PATENT LAW REVISION

May 13, 1971

HEARINGS

BEFORE THE

SUBCOMMITTEE ON PATENTS, TRADEMARKS, AND COPYRIGHTS

OF THE

COMMITTEE ON THE JUDICIARY UNITED STATES SENATE

NINETY-SECOND CONGRESS

FIRST SESSION

Pursuant to S. Res. 32

ON

S. 643, S. 1253 and S. 1255

PART 2

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PATENT LAW REVISION

THURSDAY, MAY 13, 1971

U.S. SENATE
SUBCOMMITTEE ON PATENTS, TRADEMARKS AND COPYRIGHTS
COMMITTEE ON THE JUDICIARY,
Washington, D.C.

The subcommittee met, pursuant to recess, at 10:30 a.m., in room 3302, New Senate Office Building, Senator Philip A. Hart presiding.

Present: Senator Hart (presiding).

Also present: Thomas C. Brennan, chief counsel, and Edd N. Williams, Jr., assistant counsel.

Senator HART. The subcommittee will be in order.

The able Senator from Arkansas, Mr. McClellan, chairman of this subcommittee, called these hearings to consider proposed amendments to S. 643, the patent revision bill.

The proposed amendments raise some of the most important and difficult issues of public law that have been brought to the subcommittee's attention in recent years. The amendments that have been proposed by Senator Scott, No. 23 and 24, raise substantial questions with regard to the relationship of patent licensing and the antitrust laws, as well as the estoppel doctrine, the patent misuse doctrine, the interrelationship of Federal patent policy with the State laws of unfair competition and trade secrets.

Section 6 of S. 643 proposes the repeal of section 308 of the Clean Air Act, providing for a compulsory licensing of inventions for compliance with the act.

In addition, the call of the chairman indicated that testimony will be received also on adjustment of patent fees as provided in S. 1255, and the granting of a right of priority to inventor certificates as provided in S. 1252.

I am grateful to the chairman for his willingness to extend these hearings additionally to permit certain testimony to be offered by witnesses who, to those of us who are concerned with respect to the antitrust implications, the testimony they shall present.

In introducing our first witness, it is more of a welcome than an introduction. He certainly is no stranger to this subcommittee, having served as its associate counsel for a 5-year period, and that is just 5 years in a career that has spanned both antitrust and patent law activities.

Today, he comes as a professor of law at the University of Wisconsin Law School and, indeed, it is a pleasure for us to welcome Professor Stedman.

STATEMENT OF JOHN C. STEDMAN, PROFESSOR OF LAW, UNIVERSITY OF WISCONSIN LAW SCHOOL

Mr. STEDMAN. Thank you, Senator Hart.

My name is John Stedman and I am a professor of law at the University of Wisconsin where I teach mainly in the areas of antitrust law and intellectual property law, including patents.

Senator HART. Excuse me, professor. I was distracted for a moment by a private bill.

We will order printed in the record as though given in full the professor's statement.

Now, sir, please proceed.

Mr. STEDMAN. Actually, I expect to follow rather closely the written statement as I have it.

I have given attention to the interaction of these two fields for over 30 years. During this time I have dealt with the subject in teaching, writing, speaking and in actual practice, including a period spent with the Department of Justice and a period as associate counsel to this subcommittee.

The proposals before the committee are, of course, amendments No. 23 and 24 introduced by Senator Scott as proposed amendments to S. 643, the bill providing for a general revision of the patent laws. The three subjects to which these amendments are directed are: (1) Proposed adjustments of the Patent-Antitrust Relationships, contained in amendment 24; (2) proposed modification of the stoppel doctrine, in response to the rejection of that doctrine by *Lear* v. *Adkins*, also contained in amendment 24; and (3) a proposed reaffirmation of the continued viability of "other" law, both State and Federal, both statutory and common law, which has been threatened by certain language in *Lear* v. *Adkins*. I will discuss these in order.

At the outset, let me say that I consider the proposed amendments undesirable on all three points, for reasons that will become apparent as I proceed.

A. Provisions relating to the Patent-Antitrust Relationship—amendment 24:

The provisions in question are contained in amendment 24. They consist of a proposed addition of a section (b)(2) to section 261 and the addition of two new subsections (f) and (g) to section 271 of title 25.

Section 261(b)(2), as I read it—the language is quite general, ambiguous and unclear in certain respects—would permit a patentee or patent applicant to parcel out his rights by means of exclusive or nonexclusive licenses on a geographical basis, a subject matter basis, on the basis of less than the entire right to make, use and sell, and so on.

Section 271(f) states, also in rather general and sweeping language, that a patent owner shall not be "guilty of misuse or illegal extension" of his patent rights by virtue of having granted less than all of his rights under the patent or imposed restrictions that are "reasonable under the circumstances" to secure to him "the full benefit of his invention and patent grant."

Section 271(g) states, in more specific language, that the owner of a patent or patent application may require as consideration for a license (1) a nonexclusive grant-back or (2) a royalty or purchase price (a) of any amount. (b) payable after the patent has expired, if based upon conduct occurring prior to expiration, (c) based upon practices or production outside the scope of the patent, (d) based upon a package of patents rather than on individual patents, or (e) which is discriminatory.

My objections to these proposals are five-fold: (1) They appear susceptible to interpretations that would have a seriously adverse effect upon the operation of the antitrust laws without any offsetting advantage in other respects. (2) They would inject a large measure of uncertainty and ambiguity into the present law—which already contains its share of uncertainties—inevitably resulting in extensive litigation and substantial relitigation of many now-settled points. (3) The proposals really involve the operation and scope of the antitrust laws, rather than the patent laws, and are out of place in a patent law revision bill. (4) Their inclusion in S. 643 is doubly undesirable, both because they prejudice and endanger the enactment of that bill and because they inject into it a highly controversial issue that should be considered, and accepted or rejected, on its own merits instead of being tied to the general revision. (5) The proposals, contrary to the contentions of their supporters, do not, in my opinion, promote the best interests of the patent system. I will comment on each of these five points in order.

1. UNDESIRABLE EFFECTS UPON THE ANTITRUST LAWS

In introducing the amendments, Senator Scott gave examples of practices that their enactment would permit. His statement, as given, appears quite unobjectionable on the whole. Most of the objectives sought are valid ones. Most of the practices described are salutary. They deal with the right to pick your own licensees, the right to engage in a limited field-of-use type of licensing, the right to charge whatever royalties you see fit to charge, and so forth. However, the statement, as I read it, falls short of giving the full picture in two respects.

First, it neglects to make clear that most of the situations it describes are probably legal under present law and consequently require no amendments to legalize them.

Second, in emphasizing the unobjectionable practices that the proposed amendment would permit, it ignores numerous highly objectionable practices that conceivably would be legalized, depending upon how the courts interpreted the amendments. Certainly, their legalization would be vigorously urged upon the courts by the proponents of such practices.

I have listed in my prepared statement a number of illustrations of the kind of practices referred to, licensing policies that could be engaged in, as I read the language of amendment No. 24. I will not attempt to go through these arrangements or these licensing provisions in detail. Let me, however, make some general statements about them.

I have already mentioned that there are certain types of practices —such as field of use restrictions, within limits; selection of your own licensees as you see fit, again within limits; and variations as to royalties and that sort of thing—that are permissible under the present law and would, of course, be permissible under this law as well.

The bad practices, from the standpoint of the antitrust laws, which would conceivably be permitted by these provisions would have the effect of creating restraints of trade, of extending monopoly beyond the legitimate scope of the patent. As a result—and this is the inherent nature of restraints of trade and of monopoly—they would have, I think without any question, seriously adverse effects upon the consumer and that, after all, is the name of the game as far as the antitrust laws are concerned. They would have a long-range adverse effect upon both the structure of industry and upon the immediate interests of consumers.

Among the examples that would be permitted by the provisions of amendment 24, as I read them, would be an arrangement whereby a patentee could divide the territories in which various licensees could use the invention. They could balkanize the United States, so to speak, so that in each area, each one would have his own little domain and would not be sharing it with anybody else. This is what we would think of on an international basis as a cartelization type of arrangement.

Under the provisions of 261(a)(2) as proposed, a similar arrangement could be provided whereby there would be a substantial limitation of production. A limitation of production, of course, is likely to have two effects: one, of increasing the price of the product; and second, making the product unavailable to people to whom it should be available.

As another illustration, the provisions would permit a tie-in of materials with a patented process, or the imposition of price restrictions. These, as I see it, would be permitted by the provisions of section 271(f)(2) which provides in very broad and general language that a patentee should be permitted to impose such conditions as are reasonable under the circumstances to secure the benefit of his invention and of his patent.

They would also provide for an extensive grant-back. Granted that the grantbacks would not be exclusive, one can conceive of situations in which a dominant patentee, the holder of an important patent, could require of licensees that each one of them grant back to him nonexclusive licenses under any invention that they might make in the given field—or, for that matter, in any field—with the result that an individual patentee could end up as a holder or conceivably thousands—at least hundreds—of nonexclusive licneses, licneses unavailable to anybody else in the industry, thus giving the patentee an overwhelming advantage from a competitive standpoint. This kind of arrangement, I might add, was the target, and the successful target, of an antitrust action a number of years ago against RCA in which this kind of practice had been followed with the result that a dominant position had developed even though the grant-back arrangements were nonexclusive in nature.

The amendments would enable a patentee to charge royalties on the basis of unpatented activities. These, as I see it, would be permitted by the provisions of 271(g)(2). Where two patents were licensed together, they would allow for continuing royalties under one of the patents, even though it had expired, as long as the second patent was still in force.

Finally, the amendments would permit a patentee, if he saw fit, to refuse to license or license on highly disadvantageous terms, a price cutter or somebody who was otherwise engaging in vigorous competition—comparable, for example, to the refusal-to-deal approach that was the subject of the *Parke-Davis* case a number of years ago in the drug industry. This practice had been used to whip into line persons who were competing on a price basis.

Now, these are the kinds of practices, as I see it, that could be engaged in, and which might be supported and justified, depending upon how the courts construed the provisions, by the kind of language that is used in these proposed amendments.

I could go on with examples, but I think it is quite evident that the provisions in the statute would make substantial changes in the law, changes that would be quite undesirable insofar as the antitrust laws are concerned.

Change in existing law is, of course, the privilege of Congress. The difficulty here is that these amendments, if interpreted along the lines I have indicated, would have seriously adverse effects in terms of antitrust policy, effects that I doubt any person with much sympathy toward the antitrust laws and their efforts to preserve a free competitive enterprise, would find tolerable. Would the amendments be so intepreted? I do not know, and I doubt whether anyone else does—and this brings me to my second objection.

2. UNCERTAINTIES AND AMBIGUITIES RESULTING FROM ADOPTION OF THE AMENDMENTS

At the very minimum, the proposed amendments would inject numerous uncertainties and ambiguities into the law, uncertainties that it would take years, possibly decades, to straighten out. Uncertainty in the law is almost always a losing business. The public is the loser, businessmen are losers, and the Government is the loser. Even the legal profession, except for the handful of lawyers who profit from the resulting litigation, is the loser. It does the profession no good, after all, to have to say, "I do not know," to a client's question, or to say, "yes," when the right answer turns out to be "no," or say "no" when the answer turns out to be "yes."

The uncertainties are not solely a result of choice in language although this contributes to them. They arise to a considerable extent from the inherent difficulties involved in reaching a proper adjustment between the antitrust and patent laws. The courts have been struggling with this interrelationship for years. Out of it has come increasing, although concededly not complete, certainty as to what one can and cannot do. Should we, at this point, throw all this accumulated experience and clarification into the trash can and start out with a brand new ballgame—do it all over again under a new, as yet undetermined, set of rules? I suggest we should not. Most others who have been through this painful process, or witnessed it in action, will, I think, agree. The adjustment between patents and antitrust *is* a difficult one. There is no easy way out, no real shortcut. It would be folly, as I see it, to scrap all the accumulated wisdom and start over.

These observations would be less in point if the language contained in the proposed amendments really helped to clarify the situation. In my opinion, they do not. They add to the confusion. In addition to the examples I have already given, let's look at some of the specific wording. (1) Section 261(b)(2) permits waiving or licensing the whole or part of one's "rights" under a patent or application. What are one's "rights?" Are they limited to the right to exclude others from making, using or selling the claimed inventions, or do they also include rights against contributory infringers, rights to recover damages for past infringement, etcetera? (2) Conformance to the provisions of section 271(f) and (g) renders one not guilty of "misuse or illegal extension" of his rights. We have a fair idea of what constitutes "misuse," but what is the "illegal extension" the patent owner is insulated against? Does it include the antitrust laws thus creating a limitation upon the operation of those laws? Does it extend to other laws, both state and federal, that the patentee may run afoul of as a result of his licensing practices? Is the term "illegal" limited in its reference to criminal statutes, or does it extend to noncriminal regulation as well (FTC Act) and private civil actions—unfair competition? What about other parties to the arrangement? Are they also absolved of illegality? (3) Section 271(f)(2) permits conduct "reasonable under the circumstances to secure . . . the full benefit" of the invention. When one looks back on the 60-year struggle to give meaning and content to the "rule of reason" as it applies in the antitrust law, one shudders at the thought of going through the same arduous process in determining what is "reasonable" for the patentee to assert. The 45 year old statement in General Electric has been withering on the vine virtually ever since it was enunciated. It should be allowed to die and be given a decent burial, not be subjected to artificial resuscitation. The burden of determining "reasonableness" in this field is just too heavy to ask a judge to bear. It is even heavier for the lawyer who must advise a client as to what he can and cannot do with his patent.

I applaud the motives of those who would reduce this complex area to a neat set of simple rules. But I just do not think it can be done—that is, without doing violence to and distorting the delicate balance that exists between the antitrust law and the patent laws. Circumstances vary to such an extent in the antitrust field with respect to size of companies, both horizontal and vertical structures, types of practices, effects of practices, etc., that they render hard and fast, black and white rules impossible in most situations. Even in the most extreme cases, involving tie-ins, price restrictions, divisions of territory, and restrictions on production, specific exceptions have been introduced as experience dictates, either by the courts or by legislation. Comparable variations in circumstances appear where patents are involved. In addition, entirely new variances crop up—

variations involving the scope of patents, the extent of their accumulation, their competitive significance, etc. When one is faced with an interaction of these two areas of law, the variations and permutations increase at a geometrical rate. Such a situation simply does not lend itself to codification and the promulgation of simple rules. The Antitrust Division found this out in attempting to lay down antitrust guidelines. The problem is much greater where patents and antitrust interact.

3. THE PROPOSALS RELATE TO ANTITRUST POLICY AND DO NOT BELONG IN THE PATENT REVISION BILL

Up to this point, I have been discussing on the merits, the antitrust proposals contained in amendment 24 and have suggested what I feel are their shortcomings. Even if they were otherwise acceptable, I would deem it undesirable to include them in S. 643. Provisions of this type, in my opinion, do not belong in the patent laws. Perhaps I can make my point clear by suggesting an analogy. My ownership of and rights in a building or a piece of machinery constitutes a monopoly, a monopoly created by real or personal property law. If I use the building, however, or convey it to others, under circumstances or on conditions that lessen competition, the issue now becomes a matter of antitrust law, not property law. If modifications are to be made with respect to such property, we provide for them in the antitrust laws not in the property law. So it is with patents. My patent gives me a monopoly, but what I do with that monopoly beyond the clear grant given me by the patent law, becomes a matter of antitrust not patent law. Failure to recognize this, I suspect, has caused much of the confusion that sometimes exists with respect to the patent-antitrust relationship. From the patent law standpoint, as long as I assert my patent monopoly I should have no fear of the antitrust laws. At least, it is hard to imagine Congress saying in one breath that it will give me an exclusive right in my invention and in the next breath charging me with violation of the antitrust laws.

But just what is this Congressionally-given monopoly? It is the right to exclude others from making, using and selling, and nothing else. Once I go beyond this—whether I convey my monopoly rights to someone else, whether I throw my weight behind one of two competitors by granting a license to one but not the other or by licensing one on more favorable terms than the other, or whether I impose obligations upon others as a condition of not excluding them—what I have done and its effect in terms of competition and monopoly are to be tested by the antitrust laws, not the patent laws. If, for example, I require a licensee to pay me money, to buy certain goods from me, to give or sell something of value, such as a grant-back, in return for a license, impose limits upon what products the licensee may produce, dictate where he sells, what he sells, to whom he sells, at what price he sells, et cetera—in all such cases wherein the patentee engaged in any conduct other than his patent law given right to exclude others from making, using or selling, the question that must be asked in evaluating his conduct from an antitrust standpoint, is this: Is the situation worse, competitively speaking or from a monopoly standpoint, than it would have been had the patentee stood on the legal rights to exclude which the patent law gave him?

