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National Consultations on Licensing, Patents and Transfer of Technology

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RESTRICTIVE BUSINESS PRACTICES IN TRANSFER OF TECHNOLOGY 1/

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The term "restrictive business practices" or "restrictive provisions" goes back to the antitrust legislation of major industrial countries like the USA, Japan and the European Economic Community.

For the sake of clarity excerpts from some antitrust legislations are given below :

A. US Antitrust Statutes

- Section 1 of the "Sherman Act" (15 U.S.C. para 1) :

"Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is declared to be illegal."

- Section 2 of the "Sherman Act" (15 U.S.C. para 2) :

"Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolise any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of a misdemeanor ....."

- Section 3 of the "Clayton Act" (15 U.S.C. para 14) :

"It shall be unlawful for any person engaged in commerce, in the course of such commerce, to lease or make a sale or contract for sale of goods, wares, merchandise, machinery, supplies, or other commodities, whether patented or unpatented, for use, consumption or resale within the United States....or fix a price charged therefor, or discount from, or rebate upon, such price, on the condition, agreement, or understanding that the lessee or purchaser thereof shall not use or deal in the goods, wares, merchandise, machinery, supplies, or other commodities of a competitor or competitors of the lessor or seller, where the effect of such lease, sale, or contract for sale or such condition, agreement, or understanding may be to substantially lessen competition or tend to create a monopoly in any line of commerce."

- Section 7 of the "Clayton Act" (15 U.S.C. para 18) :

"No corporation engaged in commerce shall acquire, directly or indirectly, the whole or any part of the stock or other share capital and no corporation subject to the jurisdiction of the Federal Trade Commission shall acquire the whole or any part of the assets of another corporation engaged also in commerce, where in any line of commerce in any section of the country, the effect of such acquisition may be substantially to lessen competition, or to tend to create a monopoly".

- Section 5 (a) (1) of the "Federal Trade Commission Act" (15 U.S.C. para 45(a) (1):

"Unfair methods of competition in commerce, and unfair or deceptive acts or practices in commerce, are declared unlawful."

B. The EEC Rules of Competition

- Article 85: Prohibited Practices :

"(1) The following shall be prohibited as incompatible with the common market: all agreements between undertakings, decisions by associations of undertakings and concerted practices which may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition within the common market, and in particular those which :

(a) directly or indirectly fix purchase or selling prices or any other trading conditions;

(b) limit or control production, markets, technical development, or investment;

(c) share markets or sources of supply;

(d) apply dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage;

(e) make the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts.

(2) Any agreements or decisions prohibited pursuant to this Article shall be automatically void.

(3) The provisions of paragraph (1) may, however, be declared inapplicable in the case of :

- any agreement or category of agreements between undertakings;
- any decision or category of decisions by associations of undertakings;
- any concerted practice or category of concerted practices;

which contributes to improving the production or distribution of goods or to promoting technical or economic progress, while allowing consumers a fair share of the resulting benefit, and which does not :

(a) impose on the undertakings concerned restrictions which are not indispensable to the attainment of these objectives;

(b) afford such undertakings the possibility of eliminating competition in respect of a substantial part of the products in question."

- **Article 86: Abuse of Dominant Market Position :**

"Any abuse by one or more undertakings of a dominant position within the common market or in a substantial part of it shall be prohibited as incompatible with the common market in so far as it may affect trade between Member States. Such abuse may, in particular, consist in:

(a) directly or indirectly imposing unfair purchase or selling prices or other unfair trading conditions;

(b) limiting production, markets or technical development to the prejudice of consumers;

(c) applying dissimilar conditions to equivalent transactions, with other trading parties, thereby placing them at a competitive disadvantage;

(d) making the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts."

C. **The Fair Trade Commission Guidelines in Japan**

I. Among the restrictions which are liable to come under unfair business practices in international licensing agreements on patent rights or utility model rights (hereinafter referred to as patent rights, etc.) the following are the outstanding :

(1) To restrict the area to which the licensee may export the goods covered by patent rights, etc. (hereinafter referred to as patented goods).

However, cases coming under a, b, or c listed below are excluded.

a. In case the licensor has patent rights, etc. which have been registered in the area to which the licensee's export is restricted (hereinafter referred to as the restricted area);

b. In case the licensor is selling patented goods in the restricted area in his normal business;

c. In case the licensor has granted to a third party an exclusive license to sell in the restricted area.

(2) To restrict the licensee's export prices or quantities of patented goods, or to make it obligatory for the licensee to export patented goods through the licensor or a person designated by the licensor.

