

# Pacific Industrial Property Association: Non-Binding Conciliation Between Japanese And American Companies

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The Pacific Industrial Property Association (PIPA) has studied the arbitration and conciliation procedures applicable to industrial property disputes between Japanese and Americans, and has sponsored a new conciliation procedure, while suggesting that existing arbitration procedures be modified in accordance with the recommendations of certain authorities in this specialized field:

The proposed conciliation procedure of the Pacific Industrial Property Association appears to be the only formalized conciliation, or for that matter arbitration, procedure specific to industrial property issues. The procedure was developed to meet a perceived need in this complex segment of Japanese/American business relations, relating to patents, trademarks, know-how, and their licensing and exchange:

International communication is difficult in the best of circumstances. Communication between disputants at least one of whom feels wronged, having language and cultural barriers, and involving complex technical and legal issues, is indeed difficult. The member-

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ship of PIPA sought a method of opening this communication barrier between Japanese and Americans, in the fields of business interaction involving high technology and industrial property.

The philosophy of conciliation, at least in the context of Japanese/American relations, is different from the philosophy of either arbitration or litigation. It is the philosophy of compromise. It accepts all the classical reasons favoring arbitration over litigation: the complexity of high-technology subject matter, the commitment of the parties in capital and other investment, the inequity of injunction, the inadequacy of money damages, the high cost and time of litigation—and then it shifts: from an arbitrator who acts as judge and whose decision is binding, to a mediator who acts as guide and participant and who helps the parties to work out their differences voluntarily.

One generally assumes that, before resorting to either arbitration or litigation, the parties will have attempted to settle their own differences. In most cases compromises will already have been considered and will have failed. In most cases, parties to a contract containing an arbitration clause would normally, without formality, have talked things over before either party invoked the arbitration clause.

Why then would parties to a patent license want a “conciliation” clause in the contract? The PIPA membership decided that it could be helpful to provide a semi-formal method of bridging the communications gap between Japanese and Americans, as an aid to people who probably would want to bridge that gap—or at least to people who in advance know that should a dispute arise they may encounter communications problems to compound any other problems over the life of a contract.

This was a natural for the Pacific Industrial Property Association. PIPA was formed eight years ago by representatives of Japanese and American industry, usually through their chief patent or licensing officer, most of whom had frequent business dealings with the other country and were already devoting time to studying the industrial property practices of the other country. Perhaps the American and Japanese representatives were also feeling the effects of inadequate or incomplete advice on industrial property matters, frustrations with the Patent Offices and practices of the other country, and the evolution of increased complexity in the relationships between Japanese and American businesses.

The PIPA membership includes over sixty Japanese companies and over eighty United States companies, representing major users

of the patent system in each country and major participants in technology exchange between Japan and the United States. To study the industrial property issues of Japan and the United States, the membership was formed into concurrent working committees for each country. The licensing committees eventually spun off their conciliation and arbitration study groups, because of the growing interest in these areas by PIPA members. These groups studied the applicable national and international laws and procedures for both arbitration and conciliation, and eventually proposed procedures in both these areas. It was in the course of these studies that it was concluded that there could be value in providing a new and special conciliation service, specific to intellectual property and licensing.

Each national group conducted surveys of its members, to estimate the frequency and nature of disputes between Japanese and American nationals involving intellectual property, and to observe what existing services or fora were invoked in settling these disputes. The results of these surveys were remarkably similar between the group of American respondents and the Japanese group.

About 80% of the American respondents (about 1/3 of the PIPA membership) reported that they had had disputes related to industrial property matters. It is assumed that most of those who did not respond to the survey would have answered in the negative. Of those who did respond, about 75% said that the subject of their disputes was related to patents, and 40% had been involved in disputes relating to know-how and technical information. There was reference in several cases to trademarks, over and above routine trademark opposition procedures. Several of the respondents noted that they have had fairly large numbers of trademark oppositions and patent oppositions, but these were not included in the survey.

Almost all of the American respondents having patent disputes said that they involved issues relating to patent validity and patent infringement. Fifty percent of these stated that the issue was validity or interpretation of patent rights, and 60% stated that infringement was an issue. There is clearly some overlap. A few respondents said that antitrust questions were involved.

Almost half of the United States respondents stated that they had been involved in disputes with Japanese on the scope of contracts relating to industrial property transfers. One third of these stated that the contract disputes related to the royalty and payment terms; 20% stated that the licensed territory was disputed. Other areas of disagreement concerned secrecy obligations, the duration of the agreement, and other problems of interpretation of the contract.