Obviously, this approach can give rise to many collateral questions. Would the licensee, if not licensed, have challenged the patent? Would he have adopted or developed alternative techniques? Would he have done business in different areas, sold at different prices, or marketed different commodities? Would he have engaged in competition which, as a result of the license, he now shies away from? These, I suggest, are the real questions that one must face up to in dealing with the Patent-Antitrust Relationship. They are, I reiterate, fundamentally questions of antitruust law and policy, rather than patent law. The provisions of amendment 24, unfortunately, make no serious attempt to deal with these crucial issues.

The point I have just made calls for four additional brief comments:

(1) I am not suggesting that exemptions cannot be made to the antitrust laws if Congress deems this desirable. This has been done on many occasions and presumably will be done again in the future.

(2) Nor am I suggesting that exemptions, such exemptions as are written in the law, must be located physically in the antitrust laws rather than being put into the patent laws, although I think that their presence in the former would be preferable. This is where they really belong.

What I am attempting to emphasize here is that these are antitrust issues. Whether they become the subject of legislative exemptions, and whether they are put in the antitrust laws or patent laws, they should be treated and approached as antitrust matters rather than as patent matters. The amendments, as they stand at the present time, have not taken this approach.

(3) Much emphasis has been put upon the need for these amendments for the purpose of encouraging innovation and development. It is important to recognize that this is something which is not, strictly speaking, presently a part of the patent law. It may be that some laws of some kind are in order to achieve this objective. Up to now, however, Congress has not seen fit to extend the patent laws beyond the point of stimulating invention. If Congress desires to go further, it should be done with that clear purpose in mind, with a careful look to see how this can be accomplished, with the full awareness of the possible cost in terms of weakened antitrust laws, and with careful appraisal of the possible constitutional problems. The present proposal meets none of these criteria. What I am saying, in short, is that a clear case should be made for policies of the sort proposed here. No such case has been made. Rather, the proposals have been supported on vague grounds of "reasonableness," general speculation as to what the Antitrust Division may be up to or what some court might do in the future, etc.

(4) Although I have been talking in terms of the antitrust laws, most of my comments apply equally to the misuse concept. Granted that the misuse doctrine is part of the patent law, at least of its procedural aspects, it is inextricably tied in and identified with the anti-

trust law. Basically, it constitutes a recognition that a patentee who has used his patent in such a way as to violate the antitrust laws, should not be permitted to enforce that patent where the case comes up as a suit for infringement instead of as an antitrust suit.

The remaining objections that I have to the antitrust provisions of amendment 24 pertain more to their relation to the patent laws than to the antitrust laws. These are developed more fully in my prepared statement but I would like to say a few words about them here.

The first point relates to the adverse effects that injection of these amendments is likely to have upon the enactment of S. 643.

S. 643 has been kicking around for about 4 years now. There were a lot of disagreements in the early days as to what ought to be done, what the policy should be. Most of these have been ironed out. It is my impression that the Scott amendments, No. 23 and especially No. 24, are the major barriers to enactment of the patent revision bill at the present time.

In a revision bill of this sort, a bill that is designed to shape up and improve the structure of the patent system, provisions that are extraneous to this purpose (and for reasons that I have suggested, I think these provisions are extraneous) are not appropriate or proper subjects for inclusion in that bill. They simply create controversy, uncertainty and impede the enactment of the bill. Second, their inclusion puts the members of the Congress in a difficult position where they may be forced to approve something they do not want in order to get the bill through or to disapprove something they want if they are opposed to the bill generally.

Proposals like these should be handled separately, handled on the merits, stand or fall on the merits. They should not be treated as a sort of rider, analogous to a tie-in, to the patent revision bill which should be proceeding on its own as a patent law proposal as such.

These are considerations that are less relevant to the antitrust aspect, but they do suggest reasons why these amendments should not be included in S. 643.

Finally, let me suggest that the argument of those who are supporting the amendments, namely, that they are necessary for the purpose of promoting the patent system, appears to me on close examination to be rather thin. The proponents of the amendments have not made any really firm case to indicate that the patent system is falling apart for failure to include these amendments, or that the amendments would provide any useful spur to the patent system if they were enacted. If there were a case to be made, one would expect them to make it.

The argument in general has been, first, that if we had greater certainty in the law, this would provide a stimulus to the patent system; and, second, that if we had these provisions in, this would encourage and stimulate innovation.

On the matter of greater certainty, I have already indicated that in my opinion their inclusion will greatly increase the uncertainty that we have in the law. I think it is necessary to say no more about that.

As for the greater freedom to license, it may very well be that this would provide some incentive to innovation. However, I do not see how this would provide much incentive to the inventor. The picture of the inventor working his head off, struggling to make an invention that, at the moment, he has no idea will come to fruition, with the hopes that he will be able to use a tie-in arrangement, or that he will be able to license some people and not others, that he will be able to impose price restrictions, divide territories and so forth, is in my opinion somewhat fanciful.

Furthermore, insofar as the patent system, generally, is concerned, one may seriously ask whether making it easier to license will stimulate or enervate the inventive process which is the essence of the patent system. Licensing, as compared to refusal to license, may cause a licensee to sit back and not bother to make inventions of his own, especially if he is subjected to such things as grant-backs or has the protection of certain restrictive clauses. In contrast, faced with the refusal of the license, he may be forced to engage in competitive research of his own and thereby further the purposes of the patent system, rather than interfering with them.

It is rather interesting that in another context, one of the most vigorous objections that has been made to occasional suggestions in this country, that we undertake compulsory licensing as many other countries do, has been that this would act as a deterrent and discourage people from engaging in inventive activity. The reason given is that, rather than bothering to make an invention, they would simply sit back, let someone else make the invention, and then go ahead and ask for a license. If licensing has an interfering effect under such circumstances, it seems equally plausible that a similar adverse effect would occur here.

For the various reasons stated, I feel it would be undesirable to enact those provisions of amendment 24 that deal with the antitrust-patent relationship.

Let me turn to the two remaining features, the estoppel provisions of amendment 24 and the provisions of amendment 23.

Amendment 24, in addition to the antitrust provisions, would also revive to some extent the estoppel doctrine that was thrown out a couple of years ago in the case of *Lear* v. *Adkins*. This is the doctrine that the assignor of a patent, or the licensee of a patent, is estopped to challenge the validity of the patent. This doctrine was rejected by *Lear* v. *Adkins*. Amendment 24 would partially restore the doctrine.

An assignor would be estopped to challenge the validity of a patent he had assigned unless he restored the consideration he was paid for it, and only if he did not possess the information that created the invalidity at the time he made the assignment. The amendment would require that a licensee, who wished to challenge the patent, first unequivocally give up his license. Also, he would be obligated to pay for whatever use of the patent he had made prior to the time that he cancelled.

Unless they complied with these conditions, assignors and licensees would be barred from questioning the validity of a patent in a suit brought by the owner of the patent.

I recognize that there are many touchy problems involved in this question of how the relations between the patentee and licensee or the assignor of a patent and the assignee should be adjusted in situations where the patent which was the subject of the agreement ultimately turns out to be invalid. There may be circumstances in which one party keeps the money and other circumstances in which he has to give up the money. There may be situations in which he might have to continue to pay, other situations in which he might not.

These are matters that the courts have to take care of, and which the parties can frequently take care of simply by putting the necessary provisions into their agreements.

What I do deem undesirable in this connection is this: Whatever one may decide, as to who should pay and what they should pay, I find no justification for a doctrine that says that any of these parties should be estopped from challenging the validity of the patent. Maybe they should have to pay, even though the patent is invalid, but certainly they should not be estopped from at least raising the point that the patent is invalid. The Supreme Court has on many occasions—most frequently only ten days ago—pointed out the great importance of clearing out any patents that are invalid, that should not be there as an obstruction. There is a very strong public interest in getting rid of the so-called spurious patents that never should have been issued.

Just ten days ago, as I say, the United States Supreme Court in a unanimous decision, in the *Blounder-Tongue* case, made the comment that the holder of a patent should not be insulated from the assertion of defenses and thereby allowed to exact royalties for the use of an idea that is not in fact patentable or is beyond the scope of the patent monopoly granted. This has become an increasingly standard doctrine.

The estoppel doctrine as such, as distinguished from issues concerning the obligation to pay money, never made any sense. It has been gradually whittled away and was finally completely thrown out in the case of *Lear* v. *Adkins*. That, I suggest, is where it should stay.

I would grant that there may be situations in which a patentee would be disinclined to license a patent if he did not have the benefit of the estoppel doctrine. I think this is a chance that we can properly take. The cases where rejection of the estoppel doctrine is most likely to act as a deterrent to licensing, are those where there would be serious doubt as to the validity of a patent, or where the patentee was disposed to buy off, through the granting of a license, a person who would otherwise be attacking the patent head-on. I think, though, that these are the kinds of licensing practices that we should not encourage by restoring any part of the estoppel doctrine.

I grant that there are difficult problems, but they are not problems that stem from the estoppel doctrine. The problem is one of invalid patents and the cost, delay and difficulty involved in litigating those patents.

If I may be permitted a mixed metaphor, I suggest that when we sweep the problem under the rug by talking about reinstating the estoppel doctrine, we are barking up the wrong tree. What we must do is to face up to the difficulties that result from the existence of invalid patents and solve that problem, not to close the mouths of those who have a public duty to speak up and say their piece, if they have knowledge that would indicate that the patent is invalid.

Let me turn now to amendment 23, dealing with the doctrine of preemption. Amendment 23 is very brief. It is all in one sentence so I can read the entire proposed amendment. It says:

> This title—

meaning title 35 of the patent law—

> shall not be construed to preempt, or otherwise affect in any manner, rights or obligations not expressly arising by operation of this title whether arising by operation of State or Federal law of contracts, of confidential or proprietary information, of trade secrets, of unfair competition, or of other nature.

We can all agree that there are many, many areas in which the State law, and other Federal laws that exist, do prevail and should prevail. The difficulty I have with amendment 23, which purports to express this doctrine—and as I say it is a doctrine that I quite agree with—are two-fold:

First, it is a provision of objectionable scope and ambiguity because of its sweep. Secondly, it is a premature provision insofar as action by Congress is concerned.

In terms of scope, for example, it would seem to permit states to grant an exclusive right comparable to a patent for an idea that would not meet the requirements for patenting under our Federal system. It would permit, for example, contracts or agreements not to challenge the validity of a patent, even though one were not licensed under the patent, a doctrine which has been uniformally rejected by the Supreme Court for over seventy years. These kinds of things, as I read the provision, would now be permitted.

The relationship between the patent law and the State laws, and for that matter, other Federal law, is a delicate, intricate relationship, like the relationship between the patent and antitrust laws. It is not a thing to be handled in the sweeping approach that is taken by amendment 23. It is not something to be handled through blunderbuss methods, or attacked with such weapons as the procrustean bed or the butcher's cleaver. It calls for careful and difficult adjustments between these laws. This has been underlined very recently, just within the last couple of weeks, in a case here in the District of Columbia, the case of *Hecht* v. *Pro-Football, Inc.*, in which the District Court pointed out the delicate relationship that exists between State law and the antitrust law, and between other Federal laws and the antitrust law. I suggest that the same delicate relationship exists insofar as the patent law is concerned. It is not a situation in which one should be saying: "everything the States do shall be okay, everything that other Federal statutes do shall be okay, and everything our contract law or our common law does shall be okay, unless it is expressly provided to the contrary in the patent law.

My other objection to Amendment 23 is its prematurity. The amendment is really directed at a case decided several years ago, the case of *Sears Roebuck & Co.* v. *Stiffel Co.*, in which the U.S. Supreme Court used the patent law and the patent clause of the Constitution as an excuse for throwing out a decision rendered under the Illinois unfair competition law. I think the rejection of the Illinois unfair competition law, as interpreted by the lower courts, was quite justified. It was a very sweeping and very unfortunate decision that the lower courts reached in that case. I hold no particular brief for the reasoning of the Supreme Court in the *Stiffel* case when it said that, unless something was expressly provided for by the patent law, it could not be done under State law. It was, I would say, a rather extreme and somewhat questionable approach to the problem. In such a situation, I think one can have considerable confidence that the courts themselves will work things out. I think it fair to say that they are working it out in this case. In any event, they are definitely on the road to working it out.

There is a subsequent case, *Lear* v. *Adkins*, in which the logic of the *Stiffel* case could have been invoked and might have been adopted. Instead, the majority opinion refused to follow *Stiffel*. It was only a minority of three judges, one of whom is no longer on the court, that urged that the *Stiffel* doctrine, in all its implications, be applied.

A still later case that came up, a rather extreme district court case, has generated a great deal of excitement. The case is *Painton & Co.* v. *Bourns, Inc.*, involving a questionable decision by a district judge. This decision has now been reversed by the Court of Appeals for the second Circuit in a well considered opinion.

All in all, I think we have evidence here that the courts are working out this problem. I suggest that, because of the delicacy of the problem, it is one that is better worked out through the judicial process than through Congress moving in on what I consider a premature basis and enacting into law a sweeping provision such as that contained in amendment 23.

Beyond that, I question the basic approach of amendment 23. We are dealing here with problems of unfair competition, of marketing—that type of thing. These are areas where I suggest it is highly desirable to have national rules that will apply uniformly throughout the entire country. That being the case, the approach of amendment 23, which in effect revitalizes the application of individual state rules to broad areas of unfair competition, trade secret law and so forth and so on, and pushes the application of these rules even further than has been the case in the past, is an unfortunate trend rather than a desirable one.

This concludes my testimony, Senator. I shall be glad to respond to questions if I can.

Senator HART. Professor, I should indicate that I have not been able to attend the 2 days of hearings already held; I was involved with other hearings. I had looked forward with less than enthusiasm to coming in here this morning for the reason that I had been told that the amendments involved complicated questions and not all of us are enthusiastic when we have to confront complicated questions. But I am grateful to you for having approached it in the fashion you have; it has made it much easier for those of us who are catching on the third day the story that has been going on here.

Professor STEDMAN. Thank you.

Senator HART. Now, you are not quarreling, I take it, over the question of whether, if you are going to amend the antitrust laws, it should be done in title 15 instead of title 35?

Professor STEDMAN. Not seriously.

Senator HART. At least, that is not your major concern.

Professor STEDMAN. It is not my major point. I think they are more appropriately included in the antitrust laws. The important thing is that they should be considered as antitrust problems and dealt with on that basis. This has been my concern.

Senator HART. You are, in that sense, telling us that you consider these to be amendments to the antitrust law in that they grant antitrust immunity to anticompetitive patent licensing practices.

Professor STEDMAN. Yes, this is the way I view them—in the same sense, for example, that protection of farm marketing co-ops from antitrust action constitutes an amendment to the antitrust laws, even though the statutory provisions happen to be in the agricultural farm marketing laws. I base my position on the fact that I think of the right under a patent as the traditional right to get a patent and then exclude everybody else from making, using, or selling. But when I, as patentee, step down from that position and start getting into licensing programs and pools and interchanges and various conditions and grant-backs, then I am moving into an area where I am having an effect that goes beyond the effect that I might have if I were simply asserting my patent in the traditional manner.

Senator HART. You mentioned, particularly with respect to amendment 23, the desirability of allowing certain judicial clarifications to develop through the courts. But you were talking there about the preemption aspect. What is the likelihood that the present state of the law in field of use licensing, and other patent and antitrust relationships, will be changed significantly by the judicial decisions?

Professor STEDMAN. I do not view amendment 23, the preemption amendment, as having any substantial effect on that. Amendment 23 relates to the states enacting their own laws and that sort of thing. In the absence of the enactment of amendment 24, however, the question comes up whether there are certain trends, certain attitudes on the part of the courts today, with the Supreme Court setting the pace, that are pushing the antitrust laws much further than they have gone in the past.

I do not see that there are. I see very little basic change in the attitude of the Supreme Court or the lower courts with respect to the patent antitrust relationship, much less than you would find in many other fields of law that the courts have to deal with.

Two changes, as I see it, are occurring. One, the courts have been catching up to some extent, by developing doctrines that could have become part of the law a long time ago and which inevitably would become part of the law once the court got around to them. I refer to cases like the *Walker* case holding that fraud on the Patent Office provides a basis for an action under the antitrust laws, on the theory that the patentee obtained a monopoly he was not entitled to and used that monopoly to restrain trade. It was only a question of time when the Supreme Court would lay down a doctrine of that sort. It is surprising they hadn't done it a long time before.

The elimination of the estoppel doctrine that I have referred to is another example. To me, it was inevitable that sooner or later the courts would get rid of this doctrine. As I have pointed out, any careful examination of the doctrine would indicate that, one, it did not make any real sense, and two, it was quite inconsistent with positions the courts had traditionally been taking.

In such respects, the courts have to some extent done some catching up. They have similarly done some catching up in recent cases involving bulk sales practices, where they have adopted a doctrine that has been in the law for a long time, namely that once I have a product, I am free to sell it and if I either buy or manufacture a product, I ought to be able to sell it. This has been in the law for decades. But it has not been applied in this particular area before.

