

Anti-competitive Clauses in Know-how Agreements FTC Decision of October 13, 1995

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I. INTRODUCTION

Decisions by the Japanese Fair Trade Commission on the exercise of intellectual property rights or know-how are a rare breed. In fact, there has been only one formal and one informal decision before the one recorded here. The formal decision concerned a production cartel of concrete makers¹. The other decision concerned a trade association that had bought some patents and utility models and licensed them only to those members who agreed to certain production limits². Certainly not much for a country with vivid activities in technology transfer such as Japan.

In order to clarify the Dos and Don'ts in licensing agreements on know-how and patents, the Fair Trade Commission in 1989 enacted a fairly elaborate guideline. It distinguishes between white clauses that do not contravene antitrust provisions, gray clauses that may do so under certain circumstances and black clauses that are almost always anti-competitive³.

II. THE ASAHI DENKA DECISION

The case concerned a know-how agreement whose two licensors were Japanese companies, *Asahi Denka* and *Oxylon*. Licensee was a Taiwanese company called *Chôshun* or *Nagaharu*. The know-how involved concerned a process of industrial mollification by using epoxy. The contract with *Asahi Denka* was concluded in April 1981 and had expired 10 years later, while the contract with *Oxylon* was concluded in April 1993 also with a 10-year period and thus was still in force. The FTC took offense against a post-contractual clause restricting the export of machines using this method to Japan. Even after the expiration of the contract, the Taiwanese company should not be able to sell products involving the secret technology to Japan, where *Oxylon* was assigned exclusive rights. Yet, the contract did not restrict the Taiwanese company to freely use the know-how after the contractual period: In fact, the know-how was rather sold than only licensed. This, as it turns out, makes out the difference in regard of the anti-competitive behaviour.

III. LEGAL AND PRACTICAL IMPLICATIONS

The case has a number of interesting aspects worth mentioning.

1. The Fair Trade Commission in Japan (hereafter FTC) is responsible for upholding the rules of fair competition. It derives the power and jurisdiction from the Anti-Monopoly Act, enacted in 1947 under the American occupation. The Anti-Monopoly Act gives the FTC boldy defined powers that require additional regulations by the FTC in order to directly apply to entrepreneurs. In order to comply with its mandate, the FTC has enacted a set of general regulations against anti-competitive acts from 1982, and on the basis of this, additional regulations concerning different fields of competition. In its regulation on patent know-how licensing of 1989, the FTC has basically been concerned about competition being hampered by excessive obligations against licensees. In order for the regime of intellectual property rights (and know-how that is) to increase competition, any obligations that go beyond the scope of intellectual property rights and know-how protection are regarded with suspicion. This is especially true for dealing arrangements on exclusive and restrictive terms (conditions that restrict the licensee in its dealings with third parties or in third markets), as well as restricting further research and developments in the area of the licensed technology. Although this looks as a protection of the licensee, in fact it is not. The licensee is protected only inso-

far as such restrictive terms reduce competition as such. The aim is not to protect licensees, but to protect competition.

2. Turning to the guidelines on patent and know-how licensing, restrictions after the expiration of a licensing contract are generally considered anti-competitive. Non-competition clauses and restrictions on the use of the licensed technology after the expiration of the licensing agreement or the term of the intellectual property right in question are black and therefore unacceptable clauses. The exception are post-contractual constrictions on the use of know-how. Here, it is deemed a justified interest of the licensor that know-how is kept secret and not used after the expiration of the contractual term. However, this exception does not apply to the present case, as the know-how in fact has not been licensed but has been sold. For this reason, the licensee was free to use the licensed know-how after the expiration of the contract and therefore could even have made it public. Thus, any post-contractual restrictions would interfere with the rights assigned to the licensee (or rather, the purchaser) of the know-how. While under a know-how licensing agreement, restrictions on the licensee to export licensed goods are acceptable insofar as the licensor assigns the area as an exclusive sales territory to third parties (as has been done in the present case), this restriction cannot apply in cases where the other party is free to use the know-how as its own property. The restriction in the present case would have been acceptable in a know-how licensing agreement, but it was not in a purchase agreement.

