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# THE JAPANESE ANTIMONOPOLY ACT AND NON-ASSERTION OF PATENTS PROVISIONS: MICROSOFT'S CONFLICT WITH THE JAPAN FAIR TRADE COMMISSION

**Courtney E. Mertes**†

*Abstract*: In recent decades, Japan has strengthened its antimonopoly regulations. Now, a country that historically favored internal collusion continues to develop a stringent antimonopoly regime that encourages competition. The Japan Fair Trade Commission ("JFTC") enforces the Japanese Act Concerning the Prohibition of Private Monopoly and the Maintenance of Fair Trade ("Antimonopoly Act") and its provisions dealing with unfair trade practices. The JFTC takes a strong stance in enforcement of the Act and violators follow its recommendations.

The JFTC has charged Microsoft Corporation ("Microsoft") with abuse of a dominant bargaining position and unfair trade practices in its use of restrictive provisions, such as non-assertion of patents provisions, in contracts and licensing agreements. Microsoft has removed the non-assertion provision from future contracts of its own accord, but indicated that it will continue to fight the JFTC's recommendation that the provisions be removed from existing contracts. Cooperating with the JFTC and removing the provision will lead to an improved image in Japan and will ensure that personal computer manufacturers will continue to develop new and innovative technologies, but removing it may also lead to backlash and an influx of litigation against Microsoft. In light of the plethora of potential problems that could result from a finding of illegality, Microsoft should continue to defend the non-assertion of patents provision and contest any unfavorable rulings from the JFTC.

## I. INTRODUCTION

In February 2004, the Japan Fair Trade Commission ("JFTC") raided Microsoft's Japan offices[1] to investigate complaints filed by Japanese original equipment manufacturers ("OEMs").[2] Over the ensuing months,

† The author would like to thank Professor Robert Gomulkiewicz of the University of Washington School of Law for his guidance and suggestions. The author also thanks the editorial staff of the *Pacific Rim Law & Policy Journal* for its hard work and editorial contributions. The author would like to dedicate this Comment to her continuously supportive family and her wonderful husband, Juan Garcia.

1 *See* P-I News Services, *Microsoft Offices in Tokyo Raided by Japan Trade Officials*, SEATTLE POST-INTELLIGENCER, Feb. 26, 2004, at E2; Bloomberg News, *Regulators Conduct Search of Microsoft's Office in Tokyo*, N.Y. TIMES, Feb. 27, 2004, at W1.

2 Press Release, Japan Fair Trade Commission, The JFTC Renders a Recommendation to Microsoft Corporation 4-5 (July 13, 2004), *available at* http://www2.jftc.go.jp/e-page/pressreleases/2004/july/040713.pdf (last visited May 31, 2005) (on file with Journal) [hereinafter JFTC Press Release]. The PC manufacturers lodged complaints with the JFTC against Microsoft out of fear that Microsoft was using their patented audio-visual technology without having to pay royalties, and they could not sue Microsoft for infringing their patents. *See generally* Japan Fair Trade Commission, *Shinpan kaishi ketteisho* [Decision to Initiate Examination], Sept. 1, 2004 (on file with Journal) [hereinafter JFTC Decision] (discussing

investigators from the JFTC conducted interviews and reviewed records to investigate the allegations that a non-assertion of patents provision ("NAP"), common to many of Microsoft's licensing agreements, violated Japan's Act Concerning the Prohibition of Private Monopoly and the Maintenance of Fair Trade of 1947 ("Antimonopoly Act")[3] and constituted an unfair trade practice.[4] After completing the investigation, the JFTC challenged the standard non-assertion of patents provision in Microsoft's licensing agreements.[5] The challenged provision potentially allows Microsoft to use proprietary, patented material without paying royalties to the patent owner.[6] Licensors use the NAP provision to facilitate the settlement of patent litigation,[7] keep transaction costs down, and ensure the careful negotiation of licensing agreements.[8]

In July 2004, the JFTC issued a recommendation[9] that Microsoft remove the provision from all past, present and future contracts.[10] Microsoft deleted the provision from its standard form licensing contract, but refused to eliminate it from existing agreements, thus beginning a legal battle with the JFTC.[11]

The Antimonopoly Act promotes competition and fair trade in a country that historically encouraged collusion.[12] Japan has strengthened the

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Microsoft's potential Antimonopoly Act violations); Japan Fair Trade Commission, *Maikurosofuto kōporēshon ni taisuru shinpan kaishi kettei nitsuite* [On the Decision to Initiate the Examination for Microsoft Corporation], Sept. 3, 2004 (on file with Journal) (notice introducing the JFTC decision against Microsoft).

[3] *Shiteki Dokusen no Kinshi Oyobi Kosei Torihiki no Kakuho ni Kansuru Horitsu* [Act Concerning Prohibition of Private Monopolization and Maintenance of Fair Trade], Law No. 54 of 1947 as amended. [hereinafter Antimonopoly Act].

[4] JFTC Press Release, *supra* note 2, at 1.

[5] *Id.*

[6] *Id.* at 4-5 (indicating that the NAP would likely preclude OEMs from recouping expenditures and would allow Microsoft to infringe on their patents).

[7] BRIAN G. BRUNSVOLD & DENNIS P. O'REILLEY, DRAFTING PATENT LICENSE AGREEMENTS 17 (4th ed. 1998) (1971).

[8] Press Release, Microsoft Corp., Statement by Microsoft Corporation on Japanese Fair Trade Commission Recommendation (July 13, 2004), *available at* http://www.microsoft.com/presspass/press/2004/Jul04/07-13JFTCStatementPR.asp (last visited May 31, 2005) (on file with Journal) [hereinafter Statement by Microsoft].

[9] While this type of recommendation decision is not binding unless accepted by the other party involved, it is nonetheless a result of a lengthy investigation by JFTC into Microsoft's licensing practices. *See* JFTC Decision, *supra* note 2.

[10] JFTC Press Release, *supra* note 2, at 5-6.

[11] *See Microsoft Filing Complaint Against Japan FTC*, JIJI PRESS ENGLISH NEWS SERV., July 26, 2004; Statement by Microsoft, *supra* note 8 (indicating that Microsoft will keep the provision in existing licensing agreements).

[12] Alex Y. Seita & Jiro Tamura, *The Historical Background of Japan's Antimonopoly Law*, 1994 U. ILL. L. REV. 115, 128-30. *See also* HIROSHI ODA, JAPANESE LAW 300 (Oxford University Press 1999) (1992) (noting that government actions fostered monopolies); MITSUO MATSUSHITA & JOHN D. DAVIS, INTRODUCTION TO JAPANESE ANTIMONOPOLY LAW 1 (1990) (stating that free enterprise and competition

Antimonopoly Act to foster competition and ensure growth and development,[13] and has also been increasingly vigilant in the Antimonopoly Act's enforcement.[14] The JFTC's recommendation marks the first instance of a regulatory body challenging a non-assertion provision under antitrust law.[15] The section of the Antimonopoly Act forbidding unfair trade practices (under which the non-assertion of patents provision falls) has traditionally been vague, requiring guidelines to aid in its interpretation.[16] Historically, the JFTC has concentrated its enforcement efforts on more egregious violations like monopolies, price fixing, and unreasonable restraint of trade.[17] In contrast, the JFTC viewed prohibition of unfair trade practices as a preventative measure against monopolies rather than a violation in its own right.[18] Also, unfair trade practices are harder to identify and more flexible than more obvious violations.[19] Due to Microsoft's large market share and high visibility, the Japan Fair Trade Commission decided to enforce the unfair trade practices provision against it.[20] Microsoft will continue to fight

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are relatively new concepts to Japanese businesses); Hiroshi Iyori, *Antitrust and Industrial Policy in Japan: Competition and Cooperation*, *in* LAW AND TRADE ISSUES OF THE JAPANESE ECONOMY: AMERICAN AND JAPANESE PERSPECTIVES 56, 61 (Gary R. Saxonhouse & Kozo Yamamura, eds., 1986) (discussing Japan's economic history and proclivity for collusion)..

[13] PETER MORICI, ANTITRUST IN THE GLOBAL TRADING SYSTEM: RECONCILING U.S., JAPANESE AND EU APPROACHES 51 (2000). *See also*, Yoichiro Hamabe, *Changing Antimonopoly Policy in the Japanese Legal System: An International Perspective*, 28 INT'L LAW. 903, 907-909 (1994) (discussing the JFTC's reasons for its belief in the importance of the Antimonopoly Act).

[14] Makoto Kurita, *Effectiveness and Transparency of Competition Law Enforcement: Causes and Consequences of a Perception Gap Between Home and Abroad on the Antimonopoly Act Enforcement in Japan*, 3 WASH. U. GLOBAL STUD. L. REV. 387, 391-92 (2004). With an increased budget and heightened scrutiny toward anti-competitive activities, the JFTC has begun enforcing the Antimonopoly Act more forcefully. *See* H. Stephen Harris, Jr., *Competition Law and Patent Protection in Japan: A Half-Century of Progress, A New Millennium of Challenges*, 16 COLUM. J. ASIAN L. 71, 104 (2002).

[15] *But cf.*, Lear, Inc. v. Adkins, 395 U.S. 653, 670-74 (1969); Foster v. Hallco Mfg Co., 947 F.2d 469, 475 (Fed. Cir. 1991); Case 65/86, Bayer AG v. Sullhofer, 1988 E.C.R. 5249, [1990] 4 C.M.L.R. 182, 186-87 (1988). The European Communities Court of Justice and the United States validated a similar clause in certain circumstances, but not under antitrust law. Also, these jurisdictions indicated that such clauses would be examined on a case-by-case basis.

[16] Antimonopoly Act, *supra* note 3, § 19. For definitions of terms and guidelines on interpreting the Antimonopoly Act, see Guidelines For Patent and Know-How Licensing, produced by the Japan Fair Trade Commission. JAPAN FAIR TRADE COMMISSION, GUIDELINES FOR PATENT AND KNOW-HOW LICENSING AGREEMENTS UNDER THE ANTIMONOPOLY ACT 19 (1999), *available at* http://www2.jftc.go.jp/e-page/legislation/ama/patentandknow-how.pdf (last visited May 31, 2005) [hereinafter GUIDELINES FOR PATENT AND KNOW-HOW LICENSING].

