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IN THIS ISSUE

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FROM THE EDITOR

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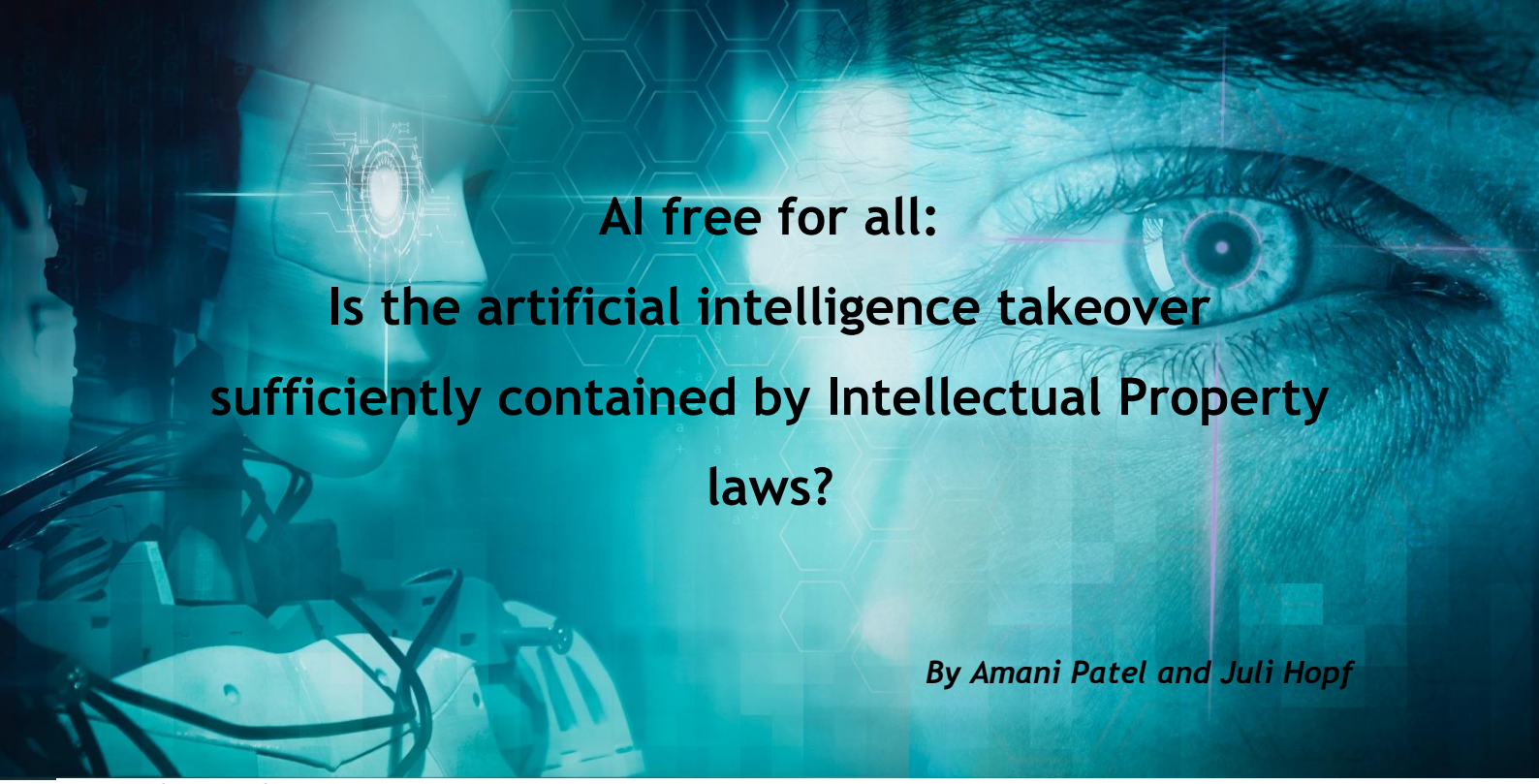
Spring is finally here! As the fresh leaves and young flowers together with "bok fever" descend upon us with enthusiasm, so did some advertising campaigns. Eskort, a leading manufacturer of processed pork products, placed a billboard outside O.R Tambo International Airport stating "GO SPRINGBOX LOVE ESKORT" and published a video that went viral across its social media channels, The video starred the "Springbox" captain, Frikkie, wearing a green and gold rugby shirt depicting the silhouette of a leaping pig, similar in some respects to the well-known Springbok emblem "People thought we fumbled the ball with a spelling mistake, but it wasn't. It was all to launch our new 'Springbox' because its spring and it's a cooler box". Funny as it may be, could it potentially be ambush marketing, trade mark infringement, or their constitutional right to freedom of expression?

Whatever the legal truth may be, a cooler box will be nearby as the South African nation watches the Springboks , who nail-bitingly made it to the finals, on the 28th of October.

Other than the box, the IP space continues to be dominated by growing Artificial Intelligence (AI) and Machine Learning (ML) that are leading the technology revolution. The continuing advancements of cutting-edge technologies such as genome editing (CRISPR) which, according to a study by the Columbia University School of Engineering and Applied Science (July 2023) combines a deep learning model with CRISPR screens to control the expression of human genes in different ways such as flicking a light switch to shut them off completely or by using a dimmer knob to partially turn down their activity. These precise gene controls could be used to develop new CRISPR-based therapies. Robotics is rapidly expanding into manufacturing, agriculture, and healthcare sectors[1]. According to WIPO's trends report[2] AI technologies will automate and streamline the process of intellectual property filing, infringement detection, and market trajectory analysis, thus improving efficiency and accuracy.

As these AI systems become more sophisticated, generating outputs such as artwork, creative writing, technical solutions, the questions about inventor, author and ownership will continue to pose a challenge in the copyright and patentability debate.

1.https://www.wipo.int/tech_trends/en/artificial_intelligence/
2. https://www.sciencedaily.com/releases/2023/07/230703133058.htm



AI free for all:
Is the artificial intelligence takeover sufficiently contained by Intellectual Property laws?

By Amani Patel and Juli Hopf

Source: Shutterstock

In an era of rapidly evolving (AI) and (ML) technologies autonomous design, music composition, art creation and predictive analytics, bear witness to the pervasive influence of AI and ML in virtually every facet of our daily lives. The seamless integration of (AI) and (ML) technologies across diverse industries has sparked a paradigm shift in the way businesses operate. While these advancements present opportunities for innovation, cost-effectiveness, and efficiency, they simultaneously pose complex legal challenges in the realm of Intellectual Property (IP) protection.

The traditional bastions of patents, copyrights, and trade marks are now being confronted with novel scenarios, courtesy of AI and ML algorithms that have become instrumental in creating, analysing, and birthing novel works, processes, and innovations. As the line between human-generated and AI-generated content begins to blur, the question of ownership and authorship looms large, demanding a fresh and astute examination of our existing IP frameworks.

AI Defined:
Artificial Intelligence (AI) can be defined as the theory and development of computer systems which are able to perform tasks normally requiring human intelligence. Machine Learning (ML) is a branch of AI which uses and advances computer systems to learn and adapt without following explicit instructions, by using algorithms and statistical models to analyse and draw inferences from patterns in data. It is based on the idea that systems can learn from data, identify patterns, and make decisions with minimal human intervention.

The Copyright Act, 1978 of South Africa governs copyright and allows for the right to control the use and distribution of certain works. One does not have to register copyright in South Africa, as it automatically exists the moment an original creative work is in a material form. Copyright generally vests in the author of a work subject to certain exemptions.

In a prior United States of America (US) copyright case where a monkey named Naruto, took a selfie on a photographer's camera, the question arose of who owned the copyright in the selfie.

The US District Court held that the concept of authorship under the US Copyright Act cannot be defined to include non-human animals. Much the same, AI generated works, would possibly (according to the SA Copyright Act) not be considered as works created by human authorship and therefore be unlikely to be protected under copyright. The making of creative works by AI therefore challenges conventional copyright principles and addressing the role of human involvement in such works becomes crucial to maintaining copyright integrity.

The intersection of AI and copyright law manifests a number of different problems. First, is the issue of how and from what/where AI tools learn, which raises the question as to whether the learning process is infringing copyright. AI companies scrape images/music/data etc from the Internet and use them to program their AI with different themes, moods and styles. Whether the outputs that AI tools produce are infringing works, would involve an assessment of whether any part of an original work was copied, and if that forms a 'substantial' part of the original work. Those who utilise AI to create works therefore need to consider whether they are using any party's work which may be copyrighted.

For example, in the US, Getty Images instituted an action against Stability AI, alleging that their copyrighted images were copied in the process of training Stability AI's image generator tool "Stable Diffusion" without their consent, and that this copying would infringe any copyright subsisting in the images.

On the other hand, in trade mark protection, AI's involvement in branding necessitates evaluating the distinctiveness of AI-generated marks and potential consumer confusion. AI's reliance on extensive datasets also raises data privacy concerns, requiring a balance between data-driven innovation and individual privacy rights.

AI and ML technologies have not merely left their mark on the creation and protection of IP rights but have also instigated a seismic shift in the enforcement of these rights. With the proliferation of digital platforms and the ever-expanding online space, the challenges in enforcing IP rights have reached an exponential magnitude. However, AI and ML offer innovative solutions that bolster the effectiveness and efficiency of IP enforcement endeavours. The scale and intricacy of IP infringements, encompassing counterfeiting, piracy, and online violations, have escalated in the digital age. Conventional manual detection and enforcement mechanisms now find themselves struggling to keep pace with the deluge of online content. In this crucible of challenges lies the untapped potential of AI and ML to revolutionize IP enforcement.

AI-powered algorithms possess the dexterity to autonomously scour the vast expanse of the Internet, unearthing instances of IP infringements with precision. These algorithms can deftly identify counterfeit products, unauthorized distribution of copyrighted content, and trade mark violations. Their swift analysis of voluminous datasets, coupled with pattern tracking, facilitates proactive and targeted enforcement actions. This technological marvel aids IP owners, enforcement agencies, and digital platforms in swiftly detecting and addressing IP infringements, thereby mitigating the deleterious economic consequences of illicit activities.

On a general note, individuals are also at risk of unknowingly agreeing to having their images freely used by third parties as they partake in online challenges such as on TikTok by uploading pictures of themselves to produce an AI generated version. These works, according to US Copyright Laws, are ineligible for copyright protection and accordingly fall within the public domain to be used by anyone for commercial or non-commercial purposes. Copyright protection is therefore not afforded for unauthorised use of such images by third parties.

