

THE NEED FOR CONSENSUS ON PATENT REFORM

Executive Summary

For Congress to act, a broad consensus must be forged on the content of comprehensive patent bill.

The core of the needed reforms must reflect the historic U.S. role as the leading advocate for strong and effective patent laws—and the world’s leader in the creation of new technology. These reforms should have as their primary objective producing a patent system that is more open and transparent, bases patent validity on publicly accessible information, and affords the public greater opportunities for participation in the decisions of the United States Patent and Trademark Office to issue patents.

Over the past three years, enactment of a patent reform bill been stymied by controversial proposals that are at odds with maintaining a strong and effective patent system. Among the problematic issues are proposals to create a new concept to limit the compensatory damages that owners of valid patents can recover from infringers, to permit multiple appeals in each patent lawsuit, to force patent owners into judicial venues distant from their witnesses and evidence in order to enforce their patents, and to subject valid patents to serial challenges. The reform bills passed in the House and awaiting action in the Senate include such unwise provisions, and lack the needed reforms noted above.

The content of needed reforms was fully laid out by the National Academies of Science in 2004. The National Academies’ recommendations would require promptly publishing all applications for patents once they are filed, affording the public an opportunity to submit relevant information to the USPTO to assist it in deciding whether a patent should be issued, implementing the so-called “first-inventor-to-file” principle to objectively determine which of rival inventors is entitled to a patent, creating a new “post-grant review” mechanism in which members of the public can force the USPTO to reconsider a mistakenly issued patent, and limiting or removing the subjective elements from patent litigation that drive the cost, complexity and uncertainty of these lawsuits. The NAS did not recommend changes regarding damages or venue.

These bills need fixing before Congress finishes its work on a comprehensive patent bill. The time for fair compromises that provide these fixes is now. Too much is at stake to delay.

THE NEED FOR CONSENSUS ON PATENT REFORM

by

Gerald J. Mossinghoff & Stephen G. Kunin¹

INTRODUCTION

In our global knowledge-based economy, technological innovation is key to the United States' economic growth and development. Across all fields of technology, the United States is currently without peer. That results, not accidentally, from the fact that the United States has the most effective patent system in the world, measured in terms of the breadth of both its geographic and economic scope and the variety of the technologies protected.² The attention that the United States patent system currently enjoys — in industry and academia and politically within the Executive Branch and in Congress — is a direct result of the importance of the United States patent system to this country's technological, economic and political leadership.

Given the diversity of those intensely interested in the patent system these days, one would expect a diversity of opinions on what needs to be improved or what needs to be preserved in its current form. Despite this diversity of opinions, there is virtually universal agreement that two underlying fundamental goals should be achieved by any patent reform:

¹ A former Assistant Secretary of Commerce and Commissioner of Patents and Trademarks, the Honorable Gerald J. Mossinghoff, is Senior Counsel to Oblon, Spivak, McClelland, Maier and Neustadt, P.C. in Alexandria, Virginia. He currently teaches Intellectual Property Law at the George Washington University Law School. A former Deputy Commissioner for Patent Examination Policy of the USPTO, Mr. Stephen G. Kunin is a Partner at the Oblon Spivak law firm. He is the Director of the LL.M. and J.D. Intellectual Property Law Programs and Adjunct Professor of Law at the George Mason School of Law. The authors give special thanks to Kenneth D. Wilcox and Richard T. Matthews, Associates at the Oblon Spivak firm, for their assistance and contributions to this paper. The expense of preparing this white paper was underwritten by the Coalition for 21st Century Patent Reform. The opinions expressed in this paper reflect the personal views of the authors and not necessarily the views of the Coalition for 21st Century Patent Reform, the Oblon Spivak law firm or its clients, the George Washington University Law School or the George Mason University School of Law.

² Intellectual Property Owners Association, White Paper: Respecting Patent Rights: Model Behavior for Patent Owners, © 2007, p. 1, at <http://www.ipo.org>; see also Joff Wild, *Europe, the US and patent reform*, IAM Magazine, June 25, 2007, at <http://www.iam-magazine.com/blog>.

quality and timeliness. Once the United States Patent and Trademark Office (“USPTO”) grants a U.S. patent, its statutory presumption of validity should be well founded. At the same time, the USPTO’s decisions to grant or refuse a U.S. patent should be made expeditiously, without inordinate delays, so that both the patent owners and third parties are promptly informed of the scope and contents of the patent rights conferred.

As the patent law reform journey continues into 2008, we should not lose focus on what needs to be accomplished to preserve the best aspects of a patent system that has served our country well for more than 200 years, while ever striving to make it better. Radical reforms are not needed and would be counterproductive to maintaining the strength of the patent system in the United States and our world leadership in intellectual property rights protection. Our patent system based on judicial interpretation of the patent statutes is working. The “sky is not falling.” The “poster child” cases and concerns raised by the “proponents of drastic reform” are being addressed judicially when any real problems are presented in appropriate cases.

The recent genesis for patent law reform in the U.S. can be traced back to February 2003, when the USPTO issued its 21st Century Strategic Plan, which emphasized the need to improve patent quality and harmonize U.S. patent law with the laws of the U.S.’s major trading partners. Closely following the Strategic Plan was a report issued by the Federal Trade Commission in October 2003, entitled “To Promote Innovation: The Proper Balance of Competition and Patent Law and Policy.” This was followed by the far more comprehensive and thoughtful study on patent law reform in April 2004 by the Committee on Intellectual Property Rights in the Knowledge-Based Economy Board on Science, Technology and Economic Policy (“STEP”) of the Policy and Global Affairs Division of the National Research Council of the National

Academies of Science in its 2004 Report entitled “A Patent System for the 21st Century” (the “NAS Report”).³

Subsequently, Congress became active in patent law reform. The impetus for the patent law reform movement focused on improving the quality of patents, litigation reform and patent law harmonization identified in the NAS Report.

Although the momentum for reform in the 108th Congress derived from the recommendations in the NAS Report regarding patent quality enhancements and sensible litigation reforms, concerns were raised by a few companies about “patent trolls” alleged “automatic injunctions” and “runaway damages awards.” The Federal Circuit was particularly singled out for criticism for affirming the grant of permanent injunctions when the patents-in-suit were determined to be infringed and not invalid. However, the basis for any such concern was soon to be vitiated in 2006 by the Supreme Court in *eBay Inc. v. MercExchange, LLC*.⁴ Instead, the Court reaffirmed the traditional four-factor equity test following a finding that a valid patent had been infringed.

Congressional activity continued into 2006. H.R. 5096, the “Patents Depend on Quality (‘PDQ’) Act,” was introduced in April by Congressmen Howard Berman (D-CA) and Rick Boucher (D-VA). Late in the 2nd Session of the 109th Congress, S. 3818, the “Patent Reform Act of 2006,” was introduced by Senators Orrin Hatch (R-UT)⁵ and Patrick Leahy (D-VT)⁶ on August 3, 2006. None of these bills were enacted.

Early in the 110th Congress, identical bills, H.R. 1908 and S. 1145, the “Patent Reform Act of 2007,” were simultaneously introduced on April 18, 2007, by Congressmen Berman and

³ The NAS Report was authored by Stephen A. Merrill, Richard C. Levin and Mark B. Myers.

⁴ 547 U.S. 388, 126 S. Ct. 1837 (2006).

⁵ Senator Hatch represents the State of Utah.

⁶ Senator Leahy represents the State of Vermont and is Chairman of the Senate Judiciary Committee.

Lamar Smith (R-TX) in the House of Representatives and Senators Leahy and Hatch in the Senate with numerous original co-sponsors. However, each bill was introduced by their sponsors with the caveat that the bills were not perfect. They were characterized as a good first start, but not the final word, with the expectation that refinements would take place during the legislative process. H.R. 1908, with amendments, was reported by the House Judiciary Committee on July 18, 2007 and was passed by the House of Representatives on September 7, 2007. In a similar manner, S. 1145 was reported out of the Senate Judiciary Committee on July 19, 2007, with additional amendments anticipated when it goes to the Senate floor. Hereafter, in this paper, when the authors refer to H.R. 1908, they are referring to the version of that bill that passed the House of Representatives on September 7, 2007; when the authors refer to S. 1145, they are referring to the version of that bill that was reported by the Senate Judiciary Committee on July 19, 2007.

