

Licensing Technology into New Zealand

A paper and panel discussion of many aspects of Trans-Tasman licensing

BY PETER MAXWELL*

The terms, conditions and provisions of contracts concerned with the licensing of industrial property tend to vary as much as the commercial situations which led to the establishment of those contracts. It is not the purpose of this paper to attempt an orderly classification of these terms, conditions and provisions in so far as New Zealand is concerned; rather, I intend to restrict my discussion to a few areas which I believe will be of particular interest.

These areas include the Legal Restraints on Trans-Tasman License Agreements, Royalty Accruals, Taxation aspects and finally Trademark Licensing. In so far as the first and last topics are concerned, I will attempt to deal with them in a general way, but the infinite array of problems and possibilities arising with royalty and tax dictates that I must discuss specific examples and these are basically relevant to licenses between related companies.

LEGAL RESTRAINTS

Most countries impose, by statute and/or case law, a measure of restraint on the arrangements which parties may lawfully make with each other. A restraint of great importance to us all is the kind embraced by the American style of antitrust laws where any agreement tending to reduce competition between the parties is bad. Moreover, the use of the patent monopoly to restrain or control any activity other than patent rights themselves may be regarded as a misuse of the patent and hence contrary to antitrust law.

This kind of restraint is now to be found in Australia, but, as it is based on statutes which refer in the widest terms to monopolization and restraint of trade it is difficult to give a definitive statement of the law, or its effects, on this end of a Trans-Tasman License Agreement. However, a point never to be overlooked in the case of a patent license, is that the main purpose of the patentee must be lawful and if there is any resulting restraint of trade it must be merely ancillary to the main purpose.

The problem is made more thorny by the newness of the act and the consequent absence of case law for there is normally a need to refer to the latter in order to gain a proper assessment of the state of the law.

As to New Zealand, the position there is more closely aligned with the United Kingdom where the right of any-

* Assistant secretary, Email Limited; delivered to LES Australia August 13, 1975.

one to run his own business and to enter into any contract he chooses is more or less absolute and any restraint must be justified mainly in terms of the Common Law doctrine of restraint of trade.

Apart from the Common Law aspect, the main restraint in New Zealand emerges from the exchange control regulations of the New Zealand Reserve Bank.

Under Regulation 3(g) of the Exchange Control Regulations 1965, the prior approval of the Reserve Bank is required before any New Zealand resident (either an individual or a company) may enter into any agreement or arrangement with an overseas resident to make any payments overseas, for any form of knowledge or assistance (such as service, patent or process) the first proprietary rights of which have originated outside New Zealand. These provisions also apply to sublicenses between New Zealand resident where the first proprietary rights have originated overseas.

The Reserve Bank has on issue guidelines concerning overseas royalty payments and these cover aspects of license agreements discussed in the following text.

RATES OF ROYALTY

There is no rigid rule that royalty payments must be limited to a certain rate and all cases are considered on their merits. The appropriate rate may therefore vary from industry to industry and with the complexity of the process and the value of the article to the New Zealand economy, taking into account such factors as:

- (i) The existing supply and quality of the goods available locally, and;
- (ii) Whether other manufacturers are paying royalties to overseas licensors or not.

Higher royalty rates naturally require greater justification. The rate of royalty should be based on the New Zealand ex-factory selling price less the cost of any components imported from the licensor for incorporation in the finished product. The deduction of the cost of such imported components is said to be required because the payment of a royalty in addition to profit to the licensor on the sale of the components is deemed to be unwarranted. If the rate of royalty is not based on the ex-factory selling price a comparison of the actual method of expression of the rate with this basis should be made.

Minimum payment clauses

Agreements which contain guaranteed minimum payment clauses are not normally approved. In other words the royalty must be calculated on actual production.

Lump-sum payments

Agreements which call for initial lump-sum payments

are not normally approved unless it can be shown that there are special features which would justify such a payment.

Duration

The duration of an agreement should be kept reasonably short; if long-term agreements (more than five years) are proposed they will normally require special justification.

Taxation

The overseas licensor's liability for any New Zealand tax payable on his royalty earnings in New Zealand must be paid by him from these earnings. The Reserve Bank will not agree to the New Zealand tax commitments of the licensor being paid by the New Zealand party and will only agree to the royalty at the approved rate net of any New Zealand tax being remitted to the overseas licensor.

