



COMMENTARY

Center for Strategic and International Studies ■ Washington D.C.

The Patent Reform Act

John Hillery and Joshua Krieger

June 14, 2007

Patent reform, which languished in the House subcommittee on IP in the last Congress, is now moving forward in both chambers. The two versions of the Patent Reform Act of 2007 reflect a repackaging of the House draft from the 109th Congress. Largely due to political power shifts, Congress now expresses greater optimism that patent reform will occur. Such reform would be significant because Congress has not substantially amended patent law since 1952, and technology firms have argued that it is out of step with the kinds of innovation produced in an information economy. However, manufacturing and pharmaceutical industries oppose many of the bill's wide-ranging changes to patent law, arguing that the current system has underpinned the successful commercialization of innovative products.

Many U.S. firms have identified a myriad of problems with the current patent system. The backlog of applications has expanded monstrously, and questionable patents have emerged from the Patent Office. Patent examination has suffered from high examiner turnover, the diversion of USPTO fees, and a workload that provides too little time for a quality assessment of applications. Examiners have an average of 20 hours to make a determination on an application.¹ The average wait for a patent application was over 31 months in 2007.² Companies have also voiced complaints about the uncertainty and inequity in the courts. Patent cases are overturned at an exceptionally high rate. Tech firms, in particular, believe that the current practices on injunctions and damages for willful infringement are unfair.

Financial services and IT firms also argue that the emergence of their new business models in the information economy requires the patent system to change in order to facilitate and promote the innovation process. These groups emphasize that new technologies are often composed of thousands of small innovations, but the current patent system suits a marketplace in which products rely chiefly on a single patent.

Nonetheless, a number of other customers of the current patent office, especially in pharmaceuticals and manufacturing, favor only limited reform and fear that a sweeping revision of U.S. patent law in the manner proposed will weaken the right-holder's position, thus reducing the incentive to innovate. These industries rely on fewer patents per product, and their research and development requires enormous capital investment.

Some of the proposed changes in the bill are less contentious than others. For example, Congress and industry have generally endorsed converting the U.S. patent system from a first-to-invent to a first-to-file system. The U.S. system has historically held that a patent should belong to whoever first created the innovation, even if he or she was not the first to file the application. As a result of this principle, scientists and inventors are sometimes entangled in disputes over who was chronologically first to think, discover, or make something truly novel.

In the past, small inventors championed the first-to-invent system, arguing that they would be disadvantaged in a first-to-file system. They believed larger, more nimble firms would beat them to the patent office with an application. Academic studies, however, have recently shown that the harm to the small inventor under a first-to-file system would be minimal, and Congress appears to be persuaded. Universities have requested a provision be added to the first-to-file change in order to protect professors' ability to publish without risking the loss of their rights.³

1 Davidson, Paul. "Patents Out of Control?" USA Today, 13 January 2004. http://www.usatoday.com/tech/news/2004-01-13-patentscover_x.htm

2 Seidenberg, Steve. "PTO proposes a new suite of patent products to streamline applications." Inside Counsel, January 2007. http://www.insidecounsel.com/issues/insidecounsel/15_244/ip/818-1.html

3 The new system would protect the ability to publish through a one year "grace period." During that year, any disclosure by "the inventor or a joint inventor or by others who obtained the subject matter disclosed directly or indirectly from the inventor or a joint inventor" is not treated as prior art to that patent application. H.R. 1908/S. 1145. "Comments on H.R. 1908 and S. 1145, The Patent Reform Act of 2007," http://www.aau.edu/intellect/STMT_ASSN_HR1908_51607.pdf.

The bill also seeks to limit forum shopping and, like the first-to-file issue, this provision faces little opposition from major firms. Current law permits plaintiffs to game the federal district courts by selecting the venue with the most favorable history (the Eastern District of Texas is the current hot venue). The bill would limit venue choice to the districts of the litigants' principal places of business.

U.S. firms would also likely support a provision to address the under-funding of the patent office, but unfortunately, the bill does not address this chronic problem.