More recently, Chat GPT has also been called into question as lawyers in a South African case utilised Chat GPT to provide cases as references in their arguments. Unfortunately, the information provided by Chat GPT was false and made up. Bringing into question the accuracy of such AI derived works and the importance of fact checking.

Global cooperation and harmonisation of IP laws are vital to address cross-border implications of AI and ML on IP rights, fostering consistency in recognition and enforcement.

To address the challenges posed by AI-generated works, we may consider adopting specific guidelines for such works, possibly amending the Copyright Act to recognize AI systems as co-authors, provided there is significant human input in the creative process. Another option is to assign authorship and IP rights to the AI programmer or developer, recognizing their role in creating the technology that enables the creation of the work's. Additionally, SA could consider creating a new category of IP rights specifically for AI-generated works, which would distinguish them from traditional artistic works.

A well-structured regulatory framework is required to infuse AI and ML technologies with a sense of responsibility and ethics within the domain of IP protection. Policymakers must synergize with technology and legal experts to craft laws that proficiently address the challenges posed by AI-generated content and inventions. The regulatory framework must define inventorship and ownership in AI-generated works, establish a balanced approach to fair use in AI-generated content, and create clear guidelines for assessing inventive steps in AI-generated inventions.

Businesses that aspire to embrace AI and ML technologies must engineer IP strategies to shield their innovations and creations. An effective IP strategy must encompass the identification, protection, and enforcement of IP rights pertaining to AI-generated works and inventions.

To unlock this realm of possibilities, businesses should:

- conduct IP Audits: Meticulously assess existing and potential IP assets to discern AI-driven innovations and creative works that demand protection.
- file for IP Protection: Spearhead the charge by filing patent applications for AI-generated inventions, registering trade marks for AI-driven branding, and adhering to copyright requirements for AI-generated content.
- review Licensing Agreements: Scrutinize licensing agreements for AI technologies, ensuring their thorough integration with unequivocal provisions on IP ownership, usage rights, and confidentiality.

- monitor IP Infringements: Embrace AI-driven tools for monitoring and detecting potential IP infringements, which shall confer the power to initiate prompt enforcement actions.
- educate the Workforce: Empower employees and stakeholders through training on IP rights, consistently emphasizing the primacy of protecting AI-generated innovations and content.

Collaborative efforts and licensing agreements possess the innate power to stoke the embers of innovation while ensuring robust IP protection. Licensing agreements shall serve as the conduit for facilitating the responsible use of AI-generated content and inventions, endowing businesses with access to cutting-edge AI technologies while dutifully respecting the rights of IP creators. Meticulously structured licensing agreements engender win-win scenarios, empowering businesses to chart new pathways of innovation while affording AI developers the recognition and remuneration they so rightfully deserve. Additionally, collaborative research and development projects hold the potential to catapult AI-driven innovation to new heights, culminating in ground-breaking advancements that augur well for society. Such collaborations also imbue a culture of responsible AI use, continually emphasizing the sanctity of IP protection and strict adherence to pertinent laws and regulations.

The advent of AI-generated works presents both opportunities and challenges for the South African IP law framework. By proactively engaging in legislative reform, fostering collaboration and dialogue, and promoting awareness and ethical guidelines, South Africa can effectively navigate these challenges and harness the potential of AI-generated works for the benefit of its community and society at large.

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FRAND, IoT, SEPs, SMEs: An Acronym "Soup"

By Matteo Sabattini[1]

As the "Internet of Everything" emerges thanks to technology convergence and limitless connectivity, some are worried that established IP licensing practices are no longer suitable for a very complex ecosystem. Without a doubt, established ways of doing business will have to adapt to reduce frictions between established players and new entrants. In fact, this is already happening. The question addressed in this article is whether top-down regulation will cause more benefit than harm, or instead whether industry is capable of regulating itself.

Introduction

Over recent decades, convergence of technologies, the advent of the mobile internet, and seamless connectivity have created a vibrant and complex ecosystem of interconnected "things" (the so-called Internet of Things, or IoT) and humans. We truly live in a hyperconnected society, where everyone of us - and in the future virtually everything we interact with - will be connected.

The complexity of this new ecosystem, and the diversity of players active within it, have created challenges and frictions. IP licensing paradigms have not been immune to these tensions. The diverse IP business models traditionally applied by established and very different industries, like the automotive industry and the telecom industry, have resulted in a tangible clash of "cultures.[2]"

[1] The views expressed in this article are the author's personal views, and they do not reflect the views of Convida or any of its employees.

[2] For example, some industries have historically heavily relied on indemnification clauses by suppliers for all IP-related matters, leveraging their market power over suppliers to offload licensing matters upstream. Other industries, on the other hand, have licensed at the finite product for decades. Over the top (OTT) providers have thus relied on the devices being licensed to access communication technologies for their services.

Some IoT history

Before delving into the complexities of a growing and complex IoT ecosystem, it is necessary to understand the historical context.

IoT is not a new concept. Connected things have been around for decades. In the early 1980's, Carnagie Mellon's students created the first IoT device. To save time when the campus Coke machine ran out, a group of students designed a way to make it broadcast its inventory status through a network. Rather than walking to the machine only to find out that there was no Coke available, students could figure that out from their campus dorms.

The first internet-connected device came shortly thereafter. In 1989, John Romkey and Simon Hackett connected a toaster to the Internet with TCP/IP networking. The toaster had one control, to turn the power on, and the darkness of the toast was controlled by how long the power was kept on.

The IoT has evolved significantly since then. Ericsson's CTO has used the term "limitless connectivity"[3]to explain how the advent of the mobile internet is accelerating the concept.

The IoT now encompasses a vast, diverse, complex ecosystem of platform providers, device manufacturers, user applications, private and public cloud providers, distributed computing, telco operators. Players large and small coexist in this complex ecosystem, some focusing on horizontal applications, others on specific verticals like industrial IoT, automotive, smart cities, just to name a few.

(Real or Perceived) Challenges in the IoT Ecosystem

There are many real or perceived challenges in a complex ecosystem. These can be very different from one vantage point compared to another. For example, an IoT module manufacturer might see a very different set than a telco provider or a cloud provider.

Focusing now on three high-level concepts that have often been cited as causing friction in the marketplace: (i) the value of the technology; (ii) who should take a license in a complex value chain; (iii) the competition between different communication technologies, and (iv) specific challenges for SMEs.

i. <u>The value of the technology</u>

The value that technology adds to a device can only be calculated based on the value-added to a user. Therefore, abstracting from the actual use leads to unreliable valuation models. Given this, the value of a license to patents covering such technology can only be properly determined for a specific use case.

Although the same technology might be used in different use cases or even verticals, price differentiation is inevitable because the value to users can be significantly different[4].

[3] https://www.ericsson.com/en/reports-and-papers/ericsson-technology-review/articles/technology-trends-2023
[4] As an extreme example, think about using asset trackers to track disposed trash as opposed to nuclear waste. Clearly the requirements and value of the latter use case are fundamentally different from the former!

Moreover, the use of the technology (resources, network access, bandwidth and quality of service requirements) can be substantially different too.

Pricing a technology at the same level across different verticals and use cases can be counterproductive. From an innovation management point of view; the same price across two widely different verticals (e.g. automotive and smart meters) could be too low to encourage innovation in one vertical, but too high in another, so hindering adoption.

ii. Who should take a license in the value chain?

Once the correct value for a license is apportioned, some claim that (1) who takes a license in the value chain is irrelevant because patent owners will be fairly compensated, and (2) other entities in the value chain will have access to the technology by virtue of either have made rights, or exhaustion.

Putting the latter point (2) to one side[5], on (1), to claim that licensing anywhere other than at the finite device (or "functional unit" as sometimes referred to[6]) would not make a difference for patent owners is either disingenuous or plainly misleading.

By licensing upstream in the value chain (i.e., to module and chip manufacturers), patent owners will face significant challenges and inefficiencies:

- First, determining the use of the technology becomes difficult, especially if similar components end up in significantly different finite devices (a car versus a phone versus a smart meter, for example).
- Second, unless all possible suppliers of components are licensed (which is an unrealistic assumption), identifying unlicensed devices becomes impossible without costly teardowns.
- Third, auditing licensees becomes a herculean task.
- Finally, and probably most importantly, the majority component suppliers simply do not have the margins to cover a license that captures the value of the technology to the user of the finite device.

iii. Competition between communication technologies

Licensors and technology providers should also carefully consider that licensees have several options, especially when it comes to communication technologies[7]. While superior technologies should be, are and will be more costly for licensees, the cost of a license should be carefully determined by licensors weighing adoption vis a vis existing alternatives in order to encourage market penetration.

[5] Several concerns and limitations do exist, for example method claims often cannot be infringed by a module not connected to power and a network, and therefore a module maker shall not take a license to those claims.
[6] https://www.lesi.org/publications/les-nouvelles/les-nouvelles-article-of-the-month/les-nouvelles-article-of-the-month-archives/les-nouvelles-article-of-the-month-october-2016
[7] For IoT specifically, options include Bluetooth, Wi-Fi, NB-IoT, LTE-M, 5G, LoraWAN, ZigBee and others,

iv. The challenge for SMEs

The complexity of the value chain of these new ecosystems has been fertile ground for many small and medium enterprises (SMEs) which are hoping to grow their market share, looking for exits, or simply playing in niche fields. Playing this game successfully, requires an understanding of IP and IP licensing, and very often access to SEPs[8]. SMEs generally lack resources dedicated to IP, and most SMEs have not dealt with in-IP licensing and/or out- IP licensing at all. Being a small player in a larger ecosystem creates certain challenges.

The licensing industry has attempted to address the challenges above, in several ways. One solution has been the creation of patent pools, where users of a technology can solve all, or most, of their licensing needs. Patent pools have been around for decades[9] and have been recently applied to the IoT industry. Two examples that gained significant critical mass and market traction are the automotive licensing platform by Avanci[10] and the Cellular IoT patent pool by Sisvel[11].

There are other industry-led proposed solutions to increase licensing transaction efficiencies, such as the LES Standards[12] initiative by the Licensing Executive Society (LES) USA and Canada.

Despite these initiatives, that can assist both SMEs and larger entities with access to technology, some regulators have signaled the intent to explore regulation. Notably, the European Commission's (EC's), DG-GROW, have stepped into the debate in full force and proposed a draft regulation on Standard Essential Patents (SEPs) which has been the subject of much criticism.

The EC Draft Regulation

The EC Directorate-General for Internal Market, Industry, Entrepreneurship and SMEs (DG-GROW) recently published[13] a proposal for "regulation of the European Parliament and of the Council on standard essential patents and amending Regulation (EU) 2017/1001".