Form of application

There is no printed form to be filled in when application for approval is made to the Reserve Bank. A draft copy of the agreement, or correspondence which clearly states all the terms of the arrangements, should be submitted to the Reserve Bank with a covering letter giving full details of the proposal.

The following information will assist the Bank in reaching a decision:

- (a) The nature of the product and the know-how involved in making it.
- (b) The likely demand for the product and the estimated cost of production.
- (c) Advantages of the product over other goods of a like nature already available.
- (d) Whether additional imports of raw materials or components will be required.
- (e) Details of any export potential or overseas exchange saving.

Remittances

Once the agreement is approved, applications to remit royalties assessed in terms of the agreement will be approved as they accrue, provided each application is supported by an auditor's certificate as to:

- (i) The date of agreement.
- (ii) The period covered by the remittance.
- (iii) The basis on which the amount of the remittance has been calculated and that this conforms to the terms of the agreement as approved by the Reserve Bank.
- (iv) The name and address of the remittee to whom the royalty is payable in terms of the agreement.

It often happens that the New Zealand licensee will need to import components or sub-assemblies from the licensor in which case the question of import licensing will arise. Consent given by the New Zealand Reserve Bank to an agreement does not constitute a commitment, given or implied, that import licenses will necessarily be granted. This is a matter for decision by the Department of Trade and Industry to whom a separate application must be made.

A royalty accrual problem

Turning now to some practical aspects of operating

under a Trans-Tasman license, I shall refer to the mechanics of royalty accrual in the specific case where the licensee in New Zealand has an operating subsidiary acting as a distributor, where a party owned subcontractor is used to manufacture the licensed products and where the royalty is struck against the selling price.

Consider that the licensee must pay the licensor 1.4% and takes to itself a return of 3.6%, making a total of 5% to be applied to the selling price. The mode of operation is such that the licensee directs the subcontractor to supply distributors (as well as the subsidiary) upon arrangement of a sale by its (that is the licensee's) sales manager.

Now, it is clear that the subcontractor's selling price cannot form a rightful basis for the computation of royalty since that is not the selling price of the licensee. However, since the licensee does not take part in the mechanics of the sales, there is no licensee's invoice upon which to assess the royalty payment.

The role of the subsidiary is one of a distributor ranking evenly with other distributors so that transactions with the subsidiary are considered as being at arms length. At first sight this may appear to be an erroneous statement, for it may be said that the subsidiary's selling price is actually the licensee's selling price. Such an argument carries with it the seeds of its own destruction, for if it were so, then all royalty paid in New Zealand should be based on the distributor selling price — a wrongful situation, because the licensee could not be expected to know the selling prices of the other distributors.

Thus, without a licensee's invoice price and with the distributor dealing at arms length, the only possible starting point for royalty calculation is the subcontractor's selling price. This is not as simple as it may at first seem. Consider the sale of \$100 worth of licensed products by the subcontractor to the distributors, be they the subsidiary of any other. As mentioned above, the licensee must collect a total payment of 5% to satisfy the licensor's fee and its own return.

A novice accountant may approach the problem by having the subcontractor enter the \$100 sale on its invoice, calculate the royalty of 5% and transfer the \$5 to the licensee. The licensee notes the invoice sale of \$100 and remits 1.4% (that is \$1.40) to the licensor and retains its 3.6% (that is \$3.60) and thus the books of accounts are nicely balanced.

The flaw here is that the licensor is receiving royalty based on the subcontractor's price and not the licensee's invoice price.

In an attempt to bridge the gap the licensee could create a fictitious invoice price made up of the \$100 plus the \$5 it receives from the subcontractor and then calculate the licensor royalty of 1.4% to be \$1.47, leaving \$3.53 as its return.

In this situation, the licensor is receiving better treatment than in the initial case, but the licensee is not receiving its full due of the 3.6% return (namely, \$3.78), and in fact the licensee is short \$0.25.

To remedy the shortfall to the licensee, our experienced accountant has the subcontractor set a fictitious invoice price to be \$105 (being the original \$100 plus the \$5 for the licensee) and then pays 5% of this (\$5.25 to the licensee). In the licensee's hands this represents an invoiced value of \$105.25 and at 1.4% the licensor should receive \$1.474 leaving \$3.776 as the licensee's share.