With renewed debates on patent law reform expected in the later part of January or the early part of February 2008, it is the authors' view that the current patent law reform bills in Congress should be driven by the recommendations of the 2004 NAS Report. In light of recent decisions of the Supreme Court and the U.S. Court of Appeals for the Federal Circuit, it is becoming increasingly clear that Congress need only implement the reforms outlined by the National Academies of Science to tweak the U.S. patent system, rather than perform radical surgery that could have serious unintended domestic and international consequences.

The NAS Report identified seven evaluation criteria for an ideal patent system for the 21st Century. These criteria included accommodating new technologies, ensuring high-quality patents, disseminating technical information, ensuring timeliness and containing the costs of decisions, accessing technology for research and development, reducing redundancies and

inconsistencies among national patent systems and maintaining a level playing field among rights holders.

Congress, in fashioning patent reform in the United States, would be well advised to not lose sight of the NAS Report as a template to apply these criteria when judging whether various suggested changes to U.S. patent law make for sound public policy.⁷ The NAS Report concluded with seven recommendations: (1) preserve a flexible, unitary, open-ended patent system; (2) reinvigorate the non-obviousness standard with particular attention paid to business method and gene sequence related inventions; (3) institute a post-grant open review procedure; (4) strengthen USPTO capabilities in personnel, electronic processing, analytic capability and financial resources; (5) shield some research uses of patented inventions from infringement liability; (6) limit the subjective elements of patent litigation such as willful infringement and enhanced damages, best mode and the inequitable conduct defense; and (7) harmonize the U.S., European and Japanese patent examination systems, including moving the U.S. to a first inventor to file system, preserving a one year personal grace period, eliminating the best mode requirement, redefining the definition of prior art, publishing at 18 months from their earliest claimed priority date all pending patent applications not subject to secrecy orders and exploring common approaches to search and examination among major patent granting authorities in the world.

While all of the NAS Report recommendations cannot be implemented without legislation, it is evident that not all patent reform needs to be done legislatively. This paper will review the current status of patent reform and those efforts which have stimulated specific

⁷ *AIPLA Response to the National Academies Report entitled "A Patent System for the 21st Century,"* AIPLA, 2007, at <http://www.aipla.org>.

proposals. Specifically, this paper will discuss separately the following major patent reform proposals:

- First-Inventor-to-File Priority
- Post-Grant Review of Issued Patents
- Inequitable Conduct in Acquiring a U.S. Patent
- Enforcement Provisions including Damages, Venue, Interlocutory Appeals and Willful Infringement
- Specific Quality Enhancements including Publication of all Applications after 18 Months and USPTO Funding with No Fee Diversion

FIRST-INVENTOR-TO-FILE PRIORITY

As between two true inventors — as contrasted with copiers — *every* nation in the world, except the United States, provides a patent to the inventor who first undertakes to use the patent system to disclose his/her invention to the public and gain protection.⁸ This is called a first-inventor-to-file system of priority. For reasons that perhaps made sense historically, the United States has a so-called first-to-invent system of priority that is intended to provide the patent to the first “inventor,” i.e., the first person to conceive and/or reduce the invention to practice under an arcane and burdensome complex of substantive and procedural rules and regulations.

As early as 1965, a major Presidential Commission studying the United States patent system strongly recommended that the United States adopt the otherwise universal first-to-file system.⁹ Given the increasing use of low-cost and easily filed provisional applications, which

⁸ At the end of 1997, there were two nations that used the so-called first-to-invent system: the United States and the Philippines. Effective January 1, 1998, under its Republic Act No. 8293, the Philippines adopted a first-to-file system, leaving the United States alone in the world in adhering to a first-to-invent system.

⁹ “*To Promote the Progress of ... Useful Arts*” in *an Age of Exploding Technology*, Report of the President’s Commission on the Patent System, Washington, D.C. (1966). This is not a partisan matter. The 1966 Commission Report was to President Johnson. In August 1992, the Advisory Commission on Patent Law Reform reached virtually identical conclusions in its report to the Secretary of Commerce in the Bush Administration. The Advisory Commission on Patent Law Reform, Report to the Secretary of Commerce (Aug. 1992).

became available in 1995, such a system would be of significant benefit to independent inventors and small businesses.

In 2005, the USPTO did a study of whether the first-to-invent rule advantaged or disadvantaged small entities. Using data from 1983 — when the small-entity status was first defined — through 2004, the USPTO found that the number of small entities disadvantaged by the first-to-invent rule was slightly higher (289) than those advantaged (286).¹⁰

A key recommendation of the NAS in its Report is:

The United States should conform its law to that of every other country and accept the first-inventor-to-file system.

In Fiscal Year 2007, the USPTO received more than 467,000 utility, reissue, plant and design patent applications. More than one-third of all applications filed in Europe and Japan are of U.S. origin; approximately that same percentage of applications in the U.S. originated in Europe and Japan. The USPTO cannot practically hope to handle its workload without effective work-sharing with other patent offices, particularly the European Patent Office and the Japan Patent Office. And such work sharing will not be possible if the U.S. continues to be isolated with an outdated first-to-invent system of priority.

Establishing a first-inventor-to-file priority will, of course, require Congressional approval. The authors are pleased that such a measure is included in H.R. 1908¹¹ and in S. 1145.

¹⁰ See Mossinghoff, *The First-To-Invent Rule in the U.S. Patent System Has Provided No Advantage to Small Entities*, 87 JPTOS 514 (2005). Those advantaged or disadvantaged are comparatively small numbers; from 1983 through 2004, the USPTO granted 2,456,479 utility, patent and reissue patents.

¹¹ Unfortunately, H.R. 1908 would condition the establishment of the first-inventor-to-file priority upon the President issuing an Executive Order . . .

. . . containing the President's finding that major patenting authorities have adopted a grace period having substantially the same effect as that contained under the amendments made by this section

The authors strongly support a one-year grace period in the U.S. and abroad, but question this approach adopted by the House of Representatives. Rather, we believe that the first-inventor-to-file priority should be adopted as a best practice for the United States, and then the Executive Branch should intensify its diplomatic efforts to “sell” the

Of all of the key recommendations of the NAS that requires legislation, it is our firm opinion that establishing a first-inventor-to-file priority in the U.S. should be at the top of the list.

POST-GRANT REVIEW OF ISSUED PATENTS

Section 6 of H.R. 1908 would establish Post-Grant Procedures under which any person not a patent owner may seek the cancellation of any claims of a granted or reissued patent. The grounds of cancellation would be any defense that one could raise in litigation.¹² Under H.R. 1908, a petition for a Post-Grant Review must be filed no later than 12 months after issuance or reissuance of a patent unless the patent owner consents in writing to the procedure. This is often referred to as a “First Window.”

S. 1145 would establish a “Two Window” Post-Grant Review system under which a petition could be filed:

- (1) Not later than 12 months after the grant of the patent or issuance of a reissued patent; or
- (2)(A) Where the petitioner establishes in the petition a substantial reason to believe that the continued existence of the challenged claim in the petition causes or is likely to cause the petitioner significant economic harm; and
- (B) The petitioner files a petition not later than 12 months after receiving notice, explicitly or implicitly, that the patent holder alleges infringement.

The NAS Report reflected a split with respect to a “One-Window” or a “Two-Window” system. It stated:

The committee is not of one view on the important issue of whether patents should be subject to challenge and review for only

grace period to our Trilateral Partners and beyond. There are also some minor technical deficiencies in the first-inventor-to-file provisions, including its effective date provisions, that are beyond the scope of this paper.

¹² Under 35 U.S.C. § 282(b)(2) or (3). Best mode is not included as a basis for instituting a proceeding in post-grant review.

a limited time after they are issued, as is the practice in Europe, or for as long as they remain in force. A majority of members recommends that the window for a challenge should be limited to one year from the date of grant so that uncertainty is reduced later in the patent's life.