[17] John O. Haley, *Japanese Antitrust Enforcement: Implications for United States Trade*, 18 N. KY. L. REV. 335, 342 (1991).

[18] MATSUSHITA & DAVIS, *supra* note 12, at 8-9. Matsushita also notes that the control of unfair trade practices is related to consumer protection laws. Segments of the unfair trade practices section of the Antimonopoly Act are specifically consumer protection measures. *Id.*

[19] HIROSHI IYORI & AKINORI UESUGI, THE ANTIMONOPOLY LAWS AND POLICIES OF JAPAN 107-08 (1994). Hiroshi Iyori is a former Commissioner of the JFTC.

[20] *See* JFTC Press Release, *supra* note 2, at 2.

the JFTC and defend the NAP provision, arguing that the European Union and the United States validated it and that it does not violate antitrust laws.[21]

Parties usually settle with the JFTC and accept its preliminary decisions.[22] If Microsoft continues to fight the ruling, the JFTC will likely choose to enforce its original request that Microsoft remove the provision from existing contracts, because the JFTC tries to fully establish the existence of a violation before issuing a recommendation.[23] While the NAP provision is not necessarily *per se* illegal, when used in conjunction with Microsoft's bargaining power, it may violate the Antimonopoly Act.[24] Microsoft has many good reasons to defend the provision, despite potential damage to its image in Japan.

This Comment asserts that Microsoft should defend the NAP provision. Part II looks at non-assertion of patents provisions, their utility, and the potential anti-competitive implications they embody. Part III examines the Antimonopoly Act, its history, and pertinent provisions and purposes of the Act that apply to Microsoft's current dilemma. Part IV outlines the recent action of the JFTC against Microsoft and suggests possible reasons for the JFTC's targeting of Microsoft. This Part will also review Microsoft's reluctance to remove the provision from existing agreements and analyze possible outcomes of Microsoft's potential courses of action. Finally, Part V will analyze potential future implications of a JFTC decision, including potential damage to Microsoft's image and market share, and increased litigation as a result of the provision's removal, and argue that Microsoft should continue to defend the provision and assert its noncompetitive aspects.

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[21] *See* Michiyo Nakamoto, *Microsoft Is Told To Alter Policy on Licenses in Japan Contracts*, FIN. TIMES, JULY 14, 2004, at 29; Yuri Kageyama, *Microsoft in Battle with Japan Over Non-sue Clause*, CHI. SUN-TIMES, Oct. 26, 2004, at 62; Todd Zaun, *World Business Briefing Asia: Japan: Microsoft Contract Warning*, N.Y. TIMES, July 14, 2004, at W1.

[22] JOHN O. HALEY, ANTITRUST IN GERMANY AND JAPAN: THE FIRST FIFTY YEARS, 1947-1998, 116-18 (2001); IYORI & UESUGI, *supra* note 19, at 221; *see also* CHRISTOPHER HEATH, THE SYSTEM OF UNFAIR COMPETITION PREVENTION IN JAPAN 48 (2001) (noting that ninety percent of cases under the Antimonopoly Act are resolved through "administrative guidance" versus formal adjudication).

[23] IYORI & UESUGI, *supra* note 19, at 219-21.

[24] *See generally*, GUIDELINES FOR PATENT AND KNOW-HOW LICENSING, *supra* note 16, at 17-19 (outlining when a restrictive contract provision becomes an unfair trade practice); JAPAN FAIR TRADE COMMISSION, JFTC NOTIFICATION NO. 15, GENERAL DESIGNATIONS FOR UNFAIR TRADE PRACTICES 3-4 (June 18, 1982), *available at* http://www2.jftc.go.jp/e- page/legislation/ama/unfairtradepractices.pdf (last visited May 31, 2005) [hereinafter GENERAL DESIGNATIONS] (outlining the different violations that constitute unfair trade practices).

## II. A NON-ASSERTION OF PATENTS PROVISION REPRESENTS BOTH A VALID PROTECTION AND A POTENTIALLY ILLEGAL RESTRICTION

Companies use NAP provisions to prevent costly and lengthy patent litigation and facilitate settlement of patent disputes between licensors and licensees.[25] While such provisions prevent a licensee from asserting its patent rights in some situations, they may also keep both the licensee and licensor from being sued for potential patent infringement.[26] They are also often used in the context of cross-licensing agreements, and in these situations, the licensor is also prevented from asserting patent rights.[27] Although they have not been tested under antitrust laws, the European Union and the United States examined clauses similar to the NAP provision and upheld them in certain situations.[28] However, courts in both the European Union and United States indicate that the outcome may be different in other situations.[29] Their decisions suggest that the NAP provision could potentially be in violation of the laws of the United States and European Union, but not necessarily contrary to antitrust laws.[30] Both the United States and European Union had the opportunity to examine the NAP provision under their respective antitrust laws during prior investigations and litigation against Microsoft, and decided not to challenge it.[31]

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[25] BRUNSVOLD & O'REILLEY, *supra* note 7, at 17.

[26] *See, e.g.*, 14B AM. JUR. LEGAL FORMS 2D *Patents* § 196:90 (2004) (recommending that a licensee consider using a "nonassertion clause" in licensing agreements).

[27] 1 GREGORY J. BATTERSBY & CHARLES W. GRIMES, MULTIMEDIA AND TECHNOLOGY LICENSING AGREEMENTS § 4:20 (2004).

[28] *See* Case 66/85, Bayer AG v. Sullhofer, 1988 E.C.R. 5249, [1990] 4 C.M.L.R. 182, 186-87 (no-challenge clauses are not *per se* illegal and warrant a case-by-case analysis); Lear, Inc. v. Adkins, 395 U.S. 653, 670-71 (1969) (indicating a policy of generally disfavoring restrictions on assertion of patent rights, but upholding the non-assertion of patent rights in this case); Foster v. Hallco Mfg Co., 947 F.2d 469, 477 (Fed. Cir. 1991).

[29] *See* Case 66/85, Bayer AG v. Sullhofer, 1988 E.C.R. 5249, [1990] 4 C.M.L.R. 182, 190; Lear, Inc. v. Adkins, 395 U.S. 653, 670-72 (1969); Foster v. Hallco Mfg Co., 947 F.2d 469, 475-76 (Fed. Cir. 1991).

[30] *See generally* Case 66/85, Bayer AG v. Sullhofer, 1988 E.C.R. 5287, 4 C.M.L.R. 182 (1988); Lear, Inc. v. Adkins, 395 U.S. 653 (1969); Foster v. Hallco Mfg Co., 947 F.2d 469 (Fed. Cir. 1991) (cases indicating that restrictive provisions may be violations of the law in some circumstances).

[31] In 1994, the United States Department of Justice and various individual states sued Microsoft under the Sherman Antitrust Act for anticompetitive and monopolistic practices tied with its bundling of Internet Explorer in its operating system, and its refusal to divulge source codes to OEMs. *See* U.S. v. Microsoft Corp., 253 F.3d 34, 58-62 (D.C. Cir. 2001). Later, in a status report on Microsoft's compliance with the final judgment, the Court indicated that the plaintiffs had not reached a conclusion as to whether the NAP provision violated the terms of the final antitrust judgment, but they were satisfied that Microsoft's prospective removal of the NAP provision remedied their concerns about compliance. *See* Joint Status Report on Microsoft's Compliance With the Final Judgments July 9, 2004, at 7, U.S. v. Microsoft Corp., C.A. No. 98-1232 (D.D.C. 2004) [hereinafter Microsoft Joint Status Report]. In other words, because Microsoft had already agreed to remove the NAP provision, it was no longer a concern to the plaintiffs in the case. *Id.* Shortly thereafter, the Commission of European Communities decided a

### A. *NAP Provisions Help Resolve Patent Infringement Actions and Are Standard in Many Licensing Agreements*

Part of the NAP provision's utility lies in the reduction of transaction costs: if the likelihood of costly litigation is reduced, companies that license their software, like Microsoft, can charge a lower price for the software license.[32] A typical NAP provision includes the following language:

> Company A agrees that Company A and its affiliates will not assert during the term of this Agreement and thereafter, directly or indirectly, any cause of action based, in whole or in part, upon the purported infringement by Company B or its suppliers or customers, mediate or immediate, during the terms of this Agreement of: (i) any patent (including any utility patent, design patent, patent of importation, patent of addition, certificate of addition, certificate or model of utility) granted by the United States or any other country; (ii) any reissue, continuation, parent, division, extension, renewal, or continuation-in-part of any of the foregoing.[33]

The inclusion of NAP provisions in treatises on technology licensing evidences their commonality.[34] Although NAP provisions have utility, they may be considered anti-competitive in various jurisdictions under certain circumstances.[35]

Use of the NAP provision initially served to ensure that computer manufacturers would raise any intellectual property concerns they may have before Microsoft shipped them a new version of Microsoft Windows.[36] Its original design was meant to balance "respect for intellectual property rights with the avoidance of IP disputes, ensuring that computer manufacturers did

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similar case against Microsoft tied with its bundling of media players, among other anticompetitive practices. *See* Commission Decision of Mar. 24, 2004, Case COMP/C-3/37.792 Microsoft. The Court similarly had the opportunity to examine restrictive licensing provisions, but did not mention NAP provisions. *Id.*

[32] *See* Michiyo Nakamoto, *Companies Asia—Pacific: Microsoft Is Told to Alter Policy on Licences Japan Contracts*, FIN. TIMES UK, July 14, 2004.

[33] BATTERSBY & GRIMES, *supra* note 27, § 4:20(3).

[34] *See generally* BATTERSBY & GRIMES, *supra* note 27; BRUNSVOLD & O'REILLEY, *supra* note 7, at 17; STEVEN Z. SZCEZEPANSKI, 4 ECKSTROM'S LICENSING IN FOR. & DOM. OPS. (2004).

