

Preparing Employment Agreements Regarding IP Related Business in Japan

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Question 1

- Suppose that you are an inventor and your invention achieves a high measure of success with consolidated sales of one million dollars: How much would you like to receive from the company?



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Question 2

- Suppose that you are an executive officer of a company and an invention created by an employee has a turnover of one million dollars: How much would you like to pay the inventor?



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Situation in Japan



- **Trend** -Increasing number of lawsuits where employees ask companies for a high amount of compensation for their inventions on the basis of Section 35 of the Patent Law, which is unique to Japan.

Dr. Nakamura was granted 160 million US dollars from Nichia Chemical

- **Key is Predictability** - How can employers predict lawsuits from employees who created excellent inventions and demand expensive compensation?
- **Practical Question** -When your company conducts research and development activities in Japan, what kind of employment agreement should you prepare?

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Japanese Employment System and Section 35 of the Patent Law

- **Important** – understanding of background of old Article 35 and new Article 35 of JPL
- **The Lifetime Employment System**
There is almost no career switching, and employees is generally obedient to their company. Under this condition, status of employees is generally very weak.
- **Old Article 35 of the Japanese Patent Law**
In order to protect inventors who are employed by Japanese companies, this law obliges companies to pay their employees reasonable compensation for the assignments of their inventions in addition to their wages.

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Compensation under Old Article 35 of Japan Patent Law

- **Original right to obtain patent is belongs to its inventor.**
- **An employer automatically obtains a royalty-free non-exclusive license from inventor without an assignment of the invention.**
- **When the employer wishes to receive an assignment of an invention, it must pay the inventor a reasonable compensation.**
- **Reasonable compensation** = "It must be determined in view of the amount of profits which shall be received by assigner of the patent right due to the invention, and the degree of the contribution made by assigner of the patent right when the invention is created." (Old Article 35(4)) – There is no authority for employer/employee agreement to determine the compensation
- **However, no argument has been made to specify the amount of "reasonable compensation," and companies have kept the amount of the compensation low by tradition.**

- Dr. Nakamura's case: Company paid US\$ 200 for his invention.

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Old Article 35 of JPL and Lawsuits

- **The employment situation has changed due to the recession in Japan in last ten years.**
With changes in recent employment situations, there have been a rash of complaints from employees about low compensation, and there have been many lawsuits asking the court to make judgments regarding "reasonable compensation."
- **Reasonable compensation judged by the court**
ex1: Total sale x (Loyalty rate:2% - 10%) x (contribution rate:10% - 95%)
ex2: Total profit by the invention x (contribution rate:50%)
- **Situation is not good for both employer and employee**
> Employers...puzzled by unpredictability because many decisions grant high amounts of compensation not considering each company's rule and situation.
> Employees... do not know how to respond to the recent court decisions.

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Amendment to Section 35 of the Patent Law

- **Government has decided to revise Article 35.**
 - Research and development activities in Japan could slow down.
 - Highly capable inventors could leave the country and go overseas.
- **Purpose of the revision:**
To increase the predictability of compensation in companies without causing employees to lose their motivation to invent.



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Compensation under Section 35 of the New Patent Law (1)

- **Fundamental Principle** = As long as the process of reaching an agreement between a company and its employees is not unreasonable, the content of the agreement shall be respected (new Section 35(4)).

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Compensation under Section 35 of the New Patent Law (2)

- If the process of reaching an agreement is **unreasonable** = "Compensation is determined in view of the amount of profits which shall be received by executors of the patent right due to the invention, and the degree of contribution made by the executors of the patent right when the invention was created." (new Section 35(5))

Thus, there is still a possibility of lawsuits asking for a high amount of compensation as was conventionally done.



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Compensation under Section 35 of the New Patent Law (3)

- If the process of reaching an agreement is **not unreasonable** = No need to follow Article 35(5). Company can decide their own compensation according to the agreement.

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Requirements for Reasonable Process of Reaching Agreements

- Regarding the process for determining compensation, the following is needed between a company and its employees:
 - A. **A substantial meeting is held,**
 - B. **A baseline standards for compensation is disclosed,** and
 - C. **Opinions are exchanged.**

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Example 1

- A company imposes an already-established rule on its new employees without explaining the compensation for employees' inventions.

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Article 35(5) will apply

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Example 2

- A company and its employees have a meeting regarding compensation for employees' inventions which are included in the wages and they reach an agreement.

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The agreement does not need to follow Article 35(5)

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Example 3

- A company introduced a low flat rate as compensation for all employees according to a result of discussion between employer and employee.

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Controversial Point

- Impossible to reach an agreement satisfying all of the requirements A, B and C with all employees and already-retired employees. Even if possible, that does not necessarily eliminate the risk of lawsuits.

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Problems for Foreign Companies

- Balance between employees in your country and employees in Japan.
- In the case of a joint invention by foreign employees and Japanese employees

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Current Trend: Securing Inventors' Motivation

- Problems between employer and employee regarding Section 35 of the Patent Law are basically related to successful inventions.
- It is important to set rules, under which a large amount of compensation can be given to an invention having great success making it easier for employees to agree.



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Practical Conclusion

- Company at least should remove from agreement existing upper limit relating to compensation.
- Follow requirements A to C as much as possible with appropriate consultation from outside advisers.
- Ask question 1 and 2 and ask both party to fill out the gap between them.

The End

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