GENERAL COUNSEL OF THE
UNITED STATES DEPARTMENT OF COMMERCE
Washington, D.C. 20230

May 16, 2007

The Honorable Howard L. Berman
Chairman, Subcommittee on Courts,
the Internet, and Intellectual Property
Committee on the Judiciary
House of Representatives
Washington, D.C. 20515

Dear Mr. Chairman:

This letter provides the views of the Department of Commerce (DOC) and, in particular, its component the U.S. Patent and Trademark Office (USPTO) on the provisions of H.R. 1908, the "Patent Reform Act of 2007," as introduced.

This new patent bill is a revised version of legislation considered in the last Congress to modernize the U.S. patent system through changes designed to improve patent quality, reduce patent litigation costs and further international harmonization of patent laws. We support these goals and commend you, Mr. Chairman, and your colleagues in the House and Senate for introducing this bicameral and bipartisan legislation.

INTRODUCTION

The bill includes reform proposals that would directly impact the USPTO. These include provisions on first-inventor-to-file, third-party submissions of prior art and post-grant review of patents. There are also litigation-management provisions relating to assessment of damages, willfulness determinations and venue considerations that do not directly impact USPTO operations, but rather patent policy in general.

There are also certain provisions that, while not currently in the bill as introduced, could usefully modernize the U.S. patent system. In the interests of providing as complete a picture as possible, we are including suggestions that are consistent with the goal of modernization.

In analyzing the provisions of H.R. 1908, and in suggesting additional items, we consider what will benefit U.S. inventors and the American public. It is from this perspective – benefit to Americans – that we approach our review and make recommendations.

QUALITY IS A SHARED RESPONSIBILITY

The U.S. patent system is predicated on disclosure. It cannot be emphasized enough that the grant of a patent right presumes an exchange of complete openness by the inventor for various rights of exclusivity. Thus, U.S. patent law requires inventors to disclose the "best mode" for reproducing their invention, and to explain their proposal in a manner clear to one skilled in a

particular art. We believe that emphasis on full disclosure – as is required for fair exchanges in all fields of enterprise – will ensure a vibrant, modern patent system.

A corollary of full disclosure must be intolerance for willful suppression or hiding of information. While, of course, fraud cannot be accepted, we also need a system that permits good-faith efforts to provide high quality and complete applications. The challenge for policymaking is to ensure modernization that both eliminates incentives for fraud and promotes full and complete applications.

1. Applicant Quality Submissions (AQSs)

Perhaps the most important element of ensuring that patent examinations are of the highest quality and processed as efficiently as possible is what the applicant files. The patent applicant has the most knowledge, the most opportunity, and the most to gain by providing the USPTO with the best possible information about his or her invention.

In the USPTO's new Accelerated Examination Program – where the first patent was issued in less than six months – applicants participate in an interview and provide the USPTO with a search and a support document. The USPTO's experience with this initiative is that both applicants and examiners realize that more written and oral information from applicants improves quality and timeliness.

The USPTO looks forward to taking the success of this model – captioned "applicant quality submissions" – to lower pendency, raise productivity and increase quality, and apply it to all patent examinations. To that end, the USPTO believes that applicants should be given every opportunity and the responsibility to provide more and better information to examiners about their inventions. For such a program to be successful, the USPTO will ensure that requirements for more and better information do not become overly burdensome in general and in particular to independent inventors and small entities.

We recognize that, in many cases, applicants have expressed strong concerns about providing the USPTO with complete information about their applications. In some cases, applicants simply do not want to provide important information for fear that it will limit the scope of the patent they may receive (though such a limitation would be proper under the facts and the law). Unfortunately, an additional percentage of applicants do not make the effort to fully define their inventions because there is currently no procedural or other deterrent to submitting an ill-defined application.

In some other cases, applicants or their attorneys fear that the legal doctrines of inequitable conduct and unenforceability may unfairly punish them with Draconian penalties for innocently omitting information. The theory is that if one provides information, he or she must do so perfectly or potentially lose the patent or face disciplinary action; whereas, a failure to share any information carries no consequences.

Under existing case law, a court that finds that an applicant has committed inequitable conduct in prosecuting a patent application must find unenforceable all claims of the patent and related

patents, even if they are otherwise valid. Thus, the only remedy available is a complete loss of the patent. Inequitable conduct can be found if the applicant deliberately withholds or inaccurately represents information material to patent prosecution. Anything the court deems that a reasonable examiner would find important can be material and the evidence necessary to show intent varies according to the nature of the omission. Accordingly, the inequitable conduct standard is uncertain and the potential penalties severe. For example, any misstatement in an affidavit, or even a failure to disclose a possible source of bias, has been held to be capable of rendering all claims of the patent unenforceable.