[35] *See* SZCEZEPANSKI, *supra* note 34, § 31:32. The treatise notes that restrictions in licensing agreements on asserting patent rights could be considered anti-competitive and might be a violation of the Japanese Antimonopoly Act. *Id.* Generally, any jurisdiction in addition to Japan could potentially find the use of a restrictive clause like this to be anticompetitive and a violation of antitrust laws. *Id.*

[36] Statement by Microsoft, *supra* note 8.

not ship a new version of Windows and then raise an IP concern years later."[37] For many licensors, especially smaller companies, NAP provisions are a vital protection. They ensure that these companies can protect themselves from larger companies who license their software. They also gain protection from a licensor company's attempts to assert its own patent rights.[38]

### B. *NAP Provisions Provide Protection from Lawsuits But May Prevent Licensees from Asserting Patent Rights*

A licensing agreement between a software developer and an OEM may include a non-assertion of patents provision to facilitate the settlement of patent disputes and avoid potential litigation.[39] Microsoft has used the provision for more than ten years[40] and other companies also include it in their licensing agreements.[41] Such licensing agreements can protect the licensee who changes its product or develops a product similar to Microsoft's software, since they often include reciprocal agreements not to bring an action for patent infringement.[42]

The NAP provision has various advantages and disadvantages. For example, it prevents computer manufacturers or other OEMs who sign it from bringing an action based on suspected infringements of the licensee's intellectual property rights by Microsoft.[43] Technology developed by a manufacturer merges into the operating system supplied by Microsoft when it is loaded onto a machine.[44] The manufacturer may make improvements or changes to the technology using its own patented devices to allow the operating system and other technology on the computer to interact more efficiently.[45] Because the NAP provision prevents assertion of patent rights,

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[37] *Id.*

[38] *See* 14B AM. JUR. LEGAL FORMS 2D *Patents* § 196:90 (2004).

[39] *See* BRUNSVOLD & O'REILLEY, *supra* note 7, at 16-17; Statement by Microsoft, *supra* note 8.

[40] *See* Statement by Microsoft, *supra* note 8.

[41] The widespread use of NAP provisions is evidenced by its inclusion in licensing forms and treatises. *See generally*, BRUNSVOLD & O'REILLEY, *supra* note 7; BATTERSBY & GRIMES, *supra* note 27; SZCZEPANSKI, *supra* note 34; Lori Krauss, *Copyright and Licensing Basics*, 567 PLI/PAT 393, 418 (1999) (presenting examples of treatises and licensing forms that include NAP provisions).

[42] For example, a cross-licensing agreement often includes a NAP provision. In these types of agreements, both companies agree not to assert their patent rights. *See* BATTERSBY & GRIMES, *supra* note 27, § 4:20.

[43] Yuri Kageyama, *Japan Orders Microsoft Deals Changed*, CHI. SUN TIMES, July 14, 2004, at 78 [hereinafter Kageyama, *Japan Orders*].

[44] *See* JFTC Press Release, *supra* note 2, at 4.

[45] This essentially encompasses the assertion made by PC manufacturers that led to the investigation of Microsoft. *See* JFTC Press Release, *supra* note 2, at 3. These Japanese OEMs feared Microsoft could

it incentivizes licensees to fully inform themselves about Microsoft technology when entering into a licensing agreement.[46] It promotes the settlement of patent disputes.[47] Unfortunately, it also potentially prevents a licensee from legitimately asserting rights over proprietary ideas and may cause the licensee to lose royalty income.[48] Despite the drawbacks, the NAP provision is essential to averting costly infringement actions because it can preclude both parties from bringing a patent infringement action against the other during the terms of the licensing agreement.[49] In this way, it helps both the licensee and the licensor.

### C. *The United States and European Union Examined Restrictive Provisions and Determined They Are Not Necessarily Legal in All Circumstances*

Both the U.S. Federal Circuit and the Supreme Court have examined clauses similar to the NAP provision. In *Foster v. Hallco Manufacturing Company*,[50] Foster attempted to assert his rights to a new device that he claimed fell outside of the patent licensing agreement with Hallco.[51] The United States Court of Appeals for the Federal Circuit explained that there was a strong public interest in the settlement of patent litigation, as it is time-consuming and expensive.[52] In the interest of preserving finality of a judgment, the court decided the case under theories of patent and contract law and not under antitrust law.[53] The court found that the issue had already been decided and Foster could not reassert his right to the device patents.[54] It did not decide, however, whether Foster could challenge the patent if the device were materially different from those included in the agreement.[55] Therefore, the court validated the restrictive provision under a specific set of circumstances.

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use their proprietary technology in its media player due to the technology's incorporation into the operating system when it was loaded onto the machines. *Id.*

[46] *See* Statement by Microsoft, *supra* note 8.

[47] *See* BRUNSVOLD & O'REILLEY, *supra* note 7, at 17. *See also* RAYMOND T. NIMMER & JEFF DODD, MODERN LICENSING LAW § 1:12 (2005) (noting that some licenses are driven primarily by avoiding litigation about intellectual property rights).

[48] JFTC Press Release, *supra* note 2, at 3-5. *See also* GUIDELINES FOR PATENT AND KNOW-HOW LICENSING, *supra* note 16, at 19.

[49] *See* BATTERSBY & GRIMES, *supra* note 27, § 4:20.

[50] Foster v. Hallco Mfg. Co., 947 F.2d 469 (Fed. Cir. 1991).

[51] *Id.* at 472-73. Foster had already entered a settlement agreement and consent judgment with Hallco conceding that Hallco owned the patents and that he was licensing them. *Id.*

[52] *Foster*, 947 F.2d at 474-75.

[53] *Id.* at 475.

[54] *Id.*

[55] *Id.* at 482.

The Supreme Court of the United States generally disfavors restrictions on challenges to patent validity. In *Lear, Inc. v. Adkins*,[56] a case concerning non-assertion of patent rights, the Supreme Court made its decision under patent law. The Court held that Adkins could not assert a patent right over ideas he had allowed Lear, Inc. to use prior to his attempts to patent those ideas.[57] The restrictive provision was upheld in this case because Adkins had already allowed Lear, Inc. to use the patentable devices before he got the patents. However, the Court noted it disfavored patent restrictions and indicated that, under different circumstances, such restrictive provisions may not have been upheld.[58]

The underlying issues in the above cases were attempts to challenge the validity of a company's patent coupled with one's assertion of his or her own patent rights. Accordingly, while the restrictive provisions were upheld in these cases, it is possible, although unlikely, that the courts could invalidate provisions restricting the exercise of patent rights under other circumstances.[59]

The European Court of Justice validated a clause similar to a non-assertion of patents provision in *Bayer AG v. Sullhofer*.[60] The Court noted that the provision itself does not necessarily constitute a barrier to trade[61] and allowed its use in this case because it did not actually cause harm to the licensee.[62] This suggests that a situation that harms the licensee could potentially be a violation of European Union law.

Although the United States and the European Union have validated clauses similar to Microsoft's NAP provision under laws other than antitrust, the courts of both countries indicated that they intend to examine such provisions on a case-by-case basis.[63] However, since the United States and the European Union already had the chance to examine the provision under antitrust laws[64] and decided to forego the opportunity, they are unlikely to

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[56] Lear, Inc. v. Adkins, 395 U.S. 653 (1969).

[57] *Id.* at 673-74.

[58] *Id.* at 670.

[59] For an explanation of other policy concerns and the specific application of the *Lear* doctrine to non-assertion provisions, see Norman E. Rosen, *Intellectual Property and the Antitrust Pendulum: Recent Developments at the Interface Between the Antitrust and Intellectual Property Laws*, 62 ANTITRUST L.J. 669, 687-92 (1994).

[60] Case 66/85, Bayer AG v. Sullhofer, 1988 E.C.R. 5249, [1990] 4 C.M.L.R. 182 (1988).

[61] *Id.* at 186.

[62] *Id.* at 190.

[63] *See* Case 66/85, Bayer AG v. Sullhofer, 1988 E.C.R. 5249; Lear, Inc. v. Adkins, 395 U.S. 653 (1969); Foster v. Hallco Mfg. Co., 947 F.2d 469 (Fed. Cir. 1991).

[64] *See generally* U.S. v. Microsoft Corp., 253 F.3d 34, 58-62; Microsoft Joint Status Report, *supra* note 31; Commission Decision of Mar. 24, 2004, Case COMP/C-3/37.792 Microsoft (U.S. and European

challenge the provision under antitrust law.

NAP provisions have economic utility for many companies without the bargaining power or market share of Microsoft. However, while preventing costly patent infringement lawsuits, they also prevent patent holders from asserting their rights should they make improvements to Microsoft's programs, or should Microsoft's programs absorb their proprietary information. This may discourage innovations for fear that the technology will be taken without the payment of royalties. Also, there exists a possibility that other jurisdictions might disfavor the NAP provision. Thus, NAP provisions both possess economic utility for Microsoft and its licensees, and potentially restrain innovation.

## III. THE ANTIMONOPOLY ACT MOVES THE JAPANESE ECONOMY FROM COLLUSION TO COMPETITION

The Japanese government enacted the Antimonopoly Act in 1947 during the United States' post-World War II occupation.[65] The Antimonopoly Act conformed to business values in Japanese society.[66] It aimed to create a stable democracy, encourage free and fair competition, and promote the creative initiative of entrepreneurs.[67] Since its inception, Japan has strengthened the Antimonopoly Act through several amendments, and its enforcement has become a focal point of the JFTC.[68] The JFTC is primarily responsible for enforcement of the Antimonopoly Act.[69] It has processes in place to investigate, issue cease and desist orders for perceived violations, and impose penalties, although generally the penalty consists of a fine rather than criminal charges.[70] Early in the Antimonopoly Act's history, the JFTC was reluctant to enforce the Act stringently. In recent years, however, the

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Commission antitrust decisions against Microsoft that did not encompass NAP provisions in their judgments).

[65] HIROSHI IYORI & AKINORI UESUGI, THE ANTIMONOPOLY LAWS OF JAPAN, 6-11 (1983).

[66] Harry First, *Antitrust in Japan: The Original Intent*, 9 PAC. RIM L. & POL'Y J. 3-4 (2000). The Act conformed to business ideals such as encouraging economic growth and increasing market access. *Id.*

[67] Hiroshi Iyori, *Competition Policy and Government Intervention in Developing Countries: An Examination of Japanese Economic Development*, 1 WASH. U. GLOBAL STUD. L. REV. 35, 39-41 (2002).

[68] Kurita, *supra* note 14, at 391-92. For a brief treatment of a more recent surge in enforcement and increased staffing and budget of the Japan Fair Trade Commission, the Antimonopoly Act's primary enforcement mechanism, see Harris, *supra* note 14.

[69] MITSUO MATSUSHITA, INTERNATIONAL TRADE AND COMPETITION LAW IN JAPAN 98 (1993).

