

Technology Transfer in Philippines

Why Philippines regulate technology transfer arrangements; a discussion of the regulations and their future

BY ANTONIO T. CARPIO*

RATIONALE OF REGULATION

In ASEAN the Philippines has pioneered the regulation of technology transfer arrangements. The Philippines was the first to take regulatory measures because it was probably the first to face three pressing problems.

First, in the early 1970s the Philippines encountered balance-of-payment difficulties. Even now, the Central Bank of the Philippines still imposes foreign exchange restrictions. Second, there has been a strong perception of the need to insure that imported foreign technology is absorbed and adapted locally to strengthen the technological base of the country. Third, there was a need to improve the bargaining position of the technology recipient to reduce the cost of imported technology and to do away with onerous restrictive business practices.

Indeed, these three problems are the reasons other developing countries regulate technology transfers today.

In the Philippines, the regulation of technology transfers dates back to 1969 when the Central Bank regulated royalty remittance. But it was only in late 1978 that a special body—the Technology Transfer Board—was created with a specific mandate to regulate technology transfers.

The question may be asked: What has been the experience of the board since late 1978?

Since October 1978 the Technology Transfer Board passed upon 332 technology transfer arrangements. Of these, only seven were denied registration. Of these seven, one was denied because of a technicality: the company failed to secure a business license. In effect, there were only six denials, representing a mere 1.8% of all arrangements acted upon. These six agreements were denied either because there was no technology involved (as in the case of simple assembly) or because they were mere distributorship agreements.

RESTRICTIVE BUSINESS PRACTICES

While the board evaluates the technical, economic and legal aspects of technology transfers, two specific

*Attorney, Carpio Villaraza Barza, Cruz & Rosell, Manila, Philippines; paper presented at LES Australia Annual Meeting, August 1981.

areas of the evaluation process are of keen interest to lawyers—restrictive business practices and royalty rates.

The board has listed 10 restrictions which must not appear in technology transfer agreements. All are also prohibited, in varying degrees, in the technology transfer regulations of other developing countries. Some even constitute unfair trade practices, or are in restraint of trade, under the laws of jurisprudence of many developed countries.

The following are the restrictive business practices most frequently found in agreement submitted to the Technology Transfer Board:

1. Post-termination restriction on use of know-how

Found in 61 of the 332 technology transfer arrangements). Almost all developing countries prohibit this on the ground that a transfer of know-how (which is non-patentable) is a sale of technology and not a mere lease. Moreover, to allow restriction would frustrate the transfer of technology which is the essence of the arrangement. Of course, if the technology is patented, and the patent is still valid when the arrangement expires, the technology recipient cannot continue using the patented technology. Incidentally, post-termination restriction on use of know-how should be distinguished from post-termination secrecy clauses which are allowed for a period of not exceeding five years.

2. Export restrictions (55)

This is allowed only if the export restriction is to the technology supplier's home market and the technology supplier manufactures the licensed products there.

3. Sole liability of technology recipient in case of infringement suits (26)

While this is not one of the 10 restrictive business practices listed in its rules, as a matter of policy the board requires at least joint liability. Suggestions that the liability of technology supplier be limited to the royalties received by it have not been accepted by the board.

4. Tie-in clause (21)

This is allowed only if the price charged by the technology supplier conforms to international market prices. If the technology recipient insists, for supply reasons, on purchasing from the technology supplier, the agreement can give the recipient the option, but not the obligation, to purchase from the technology supplier.

5. Royalty-free grant back (19)

This is allowed only if the royalty-free grant back is reciprocal.

6. Restriction on competing businesses (17)

This restriction is allowed only if the technology recipient is the *exclusive* licensee in the Philippines.

7. Minimum royalty payments (16)

Although not listed in the 10 restrictive business practices, this is also not allowed. Related to this are initial disclosure fees which are discouraged by the board, and may be allowed only if they are minimal and if, computed together with the running royalty, they do not exceed the allowable rates over the life of the agreement.