As before, however, the licensee has suffered a shortfall

of \$0.013, since it should have received 3.6% of \$105.25 (\$3.789).

Although the licensee's shortfall is greatly reduced, the revised calculation still prohibits a balancing of the licensee's books, a situation which we all know should be avoided.

To determine the correct amount to be paid by the subcontractor, a simple equation should be solved. In deriving this equation we may call the actual payment to be made by the subcontractor "X" and the sum of royalty payable to the licensor and the return payable to the licensee as "Y".

Thus, in considering a sale of \$100, the amount to be paid by the subcontractor is "X", so that the licensee's fictitious invoice figure is \$(100 + X) to which the "Y" percentage must be applied. Obviously, the payment by the subcontractor should equal the payment obligations and collections of the licensee so that:

$$\begin{aligned}
 100.x\% &= (100 + X) Y\% \\
 \text{i.e. } 100x &= 100y + xy \\
 \text{or } x &= \frac{100y}{100-y}
 \end{aligned}$$

In the case of the abovementioned royalty rate and return, the variable "Y" is 5 (3.6% plus 1.4%) and thus "X" becomes:

$$\begin{aligned}
 x &= \frac{100.5}{100-5} \\
 &= \frac{500}{95}
 \end{aligned}$$

$$x = 5.2631$$

This is easily checked by calculating each payment:

- a) 3.6% of \$105.2631 = \$3.7895
 - b) 1.4% of \$105.2631 = \$1.4736
- \$5.2631

It may appear that the number of significant figures is excessive, but, this is not really so when regard is had to the sales values that may be multiplied and the fine balance required to ensure that the two separate royalties add up to that received by the licensee.

SOME TAXATION ASPECTS

Receipts under a license are taxable like any other income and the licensee can claim any royalty paid as a business expense. The licensee in New Zealand is obliged to provide for what is termed "withholding tax". Where payments are made from one country to another, the recipient generally has to pay tax in his own country but this can be offset by the withholding tax, should a double-taxation agreement exist between the two countries. Fortunately, such a double-tax agreement does exist between Australia and New Zealand.

There have been some changes in relation to the tax aspect of Trans-Tasman licenses. Under the old arrangements, know-how payments had what was termed a deemed source in New Zealand and a real source in Australia. They were taxed in New Zealand after deduction of arbitrary expense allowances (a minimum of 15% and a maximum of 50%) and again taxed in Australia at 47.5% without relief for New Zealand taxes.

On the other hand, royalty payments had their source in New Zealand were taxed in New Zealand as above but were exempt under the rather curious Section 23(g) of the

Australian Tax Act.

Dividends from New Zealand are subject to 15% withholding tax but in Australia the tax paid is fully offset by a Section 46 rebate.

Thus, in the case of a subsidiary in New Zealand sublicensing a third party the following used to apply:

Royalty received by Subsidiary	\$1,000.00
Tax paid by Subsidiary (45%)	<u>450.00</u>
Net return after tax declared	550.00

as dividend

The New Zealand subsidiary then provides for the 15% withholding tax (\$82.50) which leaves a net after tax return to the Australian licensor of \$467.50. As mentioned above, the Section 46 rebate cancels out Australian tax. Thus, for the \$1,000 royalty provided by the sublicensee in New Zealand the Australian licensor receives only \$467.50.

The definition of royalty in New Zealand now includes know-how and thus both royalty and know-how have their real and deemed source in New Zealand. This being so, a different course of licensing now presents itself.

The New Zealand subsidiary still sub-licenses the New Zealand manufacturer but the license between the Australian licensor and its New Zealand subsidiary provides for the full transfer of royalty fees.

Thus in New Zealand subsidiary books, the receipt of a \$1,000 royalty from the New Zealand sub-licensee is balanced by a payment of an identical amount to the Australian licensor leaving the New Zealand subsidiary with a nil net taxable income. However, withholding tax comes into play and the Australian licensor receives only \$850 because 15% of the \$1,000 payment must be retained in New Zealand, but under the double-tax agreement the Australian licensor has a foreign tax credit of \$150.

