

Understanding Mexico's New Law

Objective analysis of criteria for applying the new law, and an explanation of some of its goals

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The new administration in my country is very interested in continuing to spread and extend the contents and meaning of the Law on the Transfer of Technology and use and exploitation of patents and trademarks, so that doubts that the private sector might have on interpreting its provisions can be cleared out and therefore facilitate its application and compliance.



J. Soberanis The authorities of the Secretaria de Patrimonio y Fomento Industrial wish to offer assistance. We are not interested in blocking the free flow of technology to our country. On the contrary, our purpose is to promote and encourage it so that it can contribute to the development of Mexico.

I believe that in order to achieve the goals of the Law, it is necessary to maintain constant communications between authorities and domestic or foreign enterprises which are involved in the technology transfer process. This dialogue should be established on sincere, wide, and good-faith terms.

This is precisely what the President of Mexico has mentioned during his visit to the United States, in the lunch reception offered to him by the Governor James R. Thomson of Illinois.

On that occasion, President Lopez Portillo stated:

"In this, my first State Visit, I have had the opportunity of proving that neighbors can and should be friends, that to bad things of life, hatred should not be added and that only the road of friendship and sincerity can lead toward good and positive things . . ."

Within this context, we accept this opportunity to present to you in an objective manner, some of the criteria for the application of the Law on the Transfer of Technology and attempting to solve some of the doubts you might have.

Since its establishment, the General Direction of Transfer of Technology has maintained an open policy with the private sector, which also, in every moment,

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has contributed with us in the solution of problems that appear in daily practice. The new administration believes that it is necessary to keep within the abovementioned framework.

I will not deal with all the contents of the Law but only with some of its legal provisions, mainly those that have a greater impact on the technology transfer process and therefore, produce greater concern among those that are subject to their compliance.

Key Element

We believe that technology is a key element to achieve greater economic and social development. For this reason the legislators established a simple mechanism for the inscription of technology transfer agreements in the Registry. Article 2 establishes which agreements must be registered.

That provision refers to the registration of documents where agreements that must have legal effects in the territory of Mexico are recorded, and their object must be the technology transfer in any form, like patents and trademarks use or exploitation licenses, technical assistance, the supply of training to Mexican workers or of technology by means of leaflets, investigations, designs, drawings, maps, diagrams, patterns, or instruction booklets in every possible way, the supply of basic or detailed engineering as well as company administration or management and operation services.

It is important to mention that the Law establishes the possibility that management contracts may be celebrated if they prove to be useful for the Mexican enterprises. A distinction should be made with the control of our enterprises. A management agreement may not imply an undue intervention in the administration. It is a question of preparing a good case and to present to the Registry the necessary evidence.

The export of technology from Mexico by national companies does not have to be registered. On the other hand, there is a general legal duty to register technology contracts whether or not a fee is involved.

Articles 4, 7, 8, 10 and 14 of the Law regulate the procedure for registration in the following way: During 60 days after the date of celebration of the agreements, the documents where they are recorded must be presented to the Registry for their registration. In case of existence of modifications to those agreements, after their registration, they should also be registered in the same manner. The termination of the agreements before their termination date must also be notified to the Registry within the same period of 60 days.

The Registry has a legal duty to answer back on the inscription applications within a period of 90 working days, and if this period is not met, the agreement has to be recorded automatically. This provision was established to benefit the public by saving bureaucratic delays which can block the free flow of technology to Mexico.

Listed in Article 7 of the Law are cases in which the Registry should reject the registration. The list refers essentially to agreements which are either unfavorable to the national economy or to the contracting party receiving the technology concerned.

Let us review now some of the main sections of Article 7 of the Law, and to provide you with the latest criteria about the interpretation of those sections.

1. Section II of Article 7 of the Law says that any contract in which the price or the conditions are not in proportion to the technology acquired or constitutes an unjustified and excessive burden for the national economy shall not be admitted for registration in the Registry.

The provision allows the authority to judge the fairness and justification of royalty payments to be made for the acquisition of technology, or patents and trademarks license agreements.

This section grants the Registry Administrative discretion, since it empowers it to make a technical and economic appraisal of the benefits contained in the license agreement in order to arrive at a determination of the fairness of the payments.

120 Undoubtedly the technical and economic evaluation of agreements implies great difficulties, in view of the gamut of existing technologies, and also due to the fact that there are no regulations setting the price of a certain technology.

As stated to us by some licensors, who have been quite frank about it, the price of a technology is set pursuant to what the market is willing to pay for it.

Added Characteristics

To the above characteristics should be added that the nature and scope of the technological effort being made in the world substantially changes from one economic sector to another, from one company to another, and even from one product to another.

For these reasons, it is not possible to establish a general criteria for what is adequate consideration, nor is it possible to set a maximum acceptable limit, for instance, a 3% applied by other government agencies when they were administering the now defunct Law for the Development of New and Necessary Industries, since the setting of a maximum acceptable limit implies that in many instances the supplier of technology upon knowing that his contract will be accepted, if comprised within this limit, will ask the highest price for his technology. Then, what was a maximum limit or maximum percentage becomes a minimum, and it might well be that the technology involved is not worth it.

Notwithstanding this, our agency has already established certain criteria of a general character on this subject.

First of all, it is essential that the basis to estimate

the payments for the account of the licensor during the life of the agreement must be clearly and concisely specified in the contract.

The agency in order to evaluate if the conditions are adequate, takes into account the total flow of payments involved in the contract.

Another important aspect of a practical character is that taxes to be paid for income received by licensors from payments of royalties set forth in agreements, should never be borne by the company receiving the technology.