Testimony was split at a hearing before the Senate Judiciary Committee in 2006.¹³ Those favoring a “single window” based post-grant review procedure argue that such procedure “should provide the public with an effective mechanism to promptly correct mistakes made by the USPTO in issuing patents.” These procedures should encourage the public to act promptly to correct patents with claims that are too broad or patents that should have never been granted. If no opposition is filed within the “single window” patentees should enjoy a “quiet title” without fear of later administrative challenge, except for inter partes reexamination.¹⁴ Others favoring creation of post-grant review testified that post-grant review was needed because the “patent litigation system was broken” and “the patent litigation rules themselves are now a means of enhancing patent value instead of a neutral system for resolving disputes.”¹⁵ They also advocated for the Second Window because companies do not have mechanisms in place to review and challenge patents during the initial twelve months, leaving such companies unable to administratively challenge the validity of patents later asserted against them.¹⁶ They argue that the Second Window is needed, especially if a patent owner files suit against them, in order to give time to identify which patents may affect their business operations and time to find a resolution to the effects.¹⁷ Those who testified in opposition stated that post-grant review was

¹³ *Perspectives On Patents: Post-Grant Review Procedures And Other Litigation Reforms*, Hearing, Committee on the Judiciary, U.S. Senate, May 23, 2006. (hereinafter “May 23 Hearing”).

¹⁴ Testimony of Gary Griswold, on behalf on the American Intellectual Property Law Association, June 9, 2007 Hearing at p. 11.

¹⁵ Testimony of Mark Chandler, Cisco Systems Inc., May 23 Hearing at p. 4.

¹⁶ Testimony of Andrew Cadell, J.P. Morgan Chase, on behalf of the Financial Services Roundtable and BITS, May 23 hearing at 13.

¹⁷ *Id.* at p. 16.

not needed because patent litigation was decreasing and the present reexamination procedures were gaining popularity.¹⁸ One person testified that if a post-grant review is needed, it should be limited to only a First Window that should be “designed as an immediate quality control check on newly issued patents.”¹⁹ He stated that post-grant opposition procedure will “nonetheless, come at a very substantial cost, especially to patentees who may have trouble affording the extended uncertainty of the proceedings that such an opposition approach might engender.” However “these costs are a tradeoff worth making in favor of improved patent quality and reliable enforceability to improve the overall quality of issued patents.”²⁰

Given the Second Window that would be established, S. 1145 would repeal as somewhat redundant the Optional Inter Partes Reexamination procedures that were enacted in 1999. H.R. 1908 would retain Inter Partes Reexamination.²¹

Although the authors recognize that meritorious arguments can be made on both sides of the issue, we would favor the House-passed Single Window and urge the retention of Inter Partes Reexaminations. The one-year time limit creates a fixed period in which to challenge granted patents on all conditions of patentability and provides incentives for competitors to do so. Conditions of patentability depending upon a search of published patents or publications could then be handled through Inter Partes Reexaminations at any time during a patent’s life.²²

Moreover, until there are iron-clad assurances that diversions of USPTO fee income to unrelated

¹⁸ Testimony of Nathan Myhrvold, Intellectual Ventures, May 23 Hearing at pp. 9-10.

¹⁹ Testimony of Philip Johnson, Johnson & Johnson, May 23 Hearing at p. 6.

²⁰ *Id.*

²¹ In 2005, the USPTO implemented new processes for handling reexamination proceedings to improve timeliness and quality. Since 2005, more than 250 Inter Partes Reexaminations have been filed. The retention of the Inter Partes Reexaminations would allow third parties to test patents after an initial twelve-month period on the basis of patents and printed publications in a procedure the Office has experience in handling.

²² A Single Window prevents patent owner harassment while serving the public’s interest in obtaining an early clarification of the scope of patent rights in newly issued patents. It, together with Inter Partes Reexamination, effectively answers those critics of the U.S. patent system who contend that in new areas of technology existing patent examiners are not equipped to fully appreciate what is in the prior art.

Federal programs will not occur, there is a realistic fear that subjecting the 1.7 million U.S. patents now in force to a “Second Window” Post-Grant Review could result in disastrous resource and administrative problems for the USPTO and the U.S. patent system.²³ The “Single Window” approach of H.R. 1908 would effectively limit the number of U.S. patents subject to Post-Grant Review to those patents granted during the previous 12 months.

INEQUITABLE CONDUCT IN ACQUIRING A U.S. PATENT

The inequitable conduct defense is a judge-made doctrine used to render a patent unenforceable if it was procured during prosecution through a material misrepresentation or a material omission, with intent to deceive the USPTO.²⁴ Inequitable conduct is decided by a judge, sometimes with guidance from an advisory jury verdict, and must be proved through clear and convincing evidence.²⁵ Proof of both materiality of the information and intent to deceive is required.²⁶ Once a threshold level of materiality and intent has been proven, the judge will balance the level of materiality and intent to determine whether inequitable conduct occurred.²⁷ Courts have applied a multitude of different materiality standards ranging from an objective “but for” test to the subjective determination of whether there is a substantial likelihood that a “reasonable examiner” would have considered the information important in deciding whether to issue the patent.²⁸ Courts have indicated that, the higher the materiality, the lesser the showing of intent is required and vice versa to prove inequitable conduct.²⁹ Despite an effort in 1992 by the USPTO to make the materiality test more objective, the Federal Circuit continues to apply

²³ See Testimony of USPTO Director John Dudas, “Patent Reform: the Future of American Innovation,” Hearing, Committee on the Judiciary, U.S. Senate, June 6, 2007, p. 7.

²⁴ *Frazier v. Roessel Cine Photo Tech, Inc.*, 417 F.3d 1230 (Fed. Cir. 2005).

²⁵ *Dayco Products, Inc. v. Total Containment, Inc.*, 329 F.3d 1358 (Fed. Cir. 2003).

²⁶ *Id.*

²⁷ *Id.*

²⁸ *Digital Control, Inc. v. Charles Machine Works*, 437 F.3d 1309 (Fed. Cir. 2006).

²⁹ *Id.*

the “reasonable examiner” standard of the earlier 1977 USPTO duty of disclosure rule in addition to that defined in 1992 by the USPTO.³⁰

The consequences of a finding of inequitable conduct are severe. A court may hold the entire patent unenforceable,³¹ other patent family members may be held unenforceable under the doctrine of infectious unenforceability,³² attorneys’ fees may be awarded in an exceptional case³³ and the patentee may be exposed to an antitrust claim.³⁴

The House bill codifies the inequitable conduct doctrine. It would require the patent challenger to prove inequitable conduct by “clear and convincing evidence” that material information was misrepresented or omitted with the intent to mislead or deceive the patent examiner.³⁵ The standard for materiality largely tracks the USPTO’s definition of materiality under 37 C.F.R. § 1.56 (1992): information is material if it is not cumulative and (1) a reasonable examiner would have made a *prima facie* finding of unpatentability of at least one patent claim based on the information, or (2) it refutes or is inconsistent with a position taken by the applicant in “opposing a rejection of the claim or in asserting an argument of patentability.”

In addition to materiality, H.R. 1908 requires separate proof of intent. The party alleging inequitable conduct must prove “specific facts beyond” the materiality of the information misrepresented or omitted. The facts need to show “circumstances” indicating “conscious or deliberate behavior” to omit or misrepresent the information at issue. H.R. 1908 also expands the remedies a court may impose if inequitable conduct is found. Like current law, the House bill expressly permits the court to find a patent unenforceable or hold “claims of a related patent

³⁰ *Id.*

³¹ *Kingsdown Medical Consultants, Ltd. V. Hollister Inc.*, 863 F.2d 867 (Fed. Cir. 1988).

³² *Consolidated Aluminum Corp. v. Foseco International Ltd.*, 910 F.2d 804 (Fed. Cir. 1987).

³³ *Molins PLC v. Textron, Inc.* 48 F.3d 1172 (Fed. Cir 1995).