DG-GROW cites the lack of transparency in the licensing of SEPs as one of the motivations for the draft proposal. Another justification for the regulatory zeal is to help SMEs: one of DG-GROW's concerns is that the alleged lack of transparency is hurting smaller companies the most.

[8] Standard Essential Patents (SEPs) are patents that protect technology that is incorporated in a standard. SEPs are "essential" in the sense that implementation of the standard requires use of the inventions covered by SEPs.
[9] https://www.justice.gov/sites/default/files/atr/legacy/2006/10/17/215742.pdf
[10] https://www.avanci.com/vehicle/5gvehicle/
[11] https://www.sisvel.com/news/sisvel-launches-its-cellular-iot-patent-pool/
[12] https://members.lesusacanada.org/general/custom.asp?page=lesstandards
[13] https://single-market-economy.ec.europa.eu/publications/com2023232-proposal-regulation-standard-essential-patents_en

The proposal so far has received fierce criticism from industry[14], practitioners[15], licensees and licensors[16], analysts[17], member states[18], European Unified Patent Court (UPC) judges[19], the EPO[20] (EUIPO's sister organization), and even the European Parliament itself with its Committee on Internal Trade (INTA)[21]. Some specific concerns and criticism to the proposal are:

i. The current draft cannot be implemented

The draft has been poorly constructed. The document is plagued with typos, important definitions have been omitted which leads to confusion as to what certain terms mean. It will need a significant rework even from a merely aesthetic point of view before the proposal can even be considered as a final regulation.

Moreover, if the draft is enacted in some form, it will not be implementable by the very institution that DG-GROW indicates as the one overseeing such implementation, the EU IP Office (EUIPO). This agency lacks expertise in standards and in patents (not even SEPs, but patents in general), as it is primarily the trademark and designs office of the EU[22]. In addition, the budget allocated for setting up and managing a program of this magnitude has been grossly underestimated[23].

ii. Enacting it would seriously undermine European technology leadership

Europe is homebase for two of the major contributors to the development and the deployment of mobile communications standards, Ericsson and Nokia. Both companies invest heavily in R&D by virtue of, in part at least, to royalty revenues generated by very successful SEP licensing programs. Europe is also the cradle for a vibrant R&D ecosystem of universities, SMEs and research centers.

The current draft regulation will put a significant burden on SEP licensors[24], ultimately making it harder to recoup R&D investments, while giving unwilling licensees the opportunity to delay negotiations and hold out. In addition, it would single out the EU, creating frictions in a global market for international standards that has so far worked successfully for consumers.

Lastly, while the EU is promoting its newly launched UPC system, DG-GROW with this draft regulation is basically sabotaging it by creating a hostile environment for patent owners.

[14] https://www.politico.eu/sponsored-content/eu-sep-reform-gambles-europes-long-term-future/
[15] https://www.twobirds.com/en/insights/2023/global/the-draft-eu-sep-regulation-a-practitioners-critical-view
[16] https://ipeurope.org/blog/live-blog-third-party-comments-on-the-european-commissions-seps-proposal/
[17] http://www.fosspatents.com/2023/03/european-commission-departs-from-best.html
[18] http://www.fosspatents.com/2023/10/governments-of-three-medium-sized-eu.html
[19] https://www.managingip.com/article/2bqbfr0uyrki1fniy9ou8/breaking-upc-chief-urges-eu-to-rethink-sep-plan
[20] https://www.iam-media.com/article/epo-president-letter-juri-sep-licensing-regulation and https://files.lbr.cloud/public/2023-10/EPO%20Letter%20IAM.pdf?VersionId=Xk2GKKPZ.qRisb5bU4BFaeiLe44oluGB
[21] https://www.europarl.europa.eu/doceo/document/INTA-PA-753729_EN.pdf
[22] Why DG-GROW thinks is a good idea to have the trademark and designs office oversee a program focusing on patents is baffling at best.
[23] The Commission claims (https://single-market-economy.ec.europa.eu/system/files/2023-04/COM_2023_232_1_EN_ACT_part1_v13.pdf) that the competence center can be fully funded with fees paid to EUIPO. Such claim is dubious and concerning for two reasons. First, EUIPO revenues from fees have declined recently. Second, the budget so generated can only be a fraction of what sophisticated SEP licensors allocate each ear for internal analysis and claim charting of their own portfolio.
[24] https://www.iam-media.com/article/jw-column-30th-march-2023-ec-sep-licensing-plans

iii. Draft does not help SMEs

The draft regulation does not take into any consideration the many SMEs that invest in R&D, develop technologies and license their IP.

These SMEs will be heavily and negatively impacted if this draft were enacted as it would be more difficult (even impossible?) to recoup R&D investments and license much bigger players that use their technologies.

More importantly, it is hard to recognize how this draft regulation would help SMEs in general, even those commercializing products and services that require a license to SEPs. While the draft's intention is to address efficiency (or alleged lack thereof), it simply addresses a one-sided definition of transparency, where all the burden is on licensors, and licensees have no obligations. It does not provide actionable tools for less-sophisticated licensees to actually negotiate a license more efficiently. It provides licensees solely with ploys to delay negotiations. As a result, the threat is that very large unwilling licensees rather than SMEs would be the only beneficiaries of this regulation.

An alternative proposal

It is clear that DG-GROW and the Commission are genuinely interested in tools that can help SMEs. The current draft regulation is simply ill-informed. Fortunately, there is a way to truly help SMEs negotiate a license to SEPs committed on FRAND terms.

Although some refinements and more detail might be required, the basic concept is that, if and only if, an SME is approached by a licensor for the licensing of SEPs, the SME could access a mediation[25] center where an appointed expert mediator could look at comparable agreements submitted by the licensor under confidentiality and redacted as necessary to protect sensible information. Based on the review of such comparable agreements, the mediator will be in a position to provide feedback to the SME licensee, in particular as to whether the licensor's proposed licensing terms are in fact FRAND and in line with other licenses it has granted to similarly situated licensees.

This proposal leverages the efficiency of alternative dispute resolution (ADR) methods. It provides SMEs with a tool to ensure fair treatments and prevents licensors from exploiting their power and financial means to gain unreasonable leverage. By making this tool only available to SMEs[26], it would guarantee that those who need help the most would get it, and would provide efficiency in negotiations where less-sophisticated companies are involved. The global nature of ADR implies that the EC could put in place the infrastructure that companies worldwide might want to use, without singling out Europe or undermining European technological and IP leadership.

[25] Mediation, rather than arbitration, is a much better tool in this scenario. After the result of mediation, the SME licensee will have a much higher level of comfort that the request by licensor is in line with the terms and royalty rates that the SME's competitors have been offered, in essence giving the SME comfort that they are not being charged more than its peers. Arbitration, on the other hand, is a much harder sell: parties will rarely accept to use it and be bound by it.
[26] https://single-market-economy.ec.europa.eu/smes/sme-definition_en

Conclusion

The IoT ecosystem is complex. This article highlights some of the tensions that arise within it as convergence advances and different industrial cultures clash.

About the Author

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Matteo is the President and Chief Licensing Officer of Convida, a pioneer in research and innovation for IoT and cloud services. Dr. Sabattini in the past held positions at Ericsson, the Sisvel Group, InterDigital and other leading organizations in the IP industry. He also held several teaching and research positions in wireless and mobile communications at UCSD and at the German Aerospace Centre (DLR). He has years of expertise in technology licensing and IP strategy, and his background blends business, policy and technical skills. He has published extensively and regularly speaks at industry events on IP matters. Dr. Sabattini is a member of the board of the Licensing Executive Society International (LESI). He also currently serves as the senior vice president for standards and is part of the management council of the Licensing Executives Society (LES) USA and Canada. He is an IEEE senior member, a Beta Gamma Sigma lifetime member, as well as a member of the MIT Enterprise Forum. He holds an MBA from the George Washington University (GWU), a PhD in electrical engineering from the University of California, San Diego (UCSD), and a Laurea Magistrale also in electrical engineering from the University of Bologna.

IP strategy: has the situation really changed during the last 20 years?

By Dr. A Gasnier

This article reviews basic concepts of business strategy in general and presents first learnings when these concepts are applied to IP. Based on empirical insights (from two surveys in 2008 and since 2015), the article highlights what IP professionals need to develop an IP strategy, compares it with the situation during this 20-year timeframe, and identifies the changes since 2005.

In today's growing complexity economists and academics agree that innovation is key to gaining and maintaining leadership at macro- and micro-levels. IP is the mechanism to protect such innovation for higher exploitation, dissemination and returns. Ideally, executives and investors are aware of the benefits of best practice IP management and ask for a more "strategic" approach to create and capture value and to promote growth.

More than ever, IP and business communities need a common language to look at IP through a holistic lens and not just a legal one. There is a growing need for a new type of IP professional with cross-disciplinary capacity to bridge IP and the long-term interests of the company.

Companies, or their IP law firms, ask IP professionals and lawyers to become business strategists with a long-term vision of the company's interests. However, in practice, IP professionals haven't always had the opportunity to acquire this expertise; they have technical and legal qualifications but sometimes limited business background.

Worse, if they *do* have such expertise, they often find they get diverted into the deeper business line and their focus changes to coping with the high demands of operational work.

In this article, we want to introduce some concepts that practitioners might find useful in bringing together business strategy with IP skills.

The author provides in the following sections some general principles of business strategy as applied to IP management and explores the current needs of IP professionals, management, and private practice in terms of strategy.

What IP strategy is (or should be): Back to business strategy basics.

So what is meant by the term "IP strategy" within the IP industry? Many companies think of this purely in terms of having a decent filing strategy, that is choosing which countries to protect in and how much to protect. Filing strategy has a rather well-understood meaning among IP professionals, yet forms only one part of what the whole IP strategy could be. IP strategy can be so much more if we think outside the box a little.

Alternatively, some companies from the IP service industry recognise the need to add IP strategy to their portfolios. They talk about aligning IP with business strategy and transforming the way in-house IP departments work. However, they often don't quite manage to tie together their IP practice with business strategy.

Instead, they pursue a cost effectiveness approach to seek operational efficiency and quality control through systems.

Such confusion between cost/operational efficiency and strategy is not new, especially for business strategists if we look outside the IP industry. Generally speaking, a company can outperform competition mainly in the two following ways.