[70] 2 ABA SECTION OF ANTITRUST LAW, COMPETITION LAWS OUTSIDE THE UNITED STATES 65-66 (H. Stephen Harris et al. eds., 2001) [hereinafter ABA ANTITRUST, COMPETITION LAWS].

JFTC has begun to focus more on enforcement.[71] Of particular concern is the focus of recent enforcement actions on the abuse of a dominant bargaining position.[72]

### A. *The Japanese Antimonopoly Act Was Initially a Collaboration Between Japan and the United States*

Competition laws did not spontaneously develop within Japanese society, but originated from the demands of the United States during the U.S. occupation after World War II.[73] Indeed, the Japanese economic market did not find its roots within ideals of fair competition.[74] Before U.S. occupation, Japan fostered collusion between companies, strong governmental control in the form of trade associations, and protection from excessive internal competition.[75] Japanese companies viewed foreign countries as their primary source of competition and were willing to cooperate with each other to increase profits and win the economic battle against foreign corporations.[76]

In the 1920s and 1930s, the government fostered the creation of cartels[77] in order to ensure the success of domestic companies in the face of competition from abroad.[78] The recession and depression in the economy during this period caused Japanese society to promote group welfare and look unfavorably upon competition.[79] The *zaibatsu*,[80] or trade

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[71] INTERNATIONAL COMPETITION POLICY ADVISORY COMMITTEE TO THE ATTORNEY GENERAL AND ASSISTANT ATTORNEY GENERAL FOR ANTITRUST, U.S. DEPT. OF JUSTICE, FINAL REPORT 216 (2000) [hereinafter U.S. DEPT. OF JUSTICE INT'L COMPETITION POLICY]; *see also* Harris, *supra* note 14.

[72] Antimonopoly Act, *supra* note 3, § 2(9)(v) (prohibiting as an unfair trade practice dealing with another party by unjust use of one's bargaining position); *see also* Joshua A. Newberg, *Technology Licensing Under Japanese Antitrust Law*, 32 LAW & POL'Y INT'L BUS. 705, 752-54 (2001) (outlining when a dominant bargaining position exists).

[73] KENJI SUZUKI, COMPETITION LAW REFORM IN BRITAIN AND JAPAN 18-19 (2002).

[74] *See* IYORI & UESUGI, *supra* note 65, at 1-2; Gregory K. Bader, Note, *The Keiretsu Distribution System of Japan: Its Steadfast Existence Despite Heightened Foreign and Domestic Pressure for Dissolution*, 27 CORNELL INT'L L.J. 365, 365-66 (1994); ELEANOR M. HADLEY, ANTITRUST IN JAPAN 15 (1970).

[75] First, *supra* note 66, at 6-10; *see also* SUZUKI, *supra* note 73, at 18; Iyori, *supra* note 12, at 61.

[76] First, *supra* note 66, at 8-14.

[77] HIROSHI IYORI, ANTIMONOPOLY LEGISLATION IN JAPAN 3 (1969). For more information about cartels during the period before U.S. occupation, see Takeo Kikkawa, *Functions of Japanese Trade Associations Before World War II: The Case of Cartel Organizations*, *in* TRADE ASSOCIATIONS IN BUSINESS HISTORY 60-65 (Hiroki Yamazaki & Matao Miyamoto eds., 1988).

[78] Cartels are agreements between competing companies to restrict prices and product output, among other forms of competition. HALEY, *supra* note 22, at 8-9.

[79] MICHAEL L. BEEMAN, PUBLIC POLICY AND ECONOMIC COMPETITION IN JAPAN: CHANGE AND CONTINUITY IN ANTIMONOPOLY POLICY, 1973-1995, at 14-15 (2002).

conglomerates,[81] were also prevalent in Japan prior to World War II. These oligopolies absorbed failing companies and were responsible for ten to twenty percent of market output in key areas such as manufacturing, banking, and trade.[82] Despite the promotion of cartels and existence of *zaibatsu* during this era, rivalry and competition still existed.[83] Regardless of many overtly anti-competitive policies, new *zaibatsu* and smaller manufacturing companies trickled into the market.[84]

During the U.S. occupation after World War II, U.S. directives and Japanese legislation dissolved many of these cartels and *zaibatsu*.[85] In 1947, the Japanese government drafted the Antimonopoly Act.[86] Although prompted by U.S. influence during the occupation, the Antimonopoly Act was authored by the planning section of the General Affairs Department of the Ministry of Commerce and Industry,[87] demonstrating the significant role of the Japanese government in its creation.[88]

At the time of its enactment in 1947, the Antimonopoly Act: 1) prohibited anti-competitive agreements, private monopolies, unreasonable differences in the strength of different enterprises, and the formation of holding companies and control associations; 2) restricted mergers, stockholding, transfer of management, and ownership of debt; 3) gave the Japanese government the power to issue cease and desist orders for violations of the Act and to levy fines; 4) allowed exemptions for small scale trade associations; and 5) established the JFTC and gave it the power to act independently and enforce the Antimonopoly Act.[89] Provisions of the

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[80] The term "*zaibatsu*" references the large, family-controlled industrial combines of Japan. For more information on *zaibatsu*, see generally HIDEMASA MORIKAWA, ZAIBATSU: THE RISE AND FALL OF FAMILY ENTERPRISE GROUPS IN JAPAN (1992).

[81] SUZUKI, *supra* note 73, at 18. *Zaibatsu* were replaced by *keiretsu* in later decades. *Keiretsu* are similar in structure and purpose to *zaibatsu*. To read more about *keiretsu* and their continued existence in Japan, see generally Bader, *supra* note 74. For an analysis of the antitrust implications of *keiretsu*, see Ely Razin, *Are the Keiretsu Anticompetitive?: Look to the Law*, 18 N.C. J. INT'L L. & COM. REG. 351 (1993).

[82] HALEY, *supra* note 22, at 10.

[83] *Id.* at 11.

[84] *Id.* at 11-13.

[85] IYORI, *supra* note 77. See also HALEY, *supra* note 22, at 7-42, for an interesting discussion of competition in Japan during the era of cartel and *zaibatsu* domination. The author argues that competition existed and that the U.S. insistence on an antimonopoly policy was more self-serving for the U.S. than helpful to the Japanese economy.

[86] ODA, *supra* note 12, at 300-01.

[87] Hiroshi Iyori, *A Comparison of U.S.-Japan Antitrust Law: Looking at the International Harmonization of Competition Law*, 4 PAC. RIM L. & POL'Y J. 59, 65 (1995). This Department later became the Ministry of International Trade and Industry ("MITI").

[88] *See* First, *supra* note 66, at 3-4.

[89] Iyori, *supra* note 87, at 66; *see also* HALEY, *supra* note 22, at 71-72; John O. Haley, *Antitrust Sanctions and Remedies: A Comparative Study of German and Japanese Law*, 59 WASH. L. REV. 471, 487-88 (1984).

United States' Sherman and Clayton Acts embody many of the same ideals.[90]

Much of the Antimonopoly Act remains the same today, despite periodic amendments.[91] The first version of the Act was very stringent in its outlining of antitrust violations, and Japan's more conservative factions opposed it.[92] Drafters worded the Antimonopoly Act broadly with both very general and specific prohibitions that reached beyond the scope of American legislation.[93] Amendments in 1949 and 1953 weakened the force of the Antimonopoly Act.[94] However, a 1977 amendment added new provisions and somewhat "restored in new guise earlier deletions."[95]

### B. *The Japan Fair Trade Commission Enforces the Antimonopoly Act to Maintain Fair Competition*

The original Antimonopoly Act created the JFTC and enumerated its powers and duties.[96] In turn, the JFTC enforces the Antimonopoly Act and investigates violations.[97] The JFTC is an administrative organization with quasi-legislative and quasi-judicial functions.[98] Its quasi-legislative function gives it the power to draft binding rules and guidelines on enforcing and interpreting the Antimonopoly Act's language.[99] Its quasi-judicial powers allow it to investigate and compel testimony from relevant parties and issue recommendations and decisions.[100] Violators of the Antimonopoly Act usually follow the JFTC's recommendation decisions.[101] A general sense exists in Japanese society that significant errors in the JFTC's process are unlikely because of the existence of procedural safeguards such as investigation and hearings.[102]

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[90] *See* Sherman Antitrust Act, 15 U.S.C. §§ 1-7 (2004); Clayton Act, 15 U.S.C. §§ 12-27 (2004); *see also* Yoshikazu Kawai, *Competition Policy and Industrial Policy in Japan*, *in* INTERNATIONAL HARMONIZATION OF COMPETITION LAWS 47 (Chih-Kang Wang et. al. eds., 1995) (noting that the Antimonopoly Act was modeled after U.S. antitrust law).

[91] *See* IYORI & UESUGI, ANTIMONOPOLY LAWS & POLICIES, *supra* note 19, at 30-66.

[92] BEEMAN, *supra* note 79, at 15-16.

[93] HALEY, *supra* note 22, at 71.

[94] *See* MATSUSHITA, *supra* note 69, at 78-80; BEEMAN, *supra* note 79, at 16-17.

[95] HALEY, *supra* note 22, at 71. For example, the amendment disallowed the formation of business conglomerates for any reason. It also suppressed abusive conduct by big businesses and introduced a surcharge system against cartels. *See* Iyori, *supra* note 67, at 44.

[96] Antimonopoly Act, *supra* note 3, §§ 27-76.

[97] *See* ABA ANTITRUST, COMPETITION LAWS, *supra* note 70, at 58.

[98] BEEMAN, *supra* note 79, at 27.

[99] *Id.*

[100] *Id.*

[101] IYORI & UESUGI, *supra* note 19, at 220

[102] HALEY, *supra* note 22, at 105.