³⁴ *Nobelpharma Ab v. Implant Innovations, Inc.*, 141 F.3d 1059 (Fed. Cir. 1998).

³⁵ H.R. 1908, Sec. 12, 110th Cong. (2007).

unenforceable.” Under H.R. 1908, a court may deny equitable relief and limit the remedy for infringement to reasonable royalties. Alternatively, the court may hold unenforceable only the claims-in-suit or the claims directly related to the inequitable conduct.

On the other hand, S. 1145 embodies the Federal Circuit’s subjective standard of materiality that requires judges to determine whether a reasonable examiner would consider information not disclosed or misrepresented important in deciding whether to allow the patent application. It does, however, provide a range of inequitable conduct sanctions that include holding fewer than all patent claims unenforceable or denying equitable relief to the patent owner while limiting damages to a reasonable royalty.³⁶

A patent by its very nature is affected with a public interest that is best served when, at the time an application is examined, the USPTO is aware of and evaluates the teachings of all information material to patentability prior to the grant of a patent.³⁷ Therefore, maintaining a duty to disclose information material to patentability on each individual associated with the preparation and prosecution of a patent application is clearly in the public interest in seeing that patent applications are fully examined and the USPTO has available to it all the information needed to make a complete, efficient and accurate assessment on all patentability issues.

However, permitting accused patent infringers to raise the issue of “inequitable conduct”—a defense that is pled in almost every important patent lawsuit—today works at cross-purposes to the patent quality objectives that underlie the patent applicant’s duty to disclose. For this reason, the 2004 NAS Report recommended keeping the USPTO’s duty to disclose information material to patent examination, but eliminating the ability to raise an unenforceability defense in patent lawsuits based upon allegations of inequitable conduct.

³⁶ S. 1145, Sec. 16, 110th Cong. (2007).

³⁷ 37 CFR 1.56(a) (1992).

If full elimination of this defense is not undertaken, Congress should consider at least a “safe harbor” that would apply to valid patents. Under such a “safe harbor,” unless at least one claim of a patent is invalidated by the court, the patent should be immune from any allegations in patent infringement lawsuits that the valid patent was wrongfully obtained through “inequitable conduct.”

Such a “safe harbor” for valid patents would obviously work as a strong *incentive* for inventors to obtain valid patents. This incentive to obtain a valid patent should assure greater cooperation between patent applicants and patent examiners to issue patents with only valid claims. Fostering such cooperation is, after all, what the “duty of disclose” was supposed to do in the first place—make patent applicants work as partners with the USPTO as it carries out its work to see that only fully valid patents are issued after a complete examination.

Other reforms should accompany the “valid patent safe harbor.” For example, Congress should require that inequitable conduct could only be found upon proof, by clear and convincing evidence, that an applicant knowingly and willfully deceived the Office by concealing material information, or by submitting false material information, and that, in the absence of such deception, the Office, acting reasonably, would not have allowed 1 or more of the asserted claims of the patent to issue. In addition, such knowing and willful deception should not be inferred solely from the concealment or falsification of material information. Moreover, the judge should be given the express discretion to fashion a sanction appropriate to address the public interest, a sanction which might or might not result in the patent being held unenforceable in whole or in part.

Thus, the integrity of the patent system could best be preserved by removing the specter of often meritless, lawsuit-driven “inequitable allegations,” especially in situations where the

patent in suit is indeed fully valid. The “inequitable conduct” defense as it works today forces patent applicants, in anticipation that every communication with the USPTO will go under a microscope in a patent lawsuit, to “over disclose” information to avoid later allegations of concealment and to “under explain” the significance or relevance of the information submitted to avoid allegations of possible misrepresentation. These perverse incentives, the unintended byproduct of the unenforceability defense, should be removed through implementation of the NAS recommendation. Such reforms to the unenforceability defense are especially warranted given the other patent quality measures that will accompany them: the availability to the public of Reexamination, Post-Grant Review, and 18-month publication coupled with the opportunity for third parties to cite pertinent information to the USPTO following such publication.

ENFORCEMENT PROVISIONS

Damages

Section 284 of Title 35 of the United States Code provides patent owners the right to obtain damages in an amount no less than a reasonable royalty for the economic losses suffered as a consequence of infringement of their patents. A reasonable royalty is the most common amount of damages awarded in patent litigation when the patent owner is unable to prove lost profits. Reasonable royalties are calculated on a hypothetical negotiation between a willing patentee and the infringer at the time the infringement began.³⁸ One factor used to prove such damages is based on licenses granted to similarly situated licensees of the patent owner. If the patentee has not licensed the patent, then royalty rates on comparable patents can be used in the calculation.³⁹ A hypothetical royalty may exceed an established royalty in many cases where

³⁸ *Minco, Inc. v. Combustion Engineering, Inc.*, 95 F.3d 1109, 1119 (Fed. Cir. 1996).

³⁹ *Mahurkar v. C.R. Bard, Inc.*, 79 F.3d 1572 (Fed. Cir. 1996).

widespread infringement has depressed the value of the license in the market place.⁴⁰ Courts use a multi-factored approach to guide the hypothetical negotiation.⁴¹ These factors include the actual royalties received by the patentee in licensing others; the convoyed sales effect; commercial success of the product covered by the patent; the advantages of the patented product over the prior art; the portion of the profit or sales that are customary in the business; the portion of the realizable profit attributable the value of the invention that are distinguishable from non-patent elements; the manufacturing process, business risks or significant features or improvements added by the infringer; and the amount that the licensor and licensee would have agreed upon at the time the infringement began if both parties had been reasonably and voluntarily trying to reach agreement to enable the licensee to make a reasonable profit while being acceptable to a prudent patentee.⁴²

In the business marketplace, and under existing law, the framework to be applied in calculating reasonable royalties is determined by looking to the time of license negotiation. In the case of an infringement, this is assumed to be just prior to the time the infringement began. The methodology used normally determines the reasonable royalty by identifying an appropriate royalty base that will be multiplied by an appropriate royalty rate. The royalty base is typically selected to be an easily ascertainable metric that corresponds to the magnitude of the infringement. In the case of a novel, rain-sensing windshield wiping system for use in an automobile, for example, the royalty base might be the number of cars sold including such systems, the number of systems sold, or the incremental price paid by buyers for cars with the system, just to name a few. In addition, the royalty base may be expanded to include sales of other, ancillary (unpatented) products, but only when the basis for the demand for those ancillary

⁴⁰ *Nickson Indus., Inc. v. Rol. Mfg. Co.*, 847 F.2d 795 (Fed. Cir. 1988).

⁴¹ *Georgia-Pacific Corp. v. United States Plywood Corp.*, 318 F. Supp. 1116, 1120 (S.D.N.Y. 1970).

⁴² *Id.*

products was created by patented invention. In addition, for this “entire market value” approach to apply, the unpatented component must be functionally related to, and be used with, the patented product.⁴³

Once the royalty base to be used has been determined, a fair royalty rate is then ascertained. The rate should be selected so that its multiplication with the royalty base will produce a result that represents a fair value for the use to be made of the invention by the licensee or infringer. One fair approach for determining that value is to ascertain the incremental value the licensee/infringer expects to gain from using the invention as opposed to other, then-available (non-infringing) alternatives (including the alternative of simply not using the invention). A rate is then selected that will appropriately split that incremental value between the licensee/infringer and the patent owner. While it is sometimes suggested as a “rule of thumb” that this split should result in the patent owner receiving roughly one-fourth to one-third of the infringer’s incremental profits, the actual amounts that licensees agree to pay for the use of patented technologies varies widely from this “rule of thumb” figure, depending upon business circumstances.

Except when the selection of the royalty base allows for a more accurate measurement of the magnitude of an invention’s use, the amount of reasonable royalties to be paid should essentially be independent of the royalty base selected for its calculation. In the rain-sensing wiper example mentioned above, if the expected incremental profit from using that invention is \$10 per system, and a fair sharing would result in the payment of \$2.50 to the patentee, it is irrelevant whether the royalty is paid at the rate of \$2.50 per car, or \$2.50 per wiper system. That rate might fairly differ, however, if the value of the use of the system could be more

⁴³ *Rite-Hite Corp. v. Kelley Co., Inc.*, 56 F.3d 1538 (Fed. Cir. 1995).

accurately determined, as for example if it could be easily adjusted to reflect the amount of rainfall in the place of sale.