The gross royalty payment of \$1,000 represents the Australian licensor's taxable income in Australia against which the 45% company tax is applied to create a tax liability of \$450 from which is subtracted the foreign tax credit, leaving a net tax payable of \$300.

Bearing in mind that only \$850 was received from the New Zealand subsidiary, the net return after tax to the Australian licensor is \$550 (\$850 minus \$300).

Increased Return

It will thus be seen that the change in the tax basis together with change in the license basis has increased the Australian licensor's return from 46.75% to 55%. Unfortunately, the situation really is not as simple as all that. In the above explanation I conveniently forgot the lack of parity between the Australian and New Zealand dollar and the differences in the cost of money applying in both countries.

Another aspect of taxation matters in relation to New Zealand arises where an Australian company is the licensee of an American company and a need arises to incorporate a New Zealand subsidiary into the license set up. It may happen that the American company puts forward a proposition that the Australian licensee is held responsible for its royalty payments and also those of the New Zealand subsidiary, their concern no doubt arises from their desire to avoid the burden of incurring fees and expenses to prepare and file tax returns in New Zealand. However, such an arrangement can increase the tax

liability of the Australian company and thus the following comments are of relevance.

Generally speaking, New Zealand income tax for non-resident companies reaches a maximum rate of 50% of taxable income. However, where Australian companies earn royalties in New Zealand, the New Zealand income tax is limited to 15% of the gross royalty; this is so by virtue of the Australian/New Zealand double tax agreement.

Although the maximum rate of tax in New Zealand applicable to nonresident companies is 50% of taxable income, the effective rate would be much lower because of the New Zealand authorities allow an arbitrary expense allowance of 40% off the gross royalty in order to determine taxable income.

As there is a convention for avoidance of double taxation between the governments of New Zealand and U.S.A., it seems the New Zealand tax should not cause any concern, because the American company will be allowed a "foreign tax credit" in their U.S.A. tax bill for the amount paid to the New Zealand authorities. It is incumbent on the licensee to:

- (a) Initially withhold 15% of the gross royalty and pay such amount to the Inland Revenue Department.
- (b) Lodge an annual return of income as agent of the non-resident licensor.

Therefore, the question of fees and expenses of preparing and filing tax returns should not present any problem.

If the Australian licensee was permitted to sub-license its New Zealand subsidiary then the Australian company's tax liability in New Zealand would be limited to 15% of the gross royalty. Similarly, Australian tax on royalty from the Australian portion flowing to America would be limited to 15%. However, it must be born in mind that all licensing arrangements come under the scrutiny of the Reserve Bank and the Taxation Office, both in Australia and New Zealand. Thus, there are reservations that agreements providing for the income flowing from New Zealand to Australia being equated with an expense flowing from Australia to U.S.A., would gain official approval. Superficially, it would appear to be an artificial arrangement to lower the rate of New Zealand tax and one which would, in time draw adverse comment.

TRADEMARK LICENSING

The basic principle behind the licensing of trademarks is that the public must not be deceived. In addition the owner of the trademark must retain control over the quality of the goods bearing the mark.

If a company arranges for the manufacture of goods by a subcontractor and instructs the subcontractor to apply the trademark of the company to the goods, this is use of the trademark by the company itself and no difficulty arises. In the same way, if a manufacturer allows a dealer to display the trademark of the company in connection with the sale of goods emanating from the company this does not amount to licensing and does not endanger the trademark, provided the dealer does not create the impression that the trademark belongs to him rather than to the company.

In any case where a company owning a trademark wants to enable another party to use the trademark, the party must be made a "registered user" of the trademark in ac-

cordance with the Trade Marks Act. A formal agreement should be concluded and, as the expression "registered user" implies, the other party must be entered as registered user in the register of trademarks.

The classic case in relation to permitted use of trademarks is the *Bowden* case in which it was held that the owner of the trademark in allowing others to use it had destroyed the distinctiveness of the trademark and the registration was expunged from the Trade Mark Register. The crux of the issue was that as the purpose of a trademark is to distinguish the goods of one trader, it cannot function to distinguish the goods of more than one trader.