EXCEPTIONAL CASES

The prohibition on restrictive business practices however, is, not absolute. Under the rules, restrictive business practices may be allowed if the technology offered is sufficiently valuable for substantial benefits to accrue to the economy. The rules cite, by way of example, four cases where restrictive business practices may be allowed in technology transfer arrangements, namely: technologies used in export-oriented ventures, technologies used in labor-intensive industries, technologies which use substantial local raw materials, and technologies which promote regional dispersal of industries.

This exceptional-cases provision in the rules moderates the rigidity of the prohibition on restrictive business practices and gives the board flexibility in inducing high-level technologies whose introduction in the Philippines would substantially rebound to the benefit of the economy.

ROYALTY RATES

What about royalty rates? What can be said is that no technology supplier has ever withdrawn from an arrangement because of dissatisfaction with the royalty rate approved by the Technology Transfer Board. The board appreciates the dynamism of the international supply-demand factors which govern the pricing of technologies. A technology recipient must pay the going rate for a particular technology. The board can help the technology recipient reduce excessive rates, but in the end the going rate must still be paid; otherwise the technology supplier may simply back out or both the technology supplier and recipient may utilize unofficial channels in remitting royalties. Fortunately, in the board's experience this has not happened.

Moreover, it is not desirable to be too inflexible and rigid on royalty rates. One must consider what other developing countries are paying to induce inflow of foreign technology. If a country demands unreasonably low royalties, chances are it will end up either with no technology, or with very poor technology. The better technologies will probably go to neighboring competing countries.

Nevertheless, it cannot be denied that the strong mediating presence of the Technology Transfer Board, which plays the role of a third party in the negotiating process, has resulted in reducing the cost of imported technology. The board has estimated that due to reduced royalties, the agreements approved and registered

with it have resulted in a foreign exchange saving of US\$94,065,739.00.* By any yardstick, this is indeed a substantial saving.

STRENGTHENING THE TECHNOLOGICAL BASE

The objective of strengthening the country's technological infrastructure cannot be achieved by simply regulating technology transfer arrangements. A host of other complementary measures must be implemented to create a healthy environment to induce technological creativity.

In the Philippines, we have adopted some innovative measures toward this end. We have tax incentives which allow enterprises to deduct as much as 300% of pre-investment costs incurred in commercializing new technologies. Moreover, a Technology Delivery Fund, administered by the Technology Resource Center, has been established to finance the prototyping, pilot-testing and commercialization of local inventions and utility models. The University of the Philippines Code Commission on Science and Technology has recommended that net income set aside for R&D activities be exempt from the regular income tax as well as the surtax on accumulated profits. All these and *many more*, including the regulation of technology transfers, are part of an overall strategy to accelerate the technological development of the country.

FUTURE TRENDS

The regulation of technology transfer is certainly not an end in itself. I personally view it as a *temporary measure*, and the regulatory mechanism enforcing it will automatically phase out as it succeeds in carrying out its objectives. In effect, the more the regulatory mechanism succeeds, the less important and less regulatory it becomes.

At this point, we may ask: what are the future trends in the regulation of technology transfer? Among developing countries, South Korea has, I believe, shown the way. Prior to 1978, South Korea regulated technology transfer arrangements in the same way that most developing countries regulate these arrangements today. But beginning in 1978, South Korea considerably liberalized its policies. Technology transfer arrangements are now automatically approved unless the duration exceeds 10 years, or the royalty rate exceeds 10% of net sales, or a lump-sum payment of more than \$1 million dollars is involved. (Perhaps these have been further liberalized lately).

South Korea liberalized its policies for four reasons. First, its balance of payments vastly improved. Second, the bargaining position of technology recipients improved because of better information, more experience and greater resources. Third, technology recipients have been successful in absorbing and adapting foreign technologies. Fourth, South Korea wanted to accelerate inflow of foreign technology to hasten its industrialization. The net effect of the liberalized policies was a jump in total average royalty rate from 3%

*Based on 259 technology transfer agreements.

before 1978 to 8% thereafter. But this rise must have been compensated by the high level of technology that was coming in.

I would like to see this trend of liberalization in technology transfer regulation spread to other

developing countries. Of course, there has to be an improvement on the economic and technological fronts, as in South Korea, before such trend can set in. But hopefully, insofar as the Philippines is concerned, the turnaround will not be far in the future.