- **Operational effectiveness** to improve productivity with e.g. 6sigma, total quality management and similar approaches. Usually, the competitive advantage derived from such improvements is only valid on the short run, and competitors will catch up in the long run.
- **Value leadership** based on the premise that sustainable competitive advantage can only come from offering a differentiated value proposition to the customers. Such advantage will remain if anchored in valuable unique assets; here, innovation and IP play their full role to establish a market position for the company and keep an edge over competition.

These two management approaches diverge and should not be confused with each other: strategy seeks to create value for the long-term, while cost efficiency is usually short-term driven. In other words, efficiency optimization is not a strategy.

So, what's a strategic choice? First, the company should generate as many strategy options as possible. Time honoured ways of achieving this include creating a "strategic crisis" which requires immediate response or simply taking the key staff off to some form of management retreat to weigh up options. The former will certainly produce results though the latter is probably preferable for peace of mind. Once the options are identified the company needs to make a choice, i.e. what to do but also what not to do. This choice is unbelievably hard and, as a result, many companies oscillate between two or more business models. In the arena of IP, we can see that some in-house departments oscillate between the model of in-house IP prosecution (requiring more patent/trademark attorneys) or that of tech transfer (requiring commercial skills). With an inability to make this choice, Porter (one of the business strategy thought-leaders – see references) says that the organization is doomed to be "stuck in the middle".

Making a choice requires tough decisions, dealing with uncertainty, revealing internal tensions and seeking trade-offs. Why is this? Because the growing complexity of today's organizations constructs a web of interdependent decisions. Although there are many wrong options, there are also multiple viable options tapping into core internal competences and complementary activities. Further, trade-offs typically occur when activities are incompatible due to, for example, inconsistencies in image and reputation, limitation in internal coordination, and misalignment of the current strategy.

But how to make a choice? Breakthrough strategies generally rely on the following principles:

1) Choosing a unique strategic position i.e. a unique value proposition in terms of customer target and product/service offering;
2) Making clear choices while keeping flexibility, although avoiding the "keeping all options open" strategy, and achieving a fit with the company's environment and market needs; and
3) Providing appropriate organizational support for the system to work, while institutionalizing the behaviors which support execution[1].

[1] However, institutionalising the behaviours which support execution, e.g. with systems, processes and procedures should come last not first!

Once the choice is made, the company really needs to stick to it, requiring long-term commitment from management. Guidelines need to be communicated to staff, with sufficient information and details for everyone in the company to implement the strategy.

Finally, it is worth remembering that no strategic choice remains unique forever.

The business model probably needs to be reinvented from time to time, especially in response to disruption from outside the company.

The author believes that these general principles of business strategy can be applied to IP.

IP strategy should mean a business function or process that is cross-functional, pulling in IP, legal, innovation, market, finance etc. and whose role consists of:

- Analyzing cross-disciplinary data, generating options, and making a strategic choice;
- Implementing the strategy through guided decision-making across the company; and
- Monitoring the plan execution against the business goals, external change and internal growth.

The first point involves drafting a plan or long-term set of guidelines to help make decisions regarding areas where the company wants to gain freedom or maintain freedom to operate, or exclusivity, and may include how best to promote its innovations and possibly even license its IP. The company needs to ensure that the plan is aligned with its business strategy by integrating the company goals, enabling synergy of internal resources, and taking into account market opportunities or threats.

In today's context, the position of most companies is rather paradoxical. For decades, IP professionals have tried to convince management and clients that IP brings value and should be considered a business asset. Meanwhile in those same companies, management has more often not been making IP strategies for creating and capturing value but instead managed IP with a cost-driven approach designed purely to improve operational efficiency. However, as they know from their own thought-leaders like Porter, operational or cost efficiency does not form a strategy.

The way forward is to reconcile both the IP and business communities, and we can start to address that by asking: what are the needs today of IP professionals in terms of new knowledge, skills and tools, and how can we use those to establish a common dialogue with management and across functions?

Knowledge, skills, and tools: Current needs between IP and business.

A first survey was carried out in 2006 among 8,000 patent users, during a PhD research project sponsored by the EPO. Respondents were asked to answer the open question: "How would you improve IP management in your organization?" Their responses were categorized into the three main areas as shown in Figure 1 (N=1,106) education/training, strategy, and collaboration. These three areas corresponded to those found in literature and empirically from practice.

Education and in-house training are the first response for 40% of the respondents. Generally speaking, learning and development were considered to be one of the most important processes in those companies, helping employees perform tasks better and quicker by identifying new opportunities, gaining organizational skills, and acquiring common codes of communication and procedures (Teece 1997). But meanwhile, in IP land, the key stakeholders (other than IP experts) often experienced an information deficit regarding the patent system, as regularly pointed out e.g. in WIPO (2004).

When it comes to in-house IP training, managers and executives were the first target audience cited by the respondents, mainly because the success

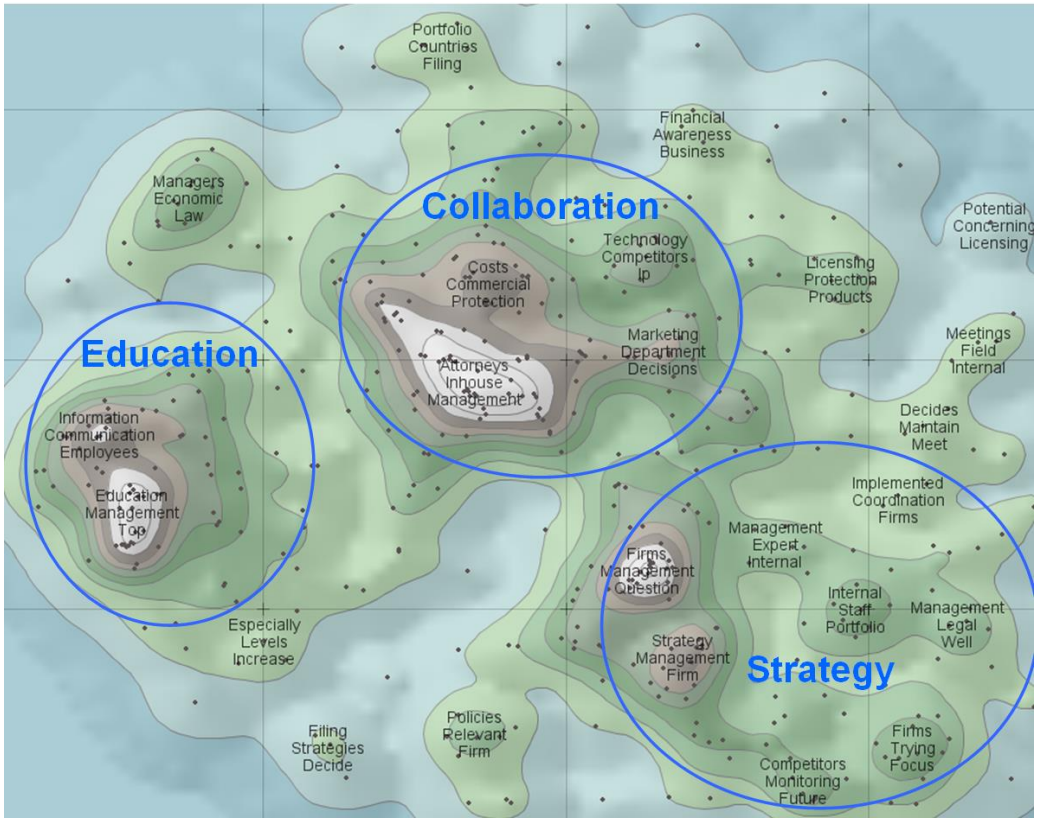

Figure 1 Survey results: Area for improvement of IP strategy in organisations (Source Gasnier 2008)

of the two other areas (collaboration and strategy) highly depended on management's awareness on the importance and impact of IP in today's economy.

The second main response area related to the need to set up a "strategy" regarding generation, protection and exploitation of innovation.

This strategy-making process required inputs from internal experts, for example business intelligence and competitor monitoring, marketing and account management, and legal for running contracts and obligations. The output of this process related to the building and exploitation of a full IP portfolio, which addressed the full gamut of patents, know-how, trademarks etc. and aligned them with the business goals.

The third area related to collaboration between in-house IP management and other functions like R&D, marketing and sales etc.

This was paramount when implementing strategies once developed, and reaching operational efficiency.

However, functions were often vertically organized in companies, creating silos and preventing adequate cross-collaboration.

As a result, the gap between functions, in particular with IP, tended to grow over time in the absence of a crisis situation and other drivers of episodic change. This gap negatively impacted top management's long-term buy-in regarding IP. The impact was worsened for smaller organisations (SMEs, start-ups) which fully outsourced their IP function/management to, and thereby completely rely on, IP law firms for advice. Worst case, companies simply did not consider IP as an efficient investment mechanism for business development and growth.

Has the situation really changed during the last 20 years?

Since 2006, we have observed a growing number of initiatives throughout Europe regarding education and training for companies. These initiatives mainly focus on raising awareness, bringing general information and theoretical knowledge, and sharing experience and some degree of best practice.

Nevertheless, from our direct contact with IP professionals, advisors and managers in Europe and beyond, it appears that the topic of IP strategy remains this "obscure object of desire". For this reason, we launched a refresher survey in 2015, to measure the readiness of today's companies and law firms when it comes to IP strategy. Hundreds of companies and private practices have responded.[1] First results show that, in industry, a growing number of IP and business professionals are now asked by management to deliver strategic plans as part of their role.

However, they tell us that getting data (business, innovation/IP, market) is easy, but analyzing the data is not! Also, many companies lack knowledge, skills and tools to prepare such plans/strategies. Others developed their own plans but now seek new structured ones. We also found that some IP law firms act as fully outsourced IP managers for their clients and need to better understand the company business. For other firms, turning (in)to consultancy is a response to the growing pressure from competition; for them, strategic advice can be a way to offer again premium services. Like in companies, IP professionals in law firms lack similar knowledge, skills and tools.

Figure 2 shows first findings from the second survey (since 2015) in terms of concerns and goals of management at companies (executives, board) and law firms (partners).

Figure 3 shows further insights from the second survey. In particular, it shows how the above concerns and goals from management and clients translate into the needs of IP professionals, both in-house and private practice.

It is important to distinguish operational effectiveness (cost-driven) from strategy (value-driven); this also applies to IP.