The other thing I would say is that the courts have developed a little more sophistication about some of these antitrust matters than they have shown in the past. We have come a long way from the days when Justice Holmes, sitting on the Supreme Court and writing in the case of *United States* v. *Winslow*—the first of the *United Shoe* cases and the case that gave *United Shoe* its start in creating its monopoly, since it approved the sale of the properties, patent rights, etc., that created that monopoly—could blithely say, in effect: Well, a patent is a monopoly, a monopoly is a monopoly, it does not really make any difference who owns it." We have come a long way from that. We have come a long way because the courts now know more about the economic intricacies of what goes on and also because they are more familiar with some of the practices that go on.

Cases like the *National Lead* case were an eye-opener. They disclosed the kinds of things that were being done by some patent owners.

I recall quite a few years ago one case in which the government had the good fortune to dig up a letter which had been written between two companies and which said, in substance: "This patent really probably is not much good, but I think we can use it as a basis for a price agreement." When things of this sort have come up, the courts' eyes are opened. This is what I mean when I say that the courts today are more sophisticated.

But beyond that increased sophistication, beyond catching up, I do not see them as pushing antitrust further in any respect.

Field of use provisions—

Senator HART. I was going to ask, because I am told that testimony is focused on that, among other things.

Professor STEDMAN. Regarding field of use, I would say this: Here again, I see no evidence of any attack on field of use agreements or geographical restrictions as such. But suppose you get a patent, an important patent. Suppose, also, there are, say, 50 competitors in the United States. Suppose, further, that you enter into a licensing agreement with all of the 50, licensing each for his own State and limiting him so he does not operate outside of his State. The result is that we end up with 50 companies that had formerly competed, each now operating in his own little bailiwick. This kind of a geographical field limitation would, I am sure, be the subject of attack. The same thing can be said about field of use agreements, for instance, if I permit one person to use a patented tire-making process for motorcycles, another to use it for bicycles, another for automobiles, another for trucks and so on. An example of a legitimate use of a field restriction would be a case in which I have a patent, I want to protect my monopoly, it is a good patent, someone wants to operate only in one area, and so I limit his license to that area. In such a case, I see no difficulty at all.

I do not see any indication of an attack on situations of that sort and I certainly see no indication that the courts would acquiesce in this kind of attack and have any sympathy with it. This is my own feeling.

It is true that one of the cases which proponents of amendment 24 wish to preserve and which they feel is threatened is, in my mind, something of an aberration. This is the *General Talking Pictures* case. I think the *General Talking Pictures* case is a somewhat questionable decision, not because of the doctrine that it laid down, but rather because of the application of the doctrine in that particular case. The court there seemed to be closing its eyes to what did appear to be a certain amount of dissembling. On the facts, the case looked like a division of fields. It also ignored the doctrine that once I have bought a product, I am free to deal with it as I please.

But this is a reservation I have about the *General Talking Pictures* case itself, not about the doctrine. I just do not see anything to indicate that the courts are questioning the doctrine provided the practice is being appropriately used.

Senator HART. I am told that the Commerce Department suggested revising amendment 24 in section 261(f)(2) to provide the test of legality to be based upon the circumstances that existed at the time the license was executed rather than at the point in time that the territory was drawn. How would that affect existing legal standing?

Professor STEDMAN. I can sympathize with the point of view that if I did something at a given time and it was perfectly legal at that time, I should not be clobbered at some later date because it turns out to be illegal. In this sense, I think there is some merit to the point. But to me, it is a limited merit.

First of all, let's recognize that the antitrust laws are not a game. The antitrust laws are a serious business of trying to preserve competition, to preserve a satisfactory competitive structure in our society. To say to a person, because what you did happened to be okay at the time that you did it, you shall be forever immune no matter to what extent you are monopolizing, no matter to what extent you are restraining trade at the present time, is not, I think, consistent with the spirit of the antitrust laws. And it is not a doctrine that has been applied in administering the antitrust laws. We have had numerous cases in which things started out innocently, at least presumably innocently, and in any event, unobjectionable at the inception. Later, when the practices became objectionable, they have then been attacked, and attacked successfully, under the antitrust laws.

Probably the most notable example of this is the *General Motors-Dupont* case in which the acquisition of stock was concededly okay at the time of acquistion. Later on, there resulted an unfortunate monopolistic situation, and an antitrust violation was found. I think the same doctrine would apply here. Consequently, these agreements have to be reexamined.

We have a number of other antitrust cases in which the same sort of approach has been taken. One must examine these agreements on the basis of what they are doing to our economy at the present time. It might be quite appropriate to refuse to enforce criminal penalties where the agreement had been innocent at the inception. It would also be appropriate to refuse to impose treble damages for any injury prior to the time that the action became illegal. But to say that we will provide a grandfather clause for people who restrain trade and monopolize simply because it happened not to restrain trade at some other time, seems to me as unreasonable as to say that I should have the privilege of driving the wrong way on a one-way street simply because I did it 10 years ago.

Senator HART. Yes, it just infuriates the person to whom you use that example when explaining why something that was once perfectly acceptable now becomes unacceptable. That is, I think, a legitimate response; there is a traffic light at that corner now and there was not need for one 50 years ago. Circumstances have changed.

Professor STEDMAN. Right.

Senator HART. Now, it is said that 72 percent of the patents that are challenged in court are held to be invalid. Help us for the record on this one. Is it that the courts are applying the standards differently from the Patent Office? Why are so many found invalid?

Professor STEDMAN. Actually, it is a rather complex situation. First of all, let us recognize that many patents are borderline; they have to be borderline, because the very nature of the patent system is one in which some marginal inventions inevitably result—in which it is possible to say either it is an invention in the patent sense or it is not. Anything along the margin like that, is going to pose difficulties. There are going to be legitimate disagreements as to whether the patent is valid or invalid.

But having said that, I do think there are a number of factors that push in the direction of creating the kind of a situation that we have.

First of all, the proceeding in the Patent Office is ex parte. Nobody is there except the examiner. Nobody is there except the examiner to stand in the way of the person getting the patent. The examiner is not in a position to check this thing out, to explore all of the various art that may exist and that sort of thing, to see whether this thing works, and so on. All he can do is look at the papers and make his decision on this basis. The applicant, after all, is there to try to get a patent, not to destroy his own case. So we have this ex parte proceeding in which there is nobody on the other side to say why the patent should not issue. This is one factor.

Another thing is this: In the matter of administration, the easy way to do your job is to say "yes" and the hard way is to say "no."

If the examiner wants to make his job a 60-hour week, including weekends, all he has to do is be tough, because then he has an everlasting fight on his hands. He is obligated to appear, for example, on appeals and so forth and so on. Under these circumstances, it is almost inevitable that where somebody is pushing from one side and nobody is pushing from the other side, it is just human nature to give a little bit simply so you can have your weekends to yourself.

Beyond that, the whole system, as I see it, is geared to the allowing of patents. If I go into the Patent Office and the examiner agrees with me that I am entitled to a patent, this is the end of it. The patent issues and not until maybe 10 years later and $100,000 in litigation expenses later, do we find out that he made a mistake.

On the other hand, if the examiner turns me down, tells me that I am not entitled to a patent, what happens? First of all, I go through this rather difficult proceeding with him in which I try to persuade him to change his mind. Then I have an appeal to the board of appeals in the Patent Office. After that, I have an appeal to the Court of Customs and Patent Appeals. So that we have lots and lots of protection against the unjustified denial of a patent, but no protection against the unjustifiable grant of a patent. All of these factors, as I see it, push in the direction of granting patents.

There is one more point that I should mention. There have been in the past, many who approach this problem on the basis that if in doubt, the patent should be granted. Why? Because if it is denied, they argue, this will be an end of it. Notwithstanding that the idea undoubtedly has some value, in this event it will never see the light of day. If the patent is granted, however, and it turns out that granting it was a mistake, the courts will correct the error. This has been an attitude in the past. It presumably is not the attitude today, ever since the Supreme Court jumped down the throat of the Patent Office in the *John Deere* case and criticized it for its laxness. But it is conceivable that this could still be the belief—and the genuine, sincere belief—of some. Added to this is the fact that, with almost a 200,000 backlog of patent applications, there is pressure to get these applications processed, for the examiner to clear his desk. Without any question, the easiest way to clear your desk is to allow the patent.

These, I think, are the factors. Then, of course, when you get into court, you do have, in contrast to the Patent Office proceeding, the advantage—and the judge has the advantage—of somebody on both sides fighting as hard as they can. Out of this is likely to come a much clearer picture than is possible to the relatively isolated examiner.

Senator HART. You commented about the uncertainty of the social costs that might be involved if the amendments were adopted, perhaps somewhat like the approval of the patent application, because it has a basic patent codification bill here that everybody wants; if we put these on, we will find out later if there is a cost. Let me ask you to develop that just a little more fully for the record, having in mind a letter that was addressed to me from the attorney general of Texas, the Honorable Crawford C. Martin. It is a letter dated May

3, 1971. If there is no objection, I would like it to be made a part of the record at this point.

(The letter referred to follows:)

THE ATTORNEY GENERAL OF TEXAS,
Austin, Texas, May 3, 1971.

HON. PHILLIP A. HART;
Antitrust Subcommittee,
U.S. Senate,
Washington, D.C.

DEAR SENATOR HART: I am writing to express my opposition to Amendments Nos. 23 and 24, intended to be proposed to E. 643, the Patent Revision Bill. The State of Texas is vitally concerned about this attempt to limit antitrust suits involving abuses of the patent system.

My State is currently engaged in two significant treble damage antitrust actions, brought against major drug companies that are alleged to have injured the State of Texas, its political subdivisions, and its citizens, by unlawful patent licensing arrangements. In one case, the *Tetracycline* litigation, we have agreed to accept some $4.6 million dollars as compensation for the injuries done as a result of an alleged conspiracy to obtain an illegal patent monopoly over an important antibiotic drug. Another case, involving another antibiotic drug, ampicillin, is now in the early stages of discovery; it appears that our State's damages here (and those of our consumers) are also quite substantial.

In addition, the State of Texas is considering the institution of still further treble damage antitrust actions with regard to other apparently unlawful restrictive patent licensing arrangements. Treble damage antitrust enforcement of this type is a significant part of the program of the State of Texas to protect its citizens from monopolistic and restrictive practices.

Our concern over the proposed legislation is that it would seek to legitimate or provide colorable excuses for restrictive practices of the type involved in these suits, and already found illegal, thereby improperly exempting from the antitrust laws a number of anticonsumer practices that unjustifiably limit competition and injure and exact monopoly tribute from the citizens of our State. Not only would this legislation seek to immunize the specific conduct involved in the above cases from the law, but it would open a number of new loopholes, because of its vague and uncertain wording. The result would be to encourage further illegal exploitation of the public by would-be monopolists, and higher prices to the public in important sectors of the economy such as drugs.

For these reasons, we strongly urge you to oppose the adoption of these amendments, or any similar to them. This office believes that the country needs stronger, not weaker, enforcement of the antitrust laws. The proposed legislation is a step in the wrong direction. We would also appreciate your placing this letter in the record of any hearings on this matter.

Sincerely yours,

CRAWFORD C. MARTIN,
Attorney General of Texas.

Senator HART. As you can see from the attorney general of Texas, his concern is the cost that is borne by governmental units as well as individual citizens when an invalid patent monopoly is at work. He cites two major actions that his office has brought. Would you comment a little more fully on the danger that you see in restricting, as the one amendment would, the opportunity that would, as these people put it, blow the whistle on such a patent arrangement?

Professor STEDMAN. Yes. I mentioned before, as you will recall, the case of *Blonder-Tongue Laboratories* v. *University of Illinois Foundation* that was just decided on the 3rd of May. Actually, the case did not involve the kinds of problems we are talking about here. It involved a question of injection into the patent system of the doctrine of collateral estoppel. But in that framework, the court pointed out and emphasized the great public importance of the public being freed of this old man of the sea on their shoulders—the invalid patent. This, I take it, is what you are concerned about.

I would say this: If we had a situation where only an occasional patent was held invalid—a situation, unfortunately, that we do not have—then, even though it is expensive to litigate and test the validity of a patent, this would not be a matter of great concern. If we had a situation where even though a lot of patents were invalid, it would be easy and inexpensive to determine the question of invalidity, it would not be a matter of great concern. What we have is a combination of a lot of patents that are invalid and a very distressing burdensome sort of procedure for determining this question of validity. I do not know what it costs. I remember 20 years ago asking a very experienced patent lawyer who had been Commissioner of Patents—Ex-Commissioner Ooms—what would it cost to try a patent case. He said, in substance, this: "of course, you cannot generalize, but on the whole, I would rarely advise a client, it would be an unusual case where I would advise a client, either to prosecute a patent or defend against a patent unless he were prepared to spend $50,000." Subsequently, I have seen figures by people who are experienced in this field running up into six figures rather than five.

This is the problem we are faced with. What does this do? In terms of the consumer, the user of the invention, of the quasi-invention, I suppose that the cost to him is fairly obvious. Here is a monopoly—it is a perfectly proper monopoly as long as the patent is valid, but it is a monopoly—and it carries with it all of the connotations of monopoly. It means that the person is in a position to charge higher prices because nobody else can use it, in a position to keep it off the market, to limit it, to avoid the pressures of competition which might compel him to put out a better product. All of the things, really, that we talk about when we talk about the antitrust law, are involved in this particular monopoly if it is an important and significant patent. So it has this effect. To the extent that the patent is invalid, these are effects that are quite unwarranted. This is what the court is worrying about, for example, when it uses the language that I quoted from the *Blonder-Tongue* case: we must have a system in which we can open these things up so they are not a burden on the public in these respects.

This is the problem as far as the consumer is concerned. There is the additional problem, which would be aggravated by the amendments that are proposed here, that the patent may provide the basis for practices that go quite far beyond the patent itself as a result of licensing arrangements, the imposition of restrictive conditions, and that sort of thing. Finally, it is a burden to the legal structure. A case that cost $100,000, let's say, to try means that a lot of work is put upon the lawyers, it is a lot of work for the judges and the courts and everybody else. It is certainly a burden to the parties.

We cannot accept with equanimity the idea that one must be a rich man in order to have his patent effective. Whether you are the patentee or whether you are the person who is being charged with infringement, this can become a very distressing and very unfortunate matter.

I recall a case years ago, one of the early misuse cases, in which there was testimony to the effect that representatives of the patentee had said, in substance, to the defendant: "Yes, I agree that maybe the patent is invalid, but we will ruin you in the process of your proving that it is invalid."

Now, this obviously is a cost as far as the parties are concerned. It is also a cost to the patent system itself.

We should be working to figure out ways to get better patents and to get these determinations on a much less expensive basis than we have at the present time. This is where the real need is, to correct these things so that we can end up with a patent system that we can be consistently proud of.

Senator HART. Professor, thank you.

Mr. Williams, do you have any questions?

Mr. WILLIAMS. No, Mr. Chairman, thank you.

Senator HART. Professor, again thank you.

(The Statement referred to follows)

STATEMENT OF JOHN C. STEDMAN

Mr. Chairman and Members of the Subcommittee:

My name is John Stedman and I am a Professor of Law at the University of Wisconsin where I teach mainly in the areas of antitrust law and intellectual property law, including patents. I have given attention to the interaction of these two fields for over 30 years. During this time I have dealt with the subject in teaching, writing, speaking and in actual practice, including a period spent with the Department of Justice and a period as associate counsel to this Subcommittee.

The proposals before the Committee are, of course, Amendments No. 23 and No. 24 introduced by Senator Scott as proposed amendments to S. 643, the bill providing for a general revision of the patent laws. The three subjects to which these amendments are directed are (1) proposed adjustments of the patent-antitrust relationships, contained in Amendment 24; (2) proposed modification of the estoppel doctrine, in response to the rejection of that doctrine by *Lear v. Adkins*, also contained in Amendment 24; and (3) a proposed reaffirmation of the continued viability of "other" law, both state and federal, both statutory and common law, which has been threatened by certain language in *Lear v. Adkins*. I will discuss these in order.

At the outset, let me say that I consider the proposed amendments undesirable on all three points, for reasons that will become apparent as I proceed.

A. PROVISIONS RELATING TO THE PATENT-ANTITRUST RELATIONSHIP—AMENDMENT 24

The provisions in question are contained in Amendment 24. They consist of a proposed addition of a § 261(b)(2) and the addition of two new subsections (f) and (g) to § 271 of Title 35.

§ 261(b)(2), as I read it (the language is quite general, ambiguous and unclear in certain respects), would permit a patentee or patent applicant to parcel out his rights by means of exclusive or non-exclusive licenses on a geographical basis, a subject matter basis, on the basis of less than the entire right to make, use and sell, and so on.

