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2004

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Recommended Citation

Daniel F. Attridge & Gregory F. Corbett, Patent and Antitrust, Happy Together?, *Legal Times*, Mar. 15, 2004, at IP16.

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Patent and Antitrust, Happy Together?

An FTC report makes **10 suggestions** on how to reach a better **balance** between laws that promote **competition** and **creativity**.

By Daniel F. Attridge
and Gregory F. Corbett

We learned in Economics 101 that competition is good because it leads to lower prices, higher-quality products, more consumer choice, and greater incentive to innovate. Antitrust law generally seeks to protect competition through free and open markets.

But free markets are not the only way to energize the creative spirit. The Framers of the Constitution realized that the prospect of exclusive rights in intellectual property would also encourage innovation. Therefore the Constitution grants Congress the power to "promote the Progress of Science and useful Arts, by securing for limited Times to Authors and Inventors the exclusive Right to their respective Writings and Discoveries."

The tension between these two opposing yet complementary legal regimes—between patent and antitrust law—has been the subject of much scholarly and legal debate in recent years. On Oct. 28, 2003, the Federal Trade Commission issued a 250-page report entitled "To Promote Innovation: The Proper Balance of Competition and Patent Law and Policy."

The report grew out of extensive public hearings held by the FTC and the Antitrust Division of the Department of Justice between February and November 2002. It relies on the testimony of more than 300 participants from the hearings, as well as 100 separate written submissions from industry experts, attorneys, economists, and academics.

The report starts from the premise that both patent and antitrust law enhance consumer welfare and that generally they work well together. Over the years, however, the relative strengths of the two regimes have fluctuated. In other words, when courts have tended to favor patent rights, they have usually disfavored antitrust concerns, and vice versa.

During the past 20 years, the report suggests, Congress and the courts have built up the patent system to the point of unnecessarily stifling competition. The FTC describes the creation of the U.S. Court of Appeals for the Federal Circuit in 1982 as a "watershed" event that has resulted in a "significant" strengthening of patent rights.

Given this new reality, the FTC expresses great concern about the grant of questionable patents by the Patent and Trademark Office. Such patents can deter competition and prevent innovation in markets that otherwise might flourish. Likewise, the FTC notes that the extremely high cost of patent litigation often forces accused infringers to license patents of debatable validity.

In short, the FTC thinks it is time for the pendulum to swing back. To that end, the report proposes 10 specific recommendations to improve the patent system in the interests of enhancing competition.

1. Create post-grant opposition proceedings in the PTO.

Under the current *ex parte* system of patent examination, PTO examiners rely primarily on prior art submitted by the patent applicant. Access to competitors' potentially valuable knowledge of prior art is limited because they do not participate in the patent-granting process. The consequence has been that even late into infringement litigation, real questions about the validity of a patent can still be raised.

The FTC suggests that allowing competitors to challenge patent validity quickly through a new post-grant opposition process would timely resolve many validity questions. The report lays out a structured procedure, overseen by an administrative law judge, in which challengers could cross-examine witnesses and conduct limited discovery. The FTC envisions that oppositions would be subject to strict time limits to protect patentees from harassment and undue delay.

2. Determine validity challenges based on a "preponderance of the evidence" standard.

The FTC finds that patent examination is tilted in favor of the applicants. In addition to having no access to competitors' knowledge, patent examiners are severely limited in time and other resources. They often spend less than 20 hours looking at an individual application.

Moreover, applicants start out with a great advantage: During examination, the burden does not fall on the applicant to demonstrate that her invention meets the statutory criteria. Instead, the PTO must demonstrate grounds for rejecting a patent. The FTC also notes that examiners receive financial incentives from the PTO to complete processing of applications.

Despite these real-world shortcomings in the review of applications, courts require challengers of issued patents to prove invalidity under a heightened standard of "clear and convincing evidence." The FTC maintains that the realities of patent examination state a compelling case against imposing the heightened standard. Thus, the report recommends lowering the proof of invalidity to a "preponderance of the evidence."

3. Tighten legal standards for obviousness.

Like the first two recommendations, this one is aimed at making it easier to challenge a patent's validity. In theory, an invention that is obvious (to those of ordinary skill in the art) cannot be patented. But under current Federal Circuit precedent, the PTO may not reject an application for an otherwise obvious invention unless the PTO can point to specific and definitive prior art references showing a clear "motivation to combine" known elements to make the claimed invention.

According to critics, this requirement assumes that those of ordinary skill in the art lack the creativity and insight to see the obvious unless it is almost spelled out for them. Thus, the Federal Circuit's standard allows patents to issue even where (to quote the FTC) "only a modicum of additional insight [would be] needed" to render the invention obvious.

The FTC recommends that the PTO tighten up obviousness requirements by giving more weight to suggestions implicit in the prior art, the nature of the problem being solved, and the knowledge of one of ordinary skill in the art.

When the PTO determines that an invention is obvious today, an applicant may rebut with objective evidence of nonobviousness. The applicant may do this by showing that her invention is commercially successful (and therefore presumably new and different). However, the FTC notes that the "commercial success" test has diluted the obviousness inquiry, and recommends that courts evaluate this factor case-by-case.

