Small Scale Industries and IP Management: Need to Recognize Intellectual Assets

Vidhan Maheshwari† and Pratishtha Bhatnagar
National Law Institute University, Bhabhada Road, Bakheri Kalan, Bhopal, Madhya Pradesh 462 003

Received 9 October 2007, revised 29 January 2008

The small-scale industries hold a very crucial position in every economy and the Indian economy is no exception. However, in the shifting frames of time, these industries have failed to cope up with the emerging challenges and to keep abreast with the latest developments especially, in the field of IPR. In India, most of these industries are lagging far behind and facing technical obscurity, being unaware about management of their knowledge-based assets like IPR. This paper deals with issues on the future of Small-Scale Industries (SSIs) in India in the present era of globalization and liberalization with the advent of TRIPS. The paper specifically focuses on the SSIs having investment of less than Rs 1 crore and discusses the importance of Indian SSIs in changing economic environment and its implications on small industries. It examines the reasons for protecting intellectual wealth in the present scenario of the economic development in India. It analyses the role of government in making the small enterprises viable and what measures should be and are being taken. The paper also deals with the steps taken for creating IPR culture and suggests the initiatives for SSIs.

Keywords: Small scale industries, globalization, TRIPS

Like in any developing country, the SSIs in India, occupy a central position in the development of the economy. But despite numerous policy measures by the Government for the past six decades, small enterprises have remained technologically backward and lack in competitive strength.¹ The business environment has changed drastically since 1990's due to the adoption of new economic policies. The radical shift in economic policies, partly, occurred due to India's own macroeconomic crisis and partly as a consequence of global trend. With the advent of World Trade Organization (WTO) and Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS), the industries in India, are facing a situation of international and internal competition. Small-scale industries face a major challenge in the new environment because they are not familiar with the best ways to manage their knowledge assets. They face different types of IPR challenges and do need to evolve strategies suiting different conditions to exist in competitive market. In this context, it is equally important to re-look at the basic issues relating to, reasons for economy environment change, need for protecting intellectual wealth, policy measures and steps taken for creating IPR culture in SSIs. The paper deals with all these issues simultaneously.

Indian Small Scale Industries in the Era of Globalization

SSI sector in India constitutes 95% of all units; 40% of value added; nearly 80% of the employment of the total manufacturing sector; and, 35% of total exports. According to the Third All India Census of SSIs, held in 2001-2002, total number of permanently registered SSIs were 23,05,725 and total number of employment generated by the sector was 34,48,356.² SSIs are very important in India not only for their contribution to the economy but also for special aid they enjoy from government. But despite numerous efforts, the Indian SSIs over the years have remained backward and are struggling in competitive economy.

This suggests a need for finding out the possible ways of improving the competitive strength and commercial viability of SSI in the changing milieu. The economic policy reforms of the last few decades that have aimed at the liberalization of domestic transactions and the opening of economy have changed the business environment for SSIs. Globalization is the main factor responsible for these critical changes, resulting in intensifying the market competition. The process of globalization which took its roots in 1990s was followed by introduction of the TRIPS Agreement in the multilateral trade agreement, now known to be implemented by the WTO. This resulted in a situation of international and internal competition for the industries in India. In order to

⁠Email: Corresponding author: vidhan159@sify.com
compete with imports or multinational corporate in the domestic market and to export successfully without any external support, Indian industrial units, especially SSIs need to improve on their productivity and quality, reduce the costs, go for higher performance products and better services, all to be delivered simultaneously. India has to bring down its tariff rates, as per the GATT Agreement to 40% for finished products and 25% to immediate group. In addition, India has been asked to remove quantitative restrictions on imports and all export subsidies. As a result, every single individual enterprise in India, small or large, whether exporting or serving the Indian market, has to face competition. In this context, it is important to gauge the future scenario of these units and the ways of dealing with it.

Need of Protecting Intellectual Wealth in Changing Environment

Pressures of globalization or internationalization were not as intense as they are today. During 1950s to 1980s, many countries including India, were able to manage without practicing a strong system of intellectual property rights. Keeping in mind the contribution of SSIs in the developing economy of India and changing environments, their strengthening in innovations and management of knowledge, should now occupy the centre stage. While the industries are obviously eyeing the potential benefits, the move is also going to cause some bureaucratic hassles. For example, a unit with an investment of Rs 1-5 crore in plant and machinery will no longer be classified a medium-scale unit but a small-scale one.