Shortly after the *Bowden* decision, the British Trade Marks Act was amended in 1938 to introduce the registered user system so as to remove the legal hazards of the commercially acceptable practice of trademark licensing. This system was adopted in New Zealand by the Trade Mark Act of 1953. Under the registered user system, use of a trademark under a license agreement by a person who has been entered as a registered user of that mark is considered to be use by the proprietor thereby avoiding the objection that the mark is being used by a person other than the proprietor. In a sense, the user system is nothing more than a legal fiction in which sleight of hand (or rather words) changes a wrongful situation into an allowable one.

Who is to be entered as a registered user in any particular situation will depend on all the circumstances of the case and the wishes of the parties — in some cases it may be convenient to have the actual manufacturer of the goods entered as the Registered User, in others it may be preferable to make the distributor the Registered User or even more than one Registered user.

Recent authoritative commentary on registered users suggests that even where a Registered User is entered on the register of trademarks the legend on the goods and supporting paper warfare such as specification sheets, advertising leaflets, etc., should state the position and in particular make quite clear who is the proprietor of the trademarks concerned.

Panel Discussion

BY GAIRE BLUNT, Allen, Allen & Hemsley

Before I deal specifically with the trade practices impact of Trans-Tasman Licensing I think I should acknowledge that I am a New Zealander, or at least a New Zealand-born-and-trained person, and I believe the importance of licensing industrial property into New Zealand really arises because of the import controls which that country has and because of the Reserve Bank which is really a watchdog or guardian of that country's very limited supply of money or limited supply of what they call overseas funds. It's very difficult for somebody outside New Zealand to export finished goods into New Zealand because New Zealand has a very strict import licensing control and most of the import licenses granted are for the import of raw materials, know-how, and the like.

If you want to arrange an import license or a patent license or a know-how license than you need to go to Wellington and sit on the door-step of the people concerned. For an import license you must talk to the import

licensing people and find out how they think and how they work. You've got to get to know the people at the Reserve Bank and how they work and get to know how the Industries and Commerce people work and really get to know somebody in there. I should say that I don't mean by that that the thing is tied up on some sort of Indonesian system of barter, under the counter, or anything like that. You want to keep your nose very clean.

When you come to talk about trade practices in New Zealand I think you do need to realize that there are many industries which couldn't possibly survive beyond the New Zealand market or even on that market plus some export, and the Government there long ago realized that the American type of antitrust laws were totally inappropriate to a market of that size. They seem to be pretty well inappropriate in many ways to a market of our size. They've got a market of some three million people. The national interest in New Zealand demands that many industries which they feel they need to survive, need to be a monopoly, need to be protected by tariff and import controls. At the very best in many industries the only possible thing that can survive is an oligopoly of two or three. For example, in the Fibreboard Industry there are two barely viable groups of companies that convert paper into corrugated fibreboard. You couldn't possibly have enough demand to create a significant sort of competitive situation. So, it's not surprising when you go to look at the trade practices laws in New Zealand, this country which has been in many ways quite forward in advanced legislation, doesn't have anything much about Trade Practices. The Trade Practices Act in New Zealand, as it is at the moment and as it is proposed, isn't anywhere near as effective as the English Act which is of course designed for a country of a much larger population. There is nothing like our antitrust rules, which we've taken for better or worse from America. The 1958 New Zealand Act simply says something to the effect that trade practices are unlawful and we have to work it out from there. There's nothing in that act about patents, trademarks, or licensing, and one would presume that somewhat more detailed patent laws would prevail over that.

In 1974, they brought in a Commerce Bill which is to deal with trade practices and the equivalent of our Prices Justification. This Commerce Bill also says that certain trade practices will be unlawful and it then goes on to list them in a very general sort of way with none of the rather difficult things that we are facing. But they are only unlawful if the Commerce Commission says that they are, so you can do anything until you have been brought up before the Commerce Commission and they have found that you are in breach of the Trade Practices Act, then it's unlawful. It doesn't go on to say that anyone has civil right of damages or what the penalty will be. And there is nothing in that bill, which is still before the house, about patents, trademarks, copyright or know-how. The only parts of the Commerce Bill which they have passed into law are those which set up the constitution of the Commission, presumably so that they can get paid, and the pyramid selling sections.

Broadly, I'm saying that as far as New Zealand law is concerned, I can't see that there can be any trade practices effect on your industrial property licensing unless, at the very least, this Commerce Bill is passed, and when it is passed the commission examines your particular industry

and holds that there has been a breach of the Act. This could perhaps happen where there is an agreement, possibly a patent agreement of some sort, which has the effect of holding the prices up far too high and the commission has held it to be unlawful. Possibly you then would have an illegal agreement.