Both H.R. 1908 and S. 1145 would change existing law by allowing a patent owner to recover reasonable royalties damages based on the entire market value of the product in which the patent is used only when the “predominant basis” for consumer demand is based upon the patent’s “specific contribution over prior art,” a phrase that is not defined in the bills. “Prior art” is a term otherwise used in patent law to refer to certain information that was known prior to the time of invention. Thus, rather than looking to what an infringer’s alternatives were just prior to the start of the infringing activity, this provision requires the valuation to be based upon the invention’s advance over a years-earlier state of the art. The result is that the royalty base will be determined using a “prior art subtraction test” that will value the invention based upon its merit as a technical advancement (years before), rather than by comparison to the commercial alternatives that have become available to the infringer by the time of the infringement. In those instances where the value of the invention resides in the unique combination of prior art elements, this approach would seem to grossly undervalue the invention. In those where subsequent competitive solutions have been developed, the opposite will most likely be the result.

The overall royalty calculation is a task assigned to the court by both the House and Senate bills; it does not require the plaintiff to prove any apportionment of damages. S. 1145⁴⁴ allows the courts the discretion to value reasonable royalties with the entire market value rule or with a market benchmark based on other comparable transactions. Prior art subtraction occurs only when neither of these categories is present. To qualify for a market determined rate, the patent owner must provide proof of a non-exclusive license for use of the patented invention or a similar product for a number of licensees sufficient to indicate a general-market-place

⁴⁴ Section 4(c)(1)(A) of S. 1145.

recognition of the reasonableness of the licensing terms. The infringer's use of the patented product must be of substantially the same scope, volume and benefit as any market benchmark.

Proponents⁴⁵ of this apportionment of damages scheme assert that the present system for judges and juries to award damages for patent infringement creates uncertainty, high transaction costs and excessive damage awards. Proponents say this measure is necessary to limit excessive royalty awards and bring them back in line with historical patent law and economic reality. By requiring the court to determine as a preliminary matter the "economic value properly attributable to the patent's specific contribution over the prior art," the bill would ensure, they assert, that only the infringer's gain attributable to the claimed invention's contribution over the prior art will be subject to a reasonable royalty. The portion of that gain owed the patent owner in the form of a reasonable royalty can then be determined by reference to other relevant factors. Complex products, the proponents contend, often rely on a number of features or processes, many of which may be unpatented. They also contend that even where the patented component is insignificant as compared to unpatented features, patentees base their damage calculations on the value of an entire end product.

These advocates seek a mandatory apportionment of damages⁴⁶ provision that the Federal Circuit's Chief Judge Paul Michel has criticized as creating insurmountable transaction inefficiencies. As pointed out by Judge Michel, he has concerns about patent reform bill provisions that do not define vague terms such as "other features and attributes" or the nature of any "specific contribution." Considerable economic judgment is left to the courts. He questions whether patent owners could meet the evidentiary standards required for access to a market

⁴⁵ Proponents include: the Coalition for Patent Fairness, Securities Industry and Financial Markets Association, the American Bankers Association, and the Financial Services Roundtable.

⁴⁶ See <http://www.patentfairness.org/> and the testimony of Mary E. Doyle, Senior Vice President and General Counsel of Palm, Inc. before the Senate Committee on the Judiciary on June 6, 2007.

analysis based damages calculation that would avoid mandatory apportionment of damages.

Judge Michel expressed his fear that “generalist judges lack experience and expertise in making such extensive, complex economic valuations, as do lay jurors,” and that the courts would face the increased danger of overcrowded dockets and the consequent delay in the administration of justice.⁴⁷

Those opposing mandatory apportionment of damages⁴⁸ raise the concern that the manner in which mandatory apportionment is defined in the patent reform bills may result in a double deduction in the value of the prior art and give infringers windfalls that work against the willing licensees who have negotiated for a license at market rates. Opponents⁴⁹ argue that Congress should not attempt to codify or prioritize the factors that a court may apply when determining reasonable royalty rates. The *Georgia-Pacific* factors provide courts with adequate guidance to determine reasonable royalty rates. The amount of a reasonable royalty should turn on the facts of each particular case.

Although intended to guard against allegedly inflated damage awards, this mandatory apportionment test would represent a dramatic departure from the market-based principles that currently govern damages calculations, opponents say. Even worse, it would result in unpredictable and artificially low damages awards for the majority of patents, no matter how inherently valuable they might be. Opponents further argue that this change would undermine existing licenses and encourage an increase in litigation. Existing and potential licensees would

⁴⁷ Letter from Chief Judge Paul R. Michel to Senators Leahy and Hatch (May 3, 2007) at <http://www.patentbaristas.com>.

⁴⁸ See for example <http://www.patentmatter.com>, and the April 26, 2007 testimony of Gary Griswold, President and Chief IP Counsel of 3M Innovative Properties Company on Behalf of the Coalition for 21st Century Patent Reform before the House Subcommittee on Intellectual Property and the Courts available at <http://judiciary.house.gov/media/pdfs/Griswold070426.pdf>.

⁴⁹ Opponents include: The Department of Commerce, Federal Circuit Court of Appeals Chief Judge Paul Michel, the Coalition for 21st Century Patent Reform, Biotechnology Industry Organization, the Medical Device Manufacturers Association, American Bar Association Section of Intellectual Property Law, the Association of University Technology Managers, the NanoBusiness Alliance and the Professional Inventors Alliance.

see little downside to “rolling the dice” in court before taking a license. This willingness to gamble was already heightened by the Supreme Court’s decision in *eBay Inc. v. MercExchange, LLC*, reaffirming the traditional four-factor equity test for determining when to grant an injunction when a court finds a patent not invalid and infringed. Once in court, this measure would lengthen the damages phase of trials, further adding to the staggering cost of patent litigation and delays in the judicial system.

The apportionment of reasonable royalties should not be confused with the apportionment of the infringer’s profits, which had been a possible award in American patent law prior to 1946, but which in practice became too difficult to apply. Congress in 1946 came to allow only reasonable royalties or actual damages, including a patent owner’s lost profits, as compensation for patent infringement. The Supreme Court ruled in 1964 that actual damages should reflect amounts that the plaintiff could have earned but for the infringement, which is entirely consistent with economic reasoning and efficient deterrence in tort cases.⁵⁰ According to those who oppose mandatory apportionment of damages, the consequence of mandating apportionment of damages in calculating a reasonable royalty would be to discourage voluntary licensing in favor of infringement, especially in light of recent Federal Circuit case law making willful infringement more difficult to prove.⁵¹ The potential presence of a court-imposed license would affect a patent owner’s willingness to negotiate a particular licensing deal which could be of particular concern for research laboratories, universities and others who must monetize their innovation.

A recent example of a major damages award case involved litigation between Alcatel-Lucent and Microsoft in which, on February 22, 2007, a San Diego jury awarded a record-

⁵⁰ *Aro Manufacturing Co. v. Convertible Top Replacement Co.*, 377 U.S. 476, 507 (1964).

⁵¹ *In re Seagate Technology, LLC*, Misc. Doc. No. 830, slip op. (Fed. Cir. Aug. 20, 2007).

breaking \$1.52 billion in damages to Alcatel-Lucent. Microsoft disputed the jury verdict as being “unsupported by the law or facts.” This highly publicized case served as a poster child for those groups advocating the need for Congress to restrict reasonable royalty awards because of the excessive damages awarded by the jury. However, on August 6, 2007 Judge Rudi Brewster granted Microsoft’s post-trial motions, saying that the jury’s decision was not supported by the evidence. The Judge’s Order found that there was insufficient evidence of Microsoft’s liability and for the damages model used by Alcatel-Lucent. Alcatel-Lucent has said that it would appeal the judge’s order.⁵² The consequence of Judge Brewster’s decision serves to demonstrate that the courts can apply an appropriate measure of damages under existing legal principles to adequately compensate patent owners for injury caused by patent infringement without the need for Congress to intervene and there is no need for a new drastic, untested process for determining changes.

