

Fordham Intellectual Property, Media and Entertainment Law Journal

Volume 26, Issue 3

2016

Article 5

VOLUME XXVI BOOK 3

A Long-Overdue Reform: China's Grant-Back Regime in Technology Transfer

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Xiaoqiong Liu

Abstract

Technology transfer occurs when the owner of a technology grants access to that technology to another party. Today, companies consider technologies—as opposed to physical assets—the most important business assets that are directly tied to their products' competitiveness. Intellectual property ("IP") law protects those technologies. One type of technology transfer is contract manufacturing, where foreign companies employ Chinese companies to manufacture products for the Chinese markets. Contract manufacturing is beneficial to foreign companies because it saves them shipping costs and time. To facilitate contract manufacturing in China, however, foreign companies—often the owners of the technologies—must authorize Chinese companies access to their proprietary technologies. Another type of technology transfer—foreign direct investment ("FDI")—involves foreign companies setting up business entities in China, either as joint venture partners with Chinese companies or as wholly-owned subsidiaries. Under FDI, foreign companies maintain a lasting ownership and control over their proprietary technologies. For FDI to operate successfully, foreign companies must transfer their proprietary technologies to their business entities in China. In 2002, China implemented a provision in the People's Republic of China ("PRC") Regulations on Administration of Technology Import and Export ("2002 Technology Regulations"), mandating that licensees own the improvements they make to proprietary technologies to which the licensees receive authorized access (hereinafter referred to as the "prohibition on grant-back clauses"). Often, foreign licensors include grant-back clauses in their licensing agreements, providing that the foreign licensors own any improvements to the technology made by the Chinese licensees. Notably, however, the 2002 Technology Regulations prohibit such grant-back clauses imposed by foreign licensors. China's grant-back regime is outdated and should be updated with the following proposed policy changes: China should (1) continue to prohibit grant-back clauses on severable improvements, which can be used without using the original licensed patent; (2) make grant-back clauses on non-severable improvements non-mandatory, and subject potential abuse of non-mandatory grant-back clauses to the rule of reason under antitrust law; (3) apply its grant-back rule to domestic and foreign companies equally and fairly; and (4) reform its grant-back regime now, rather than later. Prior to reaching these solutions, this Note first discusses

*Notes and Articles Editor, *Fordham Intellectual Property, Media & Entertainment Law Journal*, Volume XXVI; J.D. Candidate, Fordham University School of Law, May 2016; B.A., Chemistry, Franklin and Marshall College, 2010. I would like to thank Professor Mark Cohen for his insightful feedback in developing this Note and the IPLJ Editorial Board and Staff for their efforts throughout the editorial process. I would like to extend special thanks to my parents for their constant, unconditional love.

how China's prohibition on grant-back clauses affects its technology transfer, with an emphasis on empirical data. Then, this Note examines China's current grant-back regulations and compares them with China's regulatory regimes in other related areas, as well as grant-back regimes in the United States and the European Union.

KEYWORDS: China, Technology Transfers, Grant-Back Clauses, Grant-Back

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INTRODUCTION

Technology transfer occurs when the owner of a technology grants access to that technology to another party.¹ Today, companies consider technologies—as opposed to physical assets—the most important business assets that are directly tied to their products’ competitiveness.² Intellectual property (“IP”) law protects those technologies.

One type of technology transfer is contract manufacturing, where foreign companies employ Chinese companies to manufacture products for the Chinese markets.³ Contract manufacturing is beneficial to foreign companies because it saves them shipping costs and time.⁴ To facilitate contract manufacturing in China, however, foreign companies—often the owners of the technologies—must authorize Chinese companies access to their proprietary technologies.⁵ Another type of technology transfer—foreign direct investment (“FDI”)—involves foreign companies setting up business entities in China, either as joint venture partners with Chinese companies or as wholly-owned subsidiaries.⁶ Under FDI, foreign companies maintain a lasting ownership and control over their proprietary technologies.⁷ For FDI to operate successfully, foreign companies must transfer their proprietary technologies to their business entities in China.⁸

In 2002, China implemented a provision in the People’s Republic of China (“PRC”) Regulations on Administration of Technology Import and Export (“2002 Technology Regulations”),⁹

¹ See Daniel C.K. Chow, *A Comparison of EU and China Competition Laws That Apply to Technology Transfer Agreements*, 9 I/S: J.L. & POL’Y FOR INFO. SOC’Y 497, 497 (2014).

² See *id.* at 500.

³ See *id.* at 501.

⁴ See *id.*

⁵ See *id.*

⁶ See *id.* at 502.

⁷ See *id.*

⁸ See *id.*

⁹ Regulations on Administration of Import and Export of Technologies (promulgated by the St. Council, Dec. 10, 2001, effective Jan. 1, 2002), CLI.2.38107(EN) (Lawinfochina), art. 27 [hereinafter 2002 Technology Regulations].

mandating that licensees¹⁰ own the improvements they make to proprietary technologies to which the licensees receive authorized access¹¹ (hereinafter referred to as the “prohibition on grant-back clauses”). Often, foreign licensors include grant-back clauses in their licensing agreements, providing that the foreign licensors own any improvements to the technology made by the Chinese licensees. Notably, however, the 2002 Technology Regulations prohibit such grant-back clauses imposed by foreign licensors.¹²

China’s grant-back regime is outdated and should be updated with the following proposed policy changes: China should (1) continue to prohibit grant-back clauses on severable improvements, which can be used without using the original licensed patent; (2) make grant-back clauses on non-severable improvements non-mandatory, and subject potential abuse of non-mandatory grant-back clauses to the rule of reason under antitrust law; (3) apply its grant-back rule to domestic and foreign companies equally and fairly; and (4) reform its grant-back regime now, rather than later.

Prior to reaching these solutions, this Note first discusses how China’s prohibition on grant-back clauses affects its technology transfer, with an emphasis on empirical data. Then, this Note examines China’s current grant-back regulations and compares them with China’s regulatory regimes in other related areas, as well as grant-back regimes in the United States and the European Union.

¹⁰ A licensee is one to whom a license is granted. *Licensee*, BLACK’S LAW DICTIONARY (10th ed. 2014). In this Note, a licensee refers to the party to which access to a technology is granted.

¹¹ See Chow, *supra* note 1, at 518–19.

¹² See *id.* at 519; 2002 Technology Regulations, *supra* note 9.

I. EMPIRICAL DATA: HOW THE CURRENT GRANT-BACK REGIME AFFECTS TECHNOLOGY TRANSFER AGREEMENTS IN CHINA

A. Statistics

1. IP Licensing in China Is Growing Fast

Table I below shows that the number of patent licensing contracts increased drastically from 2005 to 2009. This data is extracted from the Patent Licensing Contract Record, which was implemented by the State Intellectual Property Office of the People's Republic of China ("SIPO") in 2002.¹³ Although a patent license agreement would nonetheless remain valid without recordation, it is the best practice for a foreign company to record its patent license agreement in China in order to remit royalties overseas.¹⁴ Therefore, this data is the best available to reflect the level of patent licensing activities in China.¹⁵

Table I. Patent Licensing Contracts¹⁶

Year	2004	2005	2006	2007	2008	2009
Number of Contracts	274	113	n/a	187	8,350	12,403

According to the International Licensing Industry Merchandisers' Association, the Chinese licensing market grew from \$1.1 bil-

¹³ See Toshiya Watanabe, *Recent Increase in Patent Licensing in China and Its Effect on South-South Technology Transfer*, TECH MONITOR, May-June 2011, at 31, 32 http://www.techmonitor.net/tm/images/4/4c/11may_jun_sf3.pdf [<http://perma.cc/8MEZ-K29Y>].