It is a far cry from that now. The Commerce Bill hasn't been passed and the commission has never sat on any sort of a case such as this. So for practical purposes, the Commerce Bill, when it is passed and the Trade Practices Act as it is now have no impact on your licensing, and you can forget about it. I think you have only to look to see if you are caught under the Australian Trade Practices Laws. If you made a contract in Australia about the licensing of know-how or licensing of patents which was in breach of Section 45, or which is some way provided clearly for resale price maintenance under Section 48, and if these Acts or activities were going to take place partly in Australia and partly in New Zealand, I think you could be caught up in the Australian Trade Practices Law. Don't forget that as far as monopolization is concerned or as far as exclusive dealing is concerned, you are only in breach if you are monopolizing or exclusively dealing in an Australian market. So, anything exclusive about the license of the know-how which may not be covered by the exclusions of Section 51 or the license of a patent or anything that involves monopolization by patent pooling or grant backs would have to be done in a market in Australia. Since we are discussing markets in New Zealand it's not relevant. It does seem to me that an Australian contract could be caught under our Act so that if you want to do all sorts of things in New Zealand that you can't, or don't feel that you can, do here, you not only want to have the contract governed by New Zealand law, I believe you should make the contract in New Zealand.

There is only one other point. There is in this Commerce Bill a provision dealing with monopolization. What it says is that the minister may, from time to time, require the commission to conduct an inquiry and report to him whether there exists in New Zealand or any part of New Zealand a complete or partial monopoly in the supply of goods. There is nothing like we have here where somebody can jump in and sue somebody on the basis that they are monopolizing. Before you could contemplate anything at all you would have to persuade the minister to have an inquiry into whether or not this monopoly is misusing its monopoly power. Once again the monopoly provisions are really quite ineffectual, or quite ineffective as a threat to any agreement which you might enter into.

The message, then, is don't worry about trade practices if you are licensing in New Zealand but do worry about getting on side with the government officers in those various departments. If you get your license through the Reserve Bank and through the Industries and Commerce people you have a great advantage, because you are probably the only person with those goods licensed in New Zealand and you are virtually in a monopoly position. Although getting through the bureaucratic people seems complex, the rewards sometimes are worthwhile, although they might be quite small.

BY JIM DWYER, Allen, Allen & Hemsley

I shall not go into too much detail about the New Zealand Patent Act. It is modeled very closely on the United

Kingdom Act. It provides for a term of 16 years for patents. The machinery provisions for patents or dealings with the Patents Office in New Zealand are similar to those in Australia. The New Zealand Act also provides for international recognition of convention countries.

The Act shouldn't cause licensors too much worry. There are only two sections that came to my attention and those deal with licensing. Under the Australian Act are provisions for compulsory licensing in two areas. One is where a patent hasn't been used for a period of three years and the reasonable requirements of the public are not being met. Then there's provision for applications to be made to rectify the position and for a compulsory license to be granted. The second area is the Crown Use section which gives the Australian government, and the various departments and instrumentalities which operate under it, the right to compulsorily acquire your patent or to license a third party to work it, provided they give you a royalty.

Both those sections have their equivalents in the New Zealand Act, but there are additional sections which I think are worth mentioning. The first is Section 51 which corresponds with an English section which deals with patents relating to food or medicine. A patentee who holds a patent for a substance which is either a food or a medicine finds himself in a position where any person interested may apply to the Commissioner of Patents in New Zealand for a compulsory license. In determining whether that application will succeed the Commissioner really applies a prices justification test. The test is this:

"The Commissioner shall endeavor to secure that food, medicines and surgical and curative devices shall be available to the public at the lowest price consistent with the patentee's deriving a reasonable advantage from their patent rights."

In the last 10 years in England that section's equivalent has become quite popular and many of you will be aware of the Hoffman La Roche cases involving "Valium". It is a section that erodes, in one sense, the patentee's rights where they lie in the drug field.

