create deception". (Sec.3.it.3.)

As the motivation of the act explains the consumers must be protected particularly against deception in respect of the quality of the goods.

We are at the end of the review on the roles on licensing of the Patent and Trademark Act that review is very concentrated and we have only made a very few remarks, that cannot be considered as commentaries. The question may be put now: how far these rules may come to an application in the course of international licensing? The answer is very simple: in all license agreements governed by Hungarian law. As the practice shows, such agreements are generally those the aim of which is licensing from Hungary, especially into developing countries. To the next question: which licence agreements are governed by Hungarian law, we try to give an answer in the following section.

But before passing to the next matter we have to inform simply that know-how agreements are not governed by the Patent Act. The situation is the same as in almost all other countries, there is no statutory law, but the general rules of civil law are applicable. Accordingly there are no special provisions on the protection of know-how, it is protected by the agreement itself only.

3. Contract Laws Governing Agreements Licensing from and to Hungary

As we have just told, licence agreements the subject of which is a delivery of Hungarian inventions, technology, know-how, etc. to developing countries are often governed by Hungarian law. Why? Because the parties agree in the contract that this will be governed by Hungarian law. Developing countries, the civil law of which is very often underdeveloped, often accept the law of a socialist country, e.g. the Hungarian one, as law of the contract.

The situation is just opposite when licensing from highly developed Western Europe countries to Hungary. Under such circumstances I do not know any license agreement where Hungarian law would be governing. In such agreements, as a rule, the Hungarian licensee submits himself to the law of the foreign licensor, and if he does not like to do so, the parties choose the law of a third country, e.g. that of Switzerland.

There is no rule at all under Hungarian law limiting the liberty of the parties to choose any kind of law to govern the contract.

But if the parties have not determined the law governing the contract, this question will be decided with the help of the rules of international private law. As until now such judgement has not been passed in Hungary, it would be only a theory I should be able to say about this question, therefore I think I will omit this point.

On the other hand, there is a very important rule established by the Minister of Foreign Trade in his decrees on licensing to and from abroad (1953, 1961) that says that all international licence

agreements have to be approved by the Ministry of Foreign Trade. As the Sec. 215 of the Civil Code provides that contracts, that have to be approved, are void without being duly approved this rule furnishes a basic guarantee for the State that no licence agreement will come into force that has not been approved. It is through the approval that the State exercises its economic policy: preventing to carry out agreements that may be advantageous for certain enterprises or co-operatives, but are not for the economic policy of the whole country.

There is therefore a rule of the Hungarian statutory law, the knowledge of which is important for all foreign partners: licence agreements even signed by the Hungarian party are valid only after approval of the Ministry of Foreign Trade.

It will be useful to add that the refusal of approval is only a security rule, which is applied rather seldom, normally the Ministry of Foreign Trade, the National Bank of Hungary and the authorities are informed already since the beginning about the negotiations, their aims and their results. Surely it would be meaningless for the Hungarian enterprises to negotiate for months, or sometimes years with foreign partners, if there is no hope that the licence agreement will be approved. To prevent such situations being unpleasant both for the Hungarian enterprise and for its foreign partner, there are certain administrative prescriptions (obligation to ask a preliminary consent to the negotiations licensing to Hungary) guaranting that when this prescription has been accomplished there will be no problem with the approval. And the practice is like this: if the terms of the preliminary consent to the negotiation are accomplished by the

license agreement, there is almost no probability for the refusal of the approval.

Although these intern administrative prescriptions bind only the Hungarian enterprises, I think it is useful to give an idea of the intern mechanism of the approval system, because it affects foreign licensors and licensees also indirectly.

4. Licensing Foreign Technology

Hungarian experience in licensing foreign technology through bilateral aid is in a general sense favourable. That is why the State economic policy, as we have mentioned it already, is favourable for licensing foreign technology.

The licence agreements are sometimes very voluminous (the agreement on implanting a camion-motor factory is more than 600 pages) there is no place here to give a detailed analysis, so we shall content ourselves with reporting on some claims that we think particularly important.

(a) Claims on the territorial effect of the agreement are typical for international licensing. These claims have a great importance concerning the exploitability of the licence, i.e. relating to the question into which countries the licensee is authorized to export the articles manufactured under the licence agreement.