¹⁴ See *Licensing and Technology Transfer*, CHINA IPR SME HELPDASK, <http://www.china-iprhelpdesk.eu/content/licensing-and-technology-transfer> [<https://perma.cc/K89R-XKV6>] (last visited Mar. 13, 2016).

¹⁵ See Watanabe, *supra* note 13, at 32.

¹⁶ Paik Saber, Assistant Gen. Counsel, IBM Asia Pacific, Patent Litigation and Licensing in China (Few Practical Considerations) (Mar. 10, 2011) (on file with author).

lion in 2005 to \$3.9 billion by 2010, representing a 25% year-over-year growth.¹⁷

2. China Is Currently “Under-Licensed” in Technology Transfer with the United States

Graphs I and II below show licensing revenues from 2006 to 2012, based on U.S. census data.¹⁸ The blue line in Graph I shows that, in 2012, the United States received a little less than \$5 billion from China. Although China has seen an upward trend in licensing receipts, as the red line shows (about \$500 million in 2012), the number of China’s licensing receipts was much less than that of the United States.

However, this data might deviate from the actual licensing revenues given the different pricing methods that companies adopt when recording licensing revenues with the U.S. Census Bureau. Thus, the comparison of the same data for Japan and the United States in Graph II might be more meaningful than the stand-alone data in Graph I. In 2012, Japan almost balanced the imports and exports in technology transfer with the United States.¹⁹ Assuming the same behavior by the United States in importing technologies from both China and Japan, the comparison of Graphs I and II suggests that China is “under-licensed” with the United States.²⁰ Such under-licensing is especially striking considering the large trade deficit the United States has with China.²¹ As a result, China’s under-licensed status indicates that Chinese technology export is an area with high economic growth potential.²²

¹⁷ See Hao Zhan, *SAIC Moves Closer to Antitrust Rules for Intellectual Property*, INT’L L. OFF. (July 31, 2014), <http://www.internationallawoffice.com/newsletters/detail.aspx?g=f8cbb0d5-6d93-4b19-b972-5a06cc0c92d1> [<http://perma.cc/E5KT-2SDF>].

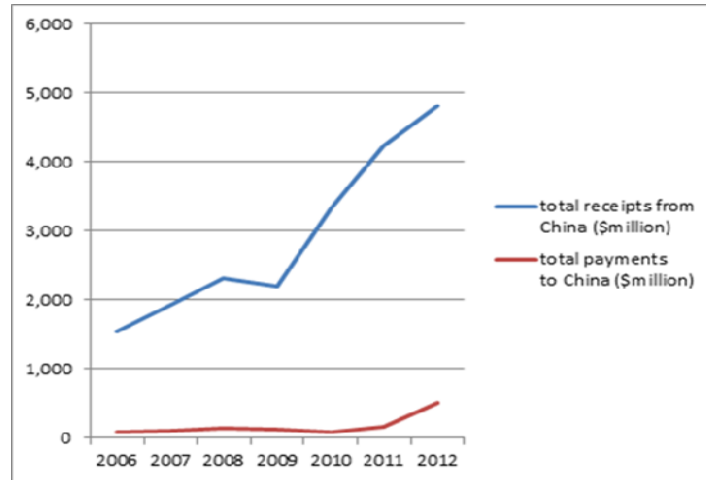
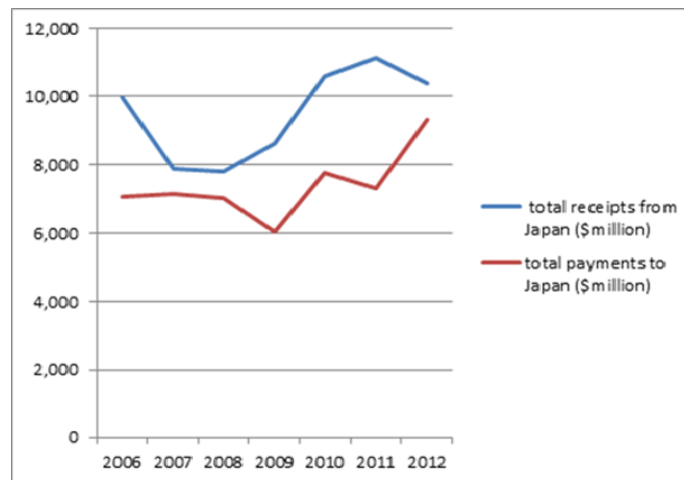
¹⁸ See Mark Cohen, Special Counsel, U.S. Patent & Trademark Office, *Licensing Impediments: Key Considerations for China-U.S. Technology Transfer* (Jan. 7, 2015) (on file with author).

¹⁹ *See id.*

²⁰ *See id.*

²¹ The U.S. trade deficit with China was \$365.7 billion in 2015, which is a new record. *U.S. China Trade Deficit: Causes, Effects and Solution*, ABOUT.COM, <http://useconomy.about.com/od/tradepolicy/p/us-china-trade.htm> [<http://perma.cc/6DUS-JBED>] (last visited Mar. 13, 2016).

²² *See infra* Section I.A.4.

Graph I. Licensing Revenues: China and the United States²³Graph II. Licensing Revenues: Japan and the United States²⁴

3. Almost All Licensing Activities in China Involve Foreign Companies

As of 2010, out of a total of 18,348 patent license transfers recorded in the Patent Licensing Contract Record, only 33 (0.17%)

²³ See Cohen, *supra* note 18.

²⁴ *Id.*

transfer technologies from Chinese companies to other Chinese companies, as opposed to foreign companies.²⁵

4. China Strives to Transform from a Technology Import Economy to a Technology Export Economy

China is traditionally a major technology import country; in 2014, with inflows at an estimated \$128 billion, China became the world's largest recipient of FDI.²⁶ Significantly, as the global FDI declined by 8% to an estimated \$1.26 trillion, inflows to China nevertheless rose by about 3% in 2014.²⁷

The Chinese government has taken numerous steps to encourage both Chinese and foreign companies to possess legal ownership of original technologies.²⁸ In 2008, the Chinese government required high-tech companies to possess a patent or receive the exclusive patent license in order to receive grant money and tax exemptions.²⁹ On a global level, China is expected to transfer more technology in the future to facilitate the growth of Least Developed Countries ("LDC").³⁰ For example, in 2006, Chinese government supported the launch of the South-South Global Assets and Technology Exchange, which provides service to support technology transfer to LDCs.³¹ Other previous technology exports from China to developing countries include China's Kpatawee Rice Project in Liberia in 1993 and technology transfer to boost food production in the China-Africa Cooperation Framework in 2007.³²

5. Economic Data on IP Licensing Is Scarce

The Chinese government has not released any specific data on the grant-back regime specifically, making it difficult to directly

²⁵ See Watanabe, *supra* note 13, at 35.

²⁶ See U.N. Conference on Trade and Development, Global FDI Flows Declined in 2014: China Becomes the World's Top FDI Recipient 2 (Jan. 29, 2015), http://unctad.org/en/PublicationsLibrary/webdiaeia2015d1_en.pdf [<http://perma.cc/VL9H-H99N>].

²⁷ See *id.* at 1-2.

²⁸ Watanabe, *supra* note 13, at 35.

²⁹ *Id.*

³⁰ See *id.* at 31.

³¹ See *id.*

³² See *id.* at 35.

study how China's current grant-back regime affects China in an economic sense. In contrast, many economic analyses have revealed that grant-back clauses are sometimes pro-competitive and sometimes anti-competitive.³³ Therefore, the absence of economic data on China's grant-back regime suggests that this issue is worth further exploring and has room for reform.

