

JAPAN ECONOMIC CURRENTS

A COMMENTARY ON ECONOMIC AND BUSINESS TRENDS

Strengthening Japan's Anti-Monopoly Law

by Masao Kobayashi, Nippon Keidanren

The Japan Fair Trade Commission (JFTC), the official Japanese government agency charged with enforcing laws regarding illegal monopolistic practices, such as price and quantity cartels and bid-rigging, attacks its targets by imposing criminal penalties and cumulative surcharges.

The JFTC is preparing a bill to amend the decades-old Anti-Monopoly Law which, if enacted by the Diet, would change the surcharge system and introduce new regulations to Japan's public utility service sector.

But the JFTC's proposal is legally flawed and premature and a number of questions posed by various groups have yet to be answered. Nippon Keidanren places a high priority on competition policy – in an environment in which deregulation and liberalization of governmental rules are underway, coupled with free competition and the need for tighter corporate discipline,

Japan's Anti-Monopoly Law must be drastically and comprehensively overhauled.

JFTC's counterparts have different tools in their anti-monopoly arsenals. The EU charges only an administrative fine against legal entities that engage in illegal cartels, and disputes between the administration and parties are judicially settled. The United States treats cartels under criminal law. Japan's Anti-Monopoly Law differs from the rest of the world in that it applies administrative measures, such as surcharges and criminal penalties, concurrently.

In Japan, government agencies or local governments can impose sanctions on parties that violate provisions of the Anti-Monopoly Law that are specifically related to biddings on public works, such as disqualifying the parties for the bidding, withholding subsidies, or exacting damages for breach of contract. These various deterrent measures should be comprehensively re-evaluated so that the sanctions are calibrated to the violation.

But the JFTC's proposed revisions to the Anti-Monopoly Law merely revise the surcharge

system under the weak assumption that the stronger the sanctions, the fewer the violations.

JFTC'S PROPOSALS

(1) An unclear basis for calculating the amount of surcharges

The surcharge system was introduced in a 1977 revision of Japan's Anti-Monopoly law because heretofore there had been few criminal indictments and the heavy burden of proof in civil cases for damages had not provided much deterrent. Nor did merely eliminating a bidder from consideration in a tender kill a cartel because undue economic gains remained in the pockets of wrong doers. The introduction of surcharges were intended to transfer those ill-gotten gains to the national treasury.

The Anti-Monopoly Law Study Group's October 28, 2003 report indicated that, "Compensation for the loss of social welfare is the fundamental basis of the proposed nature of the surcharge system." The losses to social welfare include:

(i) the dead weight loss stemming from the loss of opportunity for consumers to purchase merchandise or services because of price increases greater than those that would have

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been offered under free competition and (ii) the increases in the prices of like-kind commodities.

It is entirely unclear how JFTC's imposition of sanctions will compensate for "actual losses" of social welfare in any particular case.

(2) Surcharges and criminal penalties must be adjusted

According to JFTC's proposal, in the event of repeated violations or violations over a long period of time, the JFTC can impose additional surcharges. The JFTC has long maintained that, "Surcharges have been only an administrative measure aimed at automatically confiscating gains made through illegal cartels. Therefore, even if surcharges and criminal penalties are levied concurrently in the same case, it does not constitute the double jeopardy, as prohibited by Article 39 of the Japanese Constitution."

But the proposed new surcharges are indeed sanctions rather than a confiscation of ill-gotten gains. In addition, if "the power for compulsory investigation" is given to JFTC, the aim, objectives, and procedures of the surcharge system would be identical to those concerning criminal penalties.

The JFTC's proposed review of the surcharge system does not explain how its functions differ from

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those of criminal penalty system. Indeed, it only promises to "fully review" the states that correlation between surcharges and criminal penalties against the legal entity and provides no concrete explanation about how this goal is to be accomplished.

JFTC Chairman Kazuhiko Takeshima said on December 24, 2003, that the reason for the coexistence of surcharges and criminal penalties is that "Criminal indictments have been very rare; and it will probably remain so in the future." In order to levy criminal penalties, hard proof of an actual violation is required. But clearly, JFTC's hidden aim is to change surcharge system so that it can impose surcharges, instead of criminal penalties by lightening the burden of proof.

(3) There is no rationale for an expansion of the surcharge coverage

The JFTC's proposal holds that, in addition to price/quantity cartels, the following are subject to the surcharges: 1) monopolies and cartels to restrict price, supply quantity, suppliers, etc, 2) monopolies and

unfair trade restrictions aiming at eliminating competitors, and 3) purchasing cartels.