As the Hungarian market is not very large, in most of the cases, licensing from abroad Hungarian licensees trend to obtain the right to export the articles manufactured under licence at least to the

COMECON countries (a market with approximately 400 million inhabitants), or if it is possible to other countries too. The bigger the territorial possibilities granted by the agreement, the higher the royalties.

That is why most of these claims have three sections:

(i) the first specifying the countries where an exclusive right is granted to the licensee;

(ii) the second specifying the countries where a non exclusive right is granted (sometimes with numeral limitation of the export);

(iii) the third specifying the countries to where it is forbidden to export.

As these claims have a great economic importance it may be clear that their wording is often passionately discussed by the parties, and it also happened that agreements were not signed because the parties were not able to agree in this relation.

Specific sanctions may complete these claims, e.g. prescribing liquidated damages if violating these claims of the agreement.

(b) Claims on documentation and technical assistance assure the main delivery of the licensor. When licensing foreign technology the correct wording of these claims is of higher importance for the licensee.

The technical documentation (drawings, plans, formulas, descriptions) is generally specified and constitutes an appendix of the agreement. If the technical documentation is not complete, the realization of the licence will not be possible. Therefore, an exact specification of the technical documentation is especially important

when licensing a know-how, as this is not described by the specification of the patent.

It may seem contradictory but in the practice it happens, however, that the claims of the contract give only a basic definition of the know-how, mentioning that a specification of the documentation will be established only later. This is the case if the licensor grants know-how for a whole bundle of technologies in a certain industry. It would be meaningless to transfer centners of documentation, a great deal of which would never be used by the licensee. Under such circumstances it is wiser if the parties specify later the delivery of the kind of documentation that may take place even during several years - as the Hungarian practice shows it.[7)]

The other very important obligation of the licensor is to grant a technical assistance, teaching the employees of the licensor to be able to manage the new machines, to apply the new technology. This teaching may proceed either in the factory of the licensee (which is more usual), or also in the factory of the licensor (where generally only a limited number of persons is sent). This last solution is applied especially when the foreign technology is very complicated.

It is obvious that there are hundred of personal skills not being worth while to be described in the documentation, but can be taught personally in a short time.

Claims on technical assistance provide

(i) the number of the licensee's employees, their qualification and the time that they may spend with the licensor for learning;

(ii) the same data regarding the licensor's employees concerning the teaching at the licensee's factory;

(iii) the provision for the amount of mission, and for which of the parties should pay it;

(iv) provision for accident and illness insurance, etc.

Without delivery of documentation or technical assistance it is difficult to imagine licence agreements at all.

(c) To assure that this delivery should be correct, there are claims on guaranting the technical effect.

Buying Western European licenses Hungarian enterprises generally specify that the obtaining of the guaranted technical effect should be proved in the licensee's factory. Therefore strictly defined claims are absolutely necessary. In the practice, when the subject of the license agreement is the implantation of a new product, Hungarian enterprises define in the agreement

- technical characteristics of the product,
- its quality,
- output of the plant or the technology,
- parameters of consume of materials and energy,
- the method, instruments and term of the supervision of those characteristics and parameters.

But inspite of strictly defined claims which are only one factor of obtaining the technical effect, legal sanctions are also necessary for its observation. One could say that the normal sanctions on breach

of a contract would be sufficient, but by Hungarian specialists the necessity of special sanctions completing these clauses are underlined. [3]

The most general sanction of this kind is to bind the payment of a part of the royalties to the obtaining of the stipulated technical effect. There is a whole bundle of alternatives applied in Hungary in this respect: the most drastic one of these is the sanction of the agreements guaranting the production of a new product, which provides for not paying at all royalties until the stipulated technical effect is obtained.

Naturally if the deviation from the guaranteed technical parameters is only small such drastic sanctions are not applied, but milder ones. On the contrary, when buying the technology from a Western European enterprise relating to the manufacturing of a percolator for espresso-bars, that was not feasible for unability of documentation, the Hungarian buyer cancelled the agreement.

(d) The main obligation of the licensee is to pay <u>royalties</u>.