	Companies/executives	Law firms/partners
Challenges	• Bringing visibility for long-term in terms of where to invest and why. • Current portfolio mapping (not case-by-case). • What do we have? Aligned with business? Where to cut costs? • High workload for the IP team.	• More and more clients (companies) raise the same concerns/goals (see column aside in this table). Some may question the utility of IP. • Pressure from global competition in the IP service industry: traditional IP work is no longer a premium service but is now driven by cost leadership. • High workload: less resources and motivations for reinventing their model. • No established model regarding new, cross-disciplinary practices at intersection of IP and business.
Goals	• Competition monitoring from the company's lens. • (Re)setting up an IP strategy. • Create more value, growth and business development using IP.	• Establish a new premium service. • Expand to consultancy (strategy). • Capture growing SMEs which fully outsource IP function.

Based on empirical results, the need for combining IP expertise with business strategy has grown during the last decade, for IP professionals as well as a growing number of managers from other functions (this is good news!). IP strategy is more than having a countries list. To design and implement an IP/innovation strategy, many companies indicate they need common knowledge, analytical skills and practical tools.

The survey is still running and interested parties can participate at www.surveymonkey.com/s/PatentopolisSurvey

	Needs of IP professionals (in-house and private practice)
Knowledge	• Learn basic business concepts • Understand the business of the (client's) company • Build a common language
Skills	• Analyse cross-disciplinary data (IP/innovation, market, business) • Draft the IP plan • Communicate with higher management or client. Get buy-in • Involve other functions in the IP decision-making process • Spread the right level of information • Consolidate IP plans from product/division to corporate level • Initiate change
Tools	• Structured, straightforward and generic methodologies • Guided workflows (online) • Processes to scale up strategy planning and monitoring internally

Figure 3 Further insights from survey 2015-date

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Source: ShutterStock

MICROSOFT'S US$ 28.9 BILLION TAX DEMAND : TRANSFER PRICING AND WHAT IP PROFESSIONALS NEED TO KNOW

On 11 October 2023, Microsoft announced that it had received a demand for US $28.9 billion in back taxes from the U.S. Inland Revenue Service, plus penalties and interest.[1] The demand relates to a transfer pricing dispute concerning arrangements dating back to 2004. Although the full details of the case have not been published, it appears that the matter relates to the use of regional centres in Singapore, Dublin and Puerto Rico to distribute software, enabling the group to route profits in a way that helped to reduce its overall liability to income taxes worldwide.

Microsoft has stated that it will vigorously contest the IRS's demands, and that it considers that its existing accounting provisions for tax contingencies are adequate. Nevertheless, the announcement illustrates the significance and scale of transfer pricing risks, and the role which group and supply chain structures relating to intellectual property and other intangible assets can play.

Microsoft's transfer pricing dispute is not an isolated case. In November 2020, the U.S. Tax Court ruled in favour of the IRS in relation to a transfer pricing dispute relating to The Coca-Cola Company. In a subsequent announcement, the group estimated that the ruling will give rise to US$ 12 billion of aggregate incremental tax liability, if it is not overturned. In May 2022, McDonald's entered into a settlement agreement with the Financial Public Prosecutor in France, under which the group agreed to pay € 1.245 billion in back taxes and fines to the French tax authorities. The settlement agreement resulted from allegations of 'abnormally high' royalties transferred from McDonald's France to McDonald's Luxembourg following an intra group restructuring in 2009.

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[1] https://microsoft.gcs-web.com/node/31951/html

McDonald's France doubled its intra-group royalty payments from 5% to 10% of restaurant turnover, and instead of paying these royalties to McDonald's HQ in the United States, the royalties were paid to a Swiss establishment of a group company in Luxembourg, which resulted in the amounts not being taxable.

A common theme in all three of these high-profile transfer pricing cases – Microsoft, McDonald's and Coca-Cola – is intra-group transactions involving intangible assets, and the way that such assets are held and used within multinational group structures. Although the disciplines of intellectual property law and tax compliance have traditionally been very distinct, these cases highlight the need for cross-functional awareness of the relevant issues, so that transfer pricing risks can be identified early and managed appropriately.

This article is intended to give IP professionals an overview of the key issues and concepts relating to transfer pricing with a focus on the treatment of intangible assets. It concludes by setting out some practical do's and don'ts for IP professionals when supporting multinational group clients.

What is transfer pricing, and why it matters

Transfer pricing ('TP') refers to the international set of tax rules which determine the level of intercompany charges (e.g. service fees, royalties, prices for goods, loan interest, etc.) which may be 'properly' paid (from a tax perspective) between associated entities within a multinational group, and which in turn affect where profits are made and taxed.

The OECD has adopted the arm's length principle as the international standard for determining 'proper' transfer prices for all intra-group transactions for tax purposes. The arm's length principle applies to transactions between associated enterprises, such as members of a corporate group. This principle allows tax authorities to review the prices payable by a party to a 'controlled transaction', and tax that party based on the profits which it would have accrued, had the transaction been entered into at a price and on terms negotiated between independent third parties. This applies both to ongoing arrangements (such as licenses of intellectual property) and to one-off transactions (such as a cross-border transfer of intellectual property), and not just to legal entities, but also to branches or 'permanent establishments'.

The potential for transfer pricing challenges by individual tax administrations creates a risk of double taxation, because any adjustment of transfer prices in one tax jurisdiction implies that a corresponding change should be made in another jurisdiction. If the tax administration in that other jurisdiction does not agree to make that corresponding adjustment, the group may be taxed twice on the same profit. In addition, as noted above, interest and penalties can also apply.

In light of the size of the claims brought by tax administrations including the IRS in the cases referenced above, is not surprising that transfer pricing compliance is consistently ranked as one of the most complex and high risk areas of tax affecting multinational groups. For example, in the 2020 Global MNC Tax Complexity Survey, among fifteen tax issues, transfer pricing ranks at the top of the complexity scale.[2]

Although transfer pricing disputes affecting well-known companies tend to attract the most publicity, this issue is not confined to ultra-large corporates. Every business with cross-border operations should assess transfer pricing risks and put in place appropriate systems to manage them. As a minimum, this should involve clearly documenting the legal

[2] https://www.accounting-for-transparency.de/de/publications/2020-global-mnc-tax-complexity-survey/

and economic substance of related-party transactions by way of implementation of intercompany agreements such as IP licence and IP assignment agreements.

The basics of transfer pricing analysis

The application of the arm's length principle to a controlled transaction as prescribed by the OECD's Transfer Pricing Guidelines requires a number of steps to be carried out. These include (i) identifying the economically significant risks involved, (ii) ascertaining how those risks are contractually assumed by the relevant entities under the terms of the transaction, (iii) carrying out a functional analysis to determine the roles of the respective entities as regards economically significant activities, (iv) identifying the assets used or contributed, and (v) assessing the control of risk as between the relevant entities. Once the transaction has been accurately 'delineated' in this way, it should be priced by reference to comparable 'uncontrolled' transactions between independent third parties. This is often referred to by TP professionals as 'benchmarking'.

A range of transfer pricing methods may be selected, including:

- Cost plus method
- Transactional net margin method (TNMM), also known as the comparable profits method (CPM)
- Resale minus method
- Transactional profit split method
- Cost sharing arrangements

Each of these methods presupposes corresponding fact patterns as regards the relevant controlled transaction, including the contractual allocation of risk between the parties.

The transfer pricing concept of 'intangibles' vs intellectual property

The OECD's Transfer Pricing Guidelines recognise that intangible assets can constitute an important value driver for multinational groups. Intra-group transactions involving the transfer, licensing or development of intangible assets are therefore a key focus area, both in the Transfer Pricing Guidelines and for tax administrations when reviewing controlled transactions and transfer pricing policies of a multinational group.

The concept of 'Intangible assets' or 'intangibles' as used in the OECD's Transfer Pricing Guidelines is broad. It is wider than registered intellectual property rights, but is subject to the qualification that an intangible asset must be capable of being 'owned' or 'controlled':

> *"In these Guidelines, therefore, the word "intangible" is intended to address something which is not a physical asset or a financial asset, which is capable of being owned or controlled for use in commercial activities, and whose use or transfer would be compensated had it occurred in a transaction between independent parties in comparable circumstances. Rather than focusing on accounting or legal definitions, the thrust of a transfer pricing analysis in a case involving intangibles should be the determination of the conditions that would be agreed upon between independent parties for a comparable transaction."*
>
> (OECD Transfer Pricing Guidelines, 2022 Edition, Para 6.6).

The Guidelines make no attempt at a comprehensive classification of intangibles, but they do recognise commonly understood categories such as:

- patents
- know-how and trade secrets
- trademarks, trade names and brands
- rights under contract and government licences
- licences and similar rights in intangibles
- goodwill and ongoing concern value

Some characteristics may be economically relevant, but are not considered by the OECD's Transfer Pricing Guidelines to be intangibles, since they are not capable of being owned or controlled by an enterprise:

- group synergies; and
- market specific characteristics, such as high purchasing power of households in a particular market, low labour costs or weather conditions.

The concept of 'DEMPE analysis' in transfer pricing involving intangibles

The OECD's Transfer Pricing Guidelines provide a framework for analysing transactions involving intangibles between associated enterprises, which is commonly referred to as 'DEMPE analysis' – DEMPE being an acronym for Development, Enhancement, Maintenance, Protection, and Exploitation.

The term 'economic ownership' is sometimes used by transfer pricing practitioners with reference to intangible assets. This sometimes takes the form of a statement to the effect that a particular entity should be regarded as the 'economic owner' of intangible assets if it carries out DEMPE functions. Such statements may be a useful shorthand, but can in some cases be misleading because they may suggest that a transaction should be documented for transfer pricing purposes in a way which conflicts with the legal and commercial reality of the relevant group's operations and legal and beneficial ownership of IP.

It should be noted that the OECD's Transfer Pricing Guidelines do not use the term 'economic owner'. Neither do they state that an entity which performs DEMPE functions should be regarded as the owner (or co-owner) of intangible assets. Instead, the Guidelines provide that entities should be compensated on an arm's length basis for functions performed, assets used, and risks assumed or managed. It is therefore essential to identify the legal ownership of intangible assets and related rights and design the contractual mechanisms by which the relevant related parties should be compensated on an arm's length basis for their participation in the arrangements.