Venue

The issue of the appropriate venue for patent litigation has generated controversy. There are concerns that in view of liberal venue requirements for patent infringement lawsuits, cases are being brought in judicial districts perceived to be pro-plaintiff, but which lack any connection to any party.

With venue typically appropriate in many of the 94 judicial districts, patent litigators and their consultants analyze many factors prior to deciding where to file their next lawsuit. For many corporate plaintiffs, geographic convenience is the primary concern. They prefer to bring suit in their home districts, where their witnesses, documents and other information typically are located, and where they often have invested in research, development and commercialization of

⁵² See http://en.wikipedia.org/wiki/Alcatel-Lucent_v._Microsoft, and <http://www.pcworld.com/printable/article/id,135598/printable.html>.

the patented technology. Other factors that patent infringement plaintiffs may consider in deciding where to bring suit include: the reputation of the district's judges and their experience in patent matters, the swiftness of adjudication in that district, the local patent rules, the likelihood of getting to jury trial, the likelihood of winning the case, the leanings of the local jury pool and the relative reputations of the parties in the district. For example, in addition to geographic convenience, a patent owner planning to sue an infringer would likely seek a venue with speedy adjudication, plaintiff-friendly juries, and judges reluctant to grant venue transfers and summary judgments. An alleged infringer, on the other hand, might prefer a venue with urban, tech-savvy juries, slower adjudication and judges more disposed to grant summary judgments.

Professor Kimberly Moore (now a judge on the Federal Circuit) conducted the first extensive study of forum shopping, which was published in 2001.⁵³ Her study examined whether the creation of the Federal Circuit, which eliminated the possibility of patent forum shopping at the appellate level, affected patent forum shopping at the trial court level. Her study showed that almost half of all patent litigation cases filed between 1995 – 1999 were concentrated in ten districts and 29 percent were concentrated in the top five districts.⁵⁴

A more recent study, published in 2006, found that patent litigation is more concentrated than before. The top ten districts now account for half of all patent cases, with the top five districts carrying 36% of the caseload.⁵⁵ Many of the same leading districts have not changed: eight out of the ten leading districts in Judge Moore's study were still in the top ten, but Eastern

⁵³ Kimberly A. Moore, *Forum Shopping in Patent Cases: Does Geographic Choice Affect Innovation?*, 79 N.C. L. REV. 889, 904 (2001).

⁵⁴ *Id.* at 892. The ten district courts were (highest to lowest): C.D. Cal., N.D. Cal., N.D. Ill., S.D.N.Y., D. Mass., D. Del., S.D. Fla., E.D. Va., D.N.J., and D. Minn.

⁵⁵ Yan Leychkis, *Of Fire Ants and Claim Construction: An Empirical Study of the Meteoric Rise of the Eastern District of Texas as a Preeminent Forum for Patent Litigation*, 9 YALE J. L. & TECH. 193 (Spring 2006-07).

District of Virginia and Southern District of Florida have been replaced with Eastern District of Texas and Eastern District of Michigan.

Of note is the rise of a new “superstar” of patent litigation districts – the Eastern District of Texas, which had risen from almost complete obscurity only five years ago to second place in 2006, ahead of all the perennial favorites except the Central District of California.⁵⁶ Despite recent reports of lower win rates for patent holders in the Eastern District of Texas,⁵⁷ there is no indication that the popularity of the district is on the wane. Statistics for 2007 show that the Eastern District of Texas is now the most popular judicial district in the country for patent infringement suits, both in terms of number of suits and number of defendants.⁵⁸

The patent reform legislation proposes to change the venue rules for patent litigation. H.R. 1908 would limit the places where patent infringement cases and declaratory judgment actions concerning patent infringement can be filed. Patent infringement cases could be brought where: the defendant has a principal place of business; where the defendant corporation is incorporated; where “the defendant has committed a substantial portion of the acts of infringement and has a regular and established physical facility that the defendant controls and that constitutes a substantial portion of the defendant’s operations;” where the foreign defendant corporation’s U.S. subsidiary is located or any federal district if the foreign defendant corporation has no subsidiary; where plaintiff resides if the plaintiff is an inventor or a college, university or non-profit; where the plaintiff corporation or its subsidiary has a place of business that is engaged in substantial research and development, manufacturing or management of activities related to the patent(s) in dispute; or where “any of the defendants has substantial

⁵⁶ *Id.* at 204.

⁵⁷ See Peter Zura's 271 blog: <http://271patent.blogspot.com>.

⁵⁸ *Id.*

evidence and witnesses.”⁵⁹ S. 1145 is similar except it omits the provision that allows filing “where the plaintiff corporation or its subsidiary has a place of business that is engaged in substantial research and development, manufacturing or management of activities related to the patent(s) in dispute” and requires the defendant to file a motion to transfer venue where there is “substantial evidence and witnesses” and would be proper under the general venue states, 28 U.S.C. § 1391.⁶⁰

Proponents⁶¹ argue that this change would discourage forum shopping. They assert that certain jurisdictions have become magnets for patent cases because of the disproportionately high number of cases they decide in favor of patentees. This forum shopping imposes a costly burden on businesses which must collect evidence and witnesses and travel to remote jurisdictions to try complex patent cases over a period of weeks or months.

Opponents⁶² argue that this change would be a substantial departure from established practice and may not result in the most appropriate and convenient venue for litigation. Certain district courts attract patent cases not because of favoritism, they say, but because of their expertise and timeliness. They also argue that the impact of forum shopping is minimized by the existence of a single appellate court for patent cases, the Federal Circuit. The amendments to 28 U.S.C. §1400(b) “would entirely exempt declaratory judgment actions that an alleged infringer would bring against a patent owner” in the plaintiff’s “home jurisdiction.”⁶³ These opponents assert that while forum shopping by patent owners is a problem, forum shopping by alleged

⁵⁹ H.R. 1908, Sec. 11(c).

⁶⁰ S. 1145, Sec. 8(a).

⁶¹ Proponents who agree in principle to changes to the venue provisions include: the Coalition for Patent Fairness, Securities Industry and Financial Markets Association, the American Bankers Association, the Financial Services Roundtable, IPO and BIO.

⁶² Opponents include: American Bar Association Section of Intellectual Property Law and the Innovation Alliance.

⁶³ Testimony by Gary Griswold of 3M Innovative Properties Company on behalf of The Coalition for 21st Century patent Reform, before the House Subcommittee on the Judiciary, the Internet and Intellectual Property on April 26, 2007, p. 12.

infringers for the best venue to avoid the consequences of their infringing activity could be as well.⁶⁴

The NAS report did not identify the patent venue provisions as an issue for reform. It is the authors' view that changes to the venue provisions are not needed at this time. The popularity or consternation about filing patent cases in certain judicial districts waxes and wanes over time. The popularity of the Eastern District of Virginia's "rocket docket" has faded in the past several years, while the popularity of the Eastern District of Texas grew. Also, certain jurisdictions will always have a disproportional number of patent cases due to the predominance of intellectual property-based industries in that judicial district, which no reasonable modifications to the patent venue provisions would alter.⁶⁵ If the Congress determines that changes to the patent venue provisions are warranted, then the authors suggest that there be parity between the venues available to patentees and to alleged infringers.

Interlocutory Appeals

Section 8(b) of S.1145 and Section 11(b) of H.R. 1908 would permit an immediate interlocutory appeal to the U.S. Court of Appeals for the Federal Circuit of the district court judge's *Markman* order on claim construction.

Proponents⁶⁶ say these appeals would reduce the length and cost of litigation. They argue that claim construction goes to the heart of any patent infringement case. Until a claim is construed, it is impossible to establish whether infringement occurred and whether the patent is invalid. This process would narrow discovery and motion practice and thus would reduce costs. Proponents assert that an interlocutory appeal would help to mitigate the judicial inefficiency

⁶⁴ *Id.*

⁶⁵ See note 53, *supra*.