The TRIPS Agreement takes care of IPR by enforcing patent rights, copyrights, protection of industrial designs, trademarks, geographical indications and undisclosed information. It is of critical significance to Indian SSIs since majority of these industries are unknowingly involved in the unauthorized duplication of products without any formal technological transfer. In effect, the enforcement of TRIPS Agreement and Indian laws makes the production of any product possible through internal innovation or formal technology transfers by not allowing unauthorized imitation. This makes many SSIs dependant upon the multinational companies, as these are the prime developers of a majority of products, which in turn involves costs in terms of purchase of technology as well as restrictions on its usage. SSIs are most vulnerable, as these units do not have required resources and capabilities, either for innovations or for purchase of technologies. Also, their innovative and creative capacity is not always fully exploited as these sectors suffer from lack of knowledge as to the use of their intellectual wealth in today's era. It is impossible to reap the benefits of innovations unless uniform laws and rules of patents, trademarks, copyrights, etc. exist.

The small and medium-scale industries provide large employment in every country and contribute to overall industrial production in a significant manner. Therefore, this sector cannot be allowed to languish in the face of new situations arising out of liberalization and entry of WTO. These industries can stabilize and survive if they are able to innovate new products and processes to meet the market demands in time. It is at this point, that the management of knowledge and IPR become extremely crucial. IP protection will help in preventing competitors from copying or closely imitating an industry’s products or services; avoiding wasteful investment in research and development (R&D) and marketing; creating a corporate identity through a trademark and branding strategy; negotiating licensing, franchising or other IP-based contractual agreements; acquiring venture capital and enhancing access to finance; and, obtaining access to new market.

The knowledge economy places a tag of urgency on understanding and managing knowledge-based assets such as know-how and innovations. SSIs face a major challenge because they are not familiar with the best ways to manage their knowledge assets. With the opening up of trade in goods and services, IPR have become more susceptible to infringement without adequate return to the creators of knowledge. There has been a quantum jump in R&D costs with an associated jump in investment required for putting a new technology in the market place. The stakes of the developers of technology have thus, become very high and hence the need to protect the knowledge from unlawful use has become expedient. The best way to protect the knowledge is through IPR.

IPR has become an important parameter influencing trade, transfer and exploitation of technology. As generation of intellectual property is closely linked to innovations, there is now a lot of competition in innovation. In other words, each player in a given field would try to outpace its competitors by introducing new products through innovations. Therefore, it is necessary that a large number of IP rights are generated and protected in India. Looking at the need of recognizing intellectual wealth in SSIs, by depending upon their classification except from static small industries, which are conservative and mostly
inefficient, all are involved in some kind of innovative process. Traditional small industries rely on innovations made elsewhere and incremental innovations at their end, but are quite conservative in management and strategy planning. Dominated small industries involve very little scope of innovation and produces on behalf of large firms in growing sectors. Even if there were any innovations, it would be based on the suggestion of the contracting firm. Subsidiary units will fall under this category. Imitative industries tend to be innovative in a limited sense as they tend to reverse engineer existing products with some improvements. Technology based SSIs operate in a rapidly growing sector and these firms have to rely on innovations, which are usually internal, for example, telecommunication systems and automation. New technology based small industries deal with new technologies requiring high technical skills and management acumen. These will operate in emerging sectors like biotechnology and semi conductors industries. Almost all SSIs face different types of IPR challenges and do need to evolve strategies. For the imitative firms, the risk of infringing existing patents or other IPR has to be minimized or ended. The technology-based industries would follow similar situations and the path for innovation would only be at a little variance. Although, the new technology based industries have a better chance of creating new innovations, which could be candidates for patents. Therefore, these industries need to have a system of extensive information and patent search to identify new areas of research & development and to monitor day-to-day development in the relevant fields.

Analysis of Present Scenario in India

In India, by virtue of the Micro, Small and Medium Enterprises Development (MSMED) Act, 2006, a unit with an investment of Rs 1-5 crore in plant and machinery is classified as small-scale one. Awareness about intellectual property and associated rights among the Indian industries, especially, the SSIs was very low till 1995. Most of the SSIs fail to understand that by patenting their products or processes they stop the entries of their competitors in the market. The most widespread reasons for not patenting are that either patent is not considered relevant to the line of business of the company or they believe that a patent only provides wide publicity to their innovation achievement but does not prevent the emergence of competition in some form or the other, which they do not want. Another reason is that the patent system is too costly and complex. In India, small scale business owners place more emphasis on informal methods of protection of their intellectual property like relationship based on trust, limited information sharing, lead-time etc. rather than on formal registrable rights.

In India, except from some of the SSIs sectors like automobile, electrical engineering and apparel sectors most of the SSIs like handicraft, glassware, ceramics, paint, watch making, etc. often do not sufficiently exploit the potential of IP system for increasing their competitiveness, innovative capacity and market access. Also, due to lack of awareness about the legal implications of infringements, SSIs face legal suits and they do not know how to handle such matters. They fail to recognize the value of IP and therefore most of them do not conduct an IP audit annually. With the signing of the WTO Agreement and other agreements such as TRIPS, India has taken several steps towards bringing about a paradigm shift in the understanding about IPR, including the development of some new legislation in this field. Although, some changes are visible in the country from last 10 years, the interest started with curiosity and an element of apprehension in 1995, but has now graduated to a need-based compulsion and a desire to understand the nuances of IPR, which can enable Indian SSIs to be in the present competitive world.