The following steps are prescribed in para 6.34 of the OECD's Transfer Pricing Guidelines for tax administrations when analysing transactions involving intangibles :

> *"i) Identify the intangibles used or transferred in the transaction with specificity and the specific, economically significant risks associated with the development, enhancement, maintenance, protection, and exploitation of the intangibles;*
>
> *ii) Identify the full contractual arrangements, with special emphasis on determining legal ownership of intangibles based on the terms and conditions of legal arrangements, including relevant registrations, licence agreements, other relevant contracts, and other indicia of legal ownership, and the contractual rights and obligations, including contractual assumption of risks in the relations between the associated enterprises;*

iii) Identify the parties performing functions …, using assets, and managing risks related to developing, enhancing, maintaining, protecting, and exploiting the intangibles by means of the functional analysis, and in particular which parties control any outsourced functions, and control specific, economically significant risks;

iv) Confirm the consistency between the terms of the relevant contractual arrangements and the conduct of the parties, and determine whether the party assuming economically significant risks under step 4 (i) of paragraph 1.60, controls the risks and has the financial capacity to assume the risks relating to the development, enhancement, maintenance, protection, and exploitation of the intangibles;

v) Delineate the actual controlled transactions related to the development, enhancement, maintenance, protection, and exploitation of intangibles in light of the legal ownership of the intangibles, the other relevant contractual relations under relevant registrations and contracts, and the conduct of the parties, including their relevant contributions of functions, assets and risks, taking into account the framework for analysing and allocating risk under Section D.1.2.1 of Chapter I;

vi) Where possible, determine arm's length prices for these transactions consistent with each party's contributions of functions performed, assets used, and risks assumed, unless the guidance in Section D.2 of Chapter I applies."

It is worth repeating that the application of the arm's length principle in transfer pricing, as described in the OECD's Transfer Pricing Guidelines, does not relate to the pricing or valuation of intangible assets as such – rather, it relates to transactions involving intangibles. This focus on transactions requires the commercial terms of each transaction to be defined (or 'delineated'):

"*The terms of the compensation that must be paid to members of the MNE group that contribute to the development, enhancement, maintenance, protection and exploitation of intangibles is generally determined on an ex ante basis. That is, it is determined at the time transactions are entered into and before risks associated with the intangible play out. The form of such compensation may be fixed or contingent. The actual (ex post) profit or loss of the business after compensating other members of the MNE group may differ from these anticipated profits depending on how the risks associated with the intangible or the other relevant risks related to the transaction or arrangement actually play out. The accurately delineated transaction, as determined under Section D.1 of Chapter I, will determine which associated entity assumes such risks and accordingly will bear the consequences (costs or additional returns) when the risks materialise in a different manner to what was anticipated (see Section B.2.4).*"

(OECD Transfer Pricing Guidelines 2022 edition, para 6.45)

Transfer pricing documentation vs price-setting policies

The OECD's Transfer Pricing Guidelines recommend that local tax authorities adopt a three-tiered approach to the transfer pricing documentation, which each multinational group (depending on size) is required to maintain. This comprises the following:

- Master file – this is intended to present an overview of the relevant group, including the nature of its global business operations, its overall transfer pricing policies, and the global allocation of its income and economic activities. The master file must contain, amongst other things, 'a list of important agreements related to intangibles'.

- Local files – the group must prepare a local file for each individual tax jurisdiction in which it is present. Each local file provides more detailed information on the transactions affecting that tax jurisdiction, including financial information, an analysis of comparable arm's length prices and copies of all material intercompany agreements.

- Country-by-country (CbC) report – this comprises aggregated information relating to the global allocation of income, the taxes paid, and certain other indicators across all the tax jurisdictions in which the group operates. The report also requires a listing of all the 'constituent entities' for which financial information is reported. Note that the OECD recommends that CbC reports should not be required for MNE groups with annual consolidated group revenue of less than EUR 750 million.

These reports, together with supporting evidence, are commonly referred to as 'transfer pricing documentation', and are prepared after the event (i.e. on a 'look back' basis) – commonly alongside the preparation of corporation tax returns for the relevant entities in their respective tax jurisdictions.

Transfer pricing documentation should be distinguished from transfer pricing policies, also referred to as 'price-setting policies', which are created in advance of the financial periods in question. Intercompany agreements – including intra-group licenses of intellectual property – play a key role in evidencing or 'delineating' controlled transactions as part of forward-looking price-setting policies and are an essential element of TP compliance for all multinational groups. Some tax administrations, such as Germany, go further in stating explicitly that intercompany agreements must be entered into in advance, in order to be effective for transfer pricing purposes:

> *"The relevant point in time for applying the arm's length principle is the conclusion of the [intercompany] agreement, not the date on which the relevant transaction is performed."*
>
> German Administrative Principles on Transfer Pricing, Updated June 2023 (unofficial translation)

The wider considerations for intra-group transactions and intercompany agreements

Transfer pricing and intellectual property management are just two of a range of stakeholders or issues which can be affected by the form and substance of intra-group transactions and intercompany agreements. Other stakeholders or issues include:

- Corporation tax, and the disallowance of expense deductions
- Withholding taxes, such as those applying to cross-border royalty payments
- Value added taxes and other sales taxes
- Regulatory compliance
- Currency control
- Customs duties on the importation of goods

- The accounting treatment of the transactions, and impact on the statutory accounts of the participating entities
- Data protection compliance
- Ring-fencing of legal claims risks
- Directors' duties

The creation and maintenance of appropriate transfer pricing policies and intercompany agreements therefore requires a holistic, cross-functional approach, in order to manage risks appropriately.

Intercompany agreements: the double-edged sword and the one-way street

The OECD's Transfer Pricing Guidelines and the guidance issued by many tax administrations around the world contain extensive commentary on the role of intercompany agreements. The best evidence of the substance of related party transactions and the allocation of risks between related parties is an appropriate intercompany agreement, which is entered into in advance, and which is aligned with the legal ownership of assets, the conduct of the parties and the economic substance of the arrangements (including the financial capacity of the respective parties to assume risks). In addition, intercompany agreements are often among the first documents requested by tax administrations in TP audits or enquiries. If material related party transactions are not documented by appropriate intercompany agreements, the taxpayer has lost the opportunity to put forward a comprehensive, coherent, evidence-backed explanation of the arrangements. It is therefore exposed to unnecessary transfer pricing risks – and unnecessary management time and third-party costs in dealing with transfer pricing enquiries, audits and controversies.

An intercompany agreement is however a double-edged sword: if the agreement is aligned with legal and operational reality, and with the relevant transfer pricing policies, it is a powerful tool in defending transfer pricing positions. However, if the agreement is not aligned with the group's transfer pricing policies, it can seriously undermine the taxpayer's position in a transfer pricing dispute. This was the situation in the Coca-Cola litigation mentioned above: the group's purported transfer pricing policies were directly contradicted by the terms of its intercompany agreements, in particular as regards the ownership of intellectual property rights. The U.S. Tax Court commented as follows:

> "*Notably absent from this regulation is any provision authorizing the taxpayer to set aside its own contract terms or impute terms where no written agreement exists. That is not surprising: It is recurring principle of tax law that setting aside contract terms is not a two-way street. In a related-party setting such as this, the taxpayer has complete control over how contracts with its affiliates are drafted. There is thus rarely any justification for letting the taxpayer disavow contract terms it has freely chosen.*"[3]

It is therefore critical that intercompany agreements – including those dealing with intangible assets – are prepared with reference to the intended transfer pricing policies and the wider needs of the group, as referred to above and reviewed/amended periodically to ensure no misalignment on an ongoing basis. As a matter of best practice, this should be reviewed at least once a year, as part of the group's internal audit and management of key risks to the business.

[3] US Tax Court, The Coca-Cola Company & Subsidiaries v IRC (No. 31183-15) 2020

Do’s and don'ts for IP professionals when assisting multinational groups

It’s too early to predict the outcome of the Microsoft dispute (which is unlikely to be resolved for a number of years), or to analyse the role which intercompany agreements may have played in the controversy.

However, what is certain is that intellectual property professionals and in-house legal teams have a key role to play in helping the multinational groups they support to manage transfer pricing risks, including as they relate to intangibles.

The most basic contribution that an IP professional can bring to the table is probably that of issue-spotting: by having a general awareness of transfer pricing as a key risk area for the group, they can provide additional ‘eyes and ears’ for the tax function, in flagging transactions or misalignments before they are entered into and/or formalised, and ensuring that they are reviewed from a tax and transfer pricing perspective, with an eye on the legal reality and the operations of the group.

Some headline do’s and don’ts:

Do:

- Educate yourself about the transfer pricing policies adopted by the relevant group(s)
- Ensure that intellectual property management policies of the group are aligned with transfer pricing policies (and that this is periodically reviewed)
- Involve the tax or transfer pricing function in the material arrangements concerning intra-group transactions, including those involving intellectual property

Don’t:

- Finalise or conclude intercompany agreements without reference to transfer pricing and a tax review
- Use third party agreements as the starting point for intercompany agreements – they generally lack the specific functionality required for transfer pricing compliance, and often contradict the risk allocation implicit in transfer pricing policies and group operations and supply chain management

Determining the Crax of the Matter in trade mark opposition proceedings

By Thembokuhle Danca

Source: Shutterstock

A recent Supreme Court of Appeal (SCA) judgment on the case of National Brands Limited v Cape Cookies CC & Another (Case nos: 309/2022 and 567/2022) [2023] ZASCA 93 (12 June 2023) has shed light on the application of Section 10(17) of the Trade Marks Act 194 of 1993 ("the Act") in opposition proceedings. The case provides essential guidance on how this provision of the law affects opposition to trade mark registrations.

The matter concerned Cape Cookies' application to register the trade mark SNACKCRAX in class 30, covering savoury snack foods such as biscuits. The SNACKCRAX application was opposed by National Brands based on its prior registrations for SALTICRAX, SNACKTIME and VITASNACK all in class 30, also covering savoury snacks. The High Court found that National Brands had failed to establish sufficient grounds to stop Cape Cookies from registering its SNACKCRAX trade mark and therefore Cape Cookies succeeded before the High Court. However, this decision was overturned by the SCA.

Source News24

Findings and comments made by the SCA

The opposition was based on several grounds found in section 10 of the Act. In considering this matter, the SCA only considered section 10(17):

Section 10(17) provides that a mark *"shall not be registered as a trade mark if it is identical or similar to a trade mark which is already registered and which is well-known in the Republic, if the use of the mark sought to be registered would be likely to take unfair advantage of, or be detrimental to, the distinctive character or the repute of the registered trade mark, notwithstanding the absence of deception or confusion*".

Section 10 (17) of the Act is one of the anti-dilution provisions, which seeks to do more than just protect the mark as a source identifier, but it also seeks to protect the reputation, advertising value or selling power of a well-known mark.

There is no authoritative case that has dealt with the provisions of section 10(17), however there are several cases that have dealt with the application of the similar infringement provision, section 34(1)(c).