B. High-Profile Deal: High-Speed Rail

Since China first entered into the high-speed rail ("HSR") market in 2003, China has progressed from a HSR novice to the host of the world's largest high-speed network.³⁴ Indeed, China's HSR network spans more than 7,450 miles, far ahead of its nearest competitor, Spain, whose HSR network measures 1,925 miles.³⁵ Through technology transfer and reverse-engineering, China was able to become "the world's high-speed hot spot" in a little over a decade.³⁶ China required foreign companies that entered into the Chinese HSR market early to transfer their technology to their Chinese partners.³⁷ For example, in 2004, Kawasaki Heavy Industries (a Japanese company) transferred HSR technology to China South Locomotive & Rolling Stock Corporation Limited ("CSR") in a deal worth \$740 million at the time.³⁸ Also, in 2005, Siemens, a German company, transferred its HSR technology to China CNR Corporation Limited.³⁹ Almost a decade later, the tables have turned: today, CSR is exporting its own HSR technology, and CNR is competing with Siemens for international contracts.⁴⁰

Indeed, China's state-guided industry quickly took the technology, improved it to create domestic designs, and then re-entered the international market to meaningfully compete for lucrative

³³ See *infra* Section III.B.1.

³⁴ See Chris Lo, *China's Fast Track to High-Speed Rail Exports*, RAILWAY TECH. (Oct. 13, 2014), <http://www.railway-technology.com/features/featurechinas-fast-track-to-high-speed-rail-exports-4401625/> [<https://perma.cc/2LR2-GGFR>].

³⁵ *Id.*

³⁶ *Id.*

³⁷ See *id.*

³⁸ See Mukul Raheja, *The Phenomenon of "Technology Transfer": Lessons from China*, SCI. TECH. & SECURITY F. (May 17, 2014), <http://stsfor.org/content/phenomenon-technology-transfer-lessons-china> [<http://perma.cc/L7Y5-T62A>].

³⁹ See *id.*

⁴⁰ See *id.*

deals.⁴¹ In 2005, the China Railway Construction Corporation and China National Machinery Import and Export Corporation won the contract to build an HSR line in Turkey.⁴² This HSR line, inaugurated in 2014, spans 330 miles between Istanbul and Ankara in three and a half hours at speeds up to 155 miles per hour.⁴³ Turkey's Ankara-Istanbul line is just one of several Chinese HSR projects, as Chinese companies have signed or are negotiating HSR contracts in several other countries, including Saudi Arabia, Hungary, and Serbia.⁴⁴

In the past, most foreign companies willingly complied with China's restrictive technology transfer regulations to gain access to the country's massive population of consumers with disposable income.⁴⁵ The president of Bombardier China (a Canadian aerospace and transportation company) said in 2009, "Whatever technology Bombardier has, whatever the China market needs, there is no need to ask."⁴⁶ Still, despite the benefit of the Chinese market, grievances over intellectual property matters from these foreign companies have emerged.⁴⁷ Kawasaki has publicly complained that CSR's HSR technology is based on Kawasaki's design and has threatened to sue CSR if it exports that design.⁴⁸ Similarly, in 2010, executives from Siemens complained directly to the then-Premier Wen Jiabao about the rules that compel foreign companies to transfer their technologies to Chinese companies in order to gain access to the Chinese market.⁴⁹

⁴¹ See Lo, *supra* note 34.

⁴² See *id.*

⁴³ See Amy Qin, *China Exports High-Speed Rail Technology to Turkey*, N.Y. TIMES (July 28, 2014, 7:14 AM), <http://sinosphere.blogs.nytimes.com/2014/07/28/china-exports-high-speed-rail-technology-to-turkey/> [<https://perma.cc/3BDM-DJQ9>]; Lo, *supra* note 34.

⁴⁴ See Lo, *supra* note 34.

⁴⁵ See Raheja, *supra* note 38.

⁴⁶ See Lo, *supra* note 34.

⁴⁷ See Raheja, *supra* note 38.

⁴⁸ See *id.*

⁴⁹ See *id.*

II. THE CURRENT REGIME OF PROHIBITION ON GRANT-BACK CLAUSES⁵⁰

A. Legislation and Regulations

China's grant-back regime is scattered throughout several authorities, including the 2002 Technology Regulations,⁵¹ Contract Law of the PRC ("Contract Law"),⁵² Provisions on the Prohibition of the Abuse of Intellectual Property Rights to Eliminate or Restrict Competition ("IP Rights Guidelines"),⁵³ and the National Medium- and Long-Term Plan for the Development of Science and Technology ("MLP").⁵⁴

1. The PRC Regulations on the Administration of the Import and Export of Technologies

The Ministry of Commerce's⁵⁵ ("MOFCOM") predecessor, the Ministry of Foreign Trade and Economic Cooperation, promulgated the 2002 Technology Regulations.⁵⁶ The 2002 Technology Regulations apply specifically to technology imports into and ex-

⁵⁰ Chinese courts have not issued any judicial decisions related to China's mandatory grant-back regime, limiting this paper's discussion to the statutory language. Section III.A.2 discusses antitrust decisions on licensing practices.

⁵¹ 2002 Technology Regulations, *supra* note 12.

⁵² See *Zhongguo Renmin Gong he Guo Hetongfa* (中华人民共和国合同法) [Contract Law of the People's Republic of China] (promulgated by the Nat'l People's Cong., Mar. 15, 1999, effective Oct. 1, 1999) [hereinafter Contract Law].

⁵³ See State Council of the People's Republic of China, *The National Medium- and Long-Term Program for Science and Technology Development (2006–2020)* (Feb. 2006), http://www.gov.cn/jrzq/2006-02/09/content_183787.htm [<https://perma.cc/A99K-AWB2>], translated at U. Sydney, http://sydney.edu.au/global-health/international-networks/National_Outline_for_Medium_and_Long_Term_ST_Development1.doc [<https://perma.cc/QUH3-KXC6>] [hereinafter IP Rights Guidelines].

⁵⁴ See *The National Medium- and Long-Term Program for Science and Technology Development (2006–2020)*, ST. COUNCIL PEOPLE'S REPUBLIC CHINA (Feb. 2006), http://sydney.edu.au/global-health/international-networks/National_Outline_for_Medium_and_Long_Term_ST_Development1.doc [<https://perma.cc/QUH3-KXC6>] [hereinafter *MLP for Science and Technology Development*].

⁵⁵ The Ministry of Commerce is an executive agency of the State Council of China that regulates foreign trade and investment. See Dingding Tina Wang, Note, *When Antitrust Met WTO: Why U.S. Courts Should Consider U.S.–China WTO Disputes in Deciding Antitrust Cases Involving Chinese Exports*, 122 COLUM. L. REV. 1096, 1113 (2012).

⁵⁶ 2002 Technology Regulations, *supra* note 12.

ports out of China.⁵⁷ A technology import occurs, for example, when a foreign company that owns technology registers a patent for the same technology in China.⁵⁸

Article 27 of the 2002 Technology Regulations provides: “During the valid term of a technology *import* contract, the fruits of improvements to the technology shall belong to the party making the improvements.”⁵⁹ This language is often referred to as the “prohibition on grant-back clauses” because the provision mandates that improvements belong to the party making the improvements, without exception.⁶⁰ The prohibition on grant-back clauses only applies to technology import contracts, and not to technology export contracts,⁶¹ which is notable since China is currently a predominantly technology import economy.⁶²

2. The PRC Contract Law and the Judicial Interpretation

Article 345 of the Contract Law, promulgated in 1999, provides that the transferor of a patent licensing contract shall, according to the terms of the contract, permit the transferee to exploit the patent.⁶³ Under the Contract Law, in the absence of a grant-back clause in a contract, if the intent of the parties cannot be determined by other conduct, the improvement belongs to neither the licensee nor the licensor.⁶⁴ This prohibition on grant-back clauses conflicts with the prohibition on grant-back clauses under the 2002 Technology Regulations.⁶⁵

The Contract Law is a law of general application, but specifically provides for technology transfer contracts.⁶⁶ Still, the 2002 Technology Regulations, which were enacted three years after the

⁵⁷ *Id.* at art. 2.