There is a second section that is of some relevance and may be a weapon which a patentee would want to use to combat any argument that he was misusing his patent powers. Now it appears that there is no real trade practices problem in New Zealand as far as industrial property is concerned, but that may not always be the position. There is a section which once again has a corresponding English section and talks about "licenses of rights". The way this works is that a patentee applies to the commissioner for an endorsement of his patent as one of a license of rights. Once that endorsement is made, any interested person can apply to the Patent Office to have a license granted in respect of that patent. Now I mentioned trade practices earlier in relation to that section; if a patentee were to take that action I suppose he would be halfway to meeting an argument that he had monopolized his patent or misused it. In a sense, what he is doing is effectively saying, "Here I have a patent which is good; anyone can use it on reasonable terms." I would think it would reduce his vulnerability of the trade practices accusations.

The final thing about the Patents Act which occurs to me is that, although the New Zealand Trade Practices Act is very mild compared to what we have to contend with, it may occur to some enterprising defendant's lawyer that the 1958 Act (which says something like, "All trade prac-

tices are unlawful") could argue that the action of a patentee who is in a position to dominate a particular market combined with perhaps cross licensing or some other activity in relation to that patent, is disentitled to the relief that he seeks in an infringement action. A defendant may submit to a court that the patentee has, by his misconduct in relation to his patent, disentitled himself to the relief that he seeks. We may get the American situation, where this argument has been run, that misuse of your patent constitutes unclean hands and therefore the patentee shall not get his injunction or his damages. Perhaps that's a little farfetched at the present stage of the New Zealand law, but it's an argument which will no doubt be raised in future patent actions here as it has been in America.

About trademarks, I've had a little contact with Section 103 of the Trade Marks Act. I think a lot of you people know what that's all about. It's basically that a registered proprietor of a trademark, or a registered user, is entitled to contact the Department of Customs and complain that he doesn't want goods bearing a trademark substantially identical to one which he nominates entering the country. Now once the Department of Customs is satisfied that you are in fact the registered owner, or user, of the mark, and that you have put up your \$15,000, which is the bond being presently asked, he will then circulate this information to all points of entry so that the goods nominated in the forms then take on the character of prohibited imports. Now since the change of Government there has been a lot of attention drawn to this section. A lot of patent attorneys are dissatisfied at the moment with the attitude of the registrar of Trade Marks. He takes the view that pending applications of registered users are required to give some sort of disclaimer that they won't invoke this section if they become recorded as registered users.

The point of my referring to this is that I've come across a situation in which you have an Australian Registered User of the mark who fills in the forms and goes through the motions and wants to prevent goods bearing infringing trademarks entering the country. The way the section is worded it includes goods which have been made by the owner of the mark. You can get a situation where you have a New Zealand company which owns a trademark in Australia, it makes the goods in New Zealand, it puts them into the market place in New Zealand and then some third party exports them to Australia. They get to the Customs man and he won't let them into the country because the registered user of the Australian mark has gone through this customs procedure. It's a curious section and there are, I understand, some pressures to have it amended. There is a corresponding section in the New Zealand Act, so that one can imagine similar problems occurring in reverse. It's very much a policy decision and at the moment the Customs Department in this country take the view that it precludes the entry of the genuine goods.

BY CRISPIN MARSH, F. B. Rice & Co.

I will initially make reference to two further provisions of the New Zealand Patents Act which are of interest to licensors and the licensees and will then discuss a number of other stock license clauses which are affected by New Zealand government regulations.

The first of the two provisions of the New Zealand Act is Section 67 of the New Zealand Act which provides that

in the event that you have a license relating to a patent or patents the license may be determined on three months' notice by either party at the expiration of the patent, or the last of the patents to expire, and that is the equivalent of the Australian Section. But it does have a significant effect on somebody licensing into New Zealand. What it means is that you should spell out in your license very clearly the termination date of your license in respect of any know-how, trademarks, or registered designs which might also be covered by the license. You must avoid the situation in which you effectively throw in "gratis", the know-how into your patent license and then find that, once the licensee has got your know-how he can determine the license on three months' notice following on the expiration of the patent. You can spell out very clearly the fact that the license terminates, in respect of the matter other than the patents that are licensed, at a certain date or in some cases it would even be preferable to write separate licenses.