4. Provide adequate funding for the PTO.

If there is one thing that the patent community agrees on, it is that the PTO does not have enough resources. Many argue that this "crisis" in funding seriously impacts the quality of issued patents. Inadequate funds make it difficult to hire staff and spend sufficient time examining patents.

Meanwhile, applications have doubled over the last 12 years, with the PTO receiving about 1,000 a day. Backlogs are building. The FTC strongly recommends that Congress increase funding to meet these demands.

5. Modify PTO rules on prior art citations and other procedures.

Patent applicants have a duty of candor to the PTO, and they must reveal all material prior art known to them. But the FTC notes that applicants typically "flood" the PTO with more prior art than can be adequately reviewed. Examiners with limited resources cannot afford to waste time wading through a quagmire.

So the FTC recommends that the PTO allow examiners to require applicants to submit "statements of relevance" regarding prior art references. Similarly, the FTC proposes that the PTO make better use of PTO Rule 105 examiner inquiries, whereby an examiner may require other additional information from the applicant.

The FTC also recommends that the PTO expand its

use of "second pair of eyes" review, which allows examiners to flag issues to be further considered by a supervisor. The PTO began this program in 2000 in the emerging (and controversial) area of business methods, where it has successfully decreased the number of questionable patents issued.

Finally, the FTC recommends that the PTO focus on its role as a steward of the public interest, not a servant of patent applicants. In the past, improper emphasis on the latter role has caused examiners to treat applicants as if they were "customers" to be served—by the granting of patents.

6. Consider harm to competition before extending patentable subject matter.

In 1998, the Federal Circuit held in *State Street Bank & Trust v. Signature Financial Group* that business methods can be patented. But many participants in the FTC/DOJ hearings argued that business method patents, including those that do not publish their software source code, are not enabling—that is, they do not teach the public how to make and use the invention. Witnesses also noted that examiners have difficulty in identifying nonpatent prior art in this field.

The FTC stops short of recommending judicial or legislative action to restrict the patentability of business methods. But in light of the criticism, the report says that courts should be wary of extending patent coverage into new fields.

7. Publish all patent applications 18 months after filing.

Before 1999, U.S. patent applications were not published prior to patent issuance. This led to problems caused by "submarine" patents, whereby an applicant allowed its application to languish at the PTO while others made substantial investments in technology that would infringe the yet-to-be-issued patent. Once the submarine patent issued, the applicant could then demand excessive royalties from established markets.

The American Inventors Protection Act of 1999 partially remedied this problem by requiring most patent applications to be published 18 months after filing. However, about 10 percent of applicants "opt out" by certifying that their invention will not be the subject of a foreign patent application. The FTC recommends that this exception to the 18-month rule be eliminated.

8. Create intervening and prior user rights to protect against continuing applications.

Even after a patent application is published, an applicant may continue to amend its claims. Frequently, applicants will broaden and change pending claims to describe competitors' newly introduced products. This manipulation of the continuation process has been highly criticized. Indeed, the FTC states that no hearing testimony justified the use of continuations to cover competitors' existing products.

Therefore, the FTC recommends legislation to prevent

applicants who intentionally broaden their claims post-publication from asserting infringement against third parties with pre-existing or intervening rights.

9. Require actual notice or deliberate copying to establish willful infringement liability.

Currently, a company accused of infringing another's patent may be liable for willful infringement—and face treble damages—if it knew about the patent prior to the infringing activity. Companies are thus discouraged from looking at patents in their industry. This undermines the benefits otherwise gained from full public disclosure of new innovations—a key function of the patent system.

The FTC recommends that willful infringement be found only where actual written notice of infringement was given or deliberate copying occurred. This would allow competitors to review each others' patents without fear of treble damages.

10. Consider economics and competition concerns in patent law decision making.

The FTC's last recommendation aptly summarizes the critical theme of much of its report—that the patent system should encourage innovation above all. The report suggests that the PTO and the Federal Circuit can do a better job of attaining this goal.

For example, a number of hearing witnesses testified that the Federal Circuit has been unreceptive to economic arguments and does not give due credit to competition as a driver of creativity. The FTC notes that the court does not seem to view patent law as part of a "panoply of tools."

But patent law's constitutional mandate is to "promote the Progress of Science and useful Arts." In *Graham v. John Deere Co.* (1966), the Supreme Court warned that the patent monopoly must not be enlarged "without regard to the innovation, advancement or social benefit gained." Accordingly, the FTC recommends that the Federal Circuit and the PTO give much greater consideration to economic insights and the promotion of innovation as part of their decision making.

No doubt there are differences of opinion and ongoing debate in the patent community regarding many of the FTC's proposals. Whether any of these 10 recommendations will ever be implemented is uncertain. But the FTC has made its position clear.

The balance between patent and antitrust law has shifted to the detriment of innovation and competition, says the FTC. Its recommendations call for action from all the major government players—the PTO, the courts, and Congress. And the FTC itself promises to renew its commitment to filing amicus briefs in important patent cases, and to asking the PTO to re-examine questionable patents where they raise competitive issues.

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