⁵⁸ *See id.*

⁵⁹ *See id.* at art. 27 (emphasis added).

⁶⁰ *See id.*

⁶¹ *See id.* at art. 2.

⁶² *See* U.N. Conference on Trade and Development, *supra* note 26; *see also* discussion *supra* Section I.A.4 on China’s recent initiatives intended to transform from a technology import economy to export economy.

⁶³ *See* Contract Law, *supra* note 52, at art. 354.

⁶⁴ *See id.* at art. 354.

⁶⁵ *Compare* Contract Law, *supra* note 52, at art. 354, *with* 2002 Technology Regulations, *supra* note 12, at art. 27.

⁶⁶ *See* Contract Law, *supra* note 52, at art. 3.

Contract Law, are specifically-tailored to technology transfer agreements involving imported technology.⁶⁷ The 2002 Technology Regulations—which prohibit grant-back clauses—are controlling.⁶⁸

Article 329 of the Contract Law provides that technology contracts are invalid if they illegally monopolize, impede technological progress, or infringe on technologies of others.⁶⁹ To interpret Article 329, the Supreme People’s Court issued the Supreme People’s Court’s Interpretation of Several Issues on Applying Law to Trial of Cases of Technology Contract Dispute (“Judicial Interpretation”) on December 16, 2004.⁷⁰ Article 10 of the Judicial Interpretation enumerates circumstances that render contract provisions invalid for “illegally monopolizing technology and impairing technological progress” pursuant to Article 329 of the Contract Law.⁷¹ This Judicial Interpretation provides that contract provisions are invalid if they restrict a party from using improved technologies, require one party to “gratuitously” provide the other party with the improved technology, or to transfer the improved technology to the other party non-reciprocally.⁷² Although never addressed directly, Article 329 of the Contract Law—in light of Article 10 of the Judicial Interpretation—appears to make grant-back clauses a per se violation, which aligns with the 2002 Technology Regulations.

The Supreme People’s Court applied Article 329 in *Xiamen Dayang Handiwork Co. v. Xiamen Huanghe Technology and Trading*

⁶⁷ See 2002 Technology Regulations, *supra* note 12.

⁶⁸ See Contract Law, *supra* note 52, at art. 355 (stating that, where other, relevant laws or regulations differ with respect to technology import or export contracts or patent contracts, those provisions prevail); see also Chow, *supra* note 1, at 519 (stating that the chronological order of the promulgation of the two laws and the 2002 Technology Regulations’ higher degree of specificity suggests that Article 27 of the 2002 Technology Regulations is likely the controlling law on the issue).

⁶⁹ See Contract Law, *supra* note 52, at art. 329.

⁷⁰ See Interpretation of the Supreme People’s Court Concerning Some Issues on Application of Law for the Trial of Cases on Disputes over Technology Contracts (promulgated by Sup. People’s Ct., Dec. 16, 2004), CLI.2.38107(EN) (Lawinfochina), art 10.

⁷¹ See *id.*

⁷² See *id.*

Co.⁷³ In *Xiamen Dayang Handiwork*, the licensor required the licensee to purchase the licensor's equipment, even though it was seemingly unrelated to the licensed technology.⁷⁴ This provision is analogous to a grant-back clause in that both mandate actions by the licensee for the benefit of the licensor. Admittedly, a grant-back clause may impact both parties in a more profound way because it concerns the permanent ownership of technology. The court upheld the contractual provision in *Xiamen Dayang Handiwork*, finding that the licensor may require this kind of additional purchase for special equipment, and such a stipulation is not "contradictory to the provisions of any law or regulation."⁷⁵

It is unclear whether Article 329 encourages the transfer of leading technologies and therefore serves China's needs. No economic data exists to demonstrate Article 329's effect on licensing.

3. The IP Abuse Guideline Rules of China's State Administration for Industry and Commerce

Anti-Monopoly Law ("AML") applies to all monopolistic practices within China and monopolistic practices occurring outside of China's territory that impinges on economic competition within China.⁷⁶ On April 7, 2015, China's State Administration for Industry and Commerce ("SAIC")⁷⁷ released its long-awaited IP Rights Guidelines to implement the AML against abuse of IP rights.⁷⁸ The promulgation of these IP Rights Guidelines is China's first attempt to address the abuse of IP rights under the AML,⁷⁹

⁷³ See *Xiamen Dayang Handiwork Co. v. Xiamen Huanghe Tech. & Trading Co.* (大洋公司诉黄河公司专利实施许可合同纠纷案) [Dayang Company v. Huanghe Company], 2004 SUP. PEOPLE'S CT. GAZ. 9 (Sup. People's Ct. 2004) (China).

⁷⁴ See *id.*

⁷⁵ *Id.*

⁷⁶ *Zhongguo Renmin Gongheguo Fan Longduan Fa* (中华人民共和国反垄断法) [Anti-Monopoly Law of the People's Republic of China] (promulgated by the Standing Comm. Nat'l People's Cong., Aug. 30, 2007, effective Aug. 1, 2008), art. 2 (China).

⁷⁷ SAIC is responsible for "registration of enterprises (including foreign-invested enterprises) . . . [and] entities or individuals engaged in business operation . . ." *Mission*, ST. ADMIN. INDUS. & COM. PEOPLE'S REPUBLIC CHINA, <http://www.saic.gov.cn/english/aboutus/Mission/index.html> [<http://perma.cc/7XFB-YDZ2>] (last visited Oct. 31, 2015).

⁷⁸ IP Rights Guidelines, *supra* note 53.

⁷⁹ See MICHAEL GU, ANJIE LAW FIRM, BRIEF COMMENTS ON CHINA'S FIRST ANTI-MONOPOLY REGULATION IN THE IP FIELD, <http://en.anjielaw.com/downloadRepository/>

and signals the SAIC's intent to ramp up enforcement in IP licensing.⁸⁰

Article 10 of the IP Rights Guidelines specifically prohibits certain unreasonable restrictive trading conditions that may constitute an abuse, with exclusive grant-back clauses by companies with dominant market positions amongst the prohibited conditions.⁸¹ Therefore, absent a justifiable reason, grant-back clauses by companies with dominant market positions per se violate the AML, irrespective of proof of their anti-competitive or pro-competitive effects. The reference to "justifiable reason" might suggest that the SAIC will review the abuse of grant-back clauses based on an analysis similar to rule of reason, which assesses the anti-competitive or pro-competitive effects.⁸² However, it remains unknown how much the SAIC will rely on the rule of reason analysis.⁸³ Further, since such a per se prohibition only governs licensors that occupy dominant market positions, Article 10 is less sweeping than the 2002 Technology Regulations and possibly the Contract Law.

The U.S. Chamber of Commerce believes that the IP Rights Guidelines curtail patent owners' interests and that patent owners, in practice, are often foreign companies.⁸⁴ When it submitted comments on the eighth draft of the IP Rights Guidelines, the U.S. Chamber of Commerce criticized that the IP Rights Guidelines "provide Chinese courts and SAIC with great discretion to intervene in patent licensing negotiations purely based on commercial

6df0e385-4dcb-45ee-945f-4a5c4388482c.pdf [https://perma.cc/YE8W-XNEN] (last visited Mar. 13, 2016).