Adjudication by the JFTC involves four phases.[103] Phase one includes the initial review of complaints and the preliminary investigation. If the JFTC deems it necessary, it may order a formal investigation, thus commencing phase two.[104] If the JFTC refuses to formally investigate, the complainant has little ability to press the issue.[105] The JFTC may compel witnesses or experts to appear and testify, order the submission of documents pertinent to the investigation, and enter a place of business to inspect conditions of the business operation.[106] Phase three includes initial recommendation decisions and adjudicatory hearings.[107] During this phase, investigators issue reports of their findings to the commissioners who, in turn, issue a recommendation based on the reports.[108] If the alleged violator accepts the terms of this decision, it is legally binding.[109] An initial hearing session, following the adversarial format of a Japanese trial, occurs if the violator rejects the recommendation decision.[110] Consent decisions[111] and final contested (or formal) decisions result during phase four of the adjudication process.[112] The violator may contest the decision and appeal the final decision to the Tokyo High Court.[113]

### C. *Microsoft's Alleged Antitrust Violation May Constitute an Unfair Trade Practice Under the Antimonopoly Act*

Cartels, restraints of trade, and unfair trade practices thwart many goals of the Japanese economy.[114] The Antimonopoly Act attempts to

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[103] *See* HALEY, *supra* note 22, at 116-124.

[104] *Id.*

[105] *Id.* at 119. *See also* IYORI & UESUGI, *supra* note 19, at 219 (noting that the JFTC's decision to drop a case may not be appealed in court); Toshiaki Takigawa, *The Prospect of Antitrust Law and Policy in the Twenty-First Century: In Reference to the Japanese Antimonopoly Law and Japan Fair Trade Commission*, 1 WASH. U. GLOBAL STUD. L. REV. 275, 298-99 (2002) (noting that Japanese citizens can bring suit to recover damages and, more recently, injunctive relief, but this rarely occurs due to stringent causation and damages standards).

[106] Antimonopoly Act, *supra* note 3, § 46(1)(i)-(iv).

[107] HALEY, *supra* note 22, at 120.

[108] *Id.*

[109] Mitsuo Matsushita, *The Antimonopoly Law of Japan*, *in* GLOBAL COMPETITION POLICY 151, 158 (Edward M. Graham & J. David Richardson eds., 1997).

[110] HALEY, *supra* note 22, at 121.

[111] Consent decisions arise when the violator submits a written statement admitting the findings of fact and application of laws and agreeing to accept the decision without further proceedings. It is an opportunity for the violator of the Act to consent to the recommendations of the JFTC before a final decision is made. Formal decisions results after completion of the hearing proceedings. *See* IYORI & UESUGI, *supra* note 19, at 226.

[112] HALEY, *supra* note 22, at 123.

[113] *Id.*

[114] *See* First, *supra* note 66, at 45-46.

achieve a number of economic goals, including: promoting free and fair competition, stimulating initiative, encouraging business activities, raising employment and real income levels, and ensuring consumer benefits.[115] To ensure realization of these goals, the Antimonopoly Act prohibits monopolization, unreasonable restraints on trade, and unfair trade practices.[116] Additionally, it prevents disproportionate concentrations of economic power and eliminates unfair restrictions on business activities.[117]

The alleged Microsoft violation relates to unfair trade practices. Section 19 of the Antimonopoly Act states: "No entrepreneur shall employ unfair trade practices."[118] While the JFTC can order criminal penalties for monopolizing and creating unreasonable restraints of trade,[119] it cannot do so for unfair trade practices.[120] It may order the violator to cease and desist engaging in the activity, or require the company or entrepreneur to delete the relevant provisions from the licensing agreement and take any other measures necessary to eliminate the infringing act.[121]

Microsoft's commanding market share, combined with its use of a NAP provision, may well constitute an unfair trade practice under Section 19. The General Designations For Unfair Trade Practices ("General Designations"), guidelines drafted by the JFTC and used to help interpret the Antimonopoly Act, include a broad list of actions that fall under the rubric of unfair trade practices.[122] Particularly relevant to Microsoft's case is the General Designations' indication that abusing a dominant bargaining position is an unfair trade practice.[123] Microsoft controls ninety to ninety-five percent of the personal computer market in Japan.[124] As a result, it has a dominant bargaining position when negotiating licensing agreements with other less powerful companies.

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[115] U.N. COMM'N ON INV., TECH., AND RELATED FIN. ISSUES, ISSUES RELATED TO COMPETITION LAW OF PARTICULAR RELEVANCE TO DEVELOPMENT: PREPARATIONS FOR A HANDBOOK ON COMPETITION LEGISLATION at 11, U.N. DOC. TD/B/COM.2/CLP/6 (1998) [hereinafter HANDBOOK ON COMPETITION LEGISLATION].

[116] Antimonopoly Act, *supra* note 3, § 2(9).

[117] *See* HANDBOOK ON COMPETITION LEGISLATION, *supra* note 115, at 11.

[118] Antimonopoly Act, *supra* note 3, § 19.

[119] *Id.* § 2(9). Unreasonable restraint of trade refers to cartels among companies, while unfair trade practices include many types of behavior that can impede market competition. *See id.* § 2(6) and § 2(9).

[120] *See* Newberg, *supra* note 72, at 716.

[121] Antimonopoly Act, *supra* note 3, at ch. V § 20.

[122] *See* GENERAL DESIGNATIONS, *supra* note 24, at 1-4; ABA ANTITRUST, COMPETITION LAWS, *supra* note 70, at 29-30.

[123] GENERAL DESIGNATIONS, *supra* note 24, at 3-4.

[124] *See* Nakamoto, *supra* note 21. *See also* JFTC Press Release, *supra* note 2, at 2 (describing the portion of the market controlled by Microsoft).

Another document that the JFTC uses to interpret the Antimonopoly Act, the Guidelines for Patent and Know-How Licensing Agreements ("Guidelines"), describes a provision almost exactly like the one used by Microsoft to demonstrate how such provisions can violate the Act when used in conjunction with a dominant bargaining position.[125] The Guidelines describe a dominant bargaining position as one in which "the licensee is obliged to accept the licensor's requests even if they are excessively disadvantageous to the licensee, because the licensor's denial or suspension of technology transaction would present major obstacles to the licensee's business."[126] This refers to a licensor with a large market share who may be able to use its position and the licensee's need for its product to force the licensee into accepting an unfavorable contract provision. The Guidelines also note that an unjust disadvantage for the licensee results when an agreement does not allow the licensee to assert its patent rights.[127]

Microsoft's large market share forces licensees into accepting the NAP provision when their bargaining position is weaker than that of Microsoft. The NAP provision obliges licensees to accept Microsoft's requests to refrain from asserting their technology patents, even though these requests may be excessively disadvantageous to the licensee.[128] Since Microsoft's behavior in inserting NAP provisions into its licensing agreements seems to fall within the descriptions of abuse of dominant bargaining position in the General Designations and the Guidelines, it may constitute an unfair trade practice in Japan.[129] Therefore, Microsoft may be in violation of the Antimonopoly Act when dealing with a company whose bargaining position is far below that of Microsoft.

The JFTC, as the enforcer of the Antimonopoly Act, generally has the responsibility of investigating and deciding whether to bring charges against a company like Microsoft for violations of the Act. The JFTC has recommended that Microsoft remove the NAP provision from licensing agreements with Japanese OEMs, concluding that it constitutes an unfair trade practice. Microsoft is contesting the JFTC's recommendation and will continue to fight any subsequent rulings that are not in its favor.[130]

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[125] *See* GUIDELINES FOR PATENT AND KNOW-HOW LICENSING, *supra* note 16, at 17-19.
[126] *Id.* at 19.
[127] *Id.*
[128] For the text of a typical NAP provision, see *supra* Part II.A.
[129] *See* GUIDELINES FOR PATENT AND KNOW-HOW LICENSING, *supra* note 16, at 19.
[130] *See* Paul Kallender, *Microsoft, Japanese Regulators Meet Over License Terms*, INFOWORLD DAILY NEWS, Feb. 7, 2005.

## IV. THE JAPAN FAIR TRADE COMMISSION IS MAKING AN EXAMPLE OF A SOFTWARE GIANT

Microsoft had been using the non-assertion of patents provision for nearly ten years without incident when Japan decided to challenge its use under the Antimonopoly Act.[131] PC manufacturers repeatedly complained about the trade ramifications of the NAP provision, prompting the JFTC to raid Microsoft's offices.[132] After an investigation, the JFTC recommended that Microsoft remove the provision from all present and future agreements, also citing another clause in the licensing agreements that made the NAP provision effective for up to three years after the licenses expire.[133] Microsoft removed the provision from future licensing agreements, citing a change in the atmosphere of technology licensing,[134] but refused to remove it from existing contracts, arguing that it was a legal protection from costly lawsuits.[135] After the investigation and ensuing recommendation, Microsoft's refusal to comply triggered a round of hearings between the JFTC and Microsoft.[136] Little progress has been made in recent meetings with the JFTC. Both parties expect negotiations and hearings to continue through 2006 before they reach a resolution.[137]

### A. *Phase One: The JFTC Investigates Microsoft's Licensing Practices for Potential Antitrust Violations*

As a result of complaints by PC manufacturers,[138] investigators raided Microsoft Corporation's Tokyo headquarters as part of an attempt to investigate the licensing agreements and the company's software supply practices for computers in Japan.[139] Although JFTC officials indicated that

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[131] *See* Statement by Microsoft, *supra* note 8. *See, e.g.*, Case 66/85, Bayer AG v. Sullhofer, 1988 E.C.R. 5287, 4 C.M.L.R. 182 (1988); Lear, Inc. v. Adkins, 395 U.S. 653 (1969); Foster v. Hallco Mfg Co., 947 F.2d 469 (Fed. Cir. 1991) (cases examining provisions concerning assertion of patent rights).

[132] *See Regulators Conduct Search of Microsoft's Office in Tokyo*, *supra* note 1.

[133] *See* JFTC Press Release, *supra* note 2, at 3-4 (indicating that a "Survival Provision" precludes OEMs from asserting patent rights for up to three years after termination of the license).

[134] Statement by Microsoft, *supra* note 8.

[135] Yuri Kageyama, *Drop Contract Clause, Japan Tells Microsoft: Wording Sparks Patent Concerns, Japanese Firms Fear Possible Infringement*, SEATTLE TIMES, July 14, 2004, at D3 [hereinafter Kageyama, *Drop Contract*].

[136] *See* HALEY, *supra* note 22, at 120-21.

[137] *See* Yuri Kageyama, *Microsoft Says Japan Battle Hurting Image*, CRN AP, Aug. 10, 2004, *available at* http://www.crn.com/sections/breakingnews/dailyarchives.jhtml;jsessionid=5PKZDGYHPQ3E CQSNDBCCKH0CJUMEKJVN?articleId=26806928 (last visited May 31, 2005).