But if, in addition to elimination measures, new surcharges are to be levied, there must be adequate reasonable explanation as to the need and basis for them. JFTC provides no clarification as to how the "loss of social economic welfare" is manifested nor does it explain on what basis, other than the loss of social economic welfare, surcharges are to be levied.

(4) Studies on additional percentage Surcharge system and leniency program is not sufficient

The JFTC says it will introduce a system to reduce or eliminate the surcharges if cartel participants submit explanatory information and documentation to the Commission prior to the commencement of its detection (leniency program). But the requirement of the leniency program is unclear and cannot possibly function without the involvement of discretionary power on the part of the JFTC.

The Commission states that it will not seek criminal indictments

regarding those who step up to provide information. Questions remain, however – would this be guaranteed by law, or would it be a relinquishment of the exclusive right to press charges simply a matter of public policy? If the latter, legal implications, including what may be subject to criminal charges, have not been resolved at all.

If surcharges are characterized as part of sanctions, the leniency program ought to be reviewed in conjunction with the discussion of plea-bargaining system, within the context of reform of the judicial system. There is no reason whatsoever to introduce the leniency program as an administrative measure of the Anti-Monopoly law, preceding the introduction into the general judicial system.

(5) Evaluation and adjudication procedures should follow due process

If surcharges are indeed sanctions, it naturally follows that all investigations, hearings, and decisions conducted by the JFTC should be carried out according to due process. Furthermore, the principles of the judicial system (such as separation of personnel between the hearing examiners, who are relevant to executors in criminal procedure) and investigators (who are relevant to executors in criminal procedure), should apply. Both hearing examiners and investigators

should be required to pass the bar exam. Hearing examiners must be independent and their decisions must be respected by the Commission.

The JFTC's proposal maintains that, in addition to having existing authority to conduct administrative investigations, it should also have "the power for compulsory investigation." But it fails to specify how that would be accomplished beyond "ensuring due process and

efficiency." The strengthening of sanctions without guarantee of due process cannot be tolerated.

(6) In bid-rigging cases, bid-tenders should also be subject to punishment

In most bidding collusion cases, "government-created bid-rigging," under which the governmental agencies tendering the offer solicit bidders, has been very clear according to recent criminal cases.

Under the current anti-government-created bid-rigging law, if there is proof of solicitation by the agencies' personnel, the heads of the agencies must: (1) eliminate behavior leading to bid-

rigging or ensure effectiveness of the elimination measures ; (2) sue the personnel for damages; and (3) examine whether disciplinary action against the responsible official is possible. But the law does not criminally punish personnel involved in tendering orders, and therefore lacks in effectiveness.

In light of the huge success of the regulations (Article 497, Item 3 of the Commercial Code) designed to inhibit the *sokaiya* (corporate

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extortionists who ensure that shareholders' meetings go smoothly), Nippon Keidanren seeks the establishment of rules under the Anti-Monopoly Law that provide for the criminal punishment of public officials involved in "government-created bid-rigging."

NIPPON KEIDANREN'S PROPOSAL FOR AN OVERALL REVIEW OF THE ENFORCEMENT SYSTEMS

The JFTC's proposed revision of the Anti-Monopoly Law is inadequate and premature. In view of the lower House of

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JAPANESE AND US PATENT SYSTEMS

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On January 30, 2004, the day the Tokyo District Court awarded a former Nichia Chemical employee an astounding \$190 million in back-compensation for a blue LED (light-emitting diode) he had invented a decade ago, Japanese investor compensation law made headlines around the world.

The inventor, Shuji Nakamura, had received a \$200 bonus for his invention when he was an employee – one of the nearly 500 patent applications he had filed in the 20 years he worked for Nichia. Dr Nakamura, now a professor and director of the Solid-State Lighting Center at the University of California in Santa Barbara, said he was motivated to file for compensation because his former employer filed its own suit that sought to bind him to a non-disclosure clause Nakamura signed in 1977, effectively capping his employment prospects.

Nichia, a leading Japanese manufacturer of fine chemicals, immediately filed a challenge to the ruling. In its appeal, Nichia argues that the *Nakamura* decision may discourage research efforts in Japan for fear of having to pay large awards to future inventors of significant commercial motions that they may develop. Instead, Nichia posits, Japanese companies will logically conclude

that it would be safer to conduct the same research in a jurisdiction where such employee compensation laws do not exist.

EIGHT KEY DIFFERENCES BETWEEN THE US AND JAPANESE PATENT SYSTEMS

Employment Compensation. The *Nakamura* ruling could not have happened in the US because no similar law exists on the books (states have the statutory authority to act on employment compensation but no state has). Nor does the US have laws that look backwards in time to reward past innovation.