§ 271(f) states, also in rather general and sweeping language, that a patent owner shall not be "guilty of misuse or illegal extension" of his patent rights by virtue of having "granted" less than all of his rights under the patent or imposed restrictions that are "reasonable under the circumstances" to secure to him "the full benefit of his invention and patent grant."

§ 271(g) states, in more specific language, that the owner of a patent or patent application may require as consideration for a license (1) a non-exclusive grant-back or (2) a royalty or purchase price (a) of any amount, (b) payable after the patent has expired (if based upon conduct occurring prior to expiration), (c) based upon practices or production outside the scope of the patent, (d) based upon a package of patents rather than on individual patents, or (e) which is discriminatory.

My objections to these proposals are five-fold: (1) They appear susceptible to interpretations that would have a seriously adverse effect upon the operation of the antitrust laws without any offsetting advantage in other respects. (2) They would inject a large measure of uncertainty and ambiguity into the present law (which already contains its share of uncertainties) inevitably resulting in extensive litigation and substantial relitigation of many now-settled points. (3) The proposals really involve the operation and scope of the antitrust laws, rather than the patent laws, and are out of place in a patent law revision bill. (4) Their inclusion in S. 643 is doubly undesirable, both because they prejudice and endanger the enactment of that bill and because they inject into it a highly controversial issue that should be considered, and accepted or rejected, on its own merits instead of being tied to the general revision. (5) The proposals, contrary to the contentions of their supporters, do not, in my opinion, promote the best interests of the patent system. I will comment on each of these five points in order.

1. Undesirable effects upon the antitrust laws

In introducing the amendments, Senator Scott gave examples of practices that their enactment would permit. His statement, as given, appears quite unobjectionable on the whole. Most of the objectives sought are valid ones. Most of the practices described are salutary. The statement, as I read it, falls short of giving the full picture in two respects, however. First, it neglects to make clear that most of the situations it describes are probably legal under present law and consequently require no amendments to legalize them. Second, in emphasizing the unobjectionable practices that the proposed amendment would permit, it ignores numerous highly objectionable practices that conceivably would be legalized, depending upon how the courts interpreted the amendments. Certainly, their legalization would be vigorously urged upon the courts by the proponents of such practices.

Let me give you several examples, based upon a single hypothetical situation. Assume that I own a patent on an important process for building roads and also one on an equally important composition of materials used in such road building—a composition that is also usable in building construction. Starting with these facts, what would be the effect of the proposed amendments upon the following licensing practices?

(1) I grant exclusive licenses to ten different licensees, limiting use of the process and materials by each to a separate and defined area of the United States. Each licensee thereafter confines himself to his limited territory whereas previously there has been vigorous competition between them. Faced with an antitrust suit charging both the licensees and me, as patentee, with a conspiracy to divide territories, we argue that the limitations are permissible under the provisions of § 261(b)(2).

(2) I grant a license to X to manufacture the composition but only for building roads, prohibiting sale (or, if he bought the composition from me, resale) for use in building construction, thus depriving the building trade of a useful and competitive product. I defend this practice on the ground that it is permitted by § 261(b)(2).

(3) I license X to manufacture and use the composition but not to sell the composition to other road builders whom I have licensed to use only the process—thus compelling the latter to buy their materials from me. I contend that this is permitted by § 271(f)(1).

(4) I license X to use the process, provided he buys materials usable therein, whether patented or unpatented, from me. In short, I impose a tie-in arrangement. I contend this is "reasonable under the circumstances to secure . . . the full benefit of [my] invention and patent grant." §271(f)(2).

(5) I grant licenses under both patents to thousands of road builders on condition that they grant back to me nonexclusive licenses under all patents they own or acquire relating to any aspect of road building. This results in hundreds of licenses accruing to me on every conceivable new development in this field, giving me a competitive position no other road constructor can even approach and enabling me to dominate the road construction industry for the life of my present and future patents and for a long time thereafter. I contend this is permitted by § 271(g)(1).

(6) I license X, Y and Z, competitors of mine and of each other, to make and sell the patented composition at a royalty rate based upon a percentage of sales. The royalty is determined by taking a base of 25% of sales price and *decreasing* this percentage 1% for each percentage point that the licensee's price exceeds his cost, until a minimum of 5% is reached. Such an arrangement obviously creates an inducement to up one's price and imposes a burden for failure to do so. In answer to an antitrust or misuse attack, I contend that this is permitted by § 271(g) (2) (A).

(7) I license X to use the process on condition that he pay me a 10% royalty on *all* road construction work he undertakes, whether he uses the patented process or not. I argue that this is permitted by § 271(g) (2) (B).

(8) I license X to use both the process and the composition at a royalty of 10% on the value of the material he uses, the royalty to continue until the expiration of the process patent which runs for 12 years after the composition patent expires, and to be payable whether or not X uses the process. I contend that this is permitted by § 271(g) (2) (C).

(9) I license X, Y and Z, competitors of mine and of each other, to manufacture and sell the composition. I set a royalty for X and Y of $5.00 a ton, and a royalty for Z, who is a price-cutter, of $25.00 a ton. I urge that this is permitted by § 271(g) (2) (D).

I could continue at some length with additional examples but at this stage I see no particular merit in doing so. Nor is much to be gained by attempting a close comparison of the changes the proposed amendments make, or may make, in existing law. It seems quite evident that the amendments would make substantial changes in the law, many of them along the lines indicated in the hypothetical cases I have described. Indeed, if the proposals do *not* change existing law, there does not seem much point in enacting them, barring unusual circumstances that have not been shown to exist.

Change in existing law is, of course, the privilege of Congress. The difficulty here is that these amendments, if interpreted along the lines I have indicated, would have seriously adverse effects in terms of antitrust policy, effects that I doubt any person with much sympathy toward the antitrust laws and their efforts to preserve a free competitive enterprise, would find tolerable. Would the amendments be so interpreted? I do not know, and I doubt whether anyone else does—and this brings me to my second objection.

2. Uncertainties and ambiguities resulting from adoption of the Amendments

At the very minimum, the proposed amendments would inject numerous uncertainties and ambiguities into the law, uncertainties that it would take years, possibly decades, to straighten out. Uncertainty in the law is almost always a losing business. The public is the loser, businessmen are losers, and the Government is the loser. Even the legal profession, except for the handful of lawyers who profit from the resulting litigation, is the loser. It does the profession no good, after all, to have to say, "I do not know," to a client's question, or to say, "yes," when the right answer turns out to be "no," or say "no" when the answer turns out to be "yes."

The uncertainties are not solely a result of choice in language although this contributes to them. They arise to a considerable extent from the inherent difficulties involved in reaching a proper adjustment between the antitrust and patent laws. The courts have been struggling with this interrelationship for years. Out of it has come increasing, although concededly not complete, certainty as to what one can and cannot do. Should we, at this point, through all this accumulated experience and clarification into the trash can and start out with a brand new ballgame—do it all over again under a new, as yet undetermined, set of rules? I suggest we should not. Most others who have been through this painful process, or witnessed it in action, will, I think, agree. The adjustment between patents and antitrust *is* a difficult one. There is no easy way out, no real shortcut. It would be folly, as I see it, to scrap all the accumulated wisdom and start over.

These observations would be less in point if the language contained in the proposed amendments really helped to clarify the situation. In my opinion, they do not. They add to the confusion. In addition to the examples I have already given, let's look at some of the specific wording. (1) § 261(b) (2) permits waiving or licensing the whole or part of one's "rights" under a patent or application. What are one's "rights?" Are they limited to the right to exclude others from making, using or selling the claimed inventions, or do they also include rights against contributory infringers, rights to recover damages for past infringement, etc.? (2) Conformance to the provisions of § 271(f) and (g) renders one not guilty of "misuse or illegal extension" of his rights. We have a fair idea of what constitutes "misuse," but what is the "illegal extension" the patent owner is insulated against? Does it include the antitrust laws thus creating a limitation upon the operation of those laws? Does it extend to other laws, both state and federal, that the patentee may run afoul of as a result of his licensing practices? Is the term "illegal" limited in its reference to criminal statutes, or does it extend to non-criminal regulation as well (FTC Act) and private civil actions (unfair competition)? What about other parties to the arrangement? Are they also absolved of illegality? (3) § 271(f)(2) permits conduct "reasonable under the circumstances to secure . . . the full benefit" of the invention. When one looks back on the 60-year struggle to give meaning and content to the "rule of reason" as it applies in the antitrust law, one shudders at the thought of going through the same arduous process in determining what is "reasonable" for the patentee to assert. The 45 year old statement in *General Electric* has been withering on the vine virtually ever since it was enunciated. It should be allowed to die and be given a decent burial, not be subjected to artificial resuscitation. The burden of determining "reasonableness" in this field is just too heavy to ask a judge to bear. It is even heavier for the lawyer who must advise a client as to what he can and cannot do with his patent.

I applaud the motives of those who would reduce this complex area to a neat set of simple rules. But I just do not think it can be done—that is, without doing violence to and distorting the delicate balance that exists between the antitrust law and the patent laws. Circumstances vary to such an extent in the antitrust field with respect to size of companies, both horizontal and vertical structures, types of practices, effects of practices, etc., that they render hard and fast, black and white rules impossible in most situations. Even in the most extreme cases, involving tie-ins, price restrictions, divisions of territory and restrictions on production, specific exceptions have been introduced as experience dictates, either by the courts or by legislation. Comparable variations in circumstances appear where patents are involved. In addition, entirely new variances crop up—variations involving the scope of patents, the extent of their accumulation, their competitive significance, etc. When one is faced with an *interaction* of these two areas of law, the variations and permutations increase at a geometrical rate. Such a situation simply does not lend itself to codification and the promulgation of simple rules. The Antitrust Division found this out in attempting to lay down antitrust guidelines. The problem is much greater where patents and antitrust interact.

3. The proposals relate to antitrust policy and do not belong in the Patent Revision bill

Up to this point, I have been discussing on the merits, the antitrust proposals contained in Amendment 24 and have suggested what I feel are their shortcomings. Even if they were otherwise acceptable. I would deem it undesirable to include them in S. 643. Provisions of this type, in my opinion, do not belong in the patent laws. Perhaps I can make my point clear by suggesting an analogy. My ownership of and rights in a building or a piece of machinery constitutes a *monopoly*, a monopoly created by real or personal property law. If I use the building, however, or convey it to others, under circumstances or on conditions that lessen competition, the issue now becomes a matter of antitrust law, not property law. If modifications are to be made with respect to such property, we provide for them in the antitrust laws not in the property law. So it is with patents. My patent gives me a monopoly, but what I *do* with that monopoly *beyond the clear grant given me by the patent law*, become a matter of antitrust not patent law. Failure to recognize this, I suspect, has caused much of the confusion that sometimes exists with respect to the patent-antitrust relationship. From the patent law standpoint, as long as I assert my patent monopoly I should have no fear of the antitrust laws. At least, it is hard to imagine Congress saying in one breath that it will give me an exclusive right in my invention and in the next breath charging me with violation of the antitrust laws.

But just what is this Congressionally-given monopoly? It is the right to exclude others from making, using and selling, *and nothing else*. Once I go beyond this—whether I convey my monopoly rights to someone else, whether I throw my weight behind one of two competitors by granting a license to one but not the other or by licensing one on more favorable terms than the other, or whether I impose obligations upon others as a condition of *not* excluding them—what I have done and its effect in terms of competition and monopoly are to be tested by the antitrust laws, not the patent laws. If, for example, I require a licensee to pay me money, to buy certain goods from me, to give or sell something of value (such as a grant-back) in return for a license, impose limits upon what products the licensee may produce, dictate where he sells, what he sells, to whom he sells, at what price he sells, etc.—in all such cases wherein the patentee engages in any conduct other than his patent-law-given right to exclude others from making, using or selling, the question that must be asked in evaluating his conduct from an antitrust standpoint, is this: Is the situation worse, competitively speaking or from a monopoly standpoint, than it would have been had the patentee stood on the legal rights to exclude which the patent law gave him?

Obviously, this approach can give rise to many collateral questions. Would the licensee, if not licensed, have challenged the patent? Would he have adopted or developed alternative techniques? Would he have done business in different areas, sold at different prices, or marketed different commodities? Would he have engaged in competition which, as a result of the license, he now shies away from? These, I suggest, are the real questions that one must face up to in dealing with the patent-antitrust relationship. They are, I reiterate, fundamentally questions of antitrust law and policy, rather than patent law. The provisions of Amendment 24, unfortunately, make no serious attempt to deal with these crucial issues.

The point I have just made calls for four additional brief comments:

(1) I am *not* suggesting that exemptions cannot be made to the antitrust laws if Congress deems this desirable. Such exemptions have been written into the law in the past, for instance in the Miller-Tydings amendment, the Webb-Pomerene Act, etc. If such exemptions are to be made, however, they should be recognized for what they are, namely, modifications of the antitrust law.

(2) Nor does it follow that such exemptions *must* be located physically within the framework of the antitrust laws rather than being put into the patent laws. I do suggest, however, that the antitrust laws are the more appropriate place for them, if they are to be enacted, and that their incorporation into the patent laws simply contributes to the confusion that unfortunately exists with respect to patent-antitrust relationships. I reiterate, the important point, to which physical location is secondary, is to recognize them for what they are, namely, exceptions to the antitrust laws.

(3) Much emphasis has been put upon the need for these amendments in order to encourage innovation and development. It may be that some laws of some kind are in order to achieve this objective. Up to now, however, Congress has *not* seen fit to extend the patent laws beyond the point of stimulating *invention*. Invention, and only invention, is all the patent laws are intended to stimulate. If Congress desires to go further, it should be done with that clear purpose in mind, with a careful look to see *how* this can be accomplished, with the full awareness of the possible cost in terms of weakened antitrust laws, and with careful appraisal of the possible constitutional problems. The present proposal meets none of these criteria. What I am saying, in short, is that a clear case should be made for policies of the sort proposed here. No such case has been made. Rather, the proposals have been supported on vague grounds of "reasonableness," general speculation as to what the Antitrust Division may be up to or what some court might do in the future, etc.

(4) Although I have been talking in terms of the antitrust laws, most of my comments apply equally to the "misuse" concept. Granted that the misuse doctrine is part of the patent law, at least of its procedural aspects, it is inextricably tied in and identified with the antitrust law. Basically, it constitutes a recognition that a patentee who has used his patent in such a way as to violate the antitrust laws, should not be permitted to enforce that patent where the case comes up as a suit for infringement instead of as an antitrust suit.

4. Inclusion in the Patent Revision bill prejudices the latter's enactment, and impedes consideration of the amendments on the merits

There are further reasons why these amendments should not be included in S. 643. In the first place, if enactment of the Patent Revision bill is desirable, injection into it of extraneous and controversial provisions of the type here under discussion, will lessen the likelihood of its enactment. We have evidence that this has already happened. Revision proposals with respect to the patent law have been pending before this Committee since early 1967. For four years, a bill has been before you, most of whose provisions are acceptable to the majority of interested persons. Yet, the bill lies moldering because of controversial inclusions, of which the one under discussion is a prime example. I grant you that if a provision in controversy is basic to the bill, one may have no choice but to thresh out the issue and settle it once and for all. The amendment we are talking about is not in that category. Its provisions are not essential to a viable patent statute. The Patent Commission had the good sense to recognize the extraneous nature of certain issues, such as those involving government patent policy, as matters to be handled separately, outside a patent revision bill. Unfortunately, it did not take the same approach to the antitrust aspect, although the existence of reservations in this respect is indicated by the Commission's caveat that it was not intending to curtail either the antitrust laws or the misuse doctrine, and the subsequent statement of its Chairman that inclusion of the antitrust recommendation in the revision bill would be premature. In any event, the Administration bills subsequently introduced, including S. 643, have all had the wisdom to omit these provisions. In the interest of enacting the revision bill, this wisdom should prevail.

A second reason for not including these provisions is this: Highly controversial matters, such as the subject at hand, should be considered separately by the Congress. They should be reviewed on the merits and stand or fall on the merits. They should not be incorporated into a revision or omnibus bill—again, unless they are an inseparable feature that cannot properly be considered on an independent basis, not true of the present proposals. It is probably my aversion to tie-ins, of which a rider to to a bill is often an example, that causes me to feel strongly about this. Whatever the reason, it strikes me as highly desirable that members of Congress be free to vote their views on controversial matters. They should not be compelled ether to vote against proposals such as these we are talking about because they are opposed to the over-all bill, or to support such proposals when they are against them in order to get the Revision bill enacted. Yet, this is the dilemma that a member of Congress may face if these amendments are adopted.

5. There is no real evidence that the proposals are in the best interests of the patent system

My final point concerning the patent-antitrust amendments goes to their fundamental effect upon the patent laws and patent objectives. The patent laws are dedicated to, and constitutionally limited to, "promoting the progress of the useful arts." Do these amendments contribute to this objective? A casual consideration might suggest that they do, but on closer examination, the case for this seems very thin.