The disputes were settled in various ways. Twenty-five percent of the United States respondents resorted to litigation. Fifteen percent were settled by adjudication under Article 71 of the Japanese Patent Law, which provides that "with respect to the technical scope of a patented invention, an interpretation may be demanded of the Patent Office"; the Director of the Patent Office designates three judges, who follow a specified procedure and give their interpretation. There were no settlements reported by United States respondents through the use of conciliation under the Japanese law for Conciliation of Civil Affairs. Two disputes were settled by arbitration through existing organizations, namely the International Chamber of Commerce and the American Arbitration Association. Two respondents had settled their disputes through conciliation by a third party, one of these having used the conciliation procedure of the International Chamber of Commerce.

The PIPA analysis of these returns from the American group, and corresponding returns from the Japanese group, was as follows: Patent infringement is the major cause of dispute, and contract interpretation is the second cause of dispute; patent validity appears to be tied to infringement. There were an especially large number of settlements by negotiation. There was less settlement by arbitration and formal conciliation than by litigation. It isn't known how frequently negotiation between the parties had been tried and had failed. But it was becoming clearer to both the Japanese and American participants that some help in settling disputes could be of value.

### *Arbitration*

The working committees of PIPA studied the existing conciliation and arbitration services that might be most applicable to patent and licensing disputes between Japanese and American nationals. Despite the unsettled state of United States law on arbitration of patent issues, arbitration is very attractive for the settlement of patent disputes involving nationals of other countries. In 1970 the United States passed the enabling legislation for enforcement in U.S. courts of awards under the International Commercial Arbitration Convention of 1958. This convention is enforceable in Japan. This should encourage use of arbitration in Japanese/American patent disputes.

For arbitration clauses in contracts involving United States and Japanese transactions, many authors<sup>1</sup> have taken pains to point out

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<sup>1</sup> Sanders, Pieter, editor, "International Arbitration Liber Amicorum for Martin Domke," published by Martinus Nijhoff, The Hague (1967).

the pitfalls in using the brief general type of arbitration clause such as is recommended by the American Arbitration Association or the Japanese Commercial Arbitration Association. A typical and preferred form of model arbitration clause is the following, from an article by Professors Kawakami and Henderson entitled "Arbitration in U.S.-Japanese Sales Disputes."<sup>2</sup>

*"Settlement of Disputes:*

"(1) This clause is an integral part of this contract and is not separable and has no independent validity.

"(2) Questions of the validity of this contract and the scope of this arbitral clause are reserved for the court but if such questions are raised and decided in court, the loser shall pay all costs including a reasonable fee for the winner's attorney.

"(3) All other disputes, controversies, or differences which may arise between the parties, out of or in relation to or in connection with this contract, or for the breach thereof, shall be finally settled by arbitration pursuant to the Japan-American Trade Arbitration Agreement of September 16, 1952, by which each party hereto is bound except as modified by these provisions.

"(4) All arbitrations will be held in \_\_\_\_\_ [city] and this contract (including this arbitral clause), and all arbitral proceedings and awards hereunder will be governed by the internal law of \_\_\_\_\_ [usually the place of arbitration].

"(5) The parties hereto also agree that they will instruct the arbitrator in any proceeding hereunder not to specify his reasoning in his award." (pages 585-6)

The consensus of writers on this subject is that the Japanese-American Trade Arbitration Agreement, entered into by the American Arbitration Association and the Japanese Commercial Arbitration Association should be used. When this Agreement is incorporated into a contract, either by including their model arbitration clause or a modification of it such as has been recommended, arbitration in Japan is conducted under the rules of the JCAA and arbitration in the United States is conducted under the rules of the AAA. The Japanese-American Trade Arbitration Agreement itself also provides a method, albeit complex, for fixing the place of arbitration if the parties themselves do not provide in the contract for the place of the arbitration. In the context of the critical differences between the Uniform Commercial Code and Japanese sales law, as well as in the laws governing intellectual property and its transfer, decisions on substantive issues can turn on the site of arbitration, which site may not be known until the controversy shall have arisen.

There is a school of thought which views arbitration as merely

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<sup>2</sup> University of Washington Law Review, Vol. 42 (March 1967) starting at page 541.

procedural, such that the law to be applied by arbitrators in dealing with issues involving foreign interests should be the law of the site of arbitration. But in Japan, Professor Kawakami advises, the parties have by law the right to choose the applicable law, whatever the forum of arbitration and independent of how this site is chosen. If the parties' choice is not made, or is not clear, then the applicable law may be judicially determined, and has either been chosen as the law of the place where the contract is to be performed, or the court has sought for the implied intention of the parties as to governing law.