While the risk of an inequitable conduct finding is low, it is alleged relatively frequently and, when alleged, adds substantially to litigation costs and malpractice claims. The "all or nothing" result of an inequitable conduct finding understandably has a perverse effect on the actions of applicants and their attorneys with respect to "risking" a proper search in the first place. As a result, the doctrine drives counterproductive behavior before the USPTO. It discourages many applicants from conducting a search and leading others to be indiscriminate in the information they submit. In a review two years ago, we found that in over one-half of applications either no information disclosure statement was submitted or submissions included more than 20 references.

As we review and evaluate the elements of a successful and efficient AQSs program, we believe there are two related issues that would require legislative action, namely inequitable conduct and the ability of micro-entities to meet new information requirements.

(a) Inequitable Conduct

Consistent with the discussion above, DOC recommends that the bill be amended to address the doctrine of inequitable conduct and unenforceability to ensure that patent applicants are not discouraged from fully and fairly sharing relevant information with the USPTO.

Current uncertainties associated with the doctrine would be significantly reduced by clarifying the appropriate standards. First, the standard for finding intent could be explicitly separated from the materiality of the withholding, requiring proof that the misrepresentation was knowing, with intent to deceive. Second, the doctrine could be changed to a standard requiring a finding that the information would have been relevant to a reasonable examiner. The "relevance" standard could usefully be framed in terms of whether a reasonable examiner would have allowed the patent, without more, but for the misrepresentation or omission.

With respect to materiality, Congress may wish to consider requiring the USPTO to define the term (as it does now) and limit the courts to finding inequitable conduct only in circumstances in which information that the USPTO has defined as material is misrepresented or withheld.

DOC and the USPTO look forward to working with the Subcommittee and stakeholders to develop provisions that would be more effective than the current doctrine in facilitating the targeting of fraud that actually affects the examination process and in improving the quality of applicant submissions.

(b) Micro-Entity Status

We recognize that any AQSs program with requirements for more and better information must not become overly burdensome in general and in particular to independent inventors and small entities.

Accordingly, with respect to truly independent inventors and truly small entities, DOC recommends that the bill be amended to define a "micro-entity" status. The definition could be based on a number of factors including: income level; number of patent applications filed; lack of representation by a registered practitioner; and lack of assignment activity. The status would exempt an applicant from some or all of the requirements of an AQSs program.

That status also could be used to identify inventors eligible for reduced fees and other preferred treatment and assistance.

2. Prior Art Submissions

Section 9(b) of the bill expands the ability of third parties to submit information they believe is pertinent to a pending application. Specifically, the proposal would permit the submission of patents, published applications or other printed publications before the earlier of: (1) the mailing date of a notice of allowance, or (2) either six months after pre-grant publication, or the date of the first rejection of any claim by the examiner, whichever occurs later.

This proposal is consistent with the discussion above regarding AQSs and overall efforts to encourage a highly participatory examination process with more engagement by applicants as well as by other interested parties with information relevant to that examination.

Current USPTO rules permit submission of patents or printed publications within two months of publication or before the mailing of a notice of allowance, whichever occurs first.

In contrast to current USPTO rules, the bill would require that the submission include a "concise description of the asserted relevance of each submitted document." Current USPTO rules do not permit inclusion of comments or explanations concerning the submitted patents or printed publications.

DOC supports enactment of this section, with minor revisions, and anticipates that the provisions will serve to provide our examiners with information they may not otherwise obtain and should result in a more efficient examination process and a higher quality, more reliable patent. We have identified a few technical revisions that should be made prior to enactment and recommend that the provision be accompanied by regulatory authority for the Director of the USPTO to implement procedural requirements to make the submission process as efficient as possible.

Consistent with the provisions and rationale of this section, the USPTO is cooperating in a pilot program involving peer review of patent applications. Up to 250 applications, assigned to Technology Center 2100, which examines computer-related technologies, will voluntarily be placed, by the applicants, on a non-USPTO web site for an expanded and public review by a peer

group of patent users, attorneys and academics. The pilot group of applications will include applications filed by small entity filers. The public group will determine and submit to the USPTO what they consider the best available and relevant prior art. The pilot program will test whether this peer review can effectively identify prior art that might not otherwise be found by our examiners during the typical examination process. We will also make an evaluation as to whether this process results in measurable examination timesavings and quality improvements.