⁸⁰ See MICHAEL HAN & RICHARD BIRD, FRESHFIELDS BRUCKHAUS DERINGER, CHINA'S SAIC CONSULTS ON DRAFT RULES ON THE ENFORCEMENT OF THE ANTI-MONOPOLY LAW WITH REGARD TO IPR (June 2013), http://www.freshfields.com/uploadedFiles/SiteWide/Knowledge/June%202013_China_s%20SAIC%20consults%20on%20draft%20Rules%20on%20the%20enforcement%20of%20the%20Anti-Monopoly%20Law%20with%20rega.PDF [http://perma.cc/A6BJ-FFGP].

⁸¹ See IP Rights Guidelines, *supra* note 53, at art. 10.

⁸² See COVINGTON & BURLING LLP, CHINA ISSUES FINAL IP/ANTITRUST RULES (Apr. 21, 2015), https://www.cov.com/-/media/files/corporate/publications/2015/04/china_issues_final_ip_antitrust_rules.pdf [https://perma.cc/XDL2-5HJ9].

⁸³ See *id.*

⁸⁴ See U.S. CHAMBER OF COMMERCE, COMPETING INTERESTS IN CHINA'S COMPETITION LAW ENFORCEMENT: CHINA'S ANTI-MONOPOLY LAW APPLICATION AND THE ROLE OF INDUSTRIAL POLICY 70 (Sept. 9, 2014), https://www.uschamber.com/sites/default/files/aml_final_090814_final_locked.pdf [https://perma.cc/E8GT-FSX5].

considerations between the parties, and tilt the balance in favor of the Chinese licensees . . . at the expense of the patent holder.”⁸⁵ The final edition—the IP Rights Guidelines—“shows little change from previous drafts.”⁸⁶

B. The National Medium- and Long-Term Plan for the Development of Science and Technology (2006–2020)

In February 2006, the State Council unveiled a landmark document—the MLP.⁸⁷ The MLP envisions that China will establish a full-fledged major research and development infrastructure system by 2030.⁸⁸ The MLP explicitly states that a key tool for China to create its own IP will be through tweaking foreign technology, and refers to indigenous innovation as “enhancing original innovation” through co-innovation and re-innovation “based on the *assimilation* . . . of imported technologies.”⁸⁹ However, the legal definitions of “co-innovation” and “re-innovation” remain unclear.⁹⁰ Not only does the MLP encourage co-innovation and re-innovation, it “also warns against blindly importing foreign technology without plans to transform it into Chinese technology.”⁹¹ The MLP states, “[O]ne should be clearly aware that importation of technology without emphasizing the assimilation, absorption, and re-innovation is bound to weaken the nation’s indigenous [research and development] capacity.”⁹² President Hu referred to the approach as “innovation with Chinese characteristics.”⁹³ Although

⁸⁵ *Id.*

⁸⁶ SAIC Releases Rules on Anti-Monopoly IP Abuse Prohibitions, U.S. INFO. TECH. OFF., <http://www.usito.org/news/saic-releases-rules-anti-monopoly-ip-abuse-prohibitions> [<https://perma.cc/3E5R-MYWY>] (last visited Apr. 18, 2016).

⁸⁷ *MLP for Science and Technology Development*, *supra* note 54.

⁸⁸ See *National Medium- and Long-Term Plan for Major R&D Infrastructure Issued*, CHINA SCI. & TECH. NEWSL. (2013), <http://houston.china-consulate.org/eng/st/t1035062.htm> [<https://perma.cc/Y7WA-Q3A5>].

⁸⁹ JAMES MCGREGOR, GLOBAL INTELL. PROP. CTR., CHINA’S DRIVE FOR “INDIGENOUS INNOVATION”: A WEB OF INDUSTRIAL POLICIES (July 27, 2010), https://www.uschamber.com/sites/default/files/legacy/reports/100728chinareport_0.pdf [<https://perma.cc/3JRR-7CRF>] at 4 (emphasis added) (quoting *MLP for Science and Technology Development*, *supra* note 54, at 10).

⁹⁰ See *id.* at 38.

⁹¹ See *id.* at 4.

⁹² *MLP for Science and Technology Development*, *supra* note 54, at 11.

⁹³ See MCGREGOR, *supra* note 89, at 13.

not specified, the legal authority of re-innovation may lie in the prohibition on grant-back clauses.

This policy has allowed China to increase its market power in key emerging science and technology markets,⁹⁴ however, the MLP also led to a backlash from foreign governments and companies.⁹⁵ In 2011, under mounting pressure from foreign companies, governments, and trade lobbies, China's State Council abolished the policy of "forcing" foreign companies to transfer their IP to Chinese companies to bid for government contracts.⁹⁶

C. *The TRIPS Agreement and China's WTO Commitments*

There is currently no international treaty that directly addresses technology transfer, and the World Trade Organization ("WTO") does not regulate technology transfer.⁹⁷ Although the WTO regulates trades in technology under the Agreement on Trade Related Intellectual Property Rights ("TRIPS Agreement"), it merely sets forth minimum standards for IP rights, leaving regulation of technology transfer to individual countries.⁹⁸

The TRIPS Agreement, however, does create a legal obligation for developed countries to help promote and encourage "technology transfer to least-developed country Members in order to enable them to create a sound and viable technological base."⁹⁹ According to the TRIPS Agreement, "The protection and enforcement of intellectual property rights should contribute to the promotion of technological innovation and to the transfer and dissemination of

⁹⁴ See *supra* Section I.B.

⁹⁵ See *supra* Section I.B; see also Raheja, *supra* note 38.

⁹⁶ See Raheja, *supra* note 38.

⁹⁷ See Chow, *supra* note 1, at 504, 504 n.38; *Understanding the WTO—What We Do*, WORLD TRADE ORG., https://www.wto.org/english/thewto_e/whatis_e/what_we_do_e.htm [<https://perma.cc/4FPZ-2U6M>] (last visited Oct. 31, 2015). The WTO aims to provide a forum in which WTO members can agree to lower trade barriers and resolve trade disputes. See *Understanding the WTO—What We Do*, *supra*.

⁹⁸ See Chow, *supra* note 1, at 504; see also Trade-Related Aspects of Intellectual Property Rights, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1C, 1869 U.N.T.S. 299 [hereinafter TRIPS Agreement]. The TRIPS Agreement does regulate compulsory licensing to increase access to medicine, which are protected by patents, in developing countries. See *id.* This Note, however, focuses on voluntary—not compulsory—technology transfers in licensing agreements.

⁹⁹ TRIPS Agreement, *supra* note 98, at art. 66.

technology”¹⁰⁰ Importantly, “developed country Members shall provide, on request and on mutually agreed terms and conditions, technical and financial cooperation *in favour of* developing and least-developed country Members.”¹⁰¹ Notably, China is not one of the least-developed countries recognized by the WTO, and there is no WTO definition of “developing” countries.¹⁰²

When China joined the WTO in 2001, it committed that “the terms and conditions of technology transfer, particularly in the context of an investment, should be agreed between the parties to the investment without government interference.”¹⁰³ The 2002 Technology Regulations potentially raise an issue under China’s WTO commitments because the regulations treat foreign companies and domestic companies differently. Particularly, the 2002 Technology Regulations only apply to technology imports where foreign licensors transfer technologies to Chinese licensees and do not apply to exports where Chinese licensors transfer technologies to foreign licensees.¹⁰⁴

III. COMPARATIVE APPROACH

A. *How It Works in Totality: Looking at Other Laws*

1. Indemnification Provision

Article 24 (“indemnification provision”) of the 2002 Technology Regulations provides that if the licensor’s use of the technology, as agreed in the contract, infringes a third party’s rights and interests, the licensor shall bear the liability.¹⁰⁵ It results in foreign

¹⁰⁰ *Id.* at art. 7.

