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TO LICENSE OR NOT—A PROPOSAL TO IMPROVE PATENT LAW

Howard Anawalt†

The basic theory of the federal intellectual property laws has always been to reward inventive people in order to encourage them to "advance the public welfare."¹ The theory is an "upbeat" aspect of our legal system. The law speaks in terms of reward, not punishment, and the reward is for something new that an individual or group has invented. The service to the public interest often appears in the very concrete form of some excellent new product or process. In this essay, I wish to examine one improvement to the patent law that will benefit both innovators and the public.

THE POWER OF A PATENT HOLDER

Patent is one of the major systems of intellectual property. It is known to the inventor, lawyer, and layperson as the basic legal means for protecting a true "invention." The heart of patent law is its grant to the inventor of "the right to exclude others from making, using or selling the invention."² The invention might be, for example, a new device that controls electron flow in a semiconductor, or a new process for manufacturing an old product, such as a tire. If the invention can be demonstrated to be new and useful and something which would not be "obvious" to other skilled persons working in the field of the invention, the inventor is entitled to a legal monopoly under United States law.

"Monopoly" is no overstatement. The holder of the patent is entitled to practice the invention exclusively, or put the invention on the shelf for the full seventeen year period of the grant. The

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inventor (or, more often, a corporate assignee) is entitled to license the invention to others at more or less any price and to pick and choose to whom a license will be granted. Thus, patent law introduces an element of control of economic and social processes that goes far beyond reward to inventors. Indeed, the control elements introduced run counter to the constitutional goals of service to the public welfare and effective encouragement of inventiveness.

Examination of the patent creation process will illustrate the control phenomenon. Most often, a truly useful new device or process will be initiated by an existing company. An inventive person in the company will be assigned a project, keep a regular journal of his or her progress, and will ultimately execute an assignment of the patent and a power of attorney allowing the company to prosecute the patent application. As a final formality, the inventor will sign the patent application as required by the statute. The "inventor" in such an instance is, for all practical purposes, the employing company.

Because of the assignment, economic rewards for powerful new inventions flow to the employing company. Assuming that the inventor and the contributing employees have been properly compensated, the economic reward to the company is justified by the combination of capital and accumulated expertise the company has contributed. However, the reward which is justified is the economic value of the invention as such, not the leverage or control that possession of patent rights will give the company vis à vis other companies and individuals in the marketplace.

3. There are some exceptions to this plenary control over licensing, but they are so confined that they surely confirm the general rule. See 4 D. CHISUM, PATENTS § 19.04[3], at 19-110 (1978) regarding the limited illegality of a royalty based on total sales. If the total sales basis for the royalty can be regarded as a business shorthand summarizing various factors related to the business value of the privilege granted, the royalty will be sustained. One district court case has flatly rejected the notion that a royalty agreement may be invalid because of magnitude. W.L. Gore and Assoc., Inc. v. Carlisle Corp., 381 F. Supp. 680, 700 (1974). "Generally, the patent owner has discretion whether and to whom he will issue a license." 4 D. CHISUM, PATENTS § 19.04[3], at 19-120 (1978).

4. "Prosecute the patent application" is a term of patent practice meaning to pursue the process of seeking a patent.

5. 35 U.S.C. § 118 (1982) permits the assignee of the invention to execute the application in certain cases, such as when the inventor/assignor refuses to do so.

6. The authority of the patent assignee has recently been strongly reinforced by Diamond Scientific Co. v. Ambico Inc., 848 F.2d 1220 (Fed. Cir. 1988) which held that the company/assignee can preclude the inventor/assignor from attacking the validity of the patent during an infringement litigation; that is, the inventor/assignor may be estopped from claiming invalidity. The availability of "assignor estoppel" depends on an assessment of the "balance of equities between the parties." Id. at 1225.