Today, most of the SSIs in India are unfriendly with the terms of IPR like copyrights, trademarks, geographical indications, industrial designs, etc. It is equally important to obtain them in respect of any innovative work if possible. SSIs have to pay attention to build their brand equity as soon as possible through trademarks and domain names. Registration of domain names would become indispensable as soon as electronic trade picks up and industries start doing business on B2B networks (business to business networks). There is a need to go into the merits of the patent also to see if the concerned patent can be revoked or not. Unfortunately, most of the industries lack the expert knowledge and financial resources to proceed in this direction.

The reasons at times emanate from ignorance as well. Protection through trade secret is a well-established strategy but the right knowledge to maintain the trade secrets should also be applied. In the Indian context, it is important to note that there is no separate law on trade secrets and all the necessary steps to maintain the trade secret will have to be anticipated and put into practice. The industries should look for legal help. It is to be appreciated by
the industries that keeping a strong IP portfolio makes a good business sense. Further, it can help in securing loans, enhance market image and attract good alliances. Most of the patent applications in India are related to drugs and pharmaceuticals. It is a matter of concern that the filings by companies engaged in electrical engineering, electronics and telecommunication are very low although maximum recognized R&D units operate in these areas.

By the very nature of the definition of SSI in India, many software companies will fall under this category. It is unlikely that Indian companies can be successful in the development of products with very short life-cycles and low prices. There does however, seem to be an opportunity for Indian companies to develop products of intermediate complexity targeted at niche markets. If this argument is accepted then, the industry should seriously consider patenting of software in USA. It may be noted that the booming Indian software industry has shown total apathy towards protecting their intellectual property. Due to the very nature of the SSI sector in India, it has to adopt both defensive and aggressive postures in management of knowledge.

Patent laws are modified from time to time in order to meet the social and economic needs of the country. Till January 2005, the patent laws were revised and the Patent Act, 1970 was enacted, which did not allow patenting of substances emanating as a result of chemical reactions. Product patents were allowed except in respect of drugs, chemicals and food items. However, process patents were granted for drugs, food items and chemicals. In spite of the fact that such laws were in place, most of the scientific community and the Indian industry were not aware of, or were not conversant with the fundamentals of intellectual property rights and their management. The lack of financial resources to obtain and maintain patents in India has been identified as an important factor by the industry for the low activity. It may be reckoned that protecting inventions in foreign countries could be very expensive which most SSIs would not be in a position to afford and it looks imperative that states should intervene and extend a helping hand. For example, R&D type SSI may be exempted from paying the official fee for patenting and maintaining patents.

Steps Taken and Need of New Initiatives

Indian academics, industries and policy makers have shown keen interest and taken pro-active steps in establishing a sound foundation of IPRs. There is need to change the mind-set radically and evolve a different management and R&D culture. The challenge is massive and appears insurmountable. Many government agencies including the Ministry of Small-Scale Industries have taken concrete steps to create awareness about IPR. The Department of Scientific and Industrial Research under the Ministry of Science and Technology has a scheme to recognize in-house R&D units in industries, which after getting the recognition can avail the benefits. The Patent Facilitating Centre under the Department of Science and Technology along with the Ministry of Small Scale Industries has been playing a leading role in this direction by conducting awareness workshops providing free advice and consultancy for the SSIs all over the country.

Similar to many patent clinics, one can think of introducing advisory clinics on technology scouting in which some knowledgeable persons can identify patents of relevance to a specific sector and discuss with the SSIs. As many SSIs rely on technology acquisition from somewhere else and often, the issues of IPR written in the license agreement may not be completely understood by the SSIs due to many reasons. For example, an SSI may not be given any right to have the ownership on an improvement made over the licensed technology. Skills of licensing and technology acquisition should be imparted in training programmes for the SSI.

SSI should follow a three tier system for handling the IPR issues, the first level could be the internal assessment, followed by discussing with consultants or consulting agencies or publicly funded centres at the second level and at the third level, having discussions with the patent/IP attorneys. The governments could help at the second level by providing free consultant services, patent search reports and other information related to IPR and associated knowledge about other chapters of WTO such as technical barriers to trade and subsidies and countervailing measures. Further, patent fairs may also be organized, in which, the inventors discuss their inventions and seek advice on conceptual and operational issues related to obtaining patents on their inventions. However, the controlling factor in making such clinics successful would be whether the industries are able to develop confidence in the person who goes there to get advise from them. SSIs do spend time on new product designs, which many a times, would be based on reverse engineering or copying some existing design elsewhere. They should be constantly told about the risk of infringing existing
patents. Management of IPR should become an essentially a corporate function and the associated knowledge should be placed at par with any other assets of the company. Also trademarks and domain names should be extensively used for creating brand equity.