“There are eight key differences between the US and Japanese patent systems — how employee inventors are compensated, how patents are awarded, prior art, best mode, the patentability of business methods, the scope of patentability, costs, and invalidation procedures.”

The historical philosophy in the US is that the inventor’s salary is considered fair and reasonable compensation for any inventions created during a term of employment. Many American companies offer a supplemental bonus system as an incentive, but typically amount to about \$500 for an issued patent.

Japanese companies have historically awarded inventors a modest financial award for patent that is obtained. In a series of three court decisions – *Olympus*, *Hitachi* and *Nakamura* – the Japanese court system has interpreted a 1959 law (Patent Law Article 35) as voiding any provision in an employment agreement where the compensation originally given is “unreasonable,” given the amount of profits that the employer was later able to obtain. Employees or former employees are able to sue years later for a share of profits accruing from their inventions.

Awarding the Patent. Japan has a “first to file” system which awards patents to individuals or companies to the entity that files a patent application first, even if the innovations are created at generally the same time.

By contrast, the US has a “first to invent” system – patents are awarded to individuals or com-

“Patent ‘harmonization’ is a worthy and important goal that results in greater simplicity and lower costs of patenting around the world. The patent offices of the US, Japanese, and European governments regularly meet to improve harmonization.”

panies that created the invention first.

A “first to file” system, which is used by virtually every advanced country, is very simple to administer and all disputes of priority of invention are settled cleanly. The US’s unique “first to invent” system can be very difficult to administer and can create much business uncertainty.

The US Patent and Trademark Office (USPTO) is charged with determining which company or individual was the “first to invent” in an “interference proceeding.” An interference proceeding resembles a court hearing in many respects and uses the same rules of discovery and evidence. Not surprisingly, determining who was the “first to invent” often resembles a full-blown litigation – laboratory notebooks, memos and other documents are reviewed, depositions are taken, and legal briefs are prepared. A movement seems to be growing in the US to convert to a “first to invent” system.

Prior Art. The US system places a heavy burden on an applicant to specifically identify and alert the USPTO to any prior innovations that may affect the Patent Office’s decision to issue a patent. Patents are granted unless the application is an obvious variation something already protected by a patent; evidence of an earlier invention is called “prior art.” The Japanese system has no such requirement.

The thinking behind the US requirement is that the inventor is the best to know what prior art exists. Therefore, the public interest is served by requiring the inventor to tell the USPTO of earlier inventions that may adversely affect the USPTO’s decision whether to issue the patent.

Best Mode. US applicants are also required to disclose the “best mode” of making and using their invention. (The “best mode” can be loosely defined as the “best way.”)

In Japan, as in most of the world, there is no such requirement. The thinking behind the US provision is to ensure that the public fully

understands the invention so it can take advantage of its full benefits after the patent expires.

Business Methods. So-called “business methods” (software or some other technological invention that provides a business function, such as insurance, financial, and accounting services) are generally not eligible for patents in Japan but are clearly patentable in the US. This is different than the traditional patent protection given to physical products or industrial processes. In Japan, “business method” inventions can be patentable only if they are somehow tied to a computer or software.

Scope. A US patent is generally broader in its scope of protectable subject matter than is a Japanese patent. Protectable subject matter is set forth in a patent in numbered paragraphs called “claims.” The Japanese Patent Office charges according to the number of claims with each new claim being incrementally more expensive. Sets of claims from patent applications that were first filed in the US typically need to be cut down and narrowed so that the corresponding Japanese application is not prohibitively expensive. As a result, fewer claims generally appear in Japanese patents.

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LEGAL PRINCIPLE	JAPANESE SYSTEM	US SYSTEM
Employed Inventor Request to Compensation	Inventors can later sue for a share of a company's profits obtained from those their invention, to provide them "reasonable" compensation	No similar right to compensation exists
Disputes Involving Who Invented	"First-to-file" system	"First-to-invent" system
Duty to Disclose Prior Art	Inventors have no such duty	Strict duty exist
Duty to Disclose the "Best Mode"	No duty to disclose	Duty exists
Patentability of Business Method Patents	Difficult to patent	Patentable
Scope of Patent Subject Matter	Generally Narrower	More ability to be broader in scope
Cost of Getting and Keeping a Patent	Expensive	Not so expensive
Options to Invalidate a Wrongly Issued Patent	(1) An Opposition system; and, (2) Ability to challenge patent in court	(1) A "Reexamination" system (two different types); and, (2) Ability to challenge in court only if threatened or sued under the same patent

Costs. Japanese patents are generally more expensive to get and keep. In addition to the potentially prohibitive cost of additional claims, annual taxes (annuities) are due on pending applications and patents in Japan. Similar taxes are not annually required in the US and the cumulative amount of the fees is much lower. Roughly estimated, the average cost of getting and keeping a patent in the US is about \$25,000. The average cost in Japan is about double.