7. In Brulotte v. Thys Co., 379 U.S. 29 (1964), the Supreme Court denied a patent
The element of control referred to is the use of a patent, or more often, a stable of patents, to prevent competitors from performing as well in a competitive marketplace. For example, assume that the XidaFlex Company holds a group of six important patents related to a product field. The product field might be semiconductor chips, chemical processing, computers, communications facilities, or any other. XidaFlex may use any of the following methods to exercise the power of its patents:

1. **Exclusive use.** XidaFlex can seek to maintain a competitive edge by using the patented process exclusively themselves. The approach results in a classic reward envisioned by the patent system.

2. **Selective licensing.** XidaFlex may decide to license only to certain companies. Such picking and choosing is fully consistent with current provisions of the patent law: “Generally, the patent owner has discretion whether and to whom he will issue a license.” To the extent that the choice is made solely for the purposes of maximizing the rate of return from the patented device, it is a simple economic reward. Other criteria, however, may enter into the decision: Company A should not receive a license, because it is a new competitor and should be kept relatively weak. Company B should not be licensed because it is primarily a producer and not an innovator. Company C should be offered a license in return for a license to their ’512 patent, as this will allow our two companies a competitive dominance over companies D and E during the next critical years. These examples show results of patent ownership which are not direct compensation for the value of the device in and of itself, but which are, nonetheless, powerful economic rewards in the form of influence or control over other aspects of the entire production and marketing mechanism.

3. **Threat of patent enforcement.** Of course, the patentee can seek to enforce its patent. That is the point of the whole patent

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holder's enforcement of royalties for use of a hop-picking machine when the royalties accrued after the last patent on the machines had expired. The Court noted:

A patent empowers the owner to exact royalties as high as he can negotiate with the leverage of that monopoly. But to use that leverage to project those royalty payments beyond the life of the patent is analogous to an effort to enlarge the monopoly of the patent by tying the sale or use of the patented article to the purchase or use of unpatented ones.”

*Id.* at 33. As tie-ins were unlawful based on antitrust, so too, were post-patent royalties. See also *Aronson v. Quickpoint Pencil Co.*, 440 U.S. 257 (1979). The court restated the teaching of the *Brulotte* case in the form of a general principle: “The principal underlying that holding was simply that the monopoly granted under a patent cannot lawfully be used to ‘negotiate with the leverage of that monopoly.’” *Id.* at 265 (emphasis in original).

8. 4 D. CHISUM, PATENTS § 19.04[3], at 19-120 (1978).
system. If a given product is dependent on only one or two very clear and fundamental patents, then the intention of the law is fulfilled: allow exclusive rights for the seventeen year life of the patent. An example is ownership of the patent for the device to produce plain paper copies—Xerox was entitled to preserve that domain to itself for the life of the patent.

Today, many products are based on a combination of many devices or processes, some of which may be covered by one, two or a dozen smaller or more detailed patent claims. When that is the case, the threat of patent enforcement plays a very different practical role—it functions as a method of direct control over processes and devices *not covered* by the patent claims themselves. Let me illustrate the matter with a hypothetical example. XidaFlex owns the '623 patent. One claim of that patent, say, '623, claim 2, may be a minor but essential aspect of the complete product to be offered by Company A. Company A conducts its own diligent search of its product to see if it offends any patent. It discovers the '623 patent and checks its design with its own technical staff who believe that the device used in the product is different from and does not infringe the '623 claim. Company A obtains an opinion of non-infringement from its patent counsel and proceeds into production. At that point, Company A receives a letter claiming infringement, or worse, receives a summons and complaint. Even though the claim may be minor or ultimately defensible, the lawsuit places a cloud on the *entire product* as well as on Company A.

The leverage of the threatened patent claim extends far beyond the bounds of the value of the patent standing alone because its existence threatens other processes and devices. That threat allows the patent holder to thwart the economic position of its competitors. The phenomenon is at odds with the basic patent law objective which is to reward for an invention. Patent law says: "You win the race; here is the prize for that race." The patent claim threat in complex products says: "We will hobble you in a different race!"