However, such cases are excluded where the licensor grants an exclusive license and imposes no restriction on goods already being manufactured, used or sold, or technology already being utilised by the licensee.

(3) To restrict the licensee from manufacturing, using or selling goods, or employing technology which is in competition with the licensed subject.

However, such cases are excluded where the licensor grants an exclusive license and imposes no restriction on goods already being manufactured, used or sold, or technology already being utilized by the licensee.

(4) To make it obligatory for the licensee to purchase raw materials, parts, etc. from the licensor or a person designated by the licensor.

(5) To make it obligatory for the licensee to sell patented goods through the licensor or a person designated by the licensor.

(6) To restrict the resale prices of patented goods in Japan.

(7) To make it obligatory for the licensee to inform the licensor of knowledge or experience newly obtained regarding the licensed technology, or to assign the right with respect to an improved or applied invention by the licensee to the licensor or to grant the licensor a license thereon.

However, such cases are excluded where the licensor bears similar obligations and the obligations of both parties are equally balanced in substance.

(8) To charge royalties on goods which do not utilize licensed technology.

(9) To restrict the quality of raw materials, parts, etc., or of patented goods.

However, such cases are excluded where such restrictions are necessary to maintain the creditability of the registered trademark or to insure the effectiveness of the licensed technology.

II. The aforementioned guidelines shall apply to international know-how licensing agreements.

III. In international licensing agreements on patent rights, etc., the following acts shall be regarded as the exercise of rights under the Patent Act or the Utility Model Act :

(1) To grant license to manufacture, use, sell, etc. separately;

(2) To grant license for a limited period within the life of patent rights, etc., or for a limited area within the whole area covered by patent rights, etc.;

(3) To restrict the manufacture of patented goods to a limited field of technology or to restrict the sale thereof to a limited field of sales;

(4) To restrict the use of patented processes to a limited field of technology;

(5) To restrict the amount of output or the amount of sales of patented goods or to restrict the frequency of the use of patented processes.

As it may be seen quite clearly from above-quoted legislative acts, certain "rules of game" have been introduced by legislators into the area of trade a long time ago with the purpose to prevent, inter alia, any party from acquiring predominant or monopolistic market positions on the one hand, and on the other to prevent patents and know-how holders from abusing or misusing their "natural" monopolistic position in the market resulting from ownership of industrial property rights.

On the basis of the above, a review of the most frequent restrictive provisions follows. The below enumerated provisions will also show a possible impact on the relation between contractual parties in licensing and other transfer of technology agreements.

1. Tying provisions or tie-ins :

A "tie-in" is a provision under which a licensor forces his licensee to purchase or lease non-patented goods or services as a necessary condition to secure a licence under patent. Such practice is considered illegal because the patentee or licensor can effectively extend the monopoly of his patent rights beyond its scope by a condition imposed upon his licensee to commit himself to purchase or lease other goods, not covered by the patent, from the licensor (see for example the rulings of the US Supreme Court in Motion Picture Patents Co versus Universal Film Manufacturing Co or International Business Machines Corp. versus United States).

2. Provisions restricting the licencee's right to deal in competitors' products (tie-outs):

A "tie-out" is actually a corollary of a "tie-in". By a "tie-out" provision a licensor attempts to restrict his licensee's freedom to deal in a competitive product. For example, a typical tie-out provision would prevent a licensee from purchasing or using products similar to or in the same category as the products covered by the licensed patent (for more detailed description see the US Supreme Court rulings in the case "National Lockwasher Co versus Garrett Co and McCullogh versus Kammerer Co).

3. Package licensing provisions :

In principle a package licence is a licence by a patent owner, usually a corporation holding many patents, in which the licensee is granted licence under more than one patent. According to US antitrust legislation package licence, per se, is not considered as illegal unless the package licence is mandatory to the licensee. In this connexion it should be mentioned that by use of a so-called "whereas" clause at the beginning of the licence agreement, the licensor may easily counter the possible charge of coercion.

4. Extension of the scope of transfer of technology and "total sales royalties" :

It is considered a "per se" illegal for a licensor to impose a mandatory total sales royalty restriction upon his licensee. Such a restriction occurs when the licensor conditions granting of the licence upon the licensee's willingness to pay royalties on its total sales of products, regardless whether such products infringe the claims of any licensor patents. Similarly, the same problem may occur where a patent covers only part of the process and not the entire process but the royalty is determined and imposed by the use of the entire process.