¹⁰¹ *Id.* at art. 67 (emphasis added).

¹⁰² See *Understanding the WTO—Least-Developed Countries*, WORLD TRADE ORG., https://www.wto.org/english/thewto_e/whatis_e/tif_e/org7_e.htm [<https://perma.cc/X9ZT-WPQF>] (last visited Oct. 31, 2015).

¹⁰³ Working Party on the Accession of China, *Report of the Working Party on the Accession of China*, ¶ II.6.48, WT/MIN(01)/3 (Nov. 10, 2001), https://www.wto.org/english/thewto_e/acc_e/wp_acc_china_e.doc [<https://perma.cc/7645-DLRQ>].

¹⁰⁴ See *supra* note 56 and accompanying text.

¹⁰⁵ 2002 Technology Regulations, *supra* note 12, at art. 24.

licensors' *non-negotiable* statutory obligation to indemnify licensees for third-party infringement claims.¹⁰⁶

The indemnification provision is similar to the prohibition on grant-back clauses because both provisions are mandatory. Thus, a violation of the indemnification provision is arguably per se illegal under Article 329 of the Contract Law.¹⁰⁷ However, the grant-back regime differs from the indemnification provision because it creates ownership uncertainties, thereby restricting possibilities of true collaboration between the parties, while the indemnification provision merely deals with price-related cost.¹⁰⁸

2. Antitrust Law

a) *Qualcomm*

On February 9, 2015, the National Development and Reform Commission (“NDRC”)¹⁰⁹ fined Qualcomm—a U.S.-leading chip manufacturer—a record \$975 million for abusive patent licensing practices.¹¹⁰ The NDRC found that Qualcomm abused its dominant market position in three ways—excessive pricing, unfair terms, and bundling—practices that are prohibited by the AML.¹¹¹ Among these licensing practices, the practice that is the most akin to grant-back clauses is cross-licensing condition. Under its cross-licensing condition, Qualcomm required its customers to grant Qualcomm their own patent licenses for free but refused to reduce royalties by the value of these licenses.¹¹²

The Qualcomm case “is a milestone in the ramp-up Chinese antitrust law enforcement,” as it represents the highest fine to date

¹⁰⁶ See Cohen, *supra* note 18.

¹⁰⁷ See Contract Law, *supra* note 52, at art. 329.

¹⁰⁸ See 2002 Technology Regulations, *supra* note 12, at art. 24; Contract Law, *supra* note 52, at art. 329.

¹⁰⁹ The NDRC is a macroeconomic management agency responsible for enforcement with respect to alleged anticompetitive activities involving pricing. Jonathan Gowdy & Bradley S. Lui, *China Takes First Steps in Implementing New Anti-Monopoly Law*, 12 M&A LAW. 14, 14 (2008).

¹¹⁰ See Victor Ho et al., *Antitrust in China: NDRC v. Qualcomm—One All*, ALLEN & OVERY (Feb. 12, 2015), <http://www.allenoverly.com/publications/en-gb/Pages/Antitrust-in-China-NDRC-v--Qualcomm-%E2%80%93-One-All.aspx> [<http://perma.cc/H897-JKAS>].

¹¹¹ See IP Rights Guidelines, *supra* note 53, at art. 10.

¹¹² See *id.*

in China.¹¹³ Further, the Qualcomm case put the NDRC “on a par with other competition authorities around the world, such as the European Commission, for having a reputation for taking strong action against anticompetitive conduct by dominant companies.”¹¹⁴ The NDRC also imposed non-traditional “behavioral” remedies, including calculating the royalty rates based on 65%—instead of 100%—of the wholesale price.¹¹⁵ The NDRC believed that such behavioral remedies would boost Chinese mobile device manufacturers by ensuring favorable licensing terms with Qualcomm.¹¹⁶

On the one hand, the U.S. Chamber of Commerce has criticized the NDRC’s investigation as “designed to bias license negotiations in favor of would-be Chinese licensees.”¹¹⁷ On the other hand, the Qualcomm case demonstrates that Chinese authorities consider non-Chinese defendants interests in antitrust investigations because the outcome depends on the quality of arguments and evidence submitted.¹¹⁸ More importantly, the Qualcomm case demonstrates that the Chinese antitrust authorities are willing to adopt creative remedies that foreign companies propose.¹¹⁹ Indeed, Qualcomm “only agreed to slight modifications in its royalty rates in China,” which “can be looked at as nothing but a win for Qualcomm.”¹²⁰

In 2014, Qualcomm received \$13.2 billion in revenue from Chinese companies, constituting almost half of its \$26.5 billion total revenue.¹²¹ Steve Mollenkopf, Qualcomm’s CEO, acknowledged

¹¹³ See *id.*

¹¹⁴ See *id.*

¹¹⁵ See *id.*

¹¹⁶ See *id.*

¹¹⁷ See U.S. CHAMBER OF COMMERCE, COMPETING INTERESTS IN CHINA’S COMPETITION LAW ENFORCEMENT: CHINA’S ANTI-MONOPOLY LAW APPLICATION AND THE ROLE OF INDUSTRIAL POLICY 66 (Sept. 9, 2014), https://www.uschamber.com/sites/default/files/aml_final_090814_final_locked.pdf [<https://perma.cc/E8GT-FSX5>].

¹¹⁸ See Ho et al., *supra* note 110.

¹¹⁹ See *id.*

¹²⁰ Don Clark, *Qualcomm to Pay \$975 Million Antitrust Fine to China*, WALL ST. J. (Feb. 10, 2015, 4:37 AM), <http://www.wsj.com/articles/qualcomm-settles-china-probe-1423518143> [<https://perma.cc/Z6AQ-TX3V>].

¹²¹ See SAMUEL G. WILLIAMSON ET AL., KIRKLAND & ELLIS, CHINA CONTINUES ITS AGGRESSIVE ANTI-MONOPOLY LAW ENFORCEMENT WITH A RECORD-BREAKING \$975 MILLION FINE AGAINST QUALCOMM (Feb. 2015), http://www.kirkland.com/siteFiles/Publications/Alert_2232015.pdf [<https://perma.cc/CAB4-G5LG>]; *Qualcomm Under*

that the antitrust probe was a major source of uncertainty about Qualcomm's future.¹²²

b) *Huawei Technologies v. InterDigital*

InterDigital is an American company that designs and develops advanced technologies for wireless communications, and it owns patents on international wireless communications standards.¹²³ In October 2013, the Guangdong High Court of China held that InterDigital abused its dominant market position in the licensing of standard essential patents ("SEPs") for 3G wireless communications because InterDigital sought injunctive relief in the United States against Huawei, which is a willing licensee.¹²⁴

Qiu Yongqing, the Chief Judge of the Guangdong Higher People's Court, suggested that Chinese enterprises should follow Huawei's footsteps and bravely employ anti-monopoly lawsuits to break technology barriers and win space for development.¹²⁵ However, Judge Qiu's comment has received criticisms that Chinese courts pay more attention to industrial policy concerns than the legal merits of the case.¹²⁶

Patent Policy Fire, GURUFOCUS (Dec. 30, 2014), <http://www.gurufocus.com/news/302668/qualcomm-under-patent-policy-fire> [<https://perma.cc/Q5UM-JGKA>].