The use of patents to control the economic position of competitors is also contrary to basic policies of anti-trust law. The Con-

9. It is worthwhile to note here that a patent is usually made up of several *claims* to a particular invention. Thus a patent may have seventeen claims. If another person or company utilizes any of the claims without permission, then there is a complete basis for a lawsuit. It is literally the infringement of a claim that is at issue in the litigation rather than the common parlance "infringement of the patent."

stitution itself provides that the purpose of patents and copyrights is
"to promote the progress of science and useful arts. . ."\textsuperscript{11} The
Supreme Court has reasoned that the grant of a patent is a grant of
a special privilege: "The necessities or convenience of the patentee
do not justify any use of the monopoly of the patent to create an-
other monopoly."\textsuperscript{12}

**The Innovator's Point of View**

It is worthwhile to examine the problems of innovation from
the point of view of the innovator, the business person, and the peo-
ple involved in all phases of producing and marketing invention de-
pendent products. Ideas or inventions are initially entertained for
their practical utility alone. Such and such a design will produce a
new capability in a logic chip, or such and such process will reduce
the imperfections and increase yield. The inventor will consider ca-
pabilities and design and will enjoy the thrill of pursuing his or her
project. The business person will temper enthusiasm with questions
of cost, assessment of timing or entry into the marketplace, and
other practical considerations. The marketing people will be inter-
ested in the actual demand for the improvement. Sales people will
be eager to have any product that offers real advantages or "sounds
good" to the purchasing public.

The attitude of the decision makers or management toward the
prospect of obtaining a patent or some other legal protection varies
a great deal. As lawyers, we tend to assume that people with inven-
tions, or other valuable items, will want to rush to protect them
legally. That assumption is true only some of the time. Some man-
gers are very alert to patent creation and their companies are well
organized to maximize their advantage in that regard. Other man-
gers view patent creation as very secondary to the speed of entry
into the marketplace. Still others do not give much attention to the
patent question until some circumstance requires it.

One attitude that is widely shared among business people is an

\textsuperscript{11} U.S. Const. art. I, § 8.

\textsuperscript{12} Mercoid Corp. v. Mid-Continent Inv. Co., 320 U.S. 661, 666 (1944) (Mercoid I). It
is critical that patents not be diverted from their statutory purpose, because to do so would
allow them to become "a ready instrument for economic control in domains where the anti-
trust acts or other laws not the patent statutes define the public policy." Id. Congress has
amended the patent law to change rules governing contributory infringement since the Mer-
coid decisions. (The second Mercoid case was Mercoid Corp. v. Minneapolis-Honeywell Reg-
Co. v. Rohm and Haas Co., 448 U.S. 176, 202 (1980), reh'g denied, 448 U.S. 917. The prin-
ciple quoted in the text remains in force today.
aversion to legal technicalities, entanglements, and proceedings. The legal system is seen as sluggish, expensive, and risky to all concerned. Unfortunately, the reticence of some managers causes them to delay too long before taking steps to resolve a potential patent matter, whether it be applying for one’s own patent or dealing with the threat posed by a potential claim of infringement of someone else’s patent. Some outside counsel and house counsel contribute to management problems by failing to advise their clients actively on the values of planning, of compromise, and of appropriate communication of intentions to other interested parties.

The overall picture is one of a spectrum of differing levels of concern about intellectual property among businesspeople, yet one with a common view that “there are far more important matters than the lawyer’s concerns.” The shared view does not entail laxity (though it may be present) or indifference. It does indicate an attitude that legal matters, in the normal course of affairs, ought not to predominate.

START-UPS AND POWERHOUSES

There are two situations where legal protection plays a more dominant role in the business person’s thinking. One is the new company or start-up which is banking heavily on some particular innovation as its source of entry into the market. The other is the economic powerhouse which uses its stable of invention rights as a weapon to protect its overall economic posture vis-à-vis its competitors.