We are doing this because we know that American firms supplying technology may deduct in their own country the taxes paid by them in Mexico, although it is not so with European companies.

In order to appraise the conditions set forth in agreements, the agency examines the extent to which payments to be made are comparable to conditions agreed by other firms in Mexico in similar contracts, and in addition, it secures information from sources abroad. So, the analysis is made by comparison, although we also use other means, such as the bearing of royalties on profits, the complexity of the technology, etc.

Formula for Payment

It is quite difficult to say what is in my viewpoint the best formula for the payment of royalties. The most common one is the payment based on a percentage of total net sales of the products covered by the agreement. This formula may be advisable in some cases, but in other instances it has the disadvantage that the licensor may increase substantially his income simply as a result of increases in the price of the goods sold even though the licensor has made no new additions to the technology or sustained any increases in his own costs of supplying the technology. When an increase in the price of the products covered by the contract is foreseeable, we suggest resorting to the formula of paying royalties on units produced.

Obviously, what the Registry is looking for is the most advantageous payment formula in the negotiation process of the agreements. For us it is very important to obtain the technology that we need in the best terms of quality, price and opportunity that we can get. We believe that this purpose should not be considered as a disincentive to the flow of technology, but as a means of assuring that the technology being transferred is effectively beneficial to the receiving enterprise and to the national economy as a whole. This ultimately results in benefit to the supplying party since the acceptance of the agreement by the Registry is a recognition of the justice and goodness of the payments and the commercial transaction itself.

Sometimes the licensor demands a minimum payment of royalties. As a general rule, the agency does not accept minimum payment of royalties since particularly in the initial phase of operation of a company it may represent an unjustified burden on it.

On the other hand, when a licensee, in addition to acquiring technology from a foreign supplier, purchases from him certain raw materials, parts or components of the product, care should be exercised that at the time of computing the payment of royalties the

amount of such components is deducted from the said payment. Otherwise there would be triple payment of royalties, inasmuch as the technology is already included in the components being acquired from the licensor.

We advise that suppliers of technology submit their cases to the Registry, giving us all the available information, so the Registry can undertake an adequate evaluation of the specific case. It is particularly important that the supplier expresses the benefits that the agreement can bring to the country.

The approach we had followed in evaluating the price of technology is eminently pragmatic. The Registry is actively involved in the negotiation process between supplier and acquiring parties so that the royalty agreed on is acceptable to all. That is why we recommend strongly to contact us and express to us clearly and sincerely your points of view.

We know that up to now this attitude has been satisfactorily accepted by the parties involved in the transfer of technology process, and that it has brought very good results. Therefore we want to maintain it.

Section VI refers to the circumstance that in a technology agreement a clause whereby the acquiring party agrees to purchase equipment, tools, parts or raw materials of specific source is included.

This is known with the name of "Tie-in Clause," since the licensee remains tied to the supplier, who may over-price the goods he sells to the licensee and, in this way, increase his profits. Obviously, this harms the receiving enterprise, and, therefore harms the country, since the over-billing of components which are obligatorily imported, among other negative effects, reduces the competitive position of the product in the international market, in case this product would be exportable.

However, the Registry accepts the provision in those cases in which the raw materials may not be obtained in the country, or those agreements by which the supplier obligates himself to supply the goods or raw materials at the best prices of the international market.

Regarding Section IV, in no case the obligation of transferring to the supplier, for money or freely, the patents, trademarks, innovations or improvements that are developed by the purchaser will be admitted.

We consider fair restraint contained in this rule. In U.S. anti-trust regulations this is known as a "grant-back" provision, and it is a "*per se*" violation of the Sherman Act.

We think that in special cases, certain agreements in which although the licensee would grant the licensor the right to use improvements made during the life of the contract, interims of reciprocity may be accepted.

Section XIII of the Seventh Article points out the

impossibility of granting registration to agreements establishing excessive terms of duration making clear that in no case may the terms exceed 10 obligatory years for the acquiring party.

This section intends to prevent contracts from being of extremely long duration, since there are technologies whose period of obsolescence is very short, and since know-how procedures also exist that can be learned by the local companies in a relatively short time.

The wording of this section grants the National Registry the authority to determine what the length of the agreements should be, although this authority must be exercised taking into account the specific characteristics of each contract, the type of technology being transferred, and the industrial field to which the technology concerned refers.

As a general rule, it is necessary that a specific term be established in the agreements.

However, if the agreement provides for an indefinite term, but admitting the possibility of terminating it on prior notice with a certain anticipation by any of the parties thereto, the agreement may then be admitted for registration in the Registry.

In relation to the application of this section, we have the problem of the obligation to maintain in confidentiality the technical information that is imposed on the receiving party. The Registry does not accept indefinite confidentiality clauses, but agrees that such obligation on the receiving party may be limited to the life of the agreement, and even accepts that if the agreement is terminated prior to its normal expiration date for reasons attributed to the licensee, the licensor can impose complete confidentiality on the technology that has been transferred.

Section XIV provides that the authority shall not accept agreements which are submitted to foreign courts, with the purpose of interpretation or litigation.

This is not an exclusive provision of the Mexican Law, since similar provisions are found in other legal systems. We are only talking about a principle common in the International Private Law, and this is that the law which rules the act is the one where the legal effects of such act take place.

We consider that if the technical assistance is going to be given to our country and we are going to pay for it, our laws must be those which rule the legal effects of the agreements.

In connection with this section, I must confirm to you that the clause containing an arbitral commitment is accepted always by the Registry since Mexico has ratified the Convention on acknowledgment and execution of foreign arbitral judgments as established by the Decree published in the Official Journal of the Federation of June 22, 1971.