⁶⁶ Proponents of interlocutory appeals of *Markman* orders include: the Coalition for Patent Fairness, Securities Industry, Financial Markets Association, the American Bankers Association, and the Financial Services Roundtable.

that occurs when a full trial is conducted based on an incorrect interpretation of the patent, only to be reversed on appeal and sent back for a second trial. More than a third of all *Markman* orders are overturned on appeal.⁶⁷

Opponents⁶⁸ argue that interlocutory appeals from *Markman* orders would increase litigation and court congestion and offer “another bite at the apple” because the reversal rate for claim construction is fairly high. The net result, they say, will be significantly to delay final judgments from the lower court, delay potential settlements and increase litigation costs. They argue that the Federal Circuit would not be able to handle expeditiously the large number of *Markman* appeals, meaning that resolution of the underlying district court cases could be delayed for years. Opponents argue that, if this provision were to be enacted, it would result in an interlocutory appeal in virtually every patent infringement case as soon as a *Markman* order is issued. It has been estimated that this would double the number of appeals each year.⁶⁹ They also argue the change is not needed because appeals of *Markman* orders are often tied to an unfavorable summary judgment order rather than after a full trial and final judgment.

It is the authors’ view that the opponents of interlocutory appeals, especially Chief Judge Michel, have the better argument. It is unproven that the benefits of interlocutory appeals of *Markman* orders, as the proponents argue, would actually be realized. Perhaps, the better approach to addressing the perceived problem of larger numbers of *Markman* reversals would be to give district court judges’ claim construction determinations greater deference at the Federal

⁶⁷ See Kimberly A. Moore, *Are District Court Judges Equipped to Resolve Patent Cases?*, 15 HARV. J.L. & TECH. 1, 9, 11 (2001) (finding that the claim construction error rate during the period between April 23, 1996, and December 31, 2000, was 33 percent).

⁶⁸ Opponents of interlocutory appeals for *Markman* orders include: Chief Judge Michel of the U.S. Court of Appeals for the Federal Circuit, District Court Judge T.S. Ellis, BIO, the American Intellectual Property Law Association, the Coalition for 21st Century Patent Reform and Intellectual Property Owners Association.

⁶⁹ Letter from Hon. Paul R. Michel, Chief Judge of U.S. Court of Appeals for the Federal Circuit, to Hon. Patrick Leahy and Hon. Arlen Specter, United States Senate, at 2 (June 13, 2007), at <http://pub.bna.com/ptcj/MichelJuly13.pdf>, (hereafter “June 13 Michel Letter”); Letter from C.J. Michel, to Sens. Leahy and Specter, at 1 (May 3, 2007), at http://www.patentmatter.com/media/issue/legislation/20070503_Michel.pdf (hereafter “May 3 Michel Letter”).

Circuit. This may be accomplished in one of two ways: either the Federal Circuit could reverse its holding in *Cybor v. FAS*⁷⁰ to thereby remove the *de novo* review requirement or, alternatively, Congress could legislatively overrule that decision.

WILLFUL INFRINGEMENT

In its report, the NAS stated:

Section 284 of the Patent Act governs damages for patent infringement and provides that in addition to an award ‘adequate to compensate for the infringement,’ the court ‘may increase the damages up to three times.’ The statute provides no standard for the court to apply in making this determination. In practice the threshold question, usually submitted to a jury, is whether the defendant has been ‘willful’ in the infringement.

* * *

The most common defense to a claim of willful infringement is good-faith reliance on advice of counsel that the defendant’s product or method did not infringe any valid claim. . . . The net result has been a cottage industry of lawyers providing such opinions at a cost ranging from \$10,000 to \$100,000 per opinion.

Worse, in some business sectors, exposure to claims of willful infringement has led to a practice of deliberately avoiding learning about issued patents, a development sharply at odds with the disclosure function of patent law.

* * *

Lacking evidence of its beneficial deterrent effect but with evidence of its perverse antidisclosure consequences, the committee recommends elimination of the provision for enhanced damages based on a subjective finding of willful infringement; but we recognize that this is a matter of judgment and that there are a number of alternatives short of elimination that merit consideration.

In H.R. 1908, specific provisions are included to address the problems outlined by the NAS. But the NAS recommendations were made in the context of the leading 1983 Federal

⁷⁰ *Cybor Corp. v. FAS Techs., Inc.* 138 F.3d 1448 (Fed. Cir. 1998).

Circuit *Underwater Devices*,⁷¹ which was specifically overruled in *In re Seagate Technology, LLC*.⁷² In *Seagate*, the Federal Circuit, sitting *en banc*, stated:

Since *Underwater Devices*, we have recognized the practical concerns stemming from our willfulness doctrine, particularly as related to the attorney-client privilege and work product doctrine.

* * *

Recently, in *Knorr-Bremse*, we addressed another outgrowth of our willfulness doctrine. Over the years, we had held that an accused infringer's failure to produce advice from counsel 'would warrant the conclusion that it either obtained no advice of counsel or did so and was advised that its [activities] would be an infringement of valid U.S. Patents.' *Knorr-Bremse*, 383 F.3d at 1343 Recognizing that this inference imposed 'inappropriate burdens on the attorney-client relationship,' *id.*, we held that invoking the attorney-client privilege or work product protection does not give rise to an adverse inference, *id.* at 1344-45. We further held that an accused infringer's failure to obtain legal advice does not give rise to an adverse inference with respect to willfulness. *Id.* at 1345-46.

* * *

Accordingly, we overrule the standard set out in *Underwater Devices* and hold that proof of willful infringement permitting enhanced damages requires at least a showing of **objective recklessness**. Because we abandon **the affirmative duty of due care**, we also reemphasize that there is no affirmative obligation to obtain opinion of counsel.⁷³

Given the Federal Circuit's *en banc* holding in *Seagate*, it is the authors' view that the problems articulated by the NAS have been effectively addressed by the judiciary, and that there is no need for legislation, which at this point would only interrupt and confuse an orderly development of common law based upon *Seagate*. In particular, with the abandonment of the affirmative duty of due care and its replacement by a required showing of objective recklessness to prove willful

⁷¹ *Underwater Devices Inc. v. Morrison-Knudson Co.*, 717 F.2d 1380 (Fed. Cir. 1983).

⁷² 497 F.3d 1360, 1371 (Fed. Cir. 2007).

⁷³ *Id.* at 1370-71.

infringement, the bar has been raised by the Federal Circuit. At this point, in preference to new legislation, the courts should be permitted to apply the *Seagate* principles to actual fact situations, thereby alleviating the concerns expressed by the NAS and proponents of change.

SPECIFIC QUALITY ENHANCEMENTS

Publication of All Patent Applications After 18 Months

President Johnson's 1966 Commission on the Patent System⁷⁴ recommended:

Publication of a pending application shall occur eighteen to twenty-four months after its earliest effective filing date, or promptly after allowance or appeal, whichever comes first.

The rationale was that:

Early publication could prevent needless duplication of the disclosed work, promote additional technological advances based on the information disclosed, and apprise entrepreneurs of their potential liability.

That recommendation was enacted in part in the American Inventors Protection Act in 1999 in 35 U.S.C. § 122, but with a key exception: 35 U.S.C. § 122(b)(2)(B)(i) states:

If an applicant makes a request upon filing, certifying that the invention disclosed in the application has not and will not be the subject of an application filed in another country, or under a multilateral international agreement, that requires publication of applications 18 months after filing, the application shall not be published [at the 18-month deadline].

H.R. 1908 would add a second alternative to publication at 18 months namely, that an application could not be published until "three months after a second action is taken" by a patent examiner in the application. Given the enormous backlogs now being experienced by the USPTO, in practice this would mean that such applications could routinely not be published until

⁷⁴ "To Promote the Progress of... Useful Arts" in an Age of Exploding Technology, Report of the President's Commission on the Patent System, Washington, D.C. (1966).

several years after their effective filing date.⁷⁵ While this second alternative is marginally better than publication only upon grant of the patent, there is an unintended consequence. This delay of publication of U.S. - origin patent applications will adversely impact examination quality.