The second section I will mention is Section 66 of the New Zealand Act, which is approximately equivalent to our Section 112. Under Section 66 of the New Zealand Act a clause of a provision of a license which compels a licensee to take an unpatented good at the time that he takes patented goods is void unless certain provisions are fulfilled. The important difference is that under the Australian Act the effect of the provision is that the license may be void, whereas New Zealand Act Section 66 (2) provides that in proceedings against any person for infringement of patent it should be a defense to prove at the time of the infringement there was in force a contract relating to the patent made by, or with the consent of the plaintiff, and containing a condition void by virtue of this section. That means, following a decision of *Sarason v. Frenay* in England reported a 31RPC 252, it doesn't have to be a license between the plaintiff and the defendant. It can be a license between the plaintiff and any third party, and in fact in the case to which I have referred it was argued successfully that, while there might have been an infringement, there was a complete defense to that infringement. What it means is that, if you enter into a license and you want to make sure that this defense will not be called against you and in the event the licensee wants the unpatented good and he is happy to enter into an agreement whereby he gets the patented good together with the unpatented good, you must make sure in the recitals of your license that the licensee spells out that he has the option to take the patented goods without the unpatented goods, but that he opted to take the two together as a package. This is because it is a defense and a contract is not void where it can be shown that at the time of making the contract the licensor was willing to license the use of the article, or process, to the licensee without the offending condition, and also that the license provides that the licensee may get out of the provision on three months' notice upon paying the appropriate compensation to the licensor. In order to avoid the defense being called against you you've got to do two things. You must spell out the desire of the licensee to take the unpatented goods. You also must spell out that he can get out of that obligation on three months' notice with the payment of an appropriate compensation.

There are a number of other minor points that I'll go through very quickly. One is that, in view of the Trade

Practices Act it would be desirable that litigation should take place in New Zealand rather than in Australia. You want to spell out specifically that the license is subject to the law of New Zealand. This will normally appeal to the licensee because he thinks he is going to be on home ground — you needn't enlighten him!

For the same reason, tie-out or exclusive dealing clauses are okay and in fact it is covered specifically by Sub-Section 5 of Section 55. It is often useful to be able to tie the licensee to your product and may be legally included in a New Zealand license.

I might mention here as an aside that one of these points has until now been absolutely standard, but with the Treaty of Rome applying to Great Britain as well as the originally E.E.C. members, with the Trade Practices Act in Australia and the Sherman Act in the United States, New Zealand suddenly finds itself instead of being in the mainstream of licensing as we know it, suddenly finding itself to be a haven for licensors.

In my experience inflation clauses create certain difficulties in New Zealand. If you tie yourself to a percentage royalty, you are right, but if you have a license that you can't tie to a percentage of the selling price you've got problems in New Zealand. The Reserve Bank in New Zealand seems to be very reticent to allow you to include the traditional gold clause or a clause tied to some surrogate index which is not wholly New Zealand. What they are worried about is that if the inflation rate gets higher overseas than it is in New Zealand your 5% suddenly creeps up to 10% or 15% in real terms. If you are forced into having an inflation clause you've got to tie it to some index which is wholly New Zealand. I frankly haven't found any really suitable index. I think it would vary from case to case, but the using of the New Zealand consumer price index or something like that might conceivably be suitable. It's also notable that the New Zealand Reserve Bank won't allow you to write your license in anything but New Zealand currency, in my experience. We've always been forced to write in New Zealand currency so that any revaluations don't effect the real payment by the licensee.

Another thing that you should take into account is the relative myopia of the New Zealand Reserve Bank in respect to improvement clauses. It seems to me in the long term they should look very carefully at improvement clauses because, by writing appropriate improvement clauses in your license you could force the licensee to pay you a royalty long after he would otherwise have terminated his royalty payment. In my experience it is possible to include improvement clauses that are unbelievably onerous on the licensee; situations where the licensee has had to assign back to the licensor improvements, and improvements being defined widely, and then pay royalties in respect to technology they have developed themselves and the Reserve Bank doesn't seem to raise any objections to that.

One point I should make in concluding is that the New Zealand situation is in a state of flux and that there is a fluidity in the situation. What applied yesterday might well not apply tomorrow. As a general trend I think it is getting easier to get licenses through the Reserve Bank as long as they don't involve a joint venture where the overseas party has a major portion of the equity. In that situation things seem to be getting harder but otherwise things seem to be getting perhaps easier as time goes on.