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Antitrust and Direct Regulation of International Transfer of Technology Transactions: a Comparison and Evaluation, by Guillermo Cabanellas, Jr.

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II. PRIVATE INTERNATIONAL LAW

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ANTITRUST AND DIRECT REGULATION OF INTERNATIONAL TRANSFER OF TECHNOLOGY TRANSACTIONS: A COMPARISON AND EVALUATION (Vol. 7 of Studies in Industrial Property and Copyright Law). By Guillermo Cabanellas Jr. Munich, West Germany: Max Planck Institute for Foreign and International Patent, Copyright and Competition Law, 1984, 175 pp., $26.00.

This excellent, tightly written handbook of the provisions and significance of technology transfer importation regulatory systems and their comparison with similar provisions of antitrust regulation demonstrates two theses. First, the regulation of technology transfer by technology importing countries can only be successful if it forms an integrated part of a full and fairly strict regulatory scheme over foreign investment, currency exchange, and imports with appropriate taxing mechanisms. Second, partial regulation focusing solely on technology transfer is more likely to defeat the policy aims of the importing state than to further them. Indeed, the author claims that most of these policy aims can be sufficiently dealt with by antitrust regulation. In the course of demonstrating this thesis, the author, an assistant professor at the University of Buenos Aires, makes a fairly complete survey of the elements of technology transfer regulation by importing countries, analyzes the economic effect of technology transfer regulation and compares that effect with their intended purpose. The author then compares the intended purpose of technology transfer regulation with that of antitrust regulation.

In general, the intent of these two kinds of regulation is quite different. Technology transfer regulations attempt to equalize the bargaining power of the licensor and licensee of technology. They assume that the licensee, almost always from a less developed country, has inferior bargaining power because of his need for the superior technical knowledge and skill of the licensor. These regulations seek to promote the national aims of technological and economic development and to render the country competitive in the international marketplace. They do this by imposing conditions on the enforceability of technology licenses and other such agreements.

Antitrust regulations, on the other hand, are concerned with redressing inequities in bargaining power between a licensor and licensee of technology only when the licensor uses his technical power to distort competition, fix prices, or allocate the market. Antitrust legislation is not primarily concerned with the relationship between licensors and licensees of technology, but with the effects such licensing may have on competition in the relevant market. This concern means that antitrust authorities focus on the effects a business transaction exerts on competitors and customers both in and outside the regulating country rather than the effect a technology transfer agreement exerts on economic development.

The most obvious significant difference between technology transfer regulation and antitrust regulation lies in their screening procedures. Almost all technology transfer regulation systems require a review of agreements by an administrative agency. The penalty for failure to obtain this official clearance may include denial of foreign exchange approval for the remittance of fees and royalties and denial to the licensee of the business deduction of the fees and royalties from its taxable income. Further, an unreviewed agreement may not be enforceable in the courts of the host country. Antitrust statutes generally do not provide for the screening of suspect transactions, although there are notable exceptions. (The Federal Trade Commission and the Department of Justice will give review letters of proposed mergers in the United States. In Europe, the EEC Commission handles requests for negative clearances of transactions which might contravene Article 85 of the Treaty of Rome.)

This difference in screening procedures highlights the difference in enforcement procedures between these two systems. Under technology transfer statutes, the enforcement action, such as it is, consists of a registration requirement and negotiations between the public agency and the private parties prior to the agreement's validity. The agency's review rarely goes beyond the terms of the written agreement and is a formal affair. There is, thus, no possibility for a review of the parties' actual conduct, a function which, in any event, most of these agencies would not be in a position to fulfill. Enforcement under antitrust statutes is concerned more with the conduct of the parties than with their written agreements.

Technology transfer regulatory schemes attempt to control the outflow of foreign currency, to prevent tax avoidance, to favor local nationals over foreigners in respect to industrial property rights, to control the nature and kinds of imported technology as part of a coherent plan of economic and technical development and, in a similar vein, to control foreign investment. But none of these aims is pursued by antitrust regulation, though both antitrust and technology transfer regulations seek to discourage concentration of economic power in a few hands.

The level of fees and royalties paid by the licensee to the licensor has always been a major issue in technology transfer regulatory schemes. This concern is also reflected in national policies to protect the foreign exchange position of the host country, which furthers economic development at a reasonable cost and enables the host country to compete in the international marketplace. Antitrust legislation also deals with royalties, but only to prevent discrimination between different licensees, and to prevent price-fixing by the licensors.