LITIGATION MANAGEMENT ITEMS

The disclosure philosophy has even more relevance to litigation than to examination, as it exposes the economic repercussions of a failure to fully disclose. One of the purposes of the patent system authorized by the Constitution of the United States is to promote the dissemination of knowledge to the public through disclosure of inventions. Requirements for more and better information to support a patentability determination are comparable to current requirements in virtually every judicial and administrative proceeding for parties to bring the most relevant, reliable and complete information before the decision-making body.

We fully appreciate that not all industries are similarly situated, that market conditions change over time, and that practical matters – such as channels of trade – may be legitimate factors for consideration in a patent-infringement case. Therefore, we believe it is critical that litigation-management modernization efforts preserve discretion for courts that enables them to account for differences across industries, markets, and time.

3. Apportionment of Damages

Section 5(a) of the bill, in part, directs the court to ensure that a reasonable royalty is applied only to the economic value attributed to the patented invention as distinguished from the economic value attributable to other features added by the infringer. More specifically, the bill also provides that in order for the entire market rule to apply, the patentee must establish that the patent's specific improvement is the predominant basis for market demand.

Current patent law provides that a patentee is entitled to damages adequate to compensate for infringement, but in no event less than a reasonable royalty. The question of what is the value of a relatively small piece of patented technology when it is integrated as a component of a larger article has attracted substantial attention by the high-tech industry.

Under the entire market rule, the value of the entire apparatus, which includes both patented and other inventions not covered by the patent at issue, is used as the royalty base for computing reasonable royalty.

Concerns have been expressed that patent awards based on the entire market value are overly generous. Legislative proposals have attempted to solve this problem by directing courts to consider the contribution of other elements of the entire product added by the infringer. This is one of several factors, commonly referred to as the *Georgia-Pacific* factors, typically considered by courts in determining royalty rates.

While the appropriateness of damages awards in a number of patent cases may be subject to debate, DOC does not believe that a sufficient case has been made for a legislative provision to codify or emphasize any one or more factors that a court must apply when determining reasonable royalty rates. Further evaluation or research is necessary to determine whether a statutory "entire market rule" may not be readily or appropriately applicable to technology that involves something other than a physical component of a product.

It appears that the courts have adequate guidance through *Georgia-Pacific* and, as a general matter, do in fact consider numerous factors in determining royalty rates, including: rates paid by other licensees; nature and scope of the license; profitability of the product; commercial relationship between the licensee and licensor; as well as the portion of the realized profit attributable to the invention. The amount of a reasonable royalty should turn on the facts of each particular case, as best as those facts can be determined.

4. Willful Infringement

Section 5(a) of the bill, in part, limits a court's ability to award enhanced damages in the following ways: (1) codifies that increased damages are limited to instances of willful infringement; (2) requires a showing that the infringer intentionally copied the patented invention; (3) requires notice of infringement to be sufficiently specific so as to reduce the use of form letters; (4) establishes a good faith belief defense; (5) requires that determinations of willfulness can only be made after a finding of infringement; and (6) requires that determinations of willfulness be made by the judge, not the jury.

Willful patent infringement can certainly have significant consequences. The court may treble the damages and award attorney fees. With escalating patent litigation costs, the threat of treble damages can be quite substantial. Some have expressed concerns that willfulness is frequently alleged as a matter of course and alleged infringers have to bear the expense of defending such actions.

While there is some evidence to support the claim that willfulness is frequently alleged, the evidence also suggests that willfulness is currently difficult to establish. The additional requirements, limitations, and conditions set forth in the bill may significantly reduce the ability of a patentee to obtain treble damages.

Modernization efforts should avoid perverse incentives that might make infringement simply "a cost of doing business." While not the only deterrent to patent infringement, the possibility of treble damages provides an important and substantial obstacle – more than might be seriously considered in a practical business calculus.

For lack of a clear and substantiated case for major statutory reform in this area, DOC is unable to support all the provisions of section 5(a) of the bill as currently drafted. However, DOC can support a number of the narrowly drawn provisions of the section that we believe are appropriate, reasonable and fair to most interested parties.

Accordingly, the Department supports enactment of the amendments contained in section 5(a) that statutorily limit enhanced damages to determinations of willful infringement; require sufficiently specific notices of infringement; and provide that an inference of willfulness can not be drawn from the decision of an infringer not to present evidence of advice of counsel.

5. Prior User Defense

Section 5(b) of the bill expands the prior use defense, created by the American Inventors Protection Act of 1999, by eliminating the limitation that the subject claim be directed to a "method of doing or conducting business." It also enhances the safe harbor for non-patentees in that they would only have to show commercial use, or substantial preparations for commercial use, at any point before the effective filing date of the patent application (rather than that date plus one year).