[138] JFTC Press Release, *supra* note 2.

[139] *See Microsoft Offices in Tokyo Raided by Japan Trade Officials*, *supra* note 1.

they were not certain whether Microsoft had violated any patents,[140] they said that they believed use of the NAP provision in this situation was anti-competitive.[141] Microsoft removed the provision from all future contracts of its own accord and not in response to the actions of the JFTC.[142] The company issued a statement noting that there had been gradual changes in the information technology marketplace and that it was moving toward a "new [intellectual property] policy based on expanded licensing of its intellectual property rights with others in the industry."[143] As a result, the provision would no longer be needed.[144]

### B. *Phase Two: The JFTC Recommends That Microsoft Remove the Non-Assertion of Patents Provision from Future and Existing Licensing Agreements with Japanese PC Manufacturers*

After concluding its investigation, the JFTC issued a recommendation that Microsoft immediately remove the non-assertion of patents provision in current and previous agreements with Japanese PC manufacturers.[145] It found Microsoft in violation of the unfair trade practices section of the Antimonopoly Act.[146] Although Microsoft had already announced that it would remove the provision from future licensing agreements, the JFTC was concerned with existing licensing agreements as well.[147] Present licensees would not be able to claim any patent infringements for three years after they stopped distributing personal computers running the Microsoft software they had licensed.[148]

The JFTC gave Microsoft two weeks to accept or reject the recommendation.[149] If it had chosen to accept the recommendation, the decision would have been binding.[150] Microsoft rejected the recommendation to remove the NAP provision from existing contracts and

[140] Kageyama, *supra* note 135.

[141] Press Release, Microsoft Corp., Statement by Microsoft Corporation on Reports of Japanese Fair Trade Commission Inquiry (Feb. 26, 2004), *available at* http://www.microsoft.com/presspass/press/2004/Feb04/02-26JFTCStatement.asp (last visited May 31, 2005) [hereinafter Statement by Microsoft II].

[142] *See* Statement by Microsoft, *supra* note 8. *See also*, Microsoft Joint Status Report, *supra* note 31, at 7 (status report on the U.S. action against Microsoft noting the company had removed the NAP provision from future licensing agreements).

[143] Statement by Microsoft, *supra* note 8.

[144] *See* Kageyama, *supra* note 137.

[145] *See* JFTC Decision, *supra* note 2; JFTC Press Release, *supra* note 2.

[146] JFTC Press Release, *supra* note 2, at 1.

[147] *Id.*

[148] *Id.* at 4.

[149] Michiyo Nakamoto, *Microsoft Given Fair Trade Slap*, FIN. TIMES ASIA, July 14, 2004.

[150] HALEY, *supra* note 22, at 120.

decided to contest the decision.[151]

The Antimonopoly Act text is vague in its description of violations. The description within the Antimonopoly Act concerning unfair trade practices merely states that: "[n]o entrepreneur shall employ unfair trade practices."[152] However, section 2(9)(v) of the Act describes unfair trade practices as those including dealing with another party by unjust use of one's bargaining position.[153] Section 14 of the General Designations defines abuse of a dominant bargaining position as doing any number of specified acts "unjustly in the light of the normal business practices, by making use of one's dominant bargaining position over the other party," including "imposing a disadvantage on the said party regarding terms or execution of transaction."[154]

The Guidelines[155] provide direction for enforcing the Antimonopoly Act in the area of licensing agreements.[156] They divide restrictions on competition into three categories: 1) restrictions that do not constitute unfair trade practices because they have a negligible effect on competition in a market;[157] 2) restrictions that may be unfair trade practices and are evaluated based on the specific situation, content of the restriction, position of the licensor and licensee, market conditions, and the duration of the restriction in question;[158] and 3) restrictions that are highly likely to constitute unfair trade practices because they have adverse effects on market competition.[159]

The Guidelines contain a section entitled "Obligation not to assert the licensee's patent rights" that indicates some restrictions in licensing agreements are antitrust violations.[160] For example, a restrictive provision in a licensing agreement that has an adverse effect on market competition and is an abuse of a dominant bargaining position constitutes an unfair trade practice and thus violates the Antimonopoly Act.[161] The Guidelines further indicate that any restriction impeding incentives to engage in research and development of new technologies by limiting the exercise of patent rights is

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[151] *Microsoft Filing Complaint Against Japan FTC, supra* note 11.

[152] Antimonopoly Act, *supra* note 3, § 19.

[153] *Id.* § 2(9)(v).

[154] GENERAL DESIGNATIONS, *supra* note 24, at 3. The General Designations were created by the JFTC to help interpret the Antimonopoly Act.

[155] These Guidelines were drafted by the JFTC to aid in interpretation of some of the clauses concerning technology licensing in the Antimonopoly Act. See GUIDELINES FOR PATENT AND KNOW-HOW LICENSING, *supra* note 16, at 3.

[156] *See* GUIDELINES FOR PATENT AND KNOW-HOW LICENSING, *supra* note 16, at 3-5.

[157] *Id.* at 4.

[158] *Id.*

[159] *Id.*

[160] *Id.* at 28.

[161] Newberg, *supra* note 72, at 739-40.

also a violation of the Antimonopoly Act.[162] This section seems to apply to NAP provisions. Thus, the Guidelines directly guide the JFTC to interpret the Antimonopoly Act as prohibiting NAP provisions as an unfair trade practice if they impede invention or enhance the licensor's position through abuse of a dominant bargaining position.

The Guidelines reflect the overall policy goal of providing incentive for OEM innovation and development by ensuring that they are able to assert their patent rights.[163] NAP provisions appear to be problematic in some situations and some treatises caution practitioners that restricting a licensee's ability to assert patent rights could violate Japanese antitrust law.[164] To promote the goals of innovation and development, the JFTC recommended that Microsoft remove the NAP provision from licensing agreements with Japanese PC manufacturers.[165]

### C. *Phase Three: Contesting the JFTC's Recommendation Decision and Commencing Adjudicatory Hearings*

Microsoft rejected the JFTC's recommendation decision,[166] which resulted in hearings before neutral commissioners to decide whether to issue a final decision in the matter.[167] Microsoft indicated that it wanted the JFTC to hear its reasons for including the NAP provision in its licensing agreements with PC manufacturers.[168] During the first round of the hearings, Microsoft stated that it intended to contest the JFTC's decision regarding the NAP provision because it believed in the provision's general legality.[169] Microsoft and the JFTC met again for a second shorter meeting to discuss their respective positions and to allow Microsoft to prepare its refutation.[170] Microsoft Japan's president and JFTC officials indicated that they believed the legal battle could last as long as two years.[171]

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[162] GUIDELINES FOR PATENT AND KNOW-HOW LICENSING, *supra* note 16, at 19.

[163] This is reflected in the JFTC's inclusion of a specific section on assertion of licensee's patent rights in the Guidelines. *See* GUIDELINES FOR PATENT AND KNOW-HOW LICENSING, *supra* note 16, at 19.

[164] *See, e.g.*, SZCZEPANSKI, *supra* note 34, § 31:32 (noting that a provision prohibiting a licensee from exercising patent rights against the licensor is considered an unfair trade practice in Japan if it has an adverse effect on market competition).

[165] *See* JFTC Press Release, *supra* note 2, at 5-6.

[166] *See* Statement by Microsoft, *supra* note 8.

[167] *See Recent Licensing Agreements in Japan*, ECON. INTELLIGENCE UNIT, Sept. 30, 2004, at 36; HALEY, *supra* note 22, at 120.

[168] *See* Staff Reporter, *Japan Warns Microsoft Over "Unfair" Licensing Deals for Japan PC Makers*, XINHUA ECONOMIC NEWS, July 13, 2004.

[169] *See* Kageyama, *supra* note 21, at 62.

[170] *See* Paul Kallender, *Japan's FTC, Microsoft Meet Again in Licensing Case*, IDG NEWS SERVICE, Dec. 21, 2004.

[171] Kageyama, *supra* note 137.

Microsoft will present its case to the JFTC and hope for a favorable determination. In the end, the JFTC may issue a final decision, which will be binding on the legality of Microsoft's NAP provision in Japan.[172] Microsoft can choose to accept a consent decision before such final adjudication.[173] Otherwise, it will have to wait until the end of the hearings to appeal the final decision to the Tokyo High Court.[174]

The JFTC's adjudication process proceeds slowly through many different phases.[175] As a result, Microsoft can expect a long battle over the legality of its NAP provisions in Japan. The company risks further damage to its image due to continued media coverage. However, the economic and legal implications tied to the removal of the provision from existing contracts necessitates Microsoft's continued defense of it.

## V. MICROSOFT'S REACTION TO THE JFTC DECISION POTENTIALLY OPENS A PANDORA'S BOX OF PROBLEMS

Microsoft has taken a stand against the JFTC and continues to tout the legality of the NAP provision.[176] Japan's public rejection of the provision could lead to potential problems for Microsoft on a global scale.[177] The public scrutiny may cause other countries to examine the use of Microsoft's NAP provision under their own antitrust regimes. Although a provision similar to the NAP provision was upheld in the European Union, the European Court of Justice noted that it would utilize a case-by-case approach to analyze its validity.[178] This suggests that the European Union may still invalidate a provision inhibiting competitive behavior by a licensee as a violation of EU antitrust law, although the European Commission

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[172] HALEY, *supra* note 22, at 121-24. *See supra* Part III for a discussion of the general process and procedures involved when the JFTC brings an action against an Antimonopoly Act violation.

[173] See IYORI & UESUGI, *supra* note 19, at 226-27.

[174] HALEY, *supra* note 22, at 122.

[175] *See* HALEY, *supra* note 22, at 116-25 for a discussion of the different phases of a JFTC investigation and adjudication.

[176] *See* Statement by Microsoft, *supra* note 8.

[177] The JFTC's scrutiny of Microsoft comes immediately after Microsoft was fined a large sum and ordered to alter the way it deals with OEMs in the European Union. *See* Commission Decision of Mar. 24, 2004, Case COMP/C-3/37.792 Microsoft. The European Commission Decision came shortly after Microsoft was convicted of antitrust violations in the United States. *See* U.S. v. Microsoft Corp., 253 F.3d 34 (D.C. Cir. 2001). However, Microsoft is usually able to settle in these situations. While the JFTC may force Microsoft to moderate its behavior, a fine is unlikely. *See e.g.*, Microsoft Joint Status Report, *supra* note 31 (displaying the United States judgment and settlement agreement which did not include a fine); *Anti-trust Battles Leave Microsoft Dented but Undefeated*, S. CHINA MORNING POST, Mar. 2, 2004, at 2; Yuri Kageyama, *Japan to Warn Microsoft, but Fine Unlikely*, CHI. SUN-TIMES, July 10, 2004, at 32 (indicating that the JFTC is unlikely to fine Microsoft).