The proponents of the amendments have made no really firm case for the proposals. If there were one to make one would expect them to make it. Instead, the most they seem to offer is a generalization that greater certainty in the law and greater freedom to license will (1) make patents more attractive to inventors and thus stimulate more inventive effort than would otherwise occur, and (2) encourage more licensing and thus result in more use and innovation than would otherwise occur.

The argument of "greater certainty" is, for reasons already pointed out, illusory.

What about the argument that "greater freedom to license" will act as a stimulus to invention? The picture of the inventor, who at the time of his inventive effort does not even know whether he will succeed, what his invention will look like, or what the Patent Office will end up giving him, being driven by visions of charging one licensee more than another, collecting royalties on the basis of something other than use of the patented invention, demanding non-exclusive licenses back from presently unknown and unknowable licensees, and so on, is some what fanciful. Furthermore, freedom to license is a two-edged sword. Assuming, for the sake of argument, that freer opportunity to license may stimulate some inventors to some undetermined extent, it may just as likely have an enervating effect upon others who, instead of engaging in competitive research, may find it more relaxing to take a license, especially if the license contains restrictive terms that protect them (as well as the patentee and other licensees) against competition.

As for the stimulus to innovation that may result from relaxed licensing restrictions, as I have previously pointed out this is not an objective of the present patent law as such. In any event, such stimulus to innovate may well be more than overbalanced by the detrimental effect resulting from reduced competitive research and the damper that restrictive license conditions put upon competition.

All in all, I find myself unpersuaded by the argument that failure to enact these amendments will pose any substantial threat to the patent system and impede its objectives or, conversely, that their enactment will significantly further these objectives.

Conclusion.—For the reasons given, I believe it undesirable to include the provisions of Amendment 24 relating to misuse and patent-antitrust relationships in S. 643. If the proponents of these provisions wish to press their case further, I suggest that their proposals be introduced as a separate bill independent of the Patent Revision bill.

B. PROVISIONS WITH RESPECT TO THE ESTOPPEL DOCTRINE—AMENDMENT 24

Subsections (e) and (f) proposed by Amendment 24 as additions to § 261, deal with assignor and licensee estoppel. § 261(e) would provide that no assignor of a patent shall challenge its validity unless (1) he first repays to the assignee the consideration he received, *and* (2) the ground for claiming invalidity was reasonably available to him at the time the assignment was made. § 261(f) bars a licensee from contesting the validity of the licensed patent unless he renounces future rights under the license. Also, he is held to any performance due prior to renunciation.

Let me say at the outset that most inequities of a substantial nature that may result from rejection of the estoppel doctrine, can easily be taken care of by appropriate provisions in a contract. Even if the parties fail to exercise foresight in this respect, the courts are likely to see that justice is done.

My objections to these provisions are not based upon the fact that they are unnecessary, however, but upon what I consider the undesirability of restoring any aspect of the estoppel doctrine. The doctrine, as a concept, never did make sense. The courts have been whittling away at it by one means or another for a long time. Now, they have finally thrown it out. They should have done so long ago. The courts have often said[1]—and I doubt if there are many who would challenge the statement—that the "public interest" calls for sorting out the good patents from the bad and throwing out the latter so the freedom to use technology is not impeded by patents that never should have issued in the first place. Anyone having useful information bearing on the question of validity should be in a position to produce that information, whether he be a licensee, a former owner, an alleged infringer, or anyone else.

This is not to say that some financial or other adjustment may not be proper as between assignor and assignee, or between patentee and licensee. Perhaps payments previously collected should be disgorged; perhaps not. Perhaps future payments should continue; perhaps they should stop. Perhaps rights that have been conveyed should be reconveyed; perhaps they should stay where they are. The answers will depend upon the circumstances, the understandings or relations of the parties, the equities, the effect of particular acts upon the competitive situation, and so on. These are matters for the parties, the courts, perhaps, ultimately, the Congress, to rule upon. None of these actions or non-actions should, however, be a condition prerequisite to speaking out on matters that bear upon the validity of the patent. Where matters of public interest are at issue, conspiracies of silence seem peculiarly out of place whether voluntarily undertaken or imposed by statute. When one has information that should be disclosed in the public interest, one should not be discouraged—much less barred—from making such disclosure.

It is arguable that this doctrine may discourage some patentees from licensing, especially where patents are of uncertain validity or where the patentee desires to placate one who might otherwise attack the patent head on. As I

[1] Most recently, in the *Blonder-Tonque* case, decided by the United States Supreme Court only ten days ago.

have previously suggested, however, there may be fates worse than that of a patentee using his patent in the manner that the law contemplated he should. Be this as it may, stopping the mouths of those who would challenge the patent seems too high a price to pay for any slight impetus that the provisions here proposed might give to the practice of licensing.

Conclusion.—Accordingly, I would consider enactment of the proposed additions of subsections (e) and (f) to § 261, also to be undesirable. Since both major features of Amendment 24 alike appear objectionable I favor rejection of this Amendment in its entirety.

C. PROVISIONS WITH RESPECT TO THE PRESERVATION OF STATE AND FEDERAL LAW NOT EXPRESSLY PREEMPTED BY TITLE 35—AMENDMENT 23

I turn now to Amendment 23, a one-paragraph provision which would preserve the provisions of state and federal law to a very considerable, but not clearly determined, extent. It does so by adding a new section, § 301, to Title 35. A § 301 is already contained in Title 35, but Amendment 23 would make certain changes in it.

Amendment 23 strikes me as probably less objectionable than Amendment 24. It is, of course, directed to the *Stiffel* and *Compco* cases involving a question of Illinois unfair competition law, and to certain dictum in *Lear v. Adkins* relating to trade secrets.

The basic proportion that state and federal law should be preserved is hardly something one can quarrel with. Obviously, vast areas of state and federal law, statutory and otherwise, exist that are unimpaired by the provisions of Title 35, and should be left unimpaired. The difficulty with the Amendment is its scope and prematurity.

Looking first at its scope: If one takes the language of Amendment 23 literally, and I do not know how else one is supposed to take it, it says that no other law—state or federal, common law or statutory—shall be preempted or affected by Title 35 except as to rights and obligations "expressly arising by operation of this title." The language is really not very clear, but depending upon how it is interpreted, the provision could have sweeping, questionable and confusing effects. Let me give you a few examples:

(1) The State of Wisconsin enacts a statute granting exclusive rights in trade secrets (even after disclosure) or in novel but non-inventive ideas, for a period of ten years. Since these are "rights . . . not expressly arising by operation of" Title 35, would such an enactment be considered valid?

(2) X enters into a contract with a patentee agreeing not to challenge the validity of any patents owned by the latter. Since the right to challenge validity, again, is not one "expressly arising by operation of" Title 35, would such a contract be enforceable, assuming that Amendment 23 is enacted but Amendment 24 is not?

(3) The State of Wisconsin imposes a tax on all patent rights licensed or asserted in the state. Since Title 35 provides no express rights and imposes no express obligations with respect to taxation, would such an enactment be valid insofar as Title 35 is concerned?

Equally interesting, and disturbing, would be the results if one were to *imply* the converse of the express provisions namely, that *outside law* should "not be construed to preempt or otherwise affect in any manner" rights or obligations that *do* expressly arise under Title 35. (1) Would, for instance, an antitrust decree ordering compulsory licensing interfere with the right to exclude others which § 154 of Title 35 gives, and therfore no longer be permissible? (2) Would state laws regulating sellers of patent rights, upheld as a valid exercise of the police power over 60 years ago, interfere with the right to assign patent rights provided for by § 261?

I could give additional examples, but what I have said is sufficient to indicate the nature and extent of the problems that would result if Amendment 23 were enacted. At the minimum, we would suffer through a period of uncertainty, confusion, ambiguity and conflict. Beyond this, it seems quite likely that at least some unfortunate law—unfortunate from the standpoint of both the public interest and the interest of affected parties—would result. As I have pointed out with respect to the antitrust laws, the relationship between patent law and other laws, especially those relating directly or indirectly to monopoly and competition, is a delicate one, indeed, one that is extraordinarily difficult to work out except on a case-by-case basis in the light of specific circumstances. It is not a situation that lends itself either to the Procrustean bed or the butcher's cleaver approach. Yet, these are the approaches that Amendment 23 offers.

My second point is that the proposal is premature. Granted the sweeping language in the *Stiffel* case, the extensive relief granted by the lower courts in that case warranted reversal, whatever the reason given for reversing. It does not follow at all that the Supreme Court, the bell cow in this whole business, will push the reasoning of that case to its outer limits instead of keeping a tight rein on it. Indeed, *Lear v. Adkins* itself is clear evidence of this. The majority there *refused* to carry the *Stiffel* doctrine to its logical end. It is curious that the attack on the *Stiffel* doctrine intensifies (as exemplified by Amendment 23) as the tendency to limit its application becomes more manifest.

I am not here to justify the broad rationale of the *Stiffel* case. I do suggest, however, the desirability of being patient. There *are* situations in which it is important, in the public interest, to put limits upon conduct that contains the seeds of monopoly or threatens to restrain trade. There are also situations in whch one's rights in ideas, as well as other rights, call for protection even though not patented or eligible for a patent. Over the decades, the courts have worked out these adjustments fairly well. I see nothing to suggest that they will not do so here. In any event, I question the advisability of Congress moving into the picture at this early stage on the assumption that the courts are going to mess things up, instead of its waiting to see whether Congressional action is really needed. There are times when discretion and forbearance are the better part of valor. This seems to be one of them.

Beyond the reasons given, the broad arguments against Amendment 24, to wit, the contribution to confusion, uncertainty and increased litigation; the barrier and impediment to enactment of S. 643; and the undesirability of tieing this controversial issue to the revision bill as a sort of rider, apply with the same force to Amendment 23 as they do to Amendment 24.

Two additional points may be made briefly: (1) To the extent that Amendment 23 would assure greater protection to trade secret law—and this appears to be the *immediate* objective of the proposal—it seems at least as likely to impede, as to further the objectives and operation of the patent law. (2) At the very time when increased efforts are being made to move further in the direction of a *national* law relating to competition, monopoly, marketing and various competitive practices—efforts that are exemplified by S. 647, introduced jointly by the Chairman of this Subcommittee and the author of Amendments 23 and 24, and efforts that I commend—the proposals of Amendment 23, putting as much as possible back into the hands of the individual States, represent in my opinion an unfortunate step in the wrong direction.

Conclusion.—For the reasons stated, I would recommend against the enactment of Amendment 23 at this time.

Senator HART. So that there can be some planning by those who have other chores, I would suggest that we have the testimony from Mr. Scott and depending on the hour, move to Mr. Fonda or take a lunch break. In any event, there will be a lunch break in the next hour.

We welcome the distinguished Washington lawyer, knowledgeable in this field, John Scott.

You may proceed. We will order your statement printed in the record as if fully given. You may proceed and if there is any supplementary statement you wish to make, please do.

STATEMENT OF JOHN C. SCOTT, ATTORNEY AT LAW, OF THE FIRM OF ROWLEY & SCOTT, WASHINGTON, D.C.

Mr. SCOTT. Thank you, Mr. Chairman. I would like to take a few minutes to supplement what I believe is the last paragraph in my statement, in which I deal with the matter of the lack of any factual basis, as I see it, for the Scott amendments to the pending patent revision bill.

I refer to the lack of empirical evidence as to what is needed, if anything, in the way of changes in the law insofar as the relationship of antitrust law and patent law is concerned. I think it is clear from what facts are available that the patent system has greatly changed since the provision for patent was written into the Constitution. I have read statements by many authorities that the original concept of a system for rewarding an individual inventor has pretty largely disappeared from the scene today. The assistant attorney general in charge of the Antitrust Division has already, I believe, made a statement to the committee indicating that the popular concept of the inventor in the pattern of Thomas Edison is no longer accurate for possibly as much as 95 percent of the patents now in active use; that at least an overwhelming majority of the patents in use today are patents that have been assigned by the inventor to someone else. It seems to me that creates an entirely new set of economic circumstances to be dealt with by the law and before we meddle with this very complicated aspect of our economy, we should know what we are about.

Before any decision is made as to how the patent system is to function in the future in its relationship to other requirements of the law relating to competition, we need some facts on first of all, the advantages to the public, to the consumer, if you will, of protecting restrictive licensing practices of patent owners of the sort dealt with in the Scott amendments.

Does this protection of restrictive licensing practices really encourage invention in this new set of economic facts we deal with today insofar as the relationship of invention to patent ownership is concerned? In other words, does it really encourage invention to protect assignee owners of patents? It may very well be that it does; I do not know. It may very well be that the patent system as presently constituted does indeed encourage the expenditure of substantial sums of money by the research and development departments of the corporations that control most of our patents today. But before we go meddling with the system under which these research and development departments now operate and apparently thrive, I think we need a lot more facts than I have been able to find in any statements supporting or opposing, for that matter, the Scott amendments. And these facts that we need to investigate relate not only to the advantage of protecting the patent owner in his contracting for restrictive patent licensing provisions; we also need to check out what the cost is to the public of affording that protection. We have had some worthwhile examples of what the cost is in recent years. The most extreme that comes to mind at the moment is the cost to the public of the use of a patent for Tetracycline and the use of the provisions in licenses of that patent to set a price for this essential drug at something that I believe turned out to be some four or five times what it became once the price had to be set under competitive conditions.

In treble damage litigation arising out of the Government claim of the misuse of that patent, and of the procurement of that patent, indeed, by improper means, the court is in the process of accepting a proposal of, I believe, $100 million in settlement of the claims asserted there. And from all the facts I can put together about that litigation, having been involved as counsel in the fringes of that case, it appears to me that this $100 million is possibly at most 10 percent of the cost to the public of that Tetracycline patent in terms of price that could not have been charged under lawful competitive conditions.

So the question, it seems to me, before this committee is whether there is any basis for adding to these costs to the American public in restrictive licensing benefits encouraging invention. It is really this lack of supporting evidence or supporting facts that is the principal reason for my objecting to the Scott amendments' provisions that would curtail the right of the persons most interested or most likely to take action to challenge the validity of patents.

A few minutes ago, Professor Stedman answered a question of the committee's about the remarkable percentage of patents that are declared invalid once they get into litigation, and commented on the possible reasons for reaching one result in a proceeding before the Patent Office and another in a proceeding some years later before a court. And to me, the most impressive reason he gave was the simple difference in the proceedings. The adversary proceeding, I thought, in our legal system, was always recognized as being far superior to the ex parte type proceeding that is held before the Patent Office. And I am satisfied that this difference and this added advantage of an adversary proceeding accounts for a very large number of those instances when a patent is held invalid in court.

I think we also need more facts before we set about introducing into the law language in the Scott amendments broad enough to allow expansion of even lawful patent monopolies by patent owners who more often than not bought their patent rights. We are back to the same old point here: Does it really encourage invention to protect assignee owners of patents along the lines the Scott amendments propose? And again, maybe it does. But I think we have to know before we take the drastic action proposed in these amendments.

That is all I have to say unless the committee has questions.

(Prepared statement follows:)

PREPARED STATEMENT OF JOHN C. SCOTT, ESQ.

My name is John C. Scott and I am a practicing attorney here in Washington, D.C. I am here today as a representative or spokesman for no one but myself. My interest in the Scott Amendment stems from my activities as a member of the Research Staff of the Patent, Trademark and Copyright Institute of the George Washington University, but I am not authorized to speak for the Institute.

Most of my work and that of my law firm is in the field of antitrust law. However, I do not appear before this Subcommittee as an experienced practitioner of patent-antitrust law, for no significant amount of my antitrust law practice has involved patents or patent licensing. Rather, I represent myself to be a student of patent-antitrust law—an explorer and sometimes cartographer of this shoreline where the antitrust tide rises and falls at the base of the solid rock of the patent system. Because I attribute the fears of the rock's inhabitants to their failure to clock and measure the tide, I will speak in opposition to the Scott Amendments to S. 643.