The strong economic entity is able to use its patents to control the activities of start-up companies or smaller companies. When the product field calls on a complex set of devices or processes, the strong entity can threaten or initiate lawsuits to exert undue pressure on the new entrant. Remember, the new entrant can exercise all of the legal due diligence imaginable and still run afoul of a potential patent violation. The threat or commencement of a legal action can severely limit or cripple the new entrant: investment capital may become higher priced or disappear; employee morale may slip; it may be difficult to attract creative people to join the venture; purchasers may be more reluctant to commit to the new company’s products. A powerful company’s use of patents, even minor ones, to frustrate the creative new entrant is an actual prac-

13. Even in this situation, the decision makers will often choose to place market timing considerations, name recognition, and other considerations far higher than patent protection.
14. See supra note 9 and accompanying text.
A Solution: Require the Patent Holder to Choose

In any form, the use of a patent claim to gain economic control beyond a reward for the value of the invention standing alone constitutes a major aberration of the purpose of patent law: 1) It creates an economic power and financial reward (control) for something other than the use of the invention; 2) It can be and is used to thwart new innovators, even new patent holders; 3) It prevents the public from benefiting from unencumbered uses of patents and from competition among clearly improved products. 15

It is time to re-examine the three basic means by which a patentee can exercise the power of its patent: exclusive use, selective licensing, and threat of patent enforcement. Since one of these, selective licensing, distorts both patent and anti-trust policy, there is a need for legislative change.

I propose that the problem be solved by amending the patent law to establish the legal principle that a patent holder may refuse to license, but once he does license, he must grant access to a license to all others on substantially equal terms. There should be an exception allowing restricted or exclusive licensing for a limited period immediately after issuance of the patent. The exception is primarily for the purpose of allowing creation of development agreements to assist in the establishment of new technologies. The proposal is as follows:

35 USC 154a (NEW) Access to licensing. The patentee, his heirs or assigns, shall have the right subject to the provisions of this section to license or decline to license the patent or any claim thereof. The patentee, his heirs or assigns, may grant a license to any restricted group of licensees or may grant an exclusive license, provided that the term of such restricted or exclusive li-

license must terminate two years from the date of issuance of the patent. Thereafter, the patentee, his heirs or assigns, must make available a license on reasonable terms to any other party seeking a license. "Reasonable terms" as used in this section shall be determined so far as is appropriate from the prior licensing practices of the patentee (or his heirs or assigns), allowing for appropriate consideration of such factors as the financial condition, responsibility, and reliability of the party seeking the license.

The proposed amendment offers great advantages. It preserves the patentee's basic options of producing exclusively itself, licensing, or putting the patent "on the shelf." It cleanly eliminates the use of the patent as an economic lever against others for any purpose other than to gain revenue on the actual use of the patent.

The proposal preserves a small period of exclusivity (two years) for those instances where the patentee sees some particular gain to be made from such an arrangement. This particular feature is included specifically to aid one class of patentees—the new entrants who rely on new processes or devices as a principal means of entering the industry. Such start-ups sometimes use development agreements as a means of creating their initial capital. The basic exchange is:

Start-up Company  <----------------> Established Company
provides technology                provides cash, production
capacity, etc.