The benefit of a prior use defense is clearly directed toward the non-patentee. Proponents argue that this is reasonable in a competitive economy and strikes a balance between trade secret and patent protection.

Critics argue that prior user rights undermine the purpose of a patent system by creating a strong incentive to protect innovations as trade secrets. Under a prior use defense regime, if inventors are able to protect their innovations as trade secrets, they are able to use them indefinitely, even if someone else obtains a patent on the invention.

Absent a change to a first-to-file system, DOC does not support the bill's expansion of the prior user defense at this time. The existing defense has rarely been invoked and there is insufficient information to gauge the potential impact of substantially expanding it.

6. Venue

Section 10(a) of the bill limits the places where corporations may be sued by amending 28 U.S.C. § 1400(b) to provide that a corporation "resides" only where it has its principal place of business or in the State in which the corporation is incorporated.

This provision is clearly more restrictive than the current "personal jurisdiction" standard that requires "minimum contacts" for venue purposes and represents a substantial departure from established practice. While this proposal addresses forum shopping concerns expressed by many patent owners, it may not result in the most appropriate and convenient venue for litigation.

Also, the proposal expands the types of actions subject to 28 U.S.C. § 1400(b) which currently is limited to patent infringement actions. The proposal would cover any civil action arising under any federal law relating to patents, other than declaratory judgment and Patent Board decisions.

DOC has not taken a position on the provisions of this section. We will review and evaluate the proposal, along with possible alternatives, in consultation with the Department of Justice.

APPEALS

7. Interlocutory Appeals

Section 10(b) of the bill provides that parties in a patent infringement suit are permitted to have an interlocutory appeal to the Court of Appeals for the Federal Circuit after a *Markman* hearing on claim construction, rather than waiting for a final judgment to be rendered by a district court.

While proponents of this provision maintain that these appeals would reduce the length and cost of litigation, others believe that the appeals may have the opposite effect and would in fact offer "another bite at the apple" because the reversal rate for claim construction is fairly high.

DOC is unable to support this provision at this time. We will consider the merits in consultation with the Department of Justice.

PROPOSALS DIRECTLY AFFECTING THE USPTO

8. Post-Grant Review

Section 6 of the bill establishes post-grant review procedures under which any person may request the USPTO to cancel as unpatentable any claim of a patent: within 12 months after issue or reissue; when the petitioner establishes a substantial reason to believe that the continued existence of the challenged claim causes or is likely to cause the petitioner significant economic harm; or when the petitioner has received notice from the patent holder alleging infringement by the petitioner.

Post-grant review procedures would be more expansive than existing reexamination procedures and would include consideration of evidence gleaned through depositions and interrogatories as well as patents and other documents. A newly designated Patent Trial and Appeal Board would be responsible for conducting the post-grant reviews.

The USPTO Director would prescribe regulations establishing and governing the proceedings including standards for showings of "substantial reason to believe" and "significant economic harm" and procedures for the submission of supplemental information and discovery of relevant evidence. The Director would also establish by regulation reasonable fees to be paid by the person requesting the proceeding.

Final determinations would be issued within one-year with a six-month extension available for good cause shown. Regulations would address sanctions for abuses of the proceedings.

Many aspects of the post-grant review section are similar to those contained in the draft bill prepared by the USPTO in 2005. A primary difference is the scope of the "second window." While the USPTO's proposal would also provide for a one-year first window, it would limit the second window to a six-month period after receipt of a notice from the patent holder alleging infringement. Additionally, the USPTO proposal would authorize the Director to promulgate

regulations that would also require a petitioner to show substantial economic harm. That authority would enable the USPTO to control or limit an influx of potential cases.

A second significant difference is that the bill's applicability reaches back to patents issued before the effective date of the legislation. The USPTO's procedures would be available only on a prospective basis.

The broad scope of the bill's second window coupled with the substantial number of patents subject to the proposed review procedures create very legitimate concerns about the USPTO's ability to effectively handle the potential workload. Accordingly, while the Department supports the establishment of post-grant review procedures, we suggest revision of the bill's provisions to more closely align with those in the USPTO's draft bill. We would be pleased to work with the Subcommittee in that regard.

9. USPTO Regulatory Authority

Section 11 of the bill would specifically authorize the USPTO to promulgate such rules, regulations and orders that the Director determines appropriate to carry out the provisions of Title 35 or any other applicable law or that the Director determines necessary to govern the operation and organization of the USPTO.