3. Nevertheless, it can be a good idea to sell rather than license know-how. The reason for this is the rather unsatisfactory protection of know-how in Japan. Certainly, know-how that is properly managed can be protected on a contractual basis as well as under tort law. A recent decision of the Osaka High Court has clarified under what circumstances know-how can be protected: First, the knowledge must be something new when measured against the state of the art; second, the secret know-how must be properly managed insofar that its secrecy must be plain to those who handle it, and third, people who deal with the know-how must be under a secrecy obligation⁴. Although ruled under general tort law, it is quite likely that these conditions will also apply to actions under the trade secret provisions of the unfair competition law that were enacted in 1991. Proper enforcement, however, will stumble over the lack of *in camera* proceedings under the Civil Procedural Code of Japan: Since the Japanese Constitution (Art. 83) requires proceedings to be conducted in an open court, no rules have been enacted that would enable *in camera* proceedings. This is certainly disgraceful and even constitutionally dubious in cases where protection itself will be rendered impossible by the very proceedings to enforce the right. It literally means squaring the circle to enact proper laws protecting know-how, while forcing its owner to reveal such secret knowledge in the process of enforcing it⁵. Selling such know-how certainly circumvents such problems. The other possibility of resorting to arbitration very much depends on the quality of such a process, and recently arbitration proceedings have come under heavy criticism for being slow and inefficient.

4. The first Japanese guidelines on patent and know-how licensing were enacted in 1968 and carried two basic assumptions: First, that the licensee was always in a weaker position, and second, that the licensee would always be Japanese. The 1968 guidelines did only apply to international, not domestic licensing agreements. By enacting the new guidelines, the FTC responsible for monitoring anti-competitive behaviour in Japan, professed to apply the guidelines indiscriminately in two ways. First, they should also apply to domestic contracts, and second, they should apply regardless of the nationality of licensor or licensee. The present decision in this respect is quite reassuring as it is aimed at the anti-competitive behaviour of two Japanese companies against a foreign one.

5. The decision is also reassuring in yet another respect. In the old days, the FTC only used to contact the Japanese parties to an international contract if it found fault with the latter. This left foreign companies out in the cold when they themselves tried to appeal against the FTC's decision⁶. In this case, the FTC apparently had also contacted the Taiwanese party to the contract, as the Taiwanese party two months before the formal decision had been asked if the anti-competitive clause could be removed. Not unsurprisingly, the Taiwanese company had agreed to such removal.

6. The FTC can only act insofar as it obtains knowledge about a certain anti-competitive behaviour. Until 1992, all international licensing agreements had to be notified with the FTC, although it is suspected that compliance with this obligation was not overwhelming. Since 1992, this has been considerably relaxed. Now, know-how agreements have only to be reported if they contain any clauses on price restrictions or if one party to the contract has a market share of more than 10 percent in Japan in the market of the licensed technology. Certainly, a party disadvantaged by some anti-competitive clauses may at any time report the contract to the FTC or request a clearance before the contract is even concluded.

Notes

- 1 In re Nihon Concrete et. al, decision of August 5, 1970. The technology involved was a so-called "press-to-rest concrete".
- 2 *Nihon Kaiware*, informal warning of February 17, 1995.
- 3 The guideline of February 15, 1989 is reprinted in H. IYORI/A. UESUGI, *The Antimonopoly Laws and Policies of Japan*, New York 1994, 467.
- 4 Osaka High Court Decision of 26 December 1994, Hanrei Jihô No. 1553 [1996], 133.
- 5 The Achilles heel of such protection has become clear by the Tokyo District Court decision, 24 December 1991, Hanrei Times No. 769 [1992], 280 = Mitteilungen der DJJV Nr. 8 (1992), 42. Here, the plaintiff preferred not to disclose the know-how in an open court and consequently lost the action.
- 6 The Supreme Court decision In re Amano v. Novo Industri, 28 November 1975, Hanrei Jihô No. 800 (1976), 35 is a classic in this respect.