[178] *See* Case 66/85, Bayer AG v. Sullhofer, 1988 E.C.R. 5287, 4 C.M.L.R. 182 (1988).

neglected to challenge the NAP provision when it recently charged Microsoft with massive antitrust violations.[179] This could lead to a major backlash against the NAP provision and an order to remove it from Microsoft's licensing agreements in Europe.

In addition to the potential legal ramifications, practical perils also exist. If Microsoft uses its clout to fight the JFTC over the legality of a provision that it has already removed from future contracts, it could appear to be harassing the JFTC. The legal battle has already begun to damage Microsoft's image in Japan and abroad.[180]

Although Microsoft's decision to fight the JFTC caused negative publicity, the company has many valid reasons for defending the NAP provision. While it is unlikely that the United States would challenge the NAP provision because it already had the opportunity and decided not to pursue it,[181] regulatory agencies in other countries may feel compelled to examine the provision should the JFTC find it to be illegal. Microsoft would not have the opportunity to renegotiate existing contracts and bring them in line with future agreements. There could potentially be an onslaught of litigation by OEMs worldwide should Microsoft be forced to remove the provision from existing contracts in Japan.

### A. *The JFTC Targeted Microsoft Because of Its Size in an Attempt to Encourage Development and Innovation*

There are a number of reasons why the JFTC may have targeted Microsoft. First, it is likely that the JFTC's decision to target Microsoft stems from the company's command of a majority of the PC market share in Japan. The JFTC's challenge originated with an engineer at a Japanese OEM, who issued a complaint claiming the company's technology was potentially appropriated and used in Microsoft's Windows operating systems and media players.[182] Others subsequently lodged similar complaints regarding the NAP provision in Microsoft's contracts,[183] indicating that, because other operating systems are rarely used, they feel the need to obtain the license for the Windows operating system in order to be competitive in the market.[184] This is akin to Microsoft using its dominant bargaining

[179] *See* Commission Decision of Mar. 24, 2004, Case COMP/C-3/37.792 Microsoft.
[180] Kageyama, *supra* note 137.
[181] *See* Microsoft Joint Status Report, *supra* note 31, at 7; U.S. v. Microsoft Corp., 253 F.3d 34, 61-62 (D.C. Cir. 2001).
[182] *See FTC Orders Microsoft to Stop Restrictive Licensing Practices*, NIKKEI REPORT, July 14, 2004.
[183] *See* JFTC Press Release, *supra* note 2.
[184] *Id.*

position and virtual monopoly of the market to get OEMs to sign its licensing agreement.[185]

Second, the NAP provision could give Microsoft an advantage by quelling initiative for development of new technology.[186] This way, Microsoft ensures that its technology will be the most advanced on the market and licensees will continue to need it. The JFTC may have targeted Microsoft because of the PC manufacturers' perceived need to use Microsoft technology. Microsoft software is used in ninety to ninety-five percent of the country's personal computers, and many PC manufacturers feel they need to offer it to consumers to compete in the market.[187] This command of the market reflects Microsoft's great market power. However, even if manufacturers feel compelled to utilize Microsoft's software, many of them are also very large companies that command a great deal of bargaining power.[188] They generally have significant leverage to negotiate favorable deals for themselves. Microsoft's inclusion of the NAP provision may actually serve the interests of both Microsoft and its licensees by keeping transaction costs down and making the licenses more affordable.[189]

Third, the JFTC's decision on NAP provisions may also be motivated by a desire to have a moderating effect on the company.[190] Under this rationale, Microsoft might choose to moderate its behavior and allow manufacturers more leverage in negotiating licensing agreements and asserting their patent rights in order to avoid any adverse publicity related to anticompetitive behavior. The recommendations and hearings may have such an effect even if the JFTC never renders a final decision in the matter. The JFTC publishes its recommendations and accompanying media report. This adverse publicity may be a deterrent in and of itself.[191]

Fourth, the JFTC may be focusing on Microsoft due to its desire to foster the development and growth of other software companies so that manufacturers are not as dependent on Microsoft technology.[192] Perhaps the JFTC wants to curb potentially monopolistic behavior and give other systems like Linux the opportunity to gain a foothold in the market. Indeed,

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[185] *See* GENERAL DESIGNATIONS, *supra* note 24, at 3-4.

[186] *See* JFTC Press Release, *supra* note 2, at 3-5.

[187] *Id.* at 2-3.

[188] Japanese PC manufacturers include large, powerful companies such as Toshiba, Fujitsu, Sony, Sharp, Mitsubishi and Hitachi, among others. *See* John Boyd, *From Chaos to Competition: Japan's PC Industry in Transformation*, COMPUTING JAPAN ONLINE, Apr. 1997, *at* http://www.cjmag.co.jp/magazine/issues/1997/apr97/chaos.html (last visited May 31, 2005).

[189] *See* JFTC Press Release, *supra* note 2; Nakamoto, *Microsoft is Told to Alter Policy*, *supra* note 21.

[190] *See Anti-trust Battles Leave Microsoft Dented But Undefeated*, *supra* note 177.

[191] HALEY, *supra* note 22, at 170.

[192] JFTC Press Release, *supra* note 2, at 4-5.

some PC manufacturers are starting to use Linux and other open source[193] software, which are steadily gaining popularity.[194]

The JFTC's focus on Microsoft comes from a desire to make the company an example and force other companies to reevaluate the use of the NAP provision in light of their bargaining positions. There is a chance that the JFTC's scrutiny of Microsoft's NAP provision could lead to an examination of provisions used by other software companies. However, unless the company possesses a significant market share or aggravating circumstances exist, giving it a dominant bargaining position or coercive power, it is unlikely that the JFTC would look closely at its licensing agreements.[195]

Finally, very few actions are *per se* illegal under the Antimonopoly Act.[196] The JFTC evaluates most intellectual property licensing restraints under the rule of reason.[197] This means that restraints are not illegal by themselves: other circumstances[198] must exist resulting in the alleged unfair trade practice restricting competition.[199] In Microsoft's case, its control of the market ensures that PC manufacturers need to license Windows software in order to compete with other OEMs and sell their product. By vociferously pursuing the use of NAP provisions despite Microsoft's agreement to remove it from future licensing agreements, the JFTC is making Microsoft an example to send a message to other companies with large market shares that they are not exempt from scrutiny under the Antimonopoly Act.[200]

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[193] "Open source" refers to software and operating systems whose programming source code is available to the customer. Open source software makes it easier for manufacturers to alter the programs to work more efficiently with their computers. See Commission Decision of Mar. 24, 2004, Case COMP/C-3/37.792 Microsoft, at 10-11 for a description of open source software.

[194] *See* Kevin O'Brien, *New Wave Hits Software Industry: Open-source Pioneers Shake Up Bigger Rivals*, INT'L HERALD TRIB., Nov. 30, 2004, at 1 (noting Microsoft's announcement of a decrease in sales and revenue due to the increasing market acceptance of open-source software like Linux); Clement Teo, *Living with Linux*, NETWORK COMPUTING ASIA, July 2, 2004 (indicating growth statistics for Linux).

[195] GUIDELINES FOR PATENT AND KNOW-HOW LICENSING, *supra* note 16, at 18-19.

[196] *See* Newberg, *supra* note 72, at 739-41. Newberg notes that licensing restraints that may constitute unfair trade practices are divided into different categories depending on the likelihood that they are a violation of the Antimonopoly Act. *Id.* NAP provisions are found on the "grey" list, indicating that they are not a *per se* violation. *Id. See also* GUIDELINES FOR PATENT AND KNOW-HOW LICENSING, *supra* note 16; Antimonopoly Act, *supra* note 3, § 2(9).

[197] Newberg, *supra* note 72 at 746.

[198] Circumstances such as a dominant bargaining position or an additional clause lengthening the effectiveness of the restraint beyond termination of the license increase the chance of a finding that the restraint is an unfair trade practice. *See* GUIDELINES FOR PATENT AND KNOW-HOW LICENSING, *supra* note 16, at 17-19.

[199] GUIDELINES FOR PATENT AND KNOW-HOW LICENSING, *supra* note 16, at 18-19.

[200] *See* Statement by Microsoft, *supra* note 8; Statement by Microsoft II, *supra* note 141.

Therefore, Microsoft's command of the market and the extended duration of the NAP provision beyond termination of the license combined to encourage the JFTC to challenge Microsoft.

### *B. The JFTC Crackdown May Negatively Affect Microsoft in Several Ways*

More adverse publicity could call attention to Microsoft's NAP provision elsewhere in the world because the JFTC's decisions are made public. Shortly after the U.S. Department of Justice looked into Microsoft's software bundling and tying practices in the United States, the European Commission began looking into similar practices in the European Union.[201] While this may not have been the EU's only reason for its examination of Microsoft's practices, the timing coincided with the U.S. scrutiny of Microsoft.

Should Japan find the provision to be illegal, other countries may follow suit. This could lead to numerous lawsuits in countries with more stringent systems for punishing antitrust violations.[202] In order to avoid this, Microsoft should continue to defend the NAP provision.

### *C. Removing the Provision from Existing Contracts and Licensing Agreements Has Potential Legal Implications*

Because Microsoft is such a large company, it appears that the NAP provision may have outlived its original purpose. Microsoft now holds a large number of patents and has developed to the point where other methods of protecting itself, such as cross-licensing agreements, are just as useful.[203] In a cross-licensing agreement, the licensee company allows Microsoft to use its technology in exchange for using Microsoft's software.[204] Under such reciprocal arrangements, neither company can sue for patent violations. Microsoft itself has indicated that the NAP provision is no longer as useful for the company as it once was.[205]

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[201] *See* U.S. v. Microsoft Corp., 253 F.3d 34, 58-62 (D.C. Cir. 2001); Commission Decision of Mar. 24, 2004, Case COMP/C-3/37.792 Microsoft.