We thank Congress for suggesting appropriate authority for the USPTO. The USPTO has long believed that rulemaking authority is beneficial to the patent system, and welcomes authority that is necessary to promulgate regulations to ensure an efficient and quality-based patent examination process. We have concerns about unbounded discretion, and therefore want to be certain that any grant is not overbroad.

10. First Inventor to File

Section 3 of the bill converts the U.S. patent system from a first-to-invent to a first-inventor-to-file system and makes various conforming amendments. A grace period is provided to promote an inventor's disclosure of the subject matter of the claimed invention without loss of priority. Interference proceedings are replaced with a derivation proceeding to determine whether the applicant with an earlier-filed application is the proper applicant for the claimed invention.

While the rest of the world uses a first-to-file system, the United States continues to award a patent to the first to conceive an invention, provided that all patentability criteria are satisfied. Proponents of first-to-file maintain that it would simplify the patent process, reduce legal costs, improve fairness and enhance the opportunity to make progress toward a more harmonized international patent system.

Opponents of first-to-file are concerned that adoption of first-to-file could promote a rush to the USPTO with hastily prepared disclosure information resulting in a decline in quality. Also, because many independent inventors and small entities lack sufficient resources and expertise, they feel that they would be unlikely to prevail in a "race to the patent office" against large, well-endowed entities.

Conversion to a first-to-file system has been advocated by various interest groups in the United States for decades. It is still the subject of continuing controversy. While DOC recognizes the potential benefits of a first-to-file system, we do not support immediate conversion to first-to-file via this legislation.

It should be noted that U.S. conversion to first-to-file is an overriding consideration in ongoing substantive patent law harmonization discussions with foreign patent offices. We hope those discussions will lead to significant benefits for patent applicants and promote work sharing among worldwide patent offices. In this regard, we believe that any U.S. commitment to convert to first-to-file should be contingent on significant progress and international agreement in those harmonization discussions. In particular, the United States seeks a standardized one-year international grace period to protect American inventors who might disclose their invention prior to filing for a patent.

Additionally, with respect to the specific text of section 3 of the bill, DOC has identified a number of concerns regarding the scope and application of provisions relating to prior art and grace period that may require revision and clarification.

11. Assignee Filing

Section 4 of the bill proposes several changes to current practice regarding who must or may file an oath or declaration in a patent application and the application itself. A person to whom an inventor has assigned or is under an obligation to assign the invention would be able to make an application for a patent. Current practice requires that, as a general matter, applications must be filed by the inventor(s).

DOC and most members of the patent community generally favor simplifying and streamlining patent application procedures and reducing any unnecessary formalities. The proposal is an appropriate step in that direction. While the Department supports adoption of these provisions, we have identified a number of technical issues in the text of section 4 that should be addressed and clarified as the legislative process continues. Those issues relate to specific entitlement to the grace period and national security and transparency considerations.

12. 18-Month Publication

Section 9(a) of the bill eliminates the current opt-out provision for publication of patent applications. Current law permits an applicant to request upon filing that his or her application not be published at 18-months if a certification is made that the invention disclosed in the application has not and will not be the subject of an application filed in another country that requires such publication.

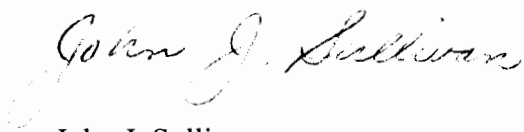
DOC is hesitant to support this provision at this time considering that the current opt-out provision is a result of the careful balancing and sensitive negotiations that took place during the legislative process that led to the enactment of the American Inventors Protection Act of 1999. It addresses the serious concerns expressed then and now by independent inventors and small

entities that large entities and foreign interests may misappropriate their inventions upon disclosure and prior to issuance of a patent.

CONCLUSION

Thank you for this opportunity to share our views on this important piece of legislation. DOC looks forward to working with the Subcommittee and the Congress to develop legislation that improves our patent system, while maintaining the balance among the interests of patent applicants, relevant third parties, the general public, and the information needs of the USPTO to serve all three. The Office of Management and Budget has advised that there is no objection to the transmittal of these views from the standpoint of the Administration's program. If you have any questions, please contact me or Nat Wienecke, Assistant Secretary for Legislative and Intergovernmental Affairs, at 202-482-3663.

Sincerely,



John J. Sullivan

cc: The Honorable John Conyers, Jr.
Chairman, House Judiciary Committee

The Honorable Lamar S. Smith
Ranking Member, House Judiciary Committee

The Honorable Howard Coble
Ranking Member, Subcommittee on Courts,
the Internet, and Intellectual Property