Industries are deeply divided over other major provisions of the bill. One would allow third parties to challenge patents shortly after they are granted, creating a post-grant opposition procedure (or "second window"). The goal of these measures is to provide a way to weed out bad patents earlier rather than later by allowing outsiders to put relevant material before the examiners. If third parties can show that the applicant's invention has already been patented or is otherwise unworthy of a patent, rejection of the application may reduce infringement litigation (and countersuits for invalidity) down the road.

Citing an excessive burden from IP lawsuits, large technology firms that produce patent-laden products have endorsed post-grant opposition. On the other side, patent-dependent manufacturers have joined pharmaceutical firms in opposing this change. The opposition coalition argues that a "second-window" will add uncertainty, reduce patent value, and discourage investment.⁴

Infringement penalties, the damages awarded when one party has profited from another's patented ideas without paying a license fee or royalties, are another highly contested area of reform. IT firms are concerned about how damages are assessed in infringement cases. Currently, it is not difficult for plaintiffs to win rulings on "willful" infringement, and such a finding trebles the damages. The bill's provisions would institute a legal presumption that infringement is not willful and require the plaintiff to prove otherwise.

Information technology firms also feel that damage awards are excessive because they are based on revenue streams from the entire product involved. A given IT product, for example, may be covered by scores of patents, but infringement of a patent related to one component can result in damages based on the value of the whole product. The legislation would require courts to apportion damages based on the value of the infringed component, not the entire product. Opponents in other industries suggest that this change could weaken the patent holders' incentive to innovate because they could expect smaller returns from litigation when other firms infringe on their property. It may also present practical difficulties because courts would need to adjudicate the infringed component's economic value, separating it from the value and contribution of other features of the product.

Abroad, U.S. IP policy receives a mixed reaction. On the one hand, foreign governments have lauded and copied the policy that shaped the commercialization of government-sponsored IP, the Bayh-Dole Act. However, foreign observers have also criticized the U.S. for patenting software and business methods, and for having lax standards and excessive litigation. Patent reform in the U.S. is of course highly pertinent abroad; Japanese firms are among the leading recipients of U.S. patents, and Chinese and other foreign owners' share of U.S. patents will likely continue to increase.⁵ Companies like the Canadian firms Nortel and Research in Motion (makers of Blackberry) have become particularly invested in patent reform after experiencing setbacks from litigation.

If the bill passes into law, patents will be more difficult to obtain and easier to challenge, and penalties for infringement would be generally reduced. The Congressional debate on patent reform should focus on whether such changes are in the best interest of the economy as a whole. Patent reform is certainly laden with abstruse legal jargon, but that should not obscure the significant role the patent system plays in U.S. innovation and national competitiveness.

4 "Bio Calls Changes to Patent Reform Bill." Drug Industry Daily 7 June 2007.

5 Japanese inventors received 19 percent of USPTO patents in 2002. Chinese ownership of USPTO patents grew from 47 patents granted in 1991, to 683 patents granted in 2002. Khan, Mosahid and Demis, Helene. "Global Overview Of Innovative Activities From The Patent Indicators Perspective." OECD Directorate for Science, Technology and Industry, 2 May 2006.

Further Readings

The Patent Reform Act of 2007

H.R. 1908, S. 3818 (available on thomas.loc.gov)

Bringardner, John. "Nothing Cash Can't Cure." *IP Law & Business*, May 2007.

<http://www.ipww.com/display.php/file=/texts/0507/micron0507>

Gross, Grant. "Groups Raise Concerns about Patent Reform Bill." *IDG News Service* 26 April 2007.

http://www.infoworld.com/article/07/04/26/HNpatentreformconcerns_1.html

Letter to Congressional Leaders from Pharmaceutical Firms May 15, 2007.

http://www.innovationalliance.net/cross_coalition_letter.pdf

Letter to Congressional Leaders from Business Software Alliance. March 6, 2007

<http://www.bsa.org/usa/policy/2007-cto-letter.pdf>

Letter from University Coalitions on Patent Reform, Association of American Universities.

http://www.aau.edu/intellect/STMT_ASSN_HR1908_51607.pdf

Weeks, Rita and Devinsky, Paul. "Patent Reform Legislation Aims To Harmonize the United States Patent System." *Mondaq*. June 14, 2007.

<http://www.mondaq.com/article.asp?articleid=49284>