We speak about these claims only to underline that there is no difference compared with the practice of no socialist countries. In the claims of agreements signed by Hungarian enterprises we find in this respect the same variety as in other countries: paying on the nail, paying of a lump sum, paying yearly or halfyearly as per account etc.

Regarding the last, licensing from abroad the Hungarian licensee subjects himself in the agreement, if the licensor desires to an accountancy if this is performed by the Hungarian Bank of Foreign

Trade, or the Hungarian Chamber of Commerce.

Finally, speaking on payment of taxes, claims provide often that the Hungarian licensee wil pay them, or -- what is equal - that he pays to the licensor "netto" royalties. Such claims simplify administration, but their logical result is, that the licensor receives less royalties as fixed by the agreement.

5. Licensing of Technology into Developing Countries

I do not know about any agreement licensing Hungarian technology into a developing country where the subject of the contract would be only a technology without the delivery of machines, equipments i.e. the "pure" licence.

On the contrary claims on licensing technology are not scarce in turn-key job arrangements concluded with developing countries. In those arrangements the claims on licensing technology are rather simple and evident, surely a turn-key job arrangement would be meaningless without the technical knowledge.

This technical knowledge, at least in the arrangements that I studied is generally not of a very high level, patents, or secret know-how are not included. In my opinion it may be the commercial and economic cause that there is generally no possibility in the developing countries to introduce the latest technical achievements, but implant only such industries which the not very learned population would be able to manage.

Speaking about these problems we can add that generally the developing countries themselves study very seriously what kind of

industry to implant, what sort of factories would be worth building. These studies are not rarely undertaken by foreign specialists, e.g. by engineering offices, they are called feasibility studies. It happens that the feasibility study is ordered with the same enterprise which will deliver the turn-key factory, but it is not rare that it is ordered at the engineering office of another country.

The feasibility study is an opinion on the possibilities, advantages, problems, needs in correlation on the implantation of the factory that is planned by the developing country.

In most of the feasibility studies there are also claims on the intellectual property of the same study. In a Hungarian feasibility study made for an African country on the implantation of a glass factory we find e.g. the following wording:

"The feasibility study to be prepared will stay the intellectual property of the supplier. The buyer may make use of the feasibility study only in his own country and only for the purposes as settled in the agreement. The buyer is forbidden to surrender the feasibility study to a third party and he is obliged to assure that it will be inaccessible for third persons".

This is an example from the practice. If the developing country will be proprietor of the intellectual property too, there is no difficulty, but very probably the price of it will be higher.

If the feasibility study is advantageous, the turn-key agreement will be concluded. The value of technology, technical knowledge is in such agreements often estimated to be 10-20 % of the whole

purchase price. But as we said it previously not too many claims deal with it. We can however consider as claims of this type those on

- studies,
- control,
- co-ordination,
- tests,
- teaching of employees.

These claims assure for the boyer to obtain the know-how necessary for a production.

From all these claims those on teaching of employees are generally the most elaborated. Let us take an example on licensing technology (in the frames of the delivery of a turn-key pickled vegetables factory) into another African country, with very strict obligations of the Hungarian supplier.

It is said here, that "the teaching of employees ought to be of such a quality that it should guarantee the good functioning of the plant" and that "the teaching of the employees for the African country should be performed partly in this country, partly in Hungary, during the mounting and the tests of the plant and during the whole period of the supplier's delivery".

A further claim obliges the supplier "to deliver in a due term

(i) the methodology of professional tuition,
(ii) the programme of tuition,
(iii) the criteria of selection of employees to be tought,
- medical,
- physical,
- psychotechnical criteria."

I think that this human feature of technical assistance is one of the most important ones, as everything may be delivered into the developing countries, except human beings. And perhaps this is just the point where international organizations like UNIDO, UNESCO, etc. may render valuable services.

NOTES

1) (1972) Ujitók Lapja 6. p. 3.

2) (1960) Ujitók Lapja 12. p. 9.

3) (1970) Hungaropress 19-20.

4) (1970) Népszabadság 26 November p. 7.

5) (1970) Industrial Property 4.

6) (1970) Industrial Property 6.

7) Gnedo - Kövesdi - Vida: Találmányok, Szabadalmak, Budapest (1971) 4th edition p. 259.

8) Gnedo - Kövesdi - Vida op. cit. p. 269-271.


15. 7. 74