Examiners would not have the ability to cite earlier-filed U.S. applications as prior art against a patent applicant if at the time of examination of a later-filed application an earlier application was not published and thus not available as prior art due to this new requirement. Quite understandably, no other patent system in the world follows such a unique regime of publication.

Adequate Funding With No Fee Diversion

Concern in the early 1980s that tax-based revenues would not be sufficient to handle the increasing workload of the USPTO prompted the Administration to recommend and Congress to enact P.L. 97-247 in 1982. That Act made two major changes in the way the USPTO was funded: (1) user fees for patents and trademarks would be substantially increased and (2) the USPTO would be able to use the increased fees to fund its operations instead of those fees being deposited in the miscellaneous receipts of the U.S. Treasury. This “fail-safe” result would guarantee, at least in theory, that an increased workload would generate increase fee income to handle it.

From the beginning, funds collected as the result of patent and trademark fees could not be used by the USPTO unless they were first appropriated by the Congress. And beginning in the 1990s, Congress began to appropriate less than the estimated fee income, diverting the “excess” to other government programs totally unrelated to patents and trademarks. From 1992 to 2004, Congress diverted almost \$600 million in patent fees alone. The direct result of that fee diversion is that the USPTO backlog has skyrocketed to more than 760,000 unexamined

⁷⁵Eric Yeager, *Patent Expert Says Reform May Make Patents Harder to Obtain and More Suspect*, PATENT, TRADEMARK & COPYRIGHT JOURNAL, BNA, Vol. 75, No. 1847, (Dec. 14, 2007), pp. 158-160.

applications.⁷⁶ On average, it now takes 32 months for the USPTO to decide whether to grant a patent, and in the most active areas of technology, that number is increased by another year.⁷⁷

The delays and uncertainties created by the backlog act as a brake on innovation and investment decisions in high-technology industries. The absolute need for adequate resources for the USPTO was recognized in every recent study on the patent system. We have identified those who have taken different positions on individual issues; no one questions this need for adequate resources for the USPTO.

The real answer to this National crisis is for Congress to outlaw fee diversions permanently and provide the USPTO with full access to patent fees that will permit it to realistically deal with the enormous workload. Until the Congress does so, the USPTO cannot realistically be expected to reduce the unacceptable backlog and deal with incoming work without seriously compromising the rights of the innovation community. Stop-gap measures not based upon adequate resources could “do more harm than good,” resulting in any number of unintended and unidentified results. Consequently, we favor providing permanent funding of the USPTO through establishing a revolving fund for the deposit of patent and trademark user fees that would allow the USPTO access to all the revenues it collects⁷⁸.

THE OBVIOUSNESS TEST IN PATENT LAW: THE SUPREME COURT’S KSR DECISION

In a section entitled “Reinvigorate the Non-Obviousness Standard,” the NAS states:

The non-obviousness determination is necessarily a judgment not something that can be resolved through a bright line test. Fundamentally, it assumes that an invention is novel and the decision maker must determine whether the hypothetically skilled

⁷⁶ Performance and Accountability Report for Fiscal Year 2007, USPTO, Table 5, p. 112; *see also*, *U.S. Patent & Trademark Office: Transforming to Meet the Challenges of the 21st Century*, National Academy of Public Administration, August 2005 at pp. 41-48 (analyzing impact of fee diversion on unexamined applications backlog).

⁷⁷ Performance and Accountability Report for Fiscal Year 2007, USPTO, Table 4, p. 112.

⁷⁸ *See* Senator Coburn’s amendment on fee diversion proffered on July 18, 2007, S. Amend. ___, 110th Cong., 1st Sess. (2007) p. 3, l. 22 - p. 4, l. 3.

person in the art would nonetheless have considered the novel invention something within the routine skill of the field. The USPTO and the reviewing courts are concerned that an invention that was genuinely non-obvious before it was made may often look obvious in retrospect.

Reversing a once obscure “non-precedential” opinion of the U.S. Court of Appeals for the Federal Circuit, Justice Anthony M. Kennedy, writing for a unanimous U.S. Supreme Court in *KSR International Co. v. Teleflex Inc.*⁷⁹ once again sought to define the elusive test of whether an invention is “obvious” — and thus not patentable — or “nonobvious” — and thus worthy of a U.S. patent. The Supreme Court reaffirmed the basic principles of the law of non-obviousness and urged an “expansive and flexible approach.” The Supreme Court advised that “common sense” would broaden the use of customary knowledge in the obviousness equation by stating that the person of ordinary skill in the art has “ordinary creativity and is not an automaton.” At one point in the analysis, the Court rejected any “rigid rule” and observed, without expressly endorsing this formulation, that the Federal Circuit had also “elaborated a broader conception of the TSM [teaching, suggestion or motivation] test than was applied” in the *KSR* case. Specifically, the Court referred to *Dystar Textilfarben GmbH & Co. v. C.H. Patrick Co.*, wherein the Federal Circuit had opined: “Our suggestion test is in actuality quite flexible and not only permits, but *requires*, consideration of common knowledge and common sense.”⁸⁰

The unanimous *KSR* opinion gives patent examiners more flexibility when analyzing the fundamental issue of nonobviousness, ensuring that allowed applications must meet the statutory standard. The USPTO has issued very detailed examination guidelines based upon the *KSR*

⁷⁹ *KSR Int'l v. Teleflex, Inc.*, 550 U.S. ___, 127 S. Ct. 1727 (2007), *see also* Hon. Gerald J. Mossinghoff, *KSR v. Teleflex: High Court's "Obviousness" Ruling No Sea Change in Patent Law*, Washington Legal Foundation, Legal Backgrounder, June 8, 2007, available at <http://www.wlf.org/upload/06-08-07mossing.pdf>, and Stephen G. Kunin & Andrew K. Beverina, Commentary, *KSR's Effect on Patent Law*, 106 Mich. L. Rev. First Impressions 50 (2007), <http://www.michiganlawreview.org/firstimpressions/vol106/kuninbeverina.pdf>.

⁸⁰ 464 F.3d 1356, 1367 (Fed. Cir. 2006) (emphasis original).

decision. Moreover, Board of Patent Appeals and Interferences of the USPTO has issued several precedential opinions, outlining best practices for examining patent applications in light *KSR*. The *KSR* opinion and its implementation by the USPTO, in the authors' view, will positively affect the USPTO's role in maintaining a strong system of only granting quality patents for nonobvious inventions.

CONCLUSION

The authors welcome the intense scrutiny of the U.S. patent system that patent reform efforts have engendered. Those efforts will, if managed properly, result in a stronger and more effective system of incentives to stimulate the creation and the use of new technology, both by innovators and by those who benefit from the innovations of others. In our view, however, care must be taken lest the fixing of "poster child" problems will actually weaken the patent system, rather than making it more effective. Clearly, First-Inventor-to-File, Post-Grant Review of Issued Patents at least initially with a Single Window, USPTO Funding with No Fee Diversion, Eliminating the Unenforceability Defense Based Upon Inequitable Conduct (or, at a minimum, Codifying the Law of Inequitable Conduct by including a "valid patent safe harbor" coupled with an objective standard for materiality with more flexibility in choice of sanctions that must redress the harm to the public interest based upon the nature of the conduct found) and Publication of All Patent Applications at 18 Months should receive legislative attention and approval as soon as possible. In our view, it is unquestioned that these changes will improve the quality and timeliness of the U.S. patent system and improve its effectiveness for all concerned. The other changes being considered in both the House and the Senate bills may be unnecessary and indeed may have been overtaken by events. A classic example would be reform of the law regarding willful infringement. Where there are major differences between important stakeholders, those

differences could very well signal that additional work may be necessary before legislation is enacted. It is the authors' view that, for the most part, those differences that do exist are based upon good-faith real-world concerns on which consensus has not been reached. However, the time for reaching consensus is now, so that legislation can be enacted in 2008. The authors would urge renewed consideration of the National Academies of Science report in looking to find consensus on the issues still in dispute.