5. Resale restriction or limitations :

According to the common law there must be freedom of alienation with respect to goods. (This doctrine has been applied recently to patented goods as well in the case of Adams versus Bucks by the Supreme Court in 1973 - "resale restrictions cannot be imposed upon a purchasing licensee").

6. Post-expiration royalties or unjustified long payments of royalties :

These restrictions impose upon a licensee the obligation to pay royalties after the patent in question has expired. In the ruling in case of Brulotte versus Thys Co., the Supreme Court found that "the exaction of royalties for use of a machine after the patent has expired is an assertion of monopoly power in the post expiration period when.... the patent has entered public domaine".

The important point emerging from above-referred case is that royalties may not be collected in the post expiration period, if they are based on use.

7. Price fixing provisions :

In principle - this issue is still under discussion in the United States - the licensor should not require a manufacturing licensee to adhere to the licensor's price schedules as such practice will be found illegal.

8. Restriction on the licensor's right to grant further licences :

This is a very interesting provision, of limited interest however to industrialized countries , which at least in the United States is considered as illegal. Namely, where a licensor and licensee are competitors and they control a substantial part of the relevant market, it is per se illegal for the licensor to give the licensee a veto power over granting of further licences. There are also recent suggestions that it is improper for a licensor to grant an exclusive licence to a licensee without also giving that licensee the power to grant sub-licences.

9. Grant-back provisions :

This type of provision usually requests the licensee to grant back either an assignment or an exclusive licence as to any improvement invention that he makes within the scope of the licensed technology.

10. Quantity or volume restrictions :

This type of restrictive clauses requesting the licensee to limit the quantity or volume of production of the licensed product became recently even in the United States an illegal provision.

The following four types of restrictive clauses are those with respect to which legality (or restrictive nature) is determined by the so-called rule of reason :

11. Field of use restriction :

"Field of use licensing" is a term of art covering agreements under which a licensor grants a licensee the restricted use of a patented subject matter but declines to grant all possible uses to one licensee, reserving some uses for self-exploitation or for exploitation by other licensees.

Worth is mentioning that field of use restriction permits a licensor to increase substantially royalty income, to regulate the use of his patent etc., etc.. Furthermore, "use restriction in licence can allow a patent owner to organize his market into a collection of discrete, non-competitive submarkets. The licensees in each of the submarkets are thereby insulated from competition with licensees in other submarkets".1/

12. Territorial restrictions :

Territorial restriction provisions belong to those which help create the monopolistic and predominant position of the parties within specified areas and over a specified period of time. Here in particular, when considering these provisions the rule of reason should be applied in each case.

13. Non-exclusive grant-backs :

In principle non-exclusive grant-back provisions of improvement of technology by the licensee would not constitute a restrictive business practice. The only problem may arise where a licensee makes a break-through invention as an improvement under the licensed technology. In such a case the licensor should agree to pay royalties to the licensee also for the non-exclusive licence under the newly developed technology.

1/ "Restrictions on International Technology Transfer" - "The Practical Effect of Restraints on the Licensing Process" by N.B. Finnegan, at the Belgrade Seminar on Licensing, October 1975

14. Cross-licensing provisions; patent pool arrangements :

In these particular cases and especially when combined patents are licensed to others, cross licensing arrangements can easily lead into illegal (from the antitrust point of view) patent pooling. Patent pooling occurs in principle when more than two companies agree to mutually share their patent properties with each other. In particular, where a patent pool is created within one branch of industry, the risks of antitrust violation are multiplied.

The developing countries in the process of protection of their legitimate national interests, have introduced recently a growing governmental intervention in transfer of technology.

These policies in principle consist of introducing a protective regulatory legislation which requires, inter alia, a compulsory registration of all transfer of technology agreements and specifies in a more or less general way which conditions of those agreements are considered as in principle not acceptable. These "non-acceptable" conditions were primarily based on the concept of "restrictive business practices" as described above with the aim of eliminating through legislative action of the state the more frequent and unfair practices of foreign suppliers of technology.

Analyses made by a number of countries, before such regulatory measures were introduced, have shown that the majority of agreements concluded by developing countries contain some if not all of the above in detail described provisions.

It seems legitimate and reasonable that practices which are not legal in industrialised countries, like the United States and Great Britain, are also considered illegal in Mexico, Nigeria or Libya. The actions taken by a government at the national level as well as at international forums are primarily oriented towards securing a greater flow of technology from industrialized to developing countries under fair and equitable conditions and as such should be accepted and understood.

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