Invalidation Procedures. The US and Japanese systems differ in the manner in which wrongly-issued

patents can be invalidated. Japan has a post-grant challenge system where patents can be invalidated by a court. No special jurisdiction is required – anyone may challenge the patent based on evidence that it is invalid.

By contrast, the US does not allow a court-based challenge to the validity of a wrongly-issued patent unless a party has been threatened by the patent owner.

If there is no threat of litigation, a party's only option for challenging the patent's validity is a proceeding known as "reexamination," which must be filed with the Patent Office.

Reexamination is a proceeding for challenging a patent's validity in the US Patent Office, based on printed publications that pre-date the filing of the patent. A reexamination can be filed at only a fraction of the cost of patent litigation. It can be initiated at any time during the enforceable life of an issued patent.

There are two types of reexamination: *ex parte* and *inter partes*. An *ex parte* type of reexamination can be filed anonymously and at lower cost than an *inter partes* reexamination, but it permits less participation (fewer chances for the

requester to argue their case). On the other hand, while inter partes reexamination is more expensive and cannot be filed anonymously, it allows for greater participation on the part of the requester (i.e. a greater opportunity to argue the case to the patent examiner).

Reexamination is not without risk. If the patent's validity is upheld in the ex parte type of reexamination, it would be harder to invalidate that patent in subsequent litigation over the same or similar publications (though there should be no heightened presumption of validity as to other grounds not considered in the reexamination).

The inter partes type of reexamination carries an even greater risk because it imposes a statutory "estoppel" on the requester. The estoppel from an inter partes reexamination bars the requester from arguing invalidity based on the same publications in subsequent litigation, and even bars the requester from arguing invalidity on grounds that could have been raised during the reexamination. For these reasons, a party contemplating reexamination should carefully consider the risks.

HARMONIZATION BETWEEN THE SYSTEMS

The above eight divergences are a brief overview of some of the key

differences between the US and Japanese patent systems. Over the last 10 years, some significant differences between the US and Japanese systems have been identified and studied so that compromises might be forged to bring the major patent systems closer together.

This process is called "harmonization" and is generally considered a worthy and important goal that results in greater simplicity and lower costs of patenting around the world. Indeed the USPTO, the Japanese Patent Office, and the European Patent Office regularly meet to discuss harmonization through trilateral discussions. To date, some of the biggest compromises so far in "harmonization" have been made by the United States. For example, the US changed the life of a patent from 17 years from date of issuance to 20 years from the date of application, in order to set common standards with Japan and most of the world.

Also, pending US applications are now published 18 months after their first priority date, which is in line with other major patent systems, including Japan, who also publishes its own patent applications 18 months after their first priority date.

While some progress has been made towards harmonization, significant differences still exist between

the US and Japanese patent systems, as pointed out in this article. These differences create many pitfalls for Japanese companies who file for protection in the US because they are not accustomed to such practices as having to disclose the best mode of their invention in the US application (a practice which is completely unnecessary for obtaining a valid patent in Japan).

Accordingly, there remains a strong need to make further progress in the global quest for patent harmonization, so that all users of the patent systems in Japan and the US are subject to the same rules. ■

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Representative's Economy and Industry Committee April 17, 2002 resolution to "urgently review the overall enforcement systems concerning conduct in violation of the law, including surcharges, criminal penalties, and the investigative authority of the Fair Trade Commission, from the standpoint of strengthening effectiveness of the endorsement of the Anti-Monopoly Law," the Commission should review the overall enforcement systems – but this time adhering to fair procedures and transparency.

Keidanren believes that the current system, under which criminal penalties and surcharges

are levied concurrently, should be drastically revised to more resemble the EU-style "administrative fine." The relationship between administrative and criminal sanctions should be clarified, or at least in the cases in which the JFTC levies surcharge, concerned legal entities should not be charged with criminal penalties.

Above all, in order to protect citizens' fundamental rights and to ensure their understanding of the Anti-Monopoly Law, the JFTC should not revise the law immediately but instead to enhance its own legal/ personnel/ organizational system so that it can adequately support the strengthening

of the sanctions system itself, as well as to ensure strict and proper execution of the law. ■

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