In this particular case, the court referred to the *Laugh It Off Promotions CC v South African Breweries International (Finance) BV t/a Sabmark International and Another* (Laugh It Off), which is the leading case when it comes to a dilution inquiry in terms of section 34(1)(c). In this case it was held that in order to establish infringement in terms of section 34(1)(c), a party has to meet the following requirements:

(a) the unauthorised use by the defendant of a mark

(b) in the course of trade

(c) in relation to any goods or services

(d) the mark must be identical or similar to a registered trademark

(e) the trademark must be well known in the Republic, and

(f) the use of the defendant's mark would be likely to take unfair advantage of, or be detrimental to, the distinctive character or repute of the registered trade mark.

The first three points were not disputed. Furthermore, it had been conceded in argument before the High Court, that National Brands' SALTICRAX trade mark was well known in South Africa, meaning that the SCA only had to consider requirements (d) and (f).

(d) - the mark must be identical or similar to a registered trademark

Cape Cookies argued that section 10(17) only applies to goods that are different to those for which the mark had been registered. As a result, with both SALTICRAX and SNACKCRAX being savoury biscuits, National Brands was not entitled to rely on section 10(17).

The court rejected Cape Cookies' argument, stating that section 10(17) is not limited to matters involving different goods or services, but also covers similar goods and services.

The court then considered the similarity of the marks. In its consideration the court applied the long-accepted approach on how to compare word marks.That is, the court considered the visual, aural, and conceptual similarities between the marks, and considered factors such as the distinctive elements, overall impression, nature of goods or services, and consumer perception.

The court found that the dominant feature was the suffix CRAX. This dispelled the arguments previously made by Cape Cookies, who submitted that the word CRAX is an abbreviation of the word "crackers", which is an ordinary and descriptive word, and thus National Brands could not claim exclusive rights in this word. In considering evidence of language use, which included consulting various dictionaries, the court found that there was no basis for concluding that the word CRAX was a word used in everyday language or that it was an abbreviation for crackers.

Furthermore, the court concluded that the prefix SNACK does not serve to distinguish SNACKCRAX from SALTICRAX either visually or aurally, as both the prefix "SALTI" and "SNACK" are descriptive words. In considering the notional use of the marks, the court further determined that the marks would be used on identical goods, which would cause further confusion among consumers.

(f) - the use of the defendant's mark would be likely to take unfair advantage of, or be detrimental to, the distinctive character or repute of the registered trade mark.

In assessing whether Cape Cookies' use of the SALTICRAX mark would be detrimental to or take unfair advantage of National Brands' reputation, the court made the following remark:

"*Concrete evidence of actual advantage or detriment is not required under 10(17). Only a likelihood need be shown…… I agree that, as opposed to bare assertions, facts supporting such an inference must be put up.*"

The court then went on to find that National Brands had proven that it had acquired a reputation in the SALTICRAX trade mark as a result of the time and money invested in marketing the brand. In this regard, the court considered, amongst other things, that

National Brands had spent more than R11 million in advertising SALTICRAX over a 15-year period and as a result had achieved a strong market penetration. Due to this, the court held that the only inference that could be drawn from Cape Cookies adoption of a mark incorporating CRAX for identical goods was that it wanted to achieve market penetration at the expense of National Brands reputation.

In conclusion, the court found that if registration was to be allowed, use of SNACKCRAX would probably, or be likely to, take unfair advantage of the distinctive character or repute of SALTICRAX.

Conclusion

The judgment clarifies that Section 10(17) is not limited to cases of dissimilar goods or services but also extends to situations where the goods or services are also similar. More importantly, it has clarified that evidence of actual harm is not a requirement under an enquiry in terms of section 10(17) and the type of evidence an applicant must adduce to show that registration of a conflicting mark would be likely to take unfair advantage of, or be detrimental to, the distinctive character or the repute of its trade mark.

About the Author

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Thembokuhle is an associate at Spoor & Fisher. He holds LLB and BA(Law) degrees from the University of Witwatersrand. He is an attorney of the High Court of South Africa and focuses on the field of trade mark prosecution and enforcement. He is a Student Member of the South African Institute of Intellectual Property Law (SAIIPL) and a member of the Legal Practice Council (LPC)

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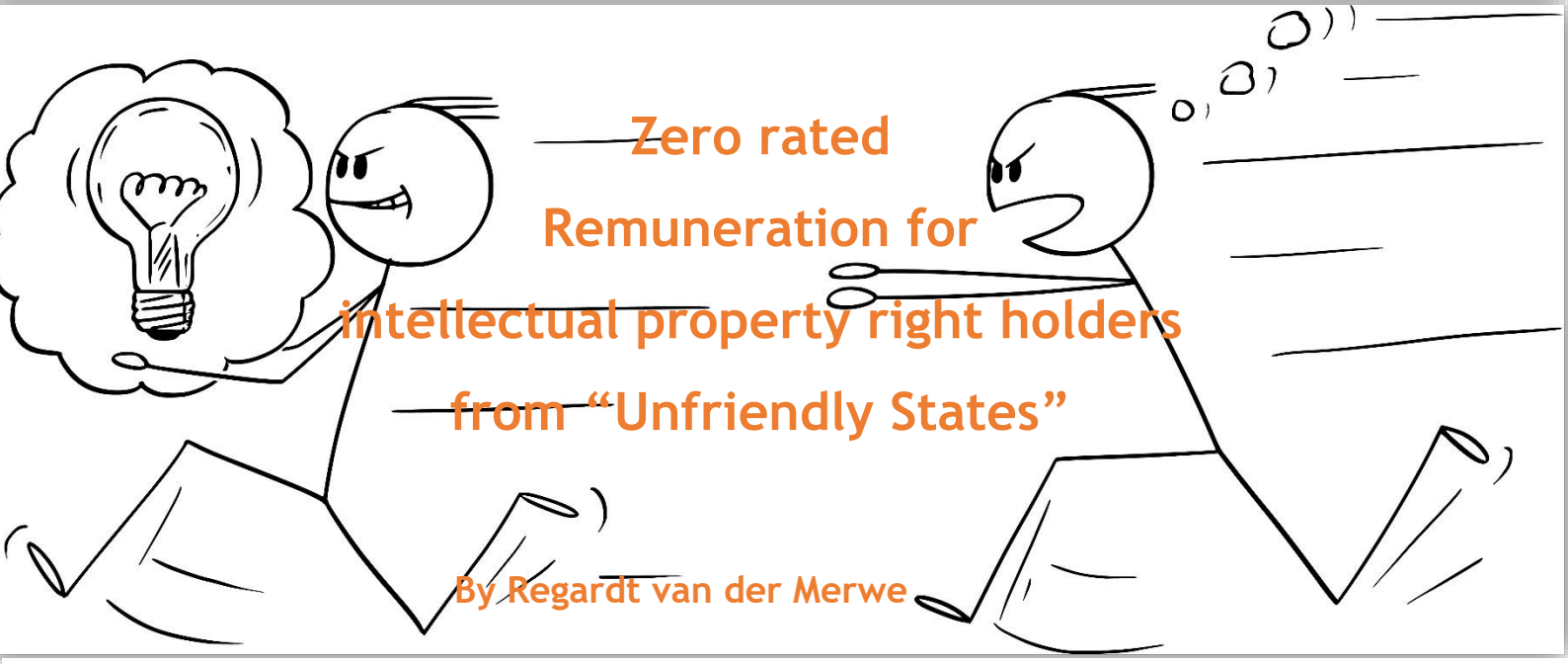
Trade Marks Act 194 of 1993



Zero rated Remuneration for intellectual property right holders from "Unfriendly States"

By Regardt van der Merwe

Shutterstock Images

An overview of the countermeasures adopted by Russia limiting the protection of intellectual property rightsholders from "unfriendly states"

Background

Under article 1358 of the Civil Code of the Russian Federation ("the Civil Code"), a patent holder owns the exclusive right to use (or authorise the use) of an invention, utility model or industrial design.

As an exception to the above provision, Article 1360 of the Civil Code entitles the Russian government to permit the use of an invention, utility model or industrial design without the consent of the patent holder, in circumstances where it is in the interests of national security to do so; provided that

i) the patent holder be notified as soon as possible; and
ii) compensation is paid to the patent holder.

The procedure for restricting patent rights under Article 1360 of the Civil Code is a common mechanism also implemented in other States, and is based on Article 30 of the TRIPS Agreement. In South Africa, a similar provision is contained in Article 4 of the Patents Act No. 57 of 1978.

On 18 October 2021, the Russian government issued Decree No. 1767 which provides an outline for calculating compensation when applying Article 1360. In terms of this decree, the amount of compensation to be paid to the patent holder is 0.5% of the actual proceeds – regardless of the nationality or place of registration of the rightsholder.

On 6 March 2022 the Russian government issued a further decree, Decree No. 299, which amended the provision for remuneration in that the remuneration amounts to zero if the rightsholders commit unfriendly actions against Russian legal entities or natural persons.[1]

[1] WIPO 'Background on the Zero Remuneration Rate' available online at https://www.wipo.int/edocs/mdocs/sct/en/sct_45/sct_45_russian_federation_info_paper_2.pdf (accessed on 18/10/2023).

The consequence of Decree No. 299 is that inventions, utility models and industrial designs owned by persons or entities from "unfriendly states", which were previously protected in Russia, may now potentially be used by Russian companies or individuals, without any compensation to the patent owner.

"Unfriendly States"

On 5 March 2022, the Russian Government issued a list of "unfriendly states". These States include all European Union member states; Australia; Albania; Andorra; Great Britain (including the island of Jersey and British oversea territories – the island of Anguilla, British Virgin Islands, Gibraltar); Iceland; Canada; Liechtenstein; Micronesia; Monaco; New Zealand; Norway; Republic of Korea; San Marino; North Macedonia; Singapore; United States of America; Taiwan; Ukraine; Montenegro; Switzerland; and Japan.

European Response

The European Patent Office (EPO) has frozen all cooperative activities with the Russian Federal Service for Intellectual Property (Rospatent), Belarus, and the Eurasian Patent Organisation (EAPO).

Insofar as trade marks and designs are concerned, the European Union Intellectual Property Office (EUIPO), have also halted all cooperation actions with Rospatent and the Eurasian Patent Organisation (EAPO).[2]

Application of Russian Decree 299

Decree No. 299 is limited to inventions, utility models and industrial designs; and does not extend to trade marks and copyright. The exit of many Western companies from Russia has however given rise to domestic imitation trade marks, as illustrated by the two examples of IKEA and McDonald's below.