From the viewpoint of drafting patent and know-how licenses with Japanese parties, it appears to be more important to name the applicable law than to decide on the site of arbitration. For instance, the parties might not consider it at all fair to decide in advance that the arbitration will be held in New York, no matter which party has committed the alleged wrong. It is usual to compromise on the site of arbitration; and if the law governing the contract is named in the contract, the site of the arbitration becomes less controlling of the outcome.<sup>3</sup>

For patent and know-how licenses of international scope, and particularly for those not unusual licenses which involve patents in several countries, and know-how which may flow in both directions, this can become exceedingly complex. It may be expressly provided in the arbitration clause that issues relating to the validity and scope of the patent shall be governed according to the law under which the patent was granted. Suppose, for example, an American firm licenses a Japanese firm under the American firm's Japanese, Australian, and Taiwanese patents for a particular subject matter. Suppose a dispute under a patent license has to do with not only patent scope, but also the contract terms, such as a dispute about royalty payments or accounting systems. It appears wise to set forth explicitly the parties' choice of governing law on all phases of the contract<sup>4</sup> since the standard clauses recommended by the AAA, the JCAA, and the International Chamber of Commerce, as well as existing treaty provisions, do not adequately deal with this problem. There does, however, seem to be some doubt as to the acceptance by all jurisdictions of the principle of applying any law other than that of the site of arbitration.<sup>5</sup>

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<sup>3</sup> Maw, "Applicable Law and Conflict Avoidance in International Contracts," Record of the Association of the Bar of the City of New York, 365 (June 1970).

<sup>4</sup> Ehrenzweig, "Contracts in the Conflict of Laws," 50 Columbia Law Review 973 (1959).

<sup>5</sup> Kitagawa, "Contractual Autonomy," International Arbitration. . . , *op.cit.*, 133,140.

In the model clause presented earlier, the arbitrators are expressly freed from the need to include their reasoning in the award, as they would otherwise be required to do—to avoid “suffocating” the arbitration with legal action. If such a provision is not expressly included, an award in Japan can be voided if the arbitrators do not include adequate details of their reasoning.<sup>6</sup> This is a pitfall for the unwary, since in the United States an arbitrator is under no duty to give his reasons.

The cited Japanese commentators also advised that the contract should state that the arbitration clause is not separable from the rest of the contract, so that the court rather than the arbitrators would determine if there was fraud in the inception of the contract. This was intended, from the Japanese viewpoint, to counteract a trend they perceived in the United States to permit the arbitrators to decide threshold questions.

It is important also to state which arbitration agreement or procedure is intended to apply, since there are several alternatives to the Japanese-American Trade Arbitration Agreement. Arbitration under the rules of the International Chamber of Commerce may be designated. There are arbitration procedures in the Japanese Civil Procedure Code, as well as the various federal and state arbitration statutes of the United States. Any of these may be selected—and depending upon the site of performance of the contract, it may be that any of these procedures would be as fair to both parties as any other choice of arbitration rules.

Thus, the consensus from the American viewpoint was that arbitration is a useful procedure for settling disputes involving Japanese and American companies, and is probably particularly well suited to the complexities of patent and know-how agreements. Nevertheless, PIPA turned to conciliation.

### *Conciliation*

The basic principle behind conciliation, and a major reason for its appeal to PIPA, is that conciliation is not binding. If the parties do not eventually enter into a contractual arrangement reflecting a voluntary settlement, with the help of the conciliator, there is no way for a court to enforce a conciliator's decision. But of course if the parties do reach an agreement, they could be way ahead. It is this possibility that was the motivating force for PIPA to provide this service.

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<sup>6</sup> Doi, “International Commercial Arbitration in Japan,” *ibid.*, 65,67.

In the United States this method of settling disputes is well established, in labor disputes and in a growing number of other areas such as community disputes. There are mediation services and agencies in most states and cities, and there is a Federal Mediation Service as an autonomous agency of the Federal Government. We keep hearing that there is a need to be flexible in settling patent disputes. It was hoped that a mediation service would provide maximum flexibility.

A key to successful mediation is that the mediator have the confidence of the parties. Mediators must be experts in tactics and in timing. They must understand the issues, even highly technical issues. In New York State, mediators are protected by statute from being required to disclose any information "relating to, or acquired in, the course of their official activities." Thus confidences received by these official mediators are protected. PIPA also recognized this problem, in its draft Rules of Conciliation. In many areas PIPA is feeling its way, spurred by the feeling of the Japanese and American members that in international contractual disputes on patent and know-how issues, the informal, private aspects of voluntary mediation may in some cases make this procedure preferable to both arbitration and litigation. In the Japanese situation, there is a disposition toward conciliation even between Japanese nationals; and there was a real enthusiasm among the PIPA Japanese members for the concept.