In a carefully argued economic analysis of the effect of regulations on different aspects of technology licenses, the author demonstrates his central thesis that much legislation does not have the desired effect of improving the bargaining position of the licensee (and thus of the host country in carrying out its economic development program). Rather, it adversely affects the licensee's position.

The price of technology is set through a different market mechanism from that for goods because normally the technology itself is not sold. Only its use is "sold." Therefore, the very same technology, unlike goods, can be made available to numerous parties; and the incremental cost to the licensor by doing so is negligible.

Much technology transfer regulation is predicated on the notion that the licensor is a monopolist (he is the only one who owns and may dispose of the subject technology) and can, therefore, charge any price he wants. Therefore, because the licensee is thus confronted with a "take-it-or-leave-it" situation, the intervention of the state is required. But actually, the situation is quite different.

The author demonstrates that the licensee often has several sources for the technology. The licensor's patents frequently do not give him much of a monopoly over the licensed field of use. In granting a license, the licensor runs the risk of creating a potentially strong competitor and losing markets. He may also be creating liabilities for himself by virtue of warranty obligations imposed by law. Finally, there is a limit to what a licensee is willing to pay (based on what it would cost him to obtain a similar technology from other sources) and, more importantly, a limit on what the licensee can pay. The licensee will not pay more for royalties than he can recover from the share of the market he can capture for the resultant product, given the price structure for the product in that market.

This summary is necessarily a great simplification of the author's argument but his point is that market forces within and without the host country are far more likely to rein in the rapaciousness of the foreign licensor and thus advance the economic goals of the host country than are the blandishments of government bureaucrats. Further, these bureaucrats ordinarily will be far less familiar than the licensee with the nature of the technology and market conditions because they have neither the time nor the resources to formulate an informed business judgment. Someone risking his own capital, however, must accurately assess the market or face financial loss.

These market forces then establish a price, or royalty, floor beneath which the licensor finds it unprofitable to enter into the transaction, because his risks are not compensated for by the royalties. Similarly, the market determines a royalty ceiling above which the licensee cannot or will not go. State intervention, in tampering with this mechanism, does not drive the "floor" down as it is intended to do. Instead, by making the terms of the license more onerous for the licensor and thereby increasing his risks, it drives the "floor" upwards and defeats the transaction by causing the licensor to refuse to go forward. This either deprives the host country of the particular technology (forcing it to import expensive goods) or makes it necessary to develop the technology indigenously, a solution which is almost always more expensive than importing the technology.

The author argues that the best way for the state to exercise control over royalty rates is to tax the royalty to the foreign licensor at the same rate charged on dividend, interest or other income earned by foreign nonresidents. Because the market will establish a "ceiling price" for royalties, this tax on the foreign remittance will be a net gain to the host country. And, if the tax rates for all foreign remittances are uniform, the parties to the license will have no interest in camouflaging royalty income in order to benefit from a better tax rate.

Despite the small size of this book, the author touches on all the major issues of technology transfer transactions. These include regulation of trademark licenses as well as the nature and extent of technology, measures to protect local technology, the imposition of warranty requirements on the licensor and limitations on post-expiration restrictions on the licensee's use of the technology. The book deals at length with the interesting but rarely litigated requirement that the laws and courts of the host country govern the agreement.

With regard to each of these issues, the author effectively demonstrates that most technology transfer legislation does not achieve its objective of securing better licensee bargaining positions, unless the host country has a complete and rigorous system of controls over foreign exchange, imports, and foreign investment. Generally, this conclusion is based on the effect such regulation has in raising the "price" for the technology to levels which discourage licensors from entering into agreements. The author argues that the state should play a different role in regulating technology transfer. First, through the laws of contract, it should seek to insure that agreements are not entered into on the basis of false representations. It may seek assurances of the value of imported technology and assure compensation to injured licensees by imposing civil liability on licensors for damages they cause the licensees. Secondly, through antitrust legislation, the state should try to prevent restrictions to free entry to the marketplace, particularly for its own citizens.

The author's argument that the state ought to rely on antitrust regulation overlooks the fact that such regulation is often not effective either because enforcement mechanisms are not adequate to the task or because enforcement is not coordinated with overall economic and social policy. The author does not examine whether the suppositions underlying antitrust legislation are economically correct or whether such systems achieve their objectives. Despite the fact that those are questions for another book, a negative finding respecting the economic efficacy of antitrust legislation might require a reconsideration of the thesis of this book.

A patient and careful reading of this work will be rewarding for anyone interested in technology transfer, particularly where the Third World is concerned, because of the cogency of its arguments and its explanation of the major elements of technology transfer regulation. The author's command of the English language is impressive, and the book contains a lengthy bibliography.

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