Actually, the development of my views of the appropriate relationship between the patent law and the antitrust law began with my original education in the fundamentals of these two fields—long before anyone could accuse me of being an antitrust lawyer. In the early 1950's as Assistant Editor of "The United States Law Week," I worked for a managing editor whose previous law practice had been more patent oriented than antitrust oriented. My earliest recollections in these areas of the law relate to the difficulty I had in grasping the importance of the distinction he repeatedly made between a patent license for use of the invention only in a designated field or fields and a license containing a positive prohibition against sales in other fields. In terms of its economic significance, the distinction escaped me again in 1966 when I wrote a series of seven articles for BNA's "Antitrust & Trade Regulation Report," which were distributed to subscribers of "The United States Patent Quarterly" as a pamphlet entitled "Patents and the Antitrust Laws." It was urged upon me with greater vehemence but no greater success last year when I assisted Professor S. Chesterfield Oppenheim in "An Empirical Study of Limitations in Domestic Patent and Know-How Licensing," sponsored by the PTC Research Institute.[1]

Field-of-use licensing is one of the three subjects to which I want to direct my specific remarks in opposition to the Scott Amendments. The other two are provisions restricting challenges to the validity of the patents and language validating patent-licensing restrictions that are "reasonable under the circumstances to secure to the patent owner the full benefit of his invention and patent grant." As for the remainder of the Scott Amendments, they appear either to anticipate judicial changes in the law that are not likely to occur, to attempt foreclosure of possible antitrust enforcement efforts the Justice Department has never threatened, or to restate existing law in new, unfamiliar language that is more likely to create than to resolve confusion in the law.[2]

Field-of-use patent licenses would be given explicit antitrust exemption by the Minority Leader's proposed amendments to both Section 261 (b) and Section 271 (j) of S. 643. Actually, as this Subcommittee knows, the legal precedents support the antitrust legality of field-of-use licensing. *General Talking Pictures Corp.* v. *Western Electric Co.*, 303 U.S. 124 (1938). Senator Scott's concern—and that of the American Patent Law Association and the President's Commission on the Patent System—is apparently traceable to the recent policy statements of the Justice Department's Antitrust Division and a series of government injunction suits attacking restricted-use clauses in patent-licensing agreements. But Assistant Attorney General McLaren has made it clear that he does not take exception to "a patentee reserving for himself a well-defined field out of the various potential applications for his invention." Rather, he plans to attack "the type of restriction which divides fields of use among licensees who otherwise would compete. Such restrictions in effect grant a submonopoly to each of the licensees, and all competition among those who would be likely competitors is eliminated." [3]

In the PTC Research Institute's "Empirical Study of Patent-Licensing Limitations, the most frequent type of explanation given by patent owners for granting field-of-use licenses were related to the needs and capabilities of the licensees. From 32 of the responding companies came information that they granted patent licenses designed to fit the licensee's needs or to conform to his particular market, and this explanation was often accompanied by the observation that field-of-use licensing enabled the licensor to hold down the royalty rate charged each licensee. Here again the Assistant Attorney General has made it clear that the Justice Department will not object to field-of-use definitions adopted purely for royalty-fixing purposes. "However, it is not necessary to eliminate, by contractual restriction, all competition between licensees, in order to achieve maximum royalties from various end-use applications. In some circumstances, the patentee may be able to maximize his return by, for example, establishing different royalty rates for the various uses and then offering to license freely throughout the range of applications." [4]

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[1] IDEA, Vol. 14, Conference Number 1970, p. 123.

[2] For an excellent summary and criticism of these proposals for legislative redundancy, see letter of November 9, 1970 from former Attorney General Herbert Brownell to the Honorable Richard W. McLaren, Assitant Attorney General in charge of the Antitrust Division.

[3] McLaren, "Patent Licenses and Antitrust Considerations," IDEA, Vol. 13, Conference Number 1969, p. 63.

[4] Ibid.

The Patent Bar has repeatedly challenged current antitrust trends as inconsistent with the Patent Code's declaration that "patents shall have the attributes of personal property" (35 U.S.C. 261). The antitrust exemptions sought for field-of-use licensing, I submit, would grant patent owners a special privilege inconsistent with the rules applied to other "personal property" owners with respect to restraints on alienation. *United States* v. *Arnold, Schwinn & Co.*, 388 U.S. 365 (1967).

My second principal area of concern about the proposed amendments under consideration here relates to language that would discourage or impede patent assignors and licensees in challenging the validity of patents. I refer specifically to the proposed addition of subsections (e) and (f) to Section 261. While the supporters of the amendments claim to seek incentives for innovation and invention, these amendments actually encourage the procurement and enforcement of patents. Ideally, of course, the two should not be distinguishable; procurement of a patent should occur only when there is true innovation or invention. But reality falls well short of the ideal, and, until the quality of patents can be substantially improved, to forestall or discourage the most likely challengers of invalid patents is to defeat the "important public interest in permitting full and free competition in the use of ideas which are in reality a part of the public domain." *Lear* v. *Atkins*, 395 U.S. 653, 670 (1969).

The most objectionable aspect of these amendments, from my point of view, is the proposal to add Section 271 (f) (2), adopting a general rule permitting, in patent licenses, whatever is "reasonable under the circumstances to secure to the patent owner the full benefit of his invention and patent grant." This is undoubtedly an accurate statement of the law as expounded in *United States* v. *General Electric Co.*, 272 U.S. 476 (1926). But the courts have been retreating from the holding of the *General Electric* case ever since it was handed down. And a legislative reinstatement of that rule in the terms of the proposed amendment, backed by the repeated emphasis given this "patent rule of reason" by Senator Scott is likely to induce the courts to find a congressional intention, should this legislation be adopted, to allow any agreement or conduct designed to maximize a patent owner's return.

No valid reason has been given why patent owners should not be subject to the same "rule of reason" as other owners of "personal property":

In considering whether to attack a particular licensing provision or practice, we ask ourselves two fundamental questions. First, is the particular provision justifiable as necessary to the patentee's exploitation of his lawful monopoly? Second, are less restrictive alternatives available to the patentee? Where the answer to the first question is no, and to the second yes, we will consider bringing a case challenging the restriction involved.[5]

The chief complaint voiced by supporters of the Scott Amendments has been the "uncertainty" of the law relating to patent licensing. Yet statutory language in a field such as this—and particularly the stressing of the special "rule of reason" for patent owners—is more likely to add to than cure the uncertainty. Indeed, such uncertainty as exists in this area is necessary to maintenance of the flexibility essential to rational application of the law to such economically complex problems as arise here.

In any event, the paramount consideration of this Subcommittee and the Congress must be that the law made clear and certain should promote the public interest. Yet absolutely no data, no empirical studies, and no factual basis have been compiled to show a need for the legislation proposed in the Scott Amendments. Indeed, there is not even empirical evidence to refute recent suggestions that the patent system may no longer in fact operate to promote innovation (*e.g.*, Assistant Attorney General Donald F. Turner, oral argument in *United States* v. *Huck Manufacturing Co.*, 382 U.S. 197 (1965)). Until a detailed factual analysis of this question is completed, there can be no sound basis in public policy for making the changes in patent-antitrust law proposed by Senator Scott.

Senator HART. Mr. Scott, I was reading as you went along your prepared testimony which has been made a part of the record. You discuss a survey in which you participated and which drew a questionnaire—my impression is you used a questionnaire attempting to

[5] Ibid.

find in this field of use area from licensors or others the reasons for the field of use decision. Am I correct on that?

Mr. SCOTT. Yes, Senator. Professor Oppenheim and I, working as members of the staff of the PTC Research Institute here in Washington prepared a questionnaire—one major question of which related to use of field of use licensing—and analyzed the results. I would be happy to answer any questions about it.

We did ask also for reasons for using field licensing or field of use licensing.

Senator HART. Did you frame the questionnaire—if you and Professor Oppenheim worked on it, I am sure the questions were carefully drawn. But did those who responded indicate that each had the same definition of field of use in mind?

Mr. SCOTT. Well, I think it might be helpful to look at the question we asked. We did not ask them if they engaged in field of use licensing. We had a question written under the heading, "Field of Use Licensing." But our question asked them to indicate the frequency with which they used a license permitting use of the invention for "a specified field or fields (that is, industrial, commercial, or home consumption)." Then we asked them, in addition, to indicate the frequency with which they used a form of license permitting use in a specified industry or industries; when they used a license permitting use of the invention at a specified stage of production, such as research, manufacturing, product testing; and finally, to indicate with what frequency they used a form of license permitting use of the invention in conjunction with a specified product, process, or apparatus. So within the body of the question, there was a fairly detailed definition of what we had in mind by field of use. To what extent the responders understood or misunderstood the words I just read to you, I cannot testify. But the answers appeared logical and understandable.

Senator HART. Given the language and the breakdown that you have just described, I am sure that those who were responding understood exactly what you were after. The reason I asked it for the record is because in conversations even I have listened to, I get the impression that many times, people are talking about field of use and they are on different wave lengths; they just have two different ideas.

In the responses, were you able to identify any instances where the restrictions were improper under antitrust law?

Mr. SCOTT. Well, our report made no attempt to make any judgment on that point, because obviously we did not have enough of the background circumstances to apply the antitrust rule of reason or if there is such, the General Electric patent rule of reason. So there is nothing like that in the report. I made some personal judgments that are not in any way related to what is in the report or in any way cleared by or discussed with the Institute on whose staff I serve. I reached that conclusion about a number of instances where the responders very candidly stated, well, we did it this way because we did not want competition.

And again, even this explanation or this reason made me conclude in the back of my mind that perhaps there was some illegal activity going on only with respect to some of the more extreme practices that the Justice Department has expressed an interest in. That was not true as to all field-of-use licensing, for example, because many of the reasons given for field-of-use licensing related to what the licensee wanted, not what the licensor wanted.

Now, I do not mean to say that any generalization can be made that this is the reason more often than not, because quite frankly, the responders more frequently than not did not give a reason for their licensing limitations. But where we had reasons, they very frequently and probably most often related to what had to be done to accommodate the licensee. The licensee could not afford to exploit the invention in half a dozen different fields or even two or three fields. So he wanted it limited to one because it would reduce his royalty in many instances. And the Justice Department, as I understand the public statements made by the assistant attorney general in the last couple of years, does not see anything wrong with a licensor setting different royalty rates for various fields of use. And this apparently was a principal reason for field-of-use licensing insofar as reasons were given to us in response to this questionnaire.

Senator HART. Based on your and Professor Oppenheim's experience with the survey, is this field-of-use area one of such significance that it would be worthwhile for Congress to undertake or have done for it a survey comparable to yours with perhaps the Trade Commission and its subpoena power and doing it in the event there is any withholding?

Mr. SCOTT. Yes, I would think so. I would think with the Commission's use of its Section 6 power under the FTC Act, you would get a much more complete response, possibly a more reliable response.

We had a very large number of responses. We had some 160 companies respond; only 108 filled out completed questionnaires because the others did not have patent portfolio or there were maybe a half dozen had other reasons for not getting into it. The questionnaire did take a substantial amount of someone's time to answer. It was not something you could sit down and put checkmarks on for two or three minutes and be finished.

I do think it would be useful, and again, I think this is the principal lack in terms of basis for the proposed changes in the law we are discussing here today. I think the other two areas of information are more important. That is, the degree to which protection for restricted patent licenses encourages invention; and second, the cost to the consuming public of providing that protection. Those facts, to me, are more important, but a really thorough survey of the effect and purpose of field of use licensing would be very worthwhile.

I think the most significant thing in my own analysis revealed by the study the PTC Research Institute made was the relatively small amount to which the licensing restrictions were actually used by the companies responding to the questionnaire. More importantly, perhaps, there was a clear distinction in the responses between those areas of activity in which application of antitrust sanctions has been threatened and those in which it has not. I can't remember the figures on field of use licensing, but I was very impressed, for example, with the figures on grants-back. In that area, there was substantial use of non-exclusive license-back agreements, but very, very limited use of exclusive license-back or assignment-back arrangements. And this was a pattern that ran through the responses of all the questions to an extent that makes me question very seriously all the claims that patent lawyers have trouble with understanding the application of the antitrust law to their field and need clarification.

Senator HART. I am advised that repeatedly, we have been told that those who engage in the patent practice, find it almost impossible to advise clients with respect to licensing restrictions; that the courts and the Department of Justice have so stirred the waters that they are really unable to respond to a great many of the inquiries that business addresses to them. You have disqualified yourself as a patent lawyer here by your own statement. Yet as you go on into the statement, I get the impression that you have done in an academic way a great deal of practice or study of patent law. Which way is it?

Mr. SCOTT. Well, I have studied it and written about it, but I have not represented clients in the field or done any litigation in the field.

Senator HART. Well, you have never been faced with a client who wanted an answer and you have or have not been able to give it to him because you have never had that client, is that right?

Mr. SCOTT. I have never been faced with the necessity of advising a client as to how far he can go with his patent license.

Senator HART. Well, I am sorely tempted to ask you what you think of the argument that it is impossible to give counsel, and yet as a lawyer, based on what you have just told me, I think I ought not ask.

Mr. Williams?

Mr. WILLIAMS. Thank you, sir.

With respect to the question of uncertainty, Mr. Scott, on page 6 of your prepared statement, you stated, and I quote: "Indeed, such uncertainty as exists in this area is necessary to maintenance of the flexibility essential to the rational application of the law to such economically complex problems as arise here." In this connection, the Supreme Court has held in a number of cases, though not necessarily in the patent field, that it is the duty of the Congress to write legislation and to spell out as clearly as possible exactly what the law is and what it is not. Therefore, would you agree that it is the responsibility of the Congress and this subcommittee to try to clear up the uncertainty surrounding this area of the law?

Mr. SCOTT. Well, you are asking me a question that requires me to assume that there is uncertainty that needs to be cleared up. The problem is if you eliminate the uncertainty—if all the provisions of the law these people want changed were certain—they would be screaming just as loud for the change. I do not think that clarification is the only purpose here in the first place; I think change is the principal purpose and that is based on lengthy conversations with supporters of this legislation, as indeed, most of my friends in this field are. Most of the people I have worked with in this particular area are, I believe, supporters of the amendments. I am somewhat at a disadvantage, I suppose, in answering your question because I find so little uncertainty among them. They are very knowledgeable people and perhaps for that reason, they are not representatives of the group that feels the need for clarification.

But I do not think it is ever going to be possible to clarify it. Professor Stedman has already pointed out this morning that there are more unclarifying features in the Scott amendments than there are in the existing law.

Mr. WILLIAMS. But, what I was referring to, Mr. Scott, was language appearing in your statement at the bottom of page 6, which indicates that you feel uncertainty is needed in this area of the law.

Mr. SCOTT. There is uncertainty throughout the antitrust field of law insofar as you have, at any time, to apply a rule of reason. It is the same uncertainty you have in applying the standard of a reasonable man in a tort action. There is no way to resolve that ambiguity and I do not think the patent bar wants it resolved if it really knows what it wants. Because the problems created in the business world, in the economic field by per se rules on competitive activity were, I thought, well known and generally accepted by the bar. So I do not—I stick with the statement that I do not—see any point in writing per se rules, which is the only way of resolving areas of uncertainty.

Mr. WILLIAMS. One of the other points, you made, which appears in your statement on page 7, is that there is not sufficient data available to show a need for this legislation. However, as I am sure you are aware, the President's Commission on the Patent System a few years ago studied the relationship between the antitrust laws and the patent laws for a period of some 2 years. One of their recommendations is contained in the Scott amendments. I take it, therefore, that you do not think the study conducted by the President's Commission was sufficient in this area?

Mr. SCOTT. No, I did not find the statistical information in there that is needed to make the judgments we are talking about today. I did not find it there at all.

Mr. WILLIAMS. One other question, Mr. Chairman.

On page 5 of your statement, you stated that one of your principal areas of concern had to do with the language to be added to section 261(1) and you stated that this language would discourage patent assignors and licensees from challenging the validity of the patent.

Well, now, under the *Lear* case do you not think that it encourages the challenging of the validity of patents? In other words, do you not think that as the situation now stands, the assignees or the licensees are encouraged to challenge the validity of these patents?

Mr. SCOTT. That is right. I think the *Lear* case adds encouragement to challenging the validity of patents.

Mr. WILLIAMS. Is that exactly what we should have in the patent system? As I read the language here, the assignor could still challenge the validity of the patent, if he returned the price paid for the assignment. Do you not think that it would be fair to require the Assignor to return the consideration received if he is going to challenge the validity of the patent?

Mr. SCOTT. I do not know whether it would be fair or not. You are looking at the problem from the point of view of the two litigants, the two parties to the assignment or the license or whatever we are dealing with and I am looking at the problem from the point of view of the public interest. I guess I feel that it is more important not to have improperly maintained monopolies around than it is to worry about fairness between the two litigants. I am not sure that is my position. Perhaps I have not thought it through carefully enough. But I am prepared to make that the answer to your question now, that I am more concerned about having the public and the consumer pay prices brought on by monopolies that do not properly exist than I am in worrying about the technicalities of the fairness between the two people who signed the agreement.

Mr. WILLIAMS. Thank you, Mr. Scott.

That is all the questions I have, Mr. Chairman.

Senator HART. Thank you very much.

I would suggest a recess until 2 o'clock.

(Whereupon, at 12:40 p.m., the subcommittee was recessed until 2 p.m. of the same day.)

AFTERNOON SESSION

Senator HART. The committee will be in order.

We are glad to have the testimony reflecting the views of the American Society of Inventors presented to us next. As I understand it, it will be done by Mr. Albert Fonda and by Mr. Burke Wilford.