The start-up will agree to apply or perfect its invention and grant an exclusive license to use the patents or other intellectual property for a limited period to the established company. The established company agrees to provide the necessary funds, production capacity, marketing, etc. to allow the start-up to get going. The proposal also avoids the problems that may be presented by compulsory licensing. While other countries have compulsory licensing laws, opinion in the United States is predictably resistant

16. I believe that legislation in the proposed simple form offers the greatest advantages. Some people, however, may find particular needs should be taken into account. For example, it might be argued that one ought to be permitted to distribute process patents on a geographic basis. Another point of view might be that the federal government ought to be in a position to authorize certain exclusive licenses in the case of foreign licensees. (Export of technology is currently subject to federal regulations established pursuant to 50 U.S.C. App. 2401 and following.) Another suggestion that has been made is that the new licensing approach ought to be tailored to allow an individual inventor (or group of individuals) who has not conveyed invention rights to another party to retain the full right to grant exclusive licenses. Such possibilities should be studied, but, I think, ought ultimately to be resisted, unless some truly compelling need is demonstrated. The proposal as it stands offers a clean and unencumbered improvement to the patent law.
to such approaches.\textsuperscript{17} No regulatory agency is needed to administer the provisions. Instead, licensing will be handled primarily by direct communication between the parties with occasional necessity of court proceedings.

The new approach will be very practical in its operation, especially in high technology areas such as the computer and communications fields. Litigation will be reduced because the ground rules on licensing will be firm and in the open. The firm with a patent will enjoy all the existing protections, such as presumption of validity, damages and injunctive relief, and attorney fees.\textsuperscript{18} In addition, the clarity of the provisions will make it possible for the patent holder to obtain a more speedy remedy in court for what is a clearly demonstrable infringement. Above all, it will be possible to settle litigation far more swiftly, with cards laid more openly on the table. The pressure will be on the company lacking a patent to settle for a license because its recalcitrance will be penalized with a damage award that could have been easily avoided.\textsuperscript{19} On the other hand, when a defendant believes that there is a valid defense (invalidity, non-infringement, etc.) it will be able to negotiate the license and counterclaim for a declaration of its rights, including annulment of obligations under an improperly


imposed arrangement. The premium will be on fair treatment of patent claims and careful assessment outside the courts.

The computer and communications sector of the economy has shown a bent toward litigiousness in the past three or four years. New lawsuits are seen weekly in all phases of these industries—the chip designers and manufacturers, the computer producers, and software producers—all seem to be getting into the act. I believe that it is true, as I have mentioned, that most business and technical people wish to avoid these legal entanglements, but in today's climate, some may be viewing litigation as a business necessity. Litigation, however, is very expensive and slow. One house counsel in the computer industry recently observed that the pace of litigation "is destroying the industry." The interest of the public is better served by a patent enforcement system that reduces litigation and encourages negotiated resolutions.

New and innovative ventures will be given access to existing technology in place of the uncertainty of litigation in products with a complex patent mix.20 This should clearly aid the inventive aspect of "American competitiveness."21 Innovative firms will be freer to concentrate on all forms of improvement, including production techniques and quality improvement, because the available technology will be subject to access at the reasonable reward contemplated by the general theory of our patent law.22 Congress has recently enacted provisions that are intended to give greater protection to United States intellectual property rights

20. See supra note 9 and accompanying text.
22. American or multinational firms of all sizes have or continue to arrange for fabrication outside the United States. Sometimes this is done to reduce labor costs, and in other instances, it is done because higher quality components may be manufactured abroad. Appropriate steps need to be taken to protect American working people in all areas, and high technology working places are not an exception. A patent access policy deals only tangentially with those needs, but if anything it should give some general boost to working people to the extent that our products continue to be more technically sound.
against imported goods and in particular to protect United States process patent holders. The proposal is fully consistent with those intentions and provisions, for it streamlines the patent system to make compliance with patent claims easier and more predictable. The inventor is more assured of reward, the innovator is encouraged to take more risk, and the public benefits by smoother and more complete delivery of patent based products.

CONCLUSION

It is time to give a hand to innovators and to the public through a simple amendment to the patent law. Give all patent holders a clear choice at the outset: practice the invention exclusively yourself, put the invention on the shelf, or license all who wish access to the technology. Temper the approach with a provision that allows exclusive or restrictive licensing in a critical short period after issuance (two years). The change will stimulate innovation, reduce costly and frustrating litigation, and serve the public.