The view has been expressed forcefully, by Americans and some Japanese, that there is no need for another structure to help people to get together and talk out their differences. However, some PIPA members believe, from their past experience, that certain disputes between Japanese and Americans in the patent field might never have become serious, and might never have ended in court, if the PIPA procedure had been available to the parties. They suggest that it might be easier for parties with a communications problem to open discussion with the aid of a conciliator, if they could know that they could choose an industrial property expert as their conciliator, or if they could have confidence in the technological capability of the conciliator.

PIPA was reluctant to organize a new formal structure unless there was a need for it and an adequate interest in using it. It had become clear that the unfilled need, if any, was to facilitate an informal conciliation, to the extent that distance and language and culture diminished opportunities for working out differences, in areas of highly complex law and technology and importance. Very

few patent or licensing disputes involve trivial sums of money or other value. Often both parties are deeply committed financially by the time a disagreement arises. And the Japanese and Americans were both mindful of the cost factor of a drawn out litigation or even of arbitration, across the Pacific Ocean.

In view of all this, PIPA made a stab at designing an optimum arrangement, tailored to these specific purposes. PIPA tried to provide simple and straightforward rules for initiating conciliation, and rather stringent time limits for completing conciliation, in order to prevent a party that is not really interested in serious conciliation from delaying the other party from pursuing its legal remedies. These requirements are more rigorous, and more specific, than in the Rules for Conciliation of the International Chamber or of the Japan Commercial Arbitration Association.

Thus, either party can advise PIPA that it has a problem and wishes to conciliate if the other party is willing. A PIPA administrative officer will handle such requests promptly. This administrative officer is required to ascertain whether the other party is interested in conciliation and move rapidly to assist in the selection of a conciliator. PIPA would maintain a list of industrial property experts and others as appropriate, who are willing to serve as conciliators in various fields. This list at present includes nationals of Japan and the United States, but conciliators from other countries are being considered. The parties can also select a conciliator who is not on the list.

Thereafter, the PIPA executive has the responsibility of bringing the parties and the conciliator together as rapidly as possible. The Rules purposely omit all mention of the need for documentation and the presentation of positions and of objections to positions. Since conciliation is optional, there is no way to force a party to make complete disclosure during the conciliation procedure. This is of course a weakness of conciliation, and inherently limits its general applicability. Nevertheless, if there is a dispute that both parties are in good faith interested in settling, they would be expected to bring forth adequate pertinent information, perhaps with a bit of prodding from the conciliator.

It is proposed in the PIPA rules that a relatively short time period be set for the completion of the entire conciliation procedure. The parties can of course extend this time by mutual agreement. However, if one of the parties is not proceeding diligently to comply with the conciliation time schedule, the other party can pursue his other remedies without much lost time.

Since conciliation is completely voluntary, it is assumed that in many cases agreement will not be reached. To encourage open discussion and offers of compromise, it was considered essential that no information produced during conciliation, and no offers of compromise, should be held against a party in subsequent litigation. The Rules provide for this, and also provide that there be no record kept of the conciliation discussions.

The PIPA Rules of Conciliation include provisions similar to those which prevail in the conciliation rules for other organizations, but in several areas PIPA was able to simplify the rules and to reduce the formalities, in part because of the narrow scope of the type of disputes intended to be covered. The Rules in their present form include the following major points:

Article 1 requires that one party to the dispute be a resident or national of Japan or the United States. Membership in PIPA is not required.

Article 2 imposes on PIPA the obligation of maintaining a Panel of at least 10 possible conciliators, experts in various aspects of industrial property. The parties need not select a member of this panel, if they agree on some other conciliator.

Article 3 sets out the method for invoking this procedure, by writing to the Secretary of either the Japanese or American Group. If the other party to the dispute is not willing to participate, that's the end of it.

Article 4 relates to selection of the conciliator, with PIPA's help.

Article 5 states some simple ground rules for carrying out the conciliation, in good faith and diligently.

Article 6 affirms the privacy of the proceedings, including the identity of the participants. Article 6(b) reflects the desirability of reaching a binding written agreement, if the parties wish.

Article 7 suggests a 30-day limit to the conciliation process, unless the parties themselves want to extend it. It affirms that nothing said in the course of an unsuccessful conciliation, for example, offers at compromise, shall be used against a party.

Article 8 provides for a fee to cover PIPA's administrative costs, and in the Regulations this is set for the present at \$100 per party. All other costs, and the conciliator's costs, are paid by the parties.

The Appendix is a suggested conciliation clause for incorporation into contracts on industrial property.

This procedure will be launched, officially, early in 1977. Statistical records will be kept, to determine its value over a trial period.