STATEMENT OF ALBERT G. FONDA AND E. BURKE WILFORD, AMERICAN SOCIETY OF INVENTORS

Mr. FONDA. Senator, my name is Albert G. Fonda. I am an engineer by training. I have long been employed in industry but am presently self-employed as a consulting engineer and would-be successful inventor, so I have seen various sides of the question. I am a past president of the American Society of Inventors. Our prepared testimony contains our remarks on behalf of the American Society of Inventors regarding the amendments as we understood them.

We appreciate the diversity of opinion regarding the probable consequences of these amendments. The individual inventor wants to have the right to divide his invention, to license it according to field of use and geographically, rather than be forced to sell it to big business. Our endorsement of these amendments is made on the assumptions that this right is currently endangered, that it can be thereby secured, and that there should be little side effect or, from our viewpoint, misuse of the rights so conferred. If these are incorrect assumptions, our endorsement would no longer apply.

I think we all agree that big business is powerful enough as it is and I believe we all share the objective of helping the small businessman and the individual inventor. The question is simply one of how to do it.

In amplification of our prepared testimony, from the small business viewpoint, which includes the individual inventor as soon as he turns from invention to marketing, there is a need for exclusive licensing to avoid fighting over an undeveloped market while paying off huge tooling, advertising, and distribution expenses.

The problem here is to distinguish this situation from that of the fully developed market in which the patent holders are attempting to preserve the status quo rather than to change it.

I would like to endorse Commissioner Brenner's suggestion of a patent continuance fee of $500 or less every 5 years. This would imply a reduction of the initial fees which discourage the shoestring inventor much more than they discourage big business. There are enough requirements of form to prevent trivial applications regardless of how small the fee, even if the inventor avoids the costs of patent drafting and the patent lawyer by doing it all himself as I have done and am continuing to do.

The continuance fee would also have the good effect of encouraging abandonment of the invention to public use in the event the holder is unable to profitably market the invention.

Actuarial study may show that the continuance fee need be only some smaller amount, such as $200. This would net $600 in three installments, at the most; on the average, it should net at least $200 per patent granted, or enough to equal the present average fee per patent at application and issuance.

I will be glad to answer your questions at this time or later. There will be further remarks offered by my fellow past president, Mr. Burke Wilford.

(Prepared statement follows:)

Statement of the American Society of Inventors Presented by Albert Fonda and E. Burke Wilford

Testimony by the American Society of Inventors on the Amendments Offered by the Minority Leader to S. 643.

The American Society of Inventors has been studying improvements in the patent system for the past five years of its 18 years of existence. We now endorse the Scott Amendments, with comments and additions as follow.

Our Society testified just four years ago before this committee of the 90th Congress, in hearings pursuant to the previous patent law revision bill, S. 1042. We are pleased to find that very few of our objections to the previous bill apply to the present bill. Whatever effect our previous appearance may have had in this regard, we are glad to have been of use in strengthening the patent system.

Our endorsement of Amendments 23 and 24 is based on the very cogent arguments presented with their introduction and published in the Congressional Record of April 8, 1970; and the further similar arguments presented as a paper by Dr. Howard I. Forman before a workshop on Anti-Trust Issues of the National Industrial Conference Board, March 11, 1971. We agree with the illustrations given of the need of the small manufacturer (more than the large) to divide the licensing of his invention geographically and by use. The illustration of Company A on page 8 of the aforementioned Congressional Record is excellent. It is further mentioned on page 9 thereof that the situation of private inventors "can readily be envisioned as even more difficult, for they must often rely on licensing to bring their inventions into public use."

The private inventor particularly needs to be able to divide his license in order to retain a field of activity for himself. His invention is usually his life's dream. Why should he be forced to sell in toto, or live in fear of an anti-trust suit? He may have spent almost his life's savings to bring his invention to the point of readiness for production. If he can then license it for use on the western side of the Mississippi to the Rockies, he can finance his own development of the area on eastern side. Furthermore, he can license it to someone, who is the right size, to want only the west coast of U.S.A.; so we end up with three thriving small businesses rather than one burgeoning big one. The argument for dividing the field of use is exactly the same. Why force inventions to be developed only by companies large enough to do the whole job themselves? To do so is actually to work in favor of monopolies and trusts!

Apparently, the Justice Department wants to make people afraid to enter into licenses for less than all of the rights of a patent. We say that this will hurt us, the inventors of America, and it will hurt America. It is actually pro-trust, not anti-trust.

The Scott Amendments will keep the judicial situation from getting any worse; they will preserve present practices; they make a lot of sense when the patent is compared with any other kind of personal property; and they fulfil the intent of the original Patent Commission Report, Recommendation XXII, as well as the Constitutional intent on which the entire patent system is founded: to promote the progress of the useful arts.

We would like to suggest some further additions to the Scott Amendments or to S. 643. Based on the recent California action (Central District, 69–75–JWC), and using much of the same wording, we propose additions to Section 261 as follows:

Inserts: additions to Section 261.

(h) It is unlawful for any assignee or licensee of any U.S. patent to (1) combine or conspire to prevent, restrain or limit the development, manufacture installation, distribution of any device covered by the patents; (2) enter into, adhere to, and force or claim any rights under any provision, agreement, understanding, plan or program with any other person to:

(a) utilize a patent pool, cross license agreement or any plan or program for the purpose of circumventing payment of royalties or moneys otherwise payable to an inventor or reduce incentives for invention.

(b) deprive an inventor the right to receive a reasonable royalty or payment for a patented invention or limiting the incentive for licensing or buying a patent.

Furthermore, in the spirit of Sections 191 and 192 of the proposed law, wherein showings of prior publications or patents may be made only within six months of issuance by the public, or within one year by the prior inventor, we propose a further statute of limitations to strengthen the patent after a considerably longer time; an addition to Section 281 as follows:

(d) No defense shall be brought in patent litigation by contest of the validity of the patent unless it is commenced within six years from issue of patent, except where the validity is contested on grounds of fraud.

This is in keeping with Japanese law; its workability there should be considered. We would like to hear arguments pro and con, on all of our suggestions, of the caliber of those presented on the present Scott amendments.

Some of the comments we made in our previous Senate testimony still apply; we have not abandoned our position in regard to the unhappy role of the employed inventor, both in regard to lack of fair compensation over and above the regular salary for inventions which his employer does use, and also with regard to discouragement of his own use of inventions which his employer has no genuine intention of using. Some version of the German patent system where there is a minimum of ½% royalty for the employed inventor, may be the solution of the former problem, perhaps to be embodied in the Moss Bill before the House Representatives. The second problem has received less attention. We did bring it to the attention of this committee four years ago, and in even greater depth in our July 22, 1968 communication published in the hearings of Subcommittees of the Select Committee on Small Business, on Planning, Regulation and Competition: Automobile Industry—1968 (page 887). We caution now, as we have before, that employers throughout the country are thoughtlessly trampling on the vineyards of inventive ability, merely because they think they "might sometime" use an invention of an employee. Many large companies are liberalizing their disclosure agreements.

The recourse should be some arrangement for recapture of the invention by the inventor on grounds of indiligence. Present Armed Services Procurement

Regulations presently have a clause (IX Part 1A–4) requiring the contractor to "provide notification, where the contractor elects not to continue prosecution of a U. S. patent application, within sufficient time to allow the government to continue prosecution." Surely, the inventor deserves the same right, if both contractor and government so elect. He should also have the right to apply for the patent even if the employer does not take it that far before abandoning the invention.

We hereby request consideration of this committee of an amendment to S. 643 which would provide for recapture of rights by an inventor on grounds of indiligence by an assignee or substantially unrestricted licensee, at least in instances of assignment agreed to as a condition of employment, prior to the date of conception of the invention, and/or for trivial specific compensation. We grant that safeguards are necessary to avoid misuse when the rightful owner sincerely contemplates future use of the invention, so that the public might best benefit from the development and marketing of the invention. Such an amendment might properly modify Section 261 to a further extent.

In summary, we endorse the Scott Amendments for the good and sufficient reasons noted above, which are for the public good, and we request the consideration of certain further amendments which may be equally to the benefit of the public.

Senator HART. I think we would be better off to hear Mr. Wilford, but first, may I thank you for the thoughtful, balanced introductory comments you have made. It reflects, I think, a very responsible tone.

Mr. FONDA. Mr. Wilford reminded me that in rewriting my notes, I left out the point that we would like to see a $500 fee applied to assignment to further help the individual inventor by reduction of the initial fees, also to discourage assignment so that the position of the inventor as the owner of the invention and licensee of the invention would be strengthened.

Senator HART. We will have that recommendation.

Mr. Wilford?

Mr. WILFORD. My life has covered, three generations, in inventing. My grandfather promoted—he did not invent it, but he developed the meat chopper which started the hamburger business. From 1875, just before the centennial, until 1910, we had successful inventors associated with the family, doing things to help the housewife in the kitchen. Coffee mills; hand irons, cherrystoner, etc.

My father helped apply electricity to dentistry. Unfortunately, he died from working too hard in his forties. My brother and I inherited that business when I was just out of college and made a success of it. In 1928, I joined the Lindbergh boom and went into aviation.

In aviation, we are one of the pioneers in the helicopter business. Sikorsky, who is generally recognized as the developer of the helicopter, credits our work with first flying the control system which is now used in all helicopters.

Today we are working in the environment, the smog field, and I am very familiar with the situation in Detroit because I was fortunate enough to work with General Doolittle and for the famous William Stout at the time of Willow Run. So I think we could say that I am pretty well acquainted with how patents are treated, inventors are treated, in the automobile industry as well as the aviation industry.

My plea here is that we have heard a lot of problems but very little on solutions. We think that the Scott amendments should be used for the purpose of clarifying the law, but should be amended to cover any real fears that the Department of Justice, the Federal Trade Commission or our professor friends have. We are certainly smart enough. You should be able to work out a solution by taking what the Scott amendments attempt to do, and add to them the improvements that we suggest and whatever the antitrust group feels are absolutely essential. I am afraid if we do not do this, the Patent Reform Act will be a mere form rather than any real help to invention or inventors, patent lawyers, or the courts.

Now, there are a few things we would like to mention. In our statement, we say that all the Scott amendments should include a provision which would bar all pooling of patents or cross licensing of patents. I know in the aircraft industry, when the Wright Bros. and Curtis were building their early planes before World War I, they had a costly patent fight over a very simple thing. The Wright's connected the ailerons with the rudder directly and Curtis connected them through the pilot. Finally, the government decided they should step in and they formed the Aircraft Manufacturers Association, which is still in existence. I think that this system, as now used, has destroyed incentive in the aircraft business for new ideas. You have to be a manufacturer to belong to it, so the private inventor is in practice barred from any compensation unless he goes through a manufacturer.

The same thing is true in the automobile industry. Although they have men and committees for new devices. The patent lawyer or the chief engineer, in any of the big companies, and the vice president of engineering, they do not want new ideas, not because they willfully bar them or contrive to bar them, but the not-invented-here complex enters into any big business. I know this for a fact because I tried to sell something to Dow at the time I was working at Dearborn. When we got all through and had a deal all worked out, a very reasonable thing, an anticorrosion treatment for magnesium, Millard Dow (God bless him, he died in an airplane crash) turned to his chief of research and said, why didn't you think of this? The not-invented-here complex should be reduced by every possible means.

Therefore we propose that pooling, cross-licensing or any plan to prevent the payment of royalties directly to inventors or patent holders should be barred. That could be added to 261.

The other thing that seems to have been the main question of these discussions here is about validity. Now, I do not know whether you know it or not, but Japan sets a time limit upon which you can attack the validity of patents. I think it has worked very well in Japan and we should do it here. We could set 6 years after issue in which you can attack the validity of patents. If a patent is issued and it is not clearly invalid, you should not attack it after that time.

So, briefly, these are two points which we brought up which will solve two of the major problems that have been discussed here. I think that the patent bar realized that if they want clarification, they should put a time limit on attacking validity and that pooling of patents should be eliminated.

Thank you very much. If there are any questions, I will be glad to answer them.

Senator HART. Thank you. As I listened, I realized how discouraging it must be for inventors to have to look to members of Congress to inhale enough of the basic problems of the inventor as the source from which he has to draw the ground rules under which he can operate. But however I would feel about that, as the kids say, that is the way the system works.

Mr. WILFORD. We are not bitter. We think it is just thoughtlessness and habit. We do not think people have conspired against us. We think everybody is for us, but it just happens that the system should be improved.

Senator HART. Mr. Wilford, you made particular reference to the pooling problem. As I understand it, section 271(g)(1) of amendment 24 provides that no patent owner shall be guilty of misuse or a legal extension of patent rights because he enters into or will enter into a license only provided it requires that the licensee give him back a non-exclusive license. It seems to say that it is all right to have an open pool, to get access to it the applicant has to put his own patents into the pool, or future patents if he gets them. Explicit to that question, how do you feel about such a thing?

Mr. WILFORD. I think all pools are bad. There are many ways that keep the inventor from getting anything. What is the use of a member of a pool licensing a patent from you to have a sales advantage, if he has to give it to everybody else?

Senator HART. You do not think that pools are the kind of arrangement that is reasonable in the circumstances, to use that phrase, to secure to the owners of the patents in the pool the benefit of their invention in the patent.

Mr. WILFORD. Individual inventors seldom belong to pools. They destroy incentive and they destroy the licensing market for the inventor.

There are other pools. I only cited two, but I think all of them should be liberalized or band.

Senator HART. And in your testimony, Mr. Fonda, you are recommending that inventors, particularly the smaller independent inventor, should be able to divide the licensing of his invention geographically and by use. Am I correct on that?

Mr. FONDA. That is correct, yes.

Senator HART. Yet how far can we go with that concept? For example, would you condition your answer on providing there is no anticompetitive effect or intent? Think for a moment of the situation you mentioned dividing the territory east and west of the Mississippi. Would you think it proper for Westinghouse and GE to license each other exclusively, one east and one west? Would that not offend you?

Mr. FONDA. This, of course, is a spectrum of situations and it is much easier to point out the extremes than to decide just where to divide them one from the other. I would not really venture to be lawyer nor to know how to divide them. I simply point out that there is the extreme, at least, that the individual inventor can't possibly develop the whole United States in a given venture and in that extreme, must be protected.

Senator HART. I do not think you would have to do much, if anything, to identify the particular example I gave you as one that would have enormous anticompetitive effect.

Mr. FONDA. I presume it would be, but I hesitate over where it would lead me. I have not given it enough thought.

Senator HART. We are stewing with the same problem ourselves. I cited as just an example the kind of problem we are wrestling with.

Mr. Brennan?

Mr. BRENNAN. No questions.

Senator HART. I wish Mr. Wilford was the last witness, because I would like to ask him about efforts, if any, he has made to sell automobile manufacturers bumpers.

Mr. WILFORD. Well, I have made efforts to sell smog devices. Unfortunately, my device was not quite perfected enough to satisfy the 1975 requirements. It would satisfy the 1972's and I hope they may put it on old cars. But it had to do with back pressure in the exhaust system which gives a better explosion when you run around town. That, of course, is removed when you get on the highway. But we found in our sales trials that we just could not sell people on putting back pressure in the exhaust system so we are now in a position where we are forced to try to get it on new cars. And I will have more experience in a little while on whether the new people—they admit the theory is good, but just how you do it, is not yet developed.

Senator HART. The automobile manufacturers feel toward Congress as inventors must feel toward us as we write patent laws. We wrote a safety standard, an environmental standard for 1975 which they are convinced to their fingertips the technology will not permit them to meet.

Mr. WILFORD. I think the 1975 standard is a little too rigid. If we had 1972 on all cars, including the old ones, we would be way ahead, rather than worrying about being so perfect in 1975.

I will tell you one other thing I want to say. And this is something the committee ought to go into. In the German and the Japanese law and some other countries, the captive inventor, over and above his salary, gets approximately a half percent royalty on what the patent covers—not the whole machine, but the particular part. And this has had a great deal to do with the scientific growth of Germany and Japan. I think we should adopt this here, including reduction cost and length of litigation in the courts and the Court of Claims.

Now, there is a bill put in by the professional engineers of California called the Moss bill. Everybody sort of laughed at it but I think your committee should study the problem of the captive inventor, because there are just not any incentives if you are working for a big company inventing things, even though they do not have to do with your job. You do not hire people to invent. You hire people to work. Invention is an excess effort.

Senator HART. But that Dow man had the incentive even without that one percent to try to avoid having Mr. Dow turn to him and ask why he hadn't thought of it.

Mr. WILFORD. My inventor associate was a Government employee and Government employees in those days had commercial rights.

Unfortunately, there has been some shadow cast on that and it has reduced incentive for invention for Government employees. It can still be done, but 80 percent now of the Government employees turn all their patents rights over to the Government. As soon as the Government owns the patent, there is no incentive to develop it commercially here. Who wants a license on something everybody else can have free.