[202] HALEY, *supra* note 22, at 115-20. The Antimonopoly Act does not provide criminal sanctions for violating the unfair trade practices provision. *Id.* at 72. Instead, it provides for open-ended remedial powers rather than fines as the enforcement mechanism of choice. *Id.* at 144. Rarely do JFTC cases proceed beyond the initial stages. Most of them are settled within the first phases of JFTC action. *Id.* at 116.

[203] *See FTC Orders Microsoft to Stop Restrictive Licensing Practices*, *supra* note 182.

[204] *See* BATTERSBY & GRIMES, *supra* note 27, § 4:20.

[205] *See* Statement by Microsoft, *supra* note 8; *FTC Orders Microsoft to Stop Restrictive Licensing Practices*, *supra* note 182.

The question remains as to why Microsoft is reluctant to remove the NAP provision from existing contracts if changes in the information technology marketplace render the provision unnecessary.[206] Microsoft may want to ensure that the NAP provision is validated in order to foreclose attempts by other governments to challenge it under their antitrust laws.

Another reason for Microsoft to pursue the issue is that removal of the NAP provision from existing licensing agreements or a finding of illegality could make Microsoft vulnerable to lawsuits for patent infringement.[207] The company is currently creating a new intellectual property policy and expanding licensing of intellectual property rights.[208] This new policy will likely include protections that create an effect similar to that of the NAP provision, but without the severe limitations on licensees. However, the agreements currently in existence do not include any protections in accordance with the new policy. Microsoft would not have the opportunity to renegotiate existing agreements once it removes the NAP provision. Thus, a finding of illegality could cause PC manufacturers and OEMs to look for their proprietary technology in the Windows operating system, potentially leading to patent infringement actions against Microsoft.

Yet another possible adverse reaction could be lawsuits against end users, consumers, or other intermediary licensees of Microsoft's technology. Individual technology developers and companies could sue the customer for using patents they did not purchase or license. When a consumer buys a computer, he is paying only for the license to the software and not for any of the technology that is incorporated into the operating system. While this is not likely to happen, the possibility of consumers being vulnerable to patent infringement lawsuits still exists.

Removal of the NAP provision could lead to increased transaction costs and a subsequent increase in the price of a technology license.[209] Additionally, removal of NAP provisions from existing contracts could have particular effects in Japan. The JFTC action against Microsoft already garnered so much publicity[210] that a finding that the NAP provision is illegal, followed by its subsequent removal, could lead to a flood of scrutiny of

[206] *See* Statement by Microsoft, *supra* note 8 (noting changes in the information technology marketplace led them to change their licensing policies).

[207] *See Japan Raid Seen to Affect Microsoft's Fight With Linux*, JIJI PRESS ENGLISH NEWS SERVICE, Feb. 26, 2004.

[208] Statement by Microsoft, *supra* note 8.

[209] *See* BRUNSVOLD & O'REILLEY, *supra* note 7, at 17; Nakamoto, *supra* note 32.

[210] *See* Nakamoto, *supra* note 21.

license agreements and a potentially large number of lawsuits.[211] Because of the widespread potential negative effects tied to a finding of illegality, Microsoft should continue to defend the provision and appeal any unfavorable rulings.

### D. *Removal of the NAP Provision May Allow PC Manufacturers and Other OEMs to Negotiate More Favorable Licensing Agreements*

The removal of the NAP provision could benefit PC manufacturers, but might cause problems for Microsoft. Individuals and companies may be able to negotiate more favorable licensing and royalty agreements.[212] However, many of these companies' bargaining positions rival that of Microsoft.[213]

Eradicating the NAP provision in existing and future contracts could lead to more technological development with the knowledge that the results are protected from unauthorized use.[214] The JFTC enforces the Antimonopoly Act to foster competition and allow for the development of new technology and growth.[215] One of the concerns regarding the NAP provision is the creation of a disincentive to develop new technology.[216] If proprietary technology can be incorporated into Microsoft's software without royalties or the ability to assert patent rights, there is less incentive to create any new technologies.[217] However, NAP provisions are sometimes reciprocal and also protect the licensee. In current licensing agreements, should the provision be removed, licensees will also be open to litigation.

Another concern of the JFTC and PC manufacturers is that existing licensing agreements give Microsoft access to information about new technology developments that it could incorporate into its software without having to pay royalties.[218] The NAP provision could also give competitors using Windows operating systems access to the OEM's proprietary

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[211] *See, e.g.*, JFTC Press Release, *supra* note 2, at 3 (noting that a number of Japanese OEMs fear their patents are being infringed upon by Microsoft).

[212] *See, e.g.*, JFTC Press Release, *supra* note 2, at 3-4 (noting that numerous OEMs felt compelled to accept the NAP provision despite its disadvantages).

[213] PC manufacturers include Fujitsu, Hitachi, Sony, and Toshiba, all large companies in their own right. *See* Yoshiko Hara, *Intel Gains Extension in Japanese Antitrust Probe*, INFO. WEEK, Mar. 18, 2005, *available at* http://informationweek.com/story/showArticle.jhtml?articleID=159902444 (last visited Apr. 6, 2005).

[214] *See* JFTC Press Release, *supra* note 2, at 4-5.

[215] For a description of the purpose of the Antimonopoly Act and the JFTC's enforcement, see *supra* Part III.B.

[216] JFTC Press Release, *supra* note 2, at 4.

[217] *Id.*

[218] *Id.*

technology.[219] There is no indication that any of these unsavory circumstances have occurred.[220] Investigators have no evidence that Microsoft has violated any OEM patents.[221]

Although removal of the NAP provision may aid PC manufacturers, many of them possess formidable bargaining power as well. The benefits of leaving the provision in existing licensing agreements far outweigh immediate detriments to Japanese OEMs that would ensue from its removal. Microsoft's decision to fight the JFTC seems logical in light of the potential problems that might occur should the provision be removed from existing licensing agreements.

### E. *The Overall Benefits of the NAP Provision Outweigh Any Potential Setbacks in Innovation*

Discontinuing the provision in existing contracts is likely to produce unfavorable results overall. Although it rehabilitates Microsoft's image and demonstrates that the company is willing to acknowledge PC manufacturers' proprietary interests and patent rights, it opens up a Pandora's Box of problems. Additionally, the OEMs are often large companies with bargaining power of their own. Removal of the provision from existing contracts could give them carte blanche to use their power against Microsoft and sue the company for whatever potential patent infringements they can find. Also, the NAP provision must be preserved for the use of smaller companies that truly need its protection.

Removal of the provision might cause other countries to examine the NAP provision.[222] If the NAP provision is found to be illegal under the Japanese Antimonopoly Act, it might pose problems for Microsoft. It could then be questioned on a global scale.

Microsoft could continue to contest the decision and eventually appeal to the Tokyo High Court. However, the JFTC is unlikely to pursue the case to this extent.[223] Most cases are settled in the initial, less formal phases of the JFTC's process.[224] Also, a finding upholding the provision would be worth any legal costs or negative publicity. Therefore, Microsoft should

[219] *See* Kageyama, *Japan to Warn Microsoft*, *supra* note 177.
[220] *See* Kageyama, *Japan Orders*, *supra* note 43, at 78.
[221] *See* Kageyama, *Drop Contract*, *supra* note 135; JFTC Press Release, *supra* note 2.
[222] For example, Japan's scrutiny of Microsoft comes right after the European Commission levied a hefty fine on the software company for engaging in anticompetitive practices. *See* Commission Decision of Mar. 24, 2004, Case COMP/C-3/37.792 Microsoft.
[223] *See Following Europe, Japan Takes Aim at Microsoft*, PROVIDENCE J., Apr. 4, 2004, at JO3 (noting that a fine is unlikely).
[224] HEATH, *supra* note 22, at 48.

continue to defend the provision and ensure that it stays in existing licensing agreements.

Microsoft should continue the battles with antitrust officials to protect itself from a great volume of potential litigation.[225] Continuing to fight the JFTC decision might damage its reputation in Japan.[226] Microsoft's Japan unit acknowledged that "the U.S. software giant's battle with Japanese anti-monopoly authorities over a controversial licensing clause has hurt its corporate image here."[227] However, the damage is likely nominal and not a crucial issue.[228] Despite such damage to its image, the best plan would be for Microsoft to defend the utility of NAP provisions.

## VI. CONCLUSION

Non-assertion of patents provisions can provide valuable protection and prevent unnecessary and potentially costly patent infringement lawsuits by protecting licensors from suit and causing licensees to consider potential patent issues before signing the licensing agreement. However, when a company has grown to a point where it can protect itself in other ways and has gained virtual control of the market, a NAP provision provides less utility. Microsoft's use of NAP provisions in its licensing agreements with Japanese PC manufacturers is likely an unfair trade practice under the Antimonopoly Act. Microsoft controls a large portion of the market and could be construed as having a dominant bargaining position.

Nevertheless, Microsoft should continue to fight the JFTC. A formal finding of illegality could lead to a potential outbreak of antitrust scrutiny of the provision. Microsoft cannot renegotiate existing licensing agreements should the provision be removed. As a result, it could be vulnerable to an onslaught of litigation from OEMs. These often-large PC manufacturing companies might use a formal finding of illegality as the opportunity to search for any potential patent infringement in order to bring lawsuits against Microsoft. While removing the non-assertion of patents provision may encourage innovation, leaving it in existing agreements does not necessarily prevent competition.

Perhaps the most important reason to defend the NAP provision is its continued utility to many companies. Although Microsoft has indicated it

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[225] *See* The Associated Press, *Microsoft Mounts Defense of Clause*, SEATTLE TIMES, Oct. 26, 2004, at C3 (noting that the NAP clause protects Microsoft from potential patent infringement lawsuits).

[226] Kageyama, *supra* note 137.

[227] *Id.*

[228] *Regulators Conduct Search of Microsoft's Office in Tokyo*, *supra* note 1.

will no longer use the provisions in future licensing agreements, this does not mean that the NAP provision will not have utility for some companies. NAP provisions keep transaction costs down, ensure that licenses will be affordable, and protect everyone from costly and potentially unnecessary patent litigation. To protect itself from potential problems and ensure that others may use the provision in the future, Microsoft should continue to fight the Japan Fair Trade Commission and defend the legality of the non-assertion of patents provision in existing licensing agreements.