¹²² See Clark, *supra* note 120.

¹²³ *Chinese Court Publishes Decisions Finding That InterDigital Violated AML Through Discriminatory Pricing, Sets FRAND Rate for Licensing InterDigital's SEPs Under Chinese Standards*, ORRICK ANTITRUST & COMPETITION NEWSL. (June 6, 2014), <http://blogs.orrick.com/antitrust/2014/06/06/chinese-court-publishes-decisions-finding-that-interdigital-violated-aml-through-discriminatory-pricing-sets-frand-rate-for-licensing-interdigitals-seps-under-chinese-standards/> [<http://perma.cc/FV7K-QXFU>].

¹²⁴ See Huawei Jishu Youxian Gongsi Su Jiaohu Shuzi Tongxin Youxian Gongsi An (华为技术有限公司诉交互数字通信有限公司案) [*Huawei v. InterDigital*], 2013 Yue Gao Fa Min San Zhong Zi No. 306, (Guangdong High People's Ct. 2013) (China); MICHAEL HAN & KEVIN LI, FRESHFIELDS BRUCKHAUS DERINGER LLP, *HUAWEI V. INTERDIGITAL: CHINA AT THE CROSSROADS OF ANTITRUST AND INTELLECTUAL PROPERTY, COMPETITION AND INNOVATION* (Nov. 28, 2013), <https://www.competitionpolicyinternational.com/assets/Uploads/AsiaNovember3.pdf> [<https://perma.cc/Z98V-4G9D>].

¹²⁵ See U.S. CHAMBER OF COMMERCE, *supra* note 117, at 76.

¹²⁶ See *id.* at 77.

B. International Perspectives: Grant-Back Regimes in Other Jurisdictions

In most countries, technology transfer is subject to some form of competition law because licensing IP rights in technology transfers may extend the monopoly to the licensees, thereby creating anticompetitive effects detrimental to the local economy.¹²⁷ Below, the competition laws of the United States and the European Union are compared with that of China.

1. The United States: Rule of Reason

In the United States, grant-back clauses are not per se illegal but rather are evaluated under the “rule of reason.”¹²⁸ The 1995 Antitrust Guidelines for the Licensing of Intellectual Property indicate that, in applying the rule of reason, anticompetitive effects should be balanced against offsetting pro-competitive effects.¹²⁹ Anticompetitive effects include reducing the licensee’s incentive to invest in improving the licensed technology while pro-competitive effects include allowing the parties to share risks and compensating the licensor for making improvements.¹³⁰ An important factor of the assessment is the licensor’s market power in the relevant market.¹³¹ In practice, IP licensing practices are rigorous in the United States, resulting in great revenues.¹³²

The rule of reason would not be entirely practicable in China because Chinese courts do not play as prominent of a role in establishing the law as U.S. courts do. Instead of being one of the three equal branches of the government, Chinese courts are viewed as subordinate to the legislative branch and part of the Communist

¹²⁷ See Chow, *supra* note 1, at 505.

¹²⁸ *Transparent Wrap Mach. Corp. v. Stokes & Smith Co.*, 329 U.S. 637, 648 (1947).

¹²⁹ U.S. DEP’T OF JUSTICE & FED. TRADE COMM’N, ANTITRUST GUIDELINES FOR THE LICENSING OF INTELLECTUAL PROPERTY § 5.6 (Apr. 6, 1995), <http://www.justice.gov/atr/antitrust-guidelines-licensing-intellectual-property#t57> [<http://perma.cc/GK89-7WK4>].

¹³⁰ See *id.*

¹³¹ See *id.*

¹³² See *supra* Section III.A.2.

Party.¹³³ Consequently, Chinese court decisions have limited authority and little precedential value.¹³⁴

Although the rule of reason does not fit into China's legal system perfectly, it nonetheless sheds light on how China should restructure its grant-back regime. China should make the rule of reason the default rule for non-severable improvements.¹³⁵ Since the rule of reason is part of antitrust law, it is less restrictive than Article 329 of the Contract Law.¹³⁶ Regardless, the rule of reason effectively invalidates any abuse of the relaxed grant-back regime.

2. The European Union: Severable Versus Non-Severable Improvements

European Community Regulation 772/2004 distinguishes between "non-severable" improvements and "severable" improvements.¹³⁷ Severable improvements can be used without using the original licensed patent, while non-severable improvements cannot be used without using the original patent.¹³⁸ On the one hand, E.U. law prohibits grant-back clauses on severable improvements, with licensees owning severable improvements.¹³⁹ On the other hand, E.U. law allows grant-back clauses on non-severable improvements,¹⁴⁰ differing from China's prohibition on grant-back clauses. In China, if the Chinese licensee makes a non-severable improvement and subsequently obtains a patent for that improvement, once the licensing agreement expires, the Chinese licensee may hinder the foreign licensor's ability to use the *original* patent in China.¹⁴¹ China's prohibition on grant-back clauses is more restrictive and

¹³³ DANIEL C.K. CHOW, *THE LEGAL SYSTEM OF CHINA IN A NUTSHELL* 198–202 (2d ed. 2009).

¹³⁴ *See id.*

¹³⁵ *See infra* Section IV.B.

¹³⁶ *See supra* Section I.A.2.

¹³⁷ Commission Regulation 772/2004 of Apr. 27, 2004, Application of Article 81(3) of the Treaty to Categories of Technology Transfer Agreements, art. 1.1(n), 2004 O.J. (L123) 11, 14.

¹³⁸ *See id.*

¹³⁹ *See id.* at art. 5.1(b).

¹⁴⁰ *See id.*

¹⁴¹ *See* Chow, *supra* note 1, at 519–20.

protective of the licensees, while E.U. law is more technical and precise.¹⁴²

China should adopt the E.U. model, prohibiting grant-back clauses on severable improvements.¹⁴³ Many argue that E.U. competition law is the most sophisticated in the world.¹⁴⁴ The European Commission constantly studies, revises, and fine-tunes E.U. competition laws based on its acquired experience.¹⁴⁵ More importantly, China has previously borrowed from E.U. competition law, rather than U.S. law, in creating its model modern competition law.¹⁴⁶ This is in part because China has adopted a civil law system that is similar to the E.U. system, where statutes and regulations are the primary sources in establishing laws.¹⁴⁷

Notably, a distinction exists regarding the ultimate authority in interpreting laws. In China, the final authority on most issues regarding competition law is the powerful MOFCOM.¹⁴⁸ In contrast, although the European Commission plays an important role in implementing its competition laws, the ultimate implementing authority lies in the Court of Justice of the European Communities, a high court.¹⁴⁹ Therefore, aside from distinguishing severable and non-severable improvements, China should subject any abuse of the relaxed grant-back regime for non-severable improvements to the rule of reason under the AML.¹⁵⁰

¹⁴² See *id.* at 528.

¹⁴³ See *supra* Section II.B.1; see also *infra* Sections IV.A–B.

¹⁴⁴ See Chow, *supra* note 1, at 498.

¹⁴⁵ See *id.* at 526.

¹⁴⁶ DANIEL C.K. CHOW & ANNA M. HAN, DOING BUSINESS IN CHINA: PROBLEMS, CASES, AND MATERIALS 227 (West 2012).

¹⁴⁷ See *id.*

¹⁴⁸ MINISTRY OF COMMERCE PEOPLE'S REPUBLIC OF CHINA, <http://english.mofcom.gov.cn> [<http://perma.cc/KC38-7CJ3>] (last visited Oct. 31, 2015); see also U.S.–CHINA BUS. COUNCIL, COMPETITION POLICY AND ENFORCEMENT IN CHINA (Sept. 2014), https://www.uschina.org/sites/default/files/AML%202014%20Report%20FINAL_0.pdf [<https://perma.cc/9AN7-JEQL>].