[3]

Despite the uncertainty about the rights of foreign patent holders in Russia and the influx of domestic imitations of Western trade marks, recent court decisions in Russia provide reassurance that the legal mechanisms for the protection and enforcement of trade mark rights remain fully in force in Russia. Two recent trade mark cases in Russia are briefly summarised below.

[2] EUIPO 'Statement on Ukraine' available online at https://euipo.europa.eu/ohimportal/en/-/news/the-euipo-has-adopted-a-number-of-measures-in-coordination-with-the-eu-institutions-1 (accessed on 18/10/2023).
[3] UK Telegraph 'Want fries with your McCopycat? Russia replaces Ikea and McDonalds with imitation brands' available online at https://www.telegraph.co.uk/world-news/2022/04/01/want-fries-mccopycat-imitation-western-brands-replace-ikea-mcdonalds/ (accessed on 18/10/2023).

PEPPA PIG vs DADDY PIG

In March 2022, the owner of the PEPPA PIG trade mark instituted trade mark infringement proceedings against a Russian national, based on the use of the offending mark DADDY PIG. The court of first instance ruled against the UK trade mark proprietor for the reason that it is a company from an "unfriendly state".[4] The decision was however overruled on appeal, later in the same year. The Appeal Court stated that, in accordance with the Berne Agreement and the Madrid Convention, equal protection of the intellectual property of foreign organisations, including those registered in the UK, must be guaranteed in the Russian Federation.[5]

FANTA vs FANT

In June 2022, the Russian Intellectual Property Court held that the trade mark FANT and its label, used in respect of a carbonated orange flavoured soft drink, is confusingly similar to the FANTA trade mark and label.[6] It reassuring to note that this decision was granted despite Coca-Cola suspending its business in Russia.

Conclusion

Although it remains to be seen how, and in respect of what, the Russian government will apply Article 1360 of the Civil Code and the zero remuneration policy; it is plausible that the Russian government may invoke Article 1360 to safeguard the availability of certain critical goods in the Russian market, such as pharmaceuticals.

It is however apparent that the zero remuneration policy under Decree No. 299 conflicts with Article 1360 of the Civil Code, as well as with Article 31 of the TRIPS Agreement, both of which requires the payment of remuneration to rightsholders.

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Regardt is a Senior Associate at Spoor & Fisher. He is a qualified Trade Mark Practitioner and an admitted Attorney of the High Court of South Africa. He holds an LLM (Intellectual Property Law) degree from Stockholm University, Sweden, and LLM (Public International Law) and LLB degrees from the University of Pretoria. His practice is focused on IP litigation – including trade mark oppositions and cancellations, trade mark and copyright infringement; as well as trade mark prosecution.

[4] Case no. A28-11930/2021 available online at https://kad.arbitr.ru/Card/a45fa186-05bb-43b5-87d9-1f0d3b640142 (accessed on 18/10/2023).
[5] Case no. A28-11930/2021 available online at https://kad.arbitr.ru/Card/a45fa186-05bb-43b5-87d9-1f0d3b640142 (accessed on 18/10/2023).
[6] Demcak, Igor 'Rule of law in the times of uncertainty for Western trademarks in Russia' available online at https://www.lexology.com/library/detail.aspx?g=00f5d29e-50ea-4449-a56e-9693b12e905e (accessed 18/10/2023).

From the Juta Law Reports

The following judgments were reported July to October 2023

Patent - *Powers of Registrar of Patents* — Registrar having discretion to grant any extension provided for in the Patents Act or the Regulations thereto, provided there is no express prohibition in the wording of the provisions — Registrar may exercise his discretionary power even after the expiry of the stipulated period — Section 42(3) of the Patents Act not ousting Registrar's discretion under s 16(2) of Act. *Mecanicos Unidos SAS v Registrar of Patents* GP case No 068030/23, **Juta 2023 JDR 3370 (GP)** (Koovertjie J), 30 August 2023, 8 pages.

Confidential information -*Alleged theft of confidential information* — Application for discharge of *Anton Piller* order — First applicant (RKSA) averring in founding affidavit that respondents, former employees, had stolen its confidential information (about edible powder colours for cake decoration) and that first respondent (Unique Colours) was, as a consequence, now unlawfully competing with it — *Anton Piller* order containing list of what to search for on respondents' electronic devices, including cell phones, computers and computer storage media — Notice of motion providing for respondents to show cause why items in the possession of sheriff should not be retained pending the directions of court — Court discharging application, noting that RKSA's frustration and anger at its erstwhile employees, while understandable, did not per se confer a claim for damages or the automatic confirmation of an *Anton Piller* order — Court pointing out, in addition, that RKSA had to convince it that it had a strong *prima facie* cause of action, that Unique Colours had vital information in its possession and that there was a real and well-founded apprehension that such information might be destroyed or hidden — Court finding that there was no clear evidence to establish that Unique colours had vital information in its possession — *Anton Piller* order discharged —Interdictory relief refused. *RKSA DC (Pty) Ltd v Unique Colours (Pty) Ltd and Others* GP case No 53194/2021, **Juta 2023 JDR 3784 (GP)** (Potterill J), 20 July 2023, 8 pages.

Copyright - *Admissibility of certain evidence on infringement of copyright* — Application for temporary and declaratory relief for alleged copyright infringement — Both parties manufacturers and sellers of medical respirators — Disputes having developed regarding the admissibility of certain evidence and the value of certain paragraphs in the heads of argument — Evidence of witness who had no personal knowledge of facts and who based his evidence on unproven hearsay evidence struck out — Application to allow evidence of email emanating from person in China disallowed under s 3(1)*(c)*(v) of Law of Evidence Amendment Act 45 of 1988 — Application for temporary relief dismissed. *Evrigard (Pty) Ltd v ENB Import and Export (Pty) Ltd and Another* GP case No 57565/2021, **Juta 2023 JDR 3415 (GJ)** (Wepener J), 11 September 2023, 5 pages.

Copyright - *Availability of temporary relief for infringement of copyright* — Applicant alleging that respondents had copied its technical drawings for the fabrication of a modular mineral processing plant (MMPP) and then used them to pre-empt, through the second respondent (Westascor), its bid to supply MMPPs to a foreign buyer (the UARI bid) — Westarcor became contracting party with UARI — First respondent, a former employee of the applicant who had obtained intimate knowledge of applicant's MMPP designs, made drawings for Westarcor's competing MMPPs — Applicant having obtained an ex parte *Anton Piller* order against respondents, in the execution of which various allegedly incriminating items were seized from them — Applicant in its main action claiming damages and final interdictory relief against the respondents based on alleged copyright infringement — Main action postponed pending applications for confirmation of applicant's *Anton Piller* order and interdictory relief — Court seized with application for interim relief pointing out that evidence clearly showed that there was close cooperation between the first respondent and Westarcor in everything done to meet their UARI bid — Court confirming *Anton Piller* order and granting interim interdict, pending determination of action proceedings, restraining Westarcor from directly or indirectly utilising any information obtained from the applicant for any purpose unless authorised by applicant. *ADP Marine & Modular (Pty) Ltd v Rocher and Others* WCC case No 5701/2022, **Juta 2023 JDR 3275 (WCC)** (Hockey AJ), 25 July 2023, 18 pages.

Trademark - *Existence of a protected right* — Application for leave to appeal against finding that applicant had no protected right to PROVITA savoury biscuit device — Registration of mark having been subject to explicit restriction that it would not give 'right to the exclusive use of a device of a biscuit as such otherwise than as shown in the application' — Court seized with application for leave to appeal pointing out that fact that registered mark shown together with, and embossed on, biscuit device should not be construed to mean that the two were bonded and therefore inseparable for purposes of identification of applicant's protected interest — Applicant not entitled to assume that it had protected rights to biscuit device merely because both registered mark and biscuit device were shown in applicant's application — Court finding that applicant could assert no infringed right to its PROVITA mark without reference to biscuit device — On this basis, applicant not entitled to final interdict — Leave to appeal refused for lack of prospects of success — Trade Marks Act 194 of 1993, s 34(1)*(c)*. *National Brands Limited v Continental Biscuit Manufacturers (Pty) Ltd (Leave to Appeal)* GP case No 43416/2020, **Juta 2023 JDR 3315 (GP)** (Mbongwe J), 1 September 2023, 4 pages.

Trademark -*Lis pendens* plea in trademark matter — Litigation between United States Polo Association and South Africa's LA Group regarding POLO marks — LA Group and USPA engaged in pending litigation in Gauteng High Court wherein LA Group *inter alia* seeking an order for the removal from the register of USPA's mark — LA Group launching separate substantive application seeking similar relief in same court, joining USPA as first respondent and Registrar of Trademarks as second respondent — Court finding that cause of action same and that elements of plea of *lis pendens* established. *United States Polo Association v LA Group (Pty) Ltd and Another* GP case No 2023/021399 **Juta 2023 JDR 3402 (GP)** (Van Niekerk AJ), 28 August 2023, 6 pages.

Intellectual Property Word Search

X Y E D R G Y K T C I O B C N Y G E K A D B U W
G U L P U K J H W M A T D W X W C D Z O Y G R M
W E F D V O G Z T X A H S N S T O A O R B K D H
B O O A U I R F H R U C P E B T A Q R R P M N U
C Y T G R T J G T C A T A S D E H Y Q I V P I K
T E O Y R F D E T E Q D T Q L V I G V V P T N H
S V P T M A G J L E H I E F F J E Y I S V R T Y
I O J W I T P A T F D A N M F D G R B R L A E C
C V S Q S O M H O E O D T E A T C Q Z G C D L U
Q K I L A S J F I E C S S V G R F N G J I E L T
J A N A P U H H X C B O R J R B K W U U G S E G
B W F C P N N Q X G A V I R N S K B W W P E C Z
D P R I O H K O R R N L G P S V J G M M G C T B
M K I M P H T V I V X M I E I P J O P R M R U M
R A N O R K A P X T G V R N Z M R T W I L E A D
A F G N I S S G F W C D T C D A K X R A M T L T
C P E O A P S O L Z E E O R L I M Z M H A Z P K
A U M C T E O H Q D X S T I P W C Z L E N X R Y
T X E E I C J P A H F A T O S L J A O K H W O A
A U N P O E P R H I R Y Z E R M C A T X B K P B
C K T C N N T U T L G Y D P D P Z Z A I N S E G
F I N A N C I A L I N C E N T I V E R X O D R P
Q X Q Q Y R T P V I R F Y L E X G X B N Y N T M
C N G I S E D L A I R T S U D N I M U J V S Y O

MISAPPOPRIATION
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GEOGRAPHICAL INDICATION
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