The Small Industries Development Organization (SIDO) is the national SME Development Agency of India. It is a major constituent of the Ministry of Small-Scale Industries of the Government of India. In 2000, an IPR Cell was set up at SIDO with the primary task of disseminating information on IPRs amongst SMEs with a view to enable them to get a better understanding of how IPR impact upon business strategy and success in the marketplace. More than 75 such programmes have been organized through SSIs all over the country. Apart from spreading awareness, these programmes have helped to identify and document success stories of SMEs in India who have succeeded in the exploitation and use of the IP system. The training material of the programme is based on local and current examples and case studies of Indian SMEs, which have profited from effective use of the IPR system in their business strategy. SIDO’s endeavour for creating IPR awareness is part of a larger plan for the internationalization and enhancing the competitiveness of Indian SMEs in a globalizing marketplace. Other elements of this plan include upgrading technology, superior infrastructure, adoption of quality systems, marketing support and credit facilitation. For instance, in Orissa, to encourage innovation, units having patents for products would be given purchase preference in all purchases made by government departments/organizations. SIDO has recently launched a new website with substantial information on intellectual property for Indian SSIs. As per the Annual Report issued by the Ministry of Small Scale Industries during the financial year 2006-07, 24 sensitization programmes were proposed to be conducted. Further, the Government of India has made policy to provide tax exemptions for IP holder’s services.8

Holding of industry specific workshops with varying emphasis on different types of IPRs as their importance differs from industry to industry, meant an extra effort for customization of awareness and training material; and, industry specific capacity building of resource persons/trainers. Along with general and industry specific workshops, steps were initiated for improving the quality of literature made available to entrepreneurs. A number of entrepreneurs and managers of SMEs in India have taken steps to evaluate options for getting their trademarks registered or seek other forms of IP protection.

Special emphasis should be placed to find out as to why the SSIs dealing in electronics, telecommunications and electrical engineering do not file patent applications. They should be empowered to do so as this sector enjoys the maximum from various incentive schemes. Software companies have contributed significantly to exports and their position needs to be strengthened. These companies would do well if they start protecting their IPR in India and other countries. As SSIs rely more on improvements, they have to keep doing patent searches and design searches in the area of interest. In order to grow vertically and horizontally in the competitive situation, SSIs will have to look towards qualified and experienced scientists working in educational institutions and publicly funded R & D institutions for new ideas, experimenting, scale up etc. and sometimes also to the government funding agencies.

Conclusion

IPR, a big and often a frightening term for small business, was largely unfamiliar in the SMEs sector in India. Those who knew something about IPRs would invariably equate it with patents. And patents were seen to be the concern of only the big, multinational companies or of big publicly funded R&D institutions. Due to poor knowledge and lack of awareness, many SMEs face stumbling blocks in dealing with patent tangles. A sound knowledge of existing patents on various products would be a prerequisite for the companies. The major companies have their own arrangements to deal with the IPR issues while SMEs have no such recourse. The formidable challenges created for the SME sector by the liberalization of the Indian economy, as well as its closer integration within the global economy, have generated a great deal of interest within India on novel approaches to SME development. If all the benefits provided by the government and the benefits that may accrue from correct tax planning are taken into account, no industry will ever rule out creating an IP portfolio for itself.

One way would be to study the existing products carefully and list those parts, components, and sub-systems, which are covered by patents in the country and identify niche areas of improvements. This is not going to be an easy task because it would call for change in the management culture, presence of
technically skilled people and a system for information collection. As these firms deal in cutting edge area, they face very high risks and they should therefore bring more scientists within their network who could help them generating and pursuing new ideas and concepts. The recent interest started with curiosity and an element of apprehension in 1995, but has now graduated to a need-based compulsion and a desire to understand the nuances of IPR so that, as a nation, India can position itself in the competitive world that has emerged after the formation of the WTO and the introduction of TRIPS Agreement.

References
6 A Biotechnology cell has been opened by the Ministry to support the SSIs on 16 August 2002.
8 Notification No: 17/2004, dated 10 September 2004: The Central Government vide the above notification notifies the exemption of taxable service provided by the holder of intellectual property right to any person in relation to intellectual property service from service tax leviable equivalent to the amount of cess paid towards the import of technology under the provisions of Section 3 of the Research and Development Cess Act, 1986, in relation to such intellectual property service under Section 66 of the Finance Act, 1994.