¹⁴⁹ See, e.g., Case T-5/02, *Tetra Laval BV v. Comm'n*, 2002 E.C.R. II-4381 (overruling the decision by the European Commission that blocked an acquisition by Tetra Laval of Sidel).

¹⁵⁰ See *infra* Section IV.B.

IV. CHINA SHOULD REFORM ITS CURRENT GRANT-BACK REGIME

A. China Should Continue to Prohibit Grant-Back Clauses on Severable Improvements

Since the European Union's approach is well received and China has followed many E.U. models, China should adopt their approach in distinguishing severable and non-severable improvements.¹⁵¹ China should not relax its grant-back regime all at once. As SAIC acknowledged in 2013, China was not ready for full-blown and tailored antitrust guidelines because China had only been enforcing the AML in the IP field for a brief period of time and thus lacked experience.¹⁵²

B. China Should Make Grant-Back Clauses on Non-Severable Improvements Non-Mandatory and Evaluate Potential Abuse Under the Rule of Reason of the Antitrust Law

China's current mandatory grant-back regime is too restrictive.¹⁵³ Therefore, the default rule for non-severable improvements should be non-mandatory, where parties are free to decide the ownership of improvements. Any potential abuse of this non-mandatory grant-back rule should be subject to antitrust law. This is because grant-back clauses have both pro-competitive and anti-competitive effects.¹⁵⁴ Grant-back clauses may be pro-competitive because they promote innovation and subsequent licensing by providing a means for the licensee and the licensor to share risks and by rewarding the licensor for making further innovation based on the licensed technology.¹⁵⁵ Grant-back clauses may also be pro-competitive if they substantially reduce the licensee's incentives to engage in research and development.¹⁵⁶ Indeed, other countries in-

¹⁵¹ See *supra* Section II.B.2.

¹⁵² Hao Zhan, *SAIC Moves Closer to Antitrust Rules for Intellectual Property*, INT'L LAW OFF. (July 31, 2014), <http://www.internationallawoffice.com/newsletters/detail.aspx?g=f8cbb0d5-6d93-4b19-b972-5a06cc0c92d1> [<http://perma.cc/Q2KF-STTA>].

¹⁵³ See *supra* Parts I, III.

¹⁵⁴ See *supra* Sections I.A–B.

¹⁵⁵ See U.S. DEP'T OF JUSTICE & FED. TRADE COMM'N, *supra* note 129, § 5.6 at 30.

¹⁵⁶ See *id.*

clude their grant-back regime as part of the antitrust law.¹⁵⁷ Further, China should adopt the United States' rule of reason when assessing abuse because the United States' high revenues from IP licensing prove that the rule of reason is well functional.¹⁵⁸

C. China Should Apply Its Grant-Back Rules to Foreign and Domestic Companies Equally and Fairly

China's grant-back regime is too protective of the recipient of the technology (usually a Chinese business entity), giving Chinese licensees unfair advantages.¹⁵⁹ China essentially uses state coercion to obtain technology transfer. Particularly, the 2002 Technology Regulations only prohibit grant-back clauses by foreign licensors but not Chinese licensors, which might have compromised China's WTO commitments.¹⁶⁰ Wang Xiaoye, a Chinese legal scholar, argues that China's technology transfer regime does not adequately take the licensor's interests into account and imposes unreasonable restrictions on the licensor.¹⁶¹

Further, foreign companies often feel pressure to cultivate relationships with enforcement authorities such as MOFCOM because, in practice, MOFCOM is the final authority with a broad discretion on technology transfer issues.¹⁶² Cultivating relationships, while necessary, brings additional risks as China has a culture of corruption.¹⁶³ In fact, China's antitrust law has already raised concerns at the highest levels of the U.S. government. In December 2014, President Obama raised concerns directly to President Xi.¹⁶⁴ White House National Security Council spokesman Patrick Ventrell explained, "The United States government is concerned that China is using numerous mechanisms, including anti-

¹⁵⁷ See *supra* Section III.B.

¹⁵⁸ See *supra* Section III.B.1.

¹⁵⁹ See *supra* Section IV.B.

¹⁶⁰ See *supra* Sections II.B-C.

¹⁶¹ See XIAOYE WANG, THE EVOLUTION OF CHINA'S ANTI-MONOPOLY LAW § 3.2, at 227 (2014).

¹⁶² See Chow, *supra* note 1, at 528.

¹⁶³ *Id.*

¹⁶⁴ See Michael Martina & Matthew Miller, *As Qualcomm Decision Looms, U.S. Presses China on Antitrust Policy*, REUTERS (Dec. 15, 2014), <http://www.reuters.com/article/2014/12/16/us-qualcomm-china-antitrust-idUSKBN0JU0AK20141216> [<http://perma.cc/BQZ3-LSZK>].

monopoly law, to lower the value of foreign-owned patents and benefit Chinese firms employing foreign technology.”¹⁶⁵

China’s unequal treatment to Chinese and foreign companies has compromised China’s reputation. As a result, Chinese companies encountered difficulties when entering foreign markets. For example, in 2004, when Lenovo (a Chinese company) proposed to purchase IBM’s personal computer division, the U.S. Congress strongly opposed the transaction.¹⁶⁶ Hostility against Chinese companies re-emerged in 2005 when COMCC (another Chinese company) attempted to acquire Unocal (a U.S. petroleum firm).¹⁶⁷ Confronted with strong reactions by U.S. politicians, this transaction was not consummated.¹⁶⁸ As a result, many Chinese companies criticized the United States for denying Chinese companies’ fair access to the United States market for fear of competition.¹⁶⁹

D. China Should Reform Its Grant-Back Regime Now Rather Than Later

In the past, China justified its prohibition on grant-back clauses by characterizing itself as a developing country.¹⁷⁰ China’s highly restrictive grant-back provision has become a remnant of a bygone era during which time China did not trust foreign companies.¹⁷¹ As recently as two decades ago, China was a developing country just starting on the path of industrialization. China was afraid that crafty and experienced business-minded foreign companies would exploit inexperienced Chinese businesses.¹⁷² This attitude may have led to such a sweeping prohibition on grant-back clauses that requires an absolute warranty from foreign licensors.

Today, however, this distrust in foreign companies is outdated. As the world’s second largest economy, China has many sophisticated businesspersons who are experienced in dealing with foreign

¹⁶⁵ *Id.*

¹⁶⁶ See Yong Huang, *Pursuing the Second Best: the History, Momentum, and Remaining Issues of China’s Anti-Monopoly Law*, 75 ANTITRUST L.J. 117, 122–23 (2008).

¹⁶⁷ See *id.* at 123.

¹⁶⁸ See *id.*

¹⁶⁹ See *id.*

¹⁷⁰ See Chow, *supra* note 1, at 499.

¹⁷¹ See *id.* at 528.

¹⁷² See CHOW & HAN, *supra* note 146, at 357.

companies.¹⁷³ China has made impressive progress in technology intensive and high-end manufacturing through technology transfer.¹⁷⁴ Although the grant-back regime may have previously helped Chinese companies gain market power as importers, it now hurts China's reputation in international trades,¹⁷⁵ thereby limiting China's potential for technology export in the future.

¹⁷³ See Chow, *supra* note 1, at 529.

¹⁷⁴ See *supra* Section I.A.

¹⁷⁵ See *supra* Section IV.D.