Mr. FONDA. Senator, our president, John Liu, hoped to be here and he asked me to remark if it fitted in, which I think it now does, first of all to identify that he is an executive in industry. Philadelphia Gear to be exact, and that he feels that the inventor is not properly compensated, the employed inventor is not properly compensated and that any steps in that direction are appropriate.

He also gave me permission to point out one thing that impresses me very much about that company, Philadelphia Gear, that they have no disclosure agreements with their employees. The employee is free to negotiate with his employer without any prior agreement and with equal rights under the patent law.

Senator HART. And the firm has prospered?

Mr. FONDA. Yes.

Mr. WILFORD. Yes. Industry and government should increase their incentives and rewards for inventors and creative scientists and liberalize disclosure and employment agreements.

Senator HART. Thank you very much, gentlemen.

(Subsequent submission follows:)

Mr. STEPHEN G. HAASER,
Chief Clerk, Senate Subcommittee on Patents, Trademarks, and Copyrights, Washington, D.C.

DEAR SIR: Following a presentation on May 13, on behalf of the American Society of Inventors by Messrs. Wilford and Fonda, it was indicated that the committee would be willing to receive a brief summary letter regarding the position of the Society in connection with patent reform.

It is the position of the Society that the individual inventor will be encouraged to develop and disclose his inventions if he will be assured of a royalty continuing for the life of any patents granted for his invention.

The Society is in favor of legislation which will prevent blanket assignments of future inventions, particularly where every employee must agree to make such an assignment as a condition of obtaining employment, either as an employee of the company or as a consultant to the company, where he is not employed to invent.

Under present conditions, the independent inventor rarely has the capital funds necessary to initiate litigation defending or asserting his patent, particularly because of the high degree of uncertainty regarding the patent rights which are granted by the U.S. Patent Office. The Society believes that the amendments proposed by Senator Scott, with proper safeguards, will clarify the rights embodied in the grant of a patent and thus will reduce some of the uncertainties in litigation and contribute to reducing the cost of litigation.

The Society is opposed to increases in government fees for filing and issuing patents, since such increases would be deterrents to the disclosure of inventions to the public. The Society believes that increased revenue, if necessary, should come from those who are profiting from the patent system, i.e. the manufacturers who are enjoying the fruits of invention by producing products in accordance with the patents, those who obtain complete disclosures of the inventions by purchase of patent copies, and those who are maintaining a competitive advantage by the use of patents to prevent others from copying their inventions. Such increased revenue may be derived from a fee based on assignments and licenses of patents, an increased fee for patent copies, and a periodic maintenance fee for the continued enforcement of patents.

Other incentives to use the patent system to encourage disclosure of inventions to the public include such provisions as a statutory period beyond which patents become incontestable as to validity, elimination by suitable legislation of industry-wide pools in which all inventions in that industry are drowned, and statutory procedures for permitting the individual inventor to enter the courts to defend his patent rights against usurpation by providing a system such as the Federal Deposit Insurance system whereby individual patent owners, through the payment of a small fee, may be assured of the opportunity to use the courts to defend the patent without entailing the risk of personal loss of the vast sums presently required to litigate.

Respectfully submitted.

AMERICAN SOCIETY OF INVENTORS,
By ALBERT G. FONDA.

Concur: JOHN K. LUI, *President*.

Senator HART. Professor Glen Weston of the law school at George Washington University—As we have with the others, professor, we will put your statement in the record in full and as you go along, feel free to make any comment you want.

STATEMENT OF GLEN E. WESTON, PROFESSOR OF ANTITRUST AND TRADE REGULATION LAW, GEORGE WASHINGTON UNIVERSITY LAW SCHOOL

Professor WESTON. Thank you, sir. I shall try not to cover all of it so as to conserve your time. I do want to hit the highlights, so I will follow fairly closely on the text of it, but will try to condense it some.

My name is Glen Weston. I am professor of antitrust and trade regulation law at George Washington University Law School, but appear here solely as an individual and not on behalf of any institution, organization or client.

My experience in antitrust law consists of former active practice with a Washington, D.C. law firm, teaching of antitrust and trade regulation law for approximately 18 years at George Washington University, at Northwestern University Law School and at the University of Michigan Law School. I am coeditor, with Prof. S. C. Oppenheim of Federal Antitrust Laws—Cases and Comments (3d ed. 1968).

I am not appearing here on behalf of any client—past, present or future—but felt moved to appear here because of my interest in both Federal antitrust policy in which I believe strongly and Federal patent policy in which I also believe strongly. I also was motivated to appear to dispel any possible notion that the group of antitrust teachers who signed a petition in opposition to the Scott amendments represented the view of all antitrust teachers. The petition that was circulated was sent to me and I declined to sign it. I am sure there were some other antitrust teachers who agree with me, though I made no attempt to circulate any counter petition.

My purpose in appearing here is to support what I consider to be the two most important objectives of the Scott amendments—(1) The proposal to codify the traditional standard for determining the validity of limitations and conditions in patent licenses, and (2) the proposed section 301 which would declare that it is lawful for business concerns to continue the long established practice of licensing technological trade secrets and know-how.

First of all, I think there is a need for legislation to codify the traditional standard for determining the validity of patent license limitations or conditions. In 1926 the Supreme Court in *United States* v. *General Electric Co.*, 272 U.S. 476 laid down the basic standard that has been used for 44 years to determine what kinds of limitations or conditions can be used in patent licenses. The Supreme Court held that a patent owner may license upon any condition that is "normally and reasonably adapted to secure the pecuniary reward" to which the patent entitles him. I think this is a flexible and reasonable standard that has been interpreted to permit a concern owning a patent to use sound business judgment in determining how it can most effectively obtain a good return on its patent. At the same time, I believe it has permitted the Department of Justice to challenge successfully the use of license limitations when they are used as an excuse to restrain trade unreasonably or in any attempt to cartelize an industry.

1. The principal reason why legislation is needed to codify this traditional standard is that the Antitrust Division has indicated that it plans to change the law on a case by case basis to create a rule that will, in my opinion, make patent license limitations or conditions presumptively unlawful.

Assistant Attorney General Richard McLaren has indicated that he will seek to apply a new and much more rigid test for determining validity of patent license limitations. Under this test he asks two questions: (1) Is the provision necessary to the patentee's exploitation of his lawful monopoly? (2) Are less restrictive alternatives available to the patentee? If the answer to the first question is "no," it is not necessary, or the second is "yes" justice will probably challenge the restriction. See McLaren, Patent Licenses and Antitrust Considerations, 13 Idea 61 (1969). For similar views by other Antitrust Division officials, see Donnem, "The Antitrust Attack on Patent License Provisions," 14 Antitrust Bull. 749 (1969); Stern, Future Look at Patent Fraud and Antitrust Laws, 52 J.P.O.S. 3 (1970).

I understand there may be some question as to whether Mr. McLaren would now adhere fully to this precise formulation. I read his statement before the committee the other day very carefully. I see nothing recanting from that formulation in any way, although he did not repeat it. I would suggest that it would be very constructive if this committee would request Mr. McLaren to make a clarification in this respect to find out what his current view on what the test for determining validity of patent license limitations is or should be.

I also want to qualify my citation here in my statement concerning Mr. Stern's article. Mr. Stern points out to me that his formulation, his article, which was, I believe, written at a time he was with the Department of Commerce, is slightly different. I do detect some differences; I think they are rather subtle differences. I am not sure that I understand them fully, but they may be of some practical significance. Nonetheless, they still strike me as being a substantial departure from what has been the traditional standard.

Now, I think what this new test means in practical terms that Mr. McLaren has stated—and that was stated, by the way, by the former director of policy planning, Mr. Donnem—is that Justice Department will ask the courts to consider patent license limitations to be presumptively unlawful, thereby shifting the burden of proof to the patentee to prove both necessity and the unavailability of less restrictive alternatives. In other words, the patentee may in good faith license his patent with limitations that have traditionally been considered as reasonable and lawful in the belief that he is acting reasonably to exploit his patent but the Department of Justice years later may apply 20–20 hindsight to decide the conditions were not necessary or that less-restrictive alternatives were available to achieve his purpose.

This analysis is based upon an analogy to the common law "ancillary restraints" doctrine. But let me point out one significant way in which I think this differs; to my knowledge I have not heard this from previous witnesses. That is that unlike the usual ancillary restraints situation, such as the sale of a business coupled with goodwill, for example, where a restraint is used to make sure that you convey the goodwill, in the case of a patent license restriction, the effect of a wrong guess is to render the patent unenforceable because of the misuse doctrine, which would result in the very harsh consequences of a forfeiture of the patent property.

Now, there is not a similar kind of penalty or forfeiture that would take place if it is the sale of a business or property of other kinds. This, I think, makes it a rather harsh consequence not to know what the existing rule will be concerning the validity of patent license limitations.

In my opinion, the Department of Justice formulations, whether you take either Mr. McLaren's statement or Mr. Stern's article, would constitute a major change in existing law, I think such a policy change if it is going to be made, should be made by Congress after full hearings and consideration of whether there is a need for such a change and the impact it would have upon the patent system.

What I am really saying is that perhaps the ones who should be here proposing a legislative change should be the Department of Justice rather than the proponents of the Scott amendments; since apparently, the Department of Justice does plan to make a change in what has been the traditional law concerning the use of patent license limitations.

Now, I want to emphasize that I have great respect for Assistant Attorney General McLaren and for Richard Stern, Chief of the patent Unit. They are both very able lawyers, both very good friends of mine and I do not in any way question their good faith and sincerity. But with all due respect, I believe this is an attempt to bypass Congress, to bring about a fundamental policy change in basic antitrust law, patent antitrust law, because they believe they can get it easier through the courts than they can get it through Congress.

To me, this is disturbing, because I think it is subverting the role of Congress to determine patent policy that it is given by the Constitution. I think it is also unwise because it seeks to make a basic policy change in the narrow context of the record of a particular case without affording everybody who may be adversely affected the full opportunity to present their views about the impact of it, without affording them an opportunity to have full evidence concerning the economic impact of that kind of change and its impact upon patent licensing.

I think there are a lot of fundamental questions that ought to be weighed carefully before that kind of basic policy change is made. For example, would the inability to use patent license limitations have a significant effect on discouraging the licensing of patents? Now, they say it would not, but there is no evidence, really, to indicate that it would not. So it is purely speculation.

Second, would the inability to use patent license limitations severely handicap smaller business concerns who may lack the capital to exploit their patents fully but need protection against larger licensees?

And finally, would the inability to use limitations result in licensors charging higher royalties? I do not purport to know the answers to these questions, but I think they are the kinds of policy questions that should be considered very carefully before a fundamental change of the type that Mr. McLaren apparently has in mind is made.

I think the result has been that the Department of Justice has created uncertainty for licensors by indicating that it is going to challenge license limitations that have long been permitted by judicial decisions. By proposing to create a presumption of invalidity for patent license limitations and by indicating that it will seek the overruling of the *General Electric* and other patent antitrust cases, the Department of Justice has created major uncertainty for patent licensors. I think the significant area and to me one that is probably the most important economically and from the standpoint of patent licensing—the type of restriction I have in mind—are field of use limitations which apparently the Department of Justice has indicated they plan to limit fairly significantly, but which have traditionally been upheld when "normally and reasonably adapted to secure pecuniary reward." Mr. McLaren's "necessity" test and an inquiry as to whether there are less restrictive alternatives available kind of test would, I think, create considerable uncertainty in licensors as to when they could or could not use field of use limitations.

To me, existing case law furnishes a useful guide under the "normally and reasonably adapted" test, but under his proposed test, there is no useful guide available.

Now, it has been asserted—I believe I have heard Mr. Ward of the Federal Trade Commission assert—that if there is uncertainty here, patent lawyers can get guidance through the Department of Justice's Business Review Letter procedure or through the FTC's advisory opinion procedure. But I think this is largely illusory here, because one of the classic limitations that you have on the use of those procedures to get advice is that they will not give you advice if it depends upon complex decisions or lengthy investigations. They may give you a "no" answer quite readily if it is one that they clearly think is unlawful, or they may merely give you a statement, we cannot undertake to grant clearance at this time, without indicating whether they would regard it as invalid or whether they would regard it as merely, say, in the general area of rule of reason and so forth. So that this does not give, really, the kind of effective advice upon which people can rely in transactions involving thousands or millions of dollars.

The same is true about the FTC advisory opinions. Their rule explicitly states that if an extensive investigation is needed to determine the effect of a proposed course of action, they will not grant an advisory opinion. So neither of these, I think, is a practical alternative to get advice in advance of the making of decisions on patent licensing.

Finally, as I pointed out in my written statement, neither a Department of Justice Business Review Letter nor a FTC Advisory Opinion is in any way binding on private litigants. So even if you get one from them, you have no assurance that you are not going to run up against a challenge and a triple damage suit or a patent infringement suit with a misuse type of defense or antitrust counterclaim.

Second, I think there is need for legislation to make it clear that the licensing of trade secrets and technological know-how is lawful. The *Lear* v. *Adkins* decision which has been adverted to a number of times in the hearing cast a giant cloud on the propriety of the long-established of licensing of trade secrets and technological know-how. The dicta of Mr. Justice Black's partial dissent, joined by Justice Douglas and Chief Justice Warren, expressed the view that such licensing is preempted by the patent laws. It is true that the majority opinion written by Justice Harlan didn't subscribe to that, but it merely reserved the question whether pending patent applications can be licensed, but in such a way that it didn't refute it, either. It still left a cloud cast upon trade secret licensing.

The recent opinion by Judge Friendly in the second Circuit in *Plainton* v. *Bourns*, which Professor Stedman referred to this morning, I would agree with him, upheld enforcement of agreements licensing trade secrets. If it were followed by the Supreme Court, there would probably be no need for section 301. But there is no assurance that the Supreme Court will follow this opinion, and since the issue is one of congressional intent to preempt such licensing, I think it is entirely appropriate for Congress to clearly articulate its intention without further delay. I think it is unfair to business concerns to make them negotiate matters involving huge sums of money with the uncertainty that is going to exist until the Supreme Court gets around to deciding the issue.

I might also note that I read with interest Mr. Ward's statement on behalf of the Federal Trade Commission. Mr. Ward merely endorses a small part of the *Painton* v. *Bourns* court of appeals decision. He does not discuss the remainder of it, but there is only a limited amount of the decision that he is really endorsing. So it is not assurance that the Federal Trade Commission will go fully with the reasoning of the opinion by Judge Friendly.

Trade secret and know-how licensing is clearly procompetitive by encouraging the sharing and use of technological data that has been acquired through research and development and business experience. Competition would be hampered if a concern possessing such data must keep it solely for its own use. I don't believe there is need for restriction of trade secret and know-how licensing agreements, because these are agreements that are negotiated by sophisticated businessmen who are not going to be willing to pay for know-how that doesn't possess some real commercial value.

In closing, I would say that the patent system, in my opinion, has basically served our country very well by contributing significantly to our unsurpassed technological progress and our standard of living. It seems to me that anyone who tries to limit it substantially or tries to make basic changes in our licensing law ought to have a heavy burden of proof that such changes would be beneficial to the American public.

(Prepared statement follows:)

STATEMENT OF GLEN E. WESTON, PROFESSOR OF LAW, GEORGE WASHINGTON UNIVERSITY

My name is Glen E. Weston. I am Professor of Antitrust and Trade Regulation Law at George Washington University Law School, but appear here solely as an individual and not on behalf of any institution, organization or client.

My experience in antitrust law consists of former active practice with a Washington, D.C. law firm, teaching of antitrust and trade regulation law for approximately 18 years at George Washington University, at Northwestern University Law School and at the Universtiy of Michigan Law School I have also frequently served as a consultant to both large and small corporations on antitrust problems—principally in establishing or implementing antitrust compliance programs. I am Co-editor, with Professor S. C. Oppenheim of *Federal Antitrust Laws—Cases and Comments* (3d ed. 1968) and also Co-author with Professor Oppenheim of a four-volume work entitled *The Lawyer's Robinson-Patman Act Sourcebook* to be published this summer by Little, Brown & Co.

I am not appearing here on behalf of any client—past, present or future—but felt moved to appear here because of my belief in both federal antitrust policy and federal patent policy. I also was motivated to appear to dispel any possible notion that the group of antitrust teachers who signed a petition in opposition to the Scott Amendments represented the view of all antitrust teachers. I declined to sign the petition and know that there are other antitrust teachers who would agree with me although I have made no attempt to circulate any counter-petition.

My purpose in appearing here is to support what I consider to be the two most important objectives of the Scott Amendments—(1) The proposal to codify the traditional standard for determining the validity of limitations and conditions in patent licenses, and (2) the proposed Section 301 which would declare that it is lawful for business concerns to continue the long established practice of licensing technological trade secrets and know-how.

THE NEED TO CODIFY THE TRADITIONAL STANDARD FOR DETERMINING THE VALIDITY OF PATENT LICENSE LIMITATIONS

There is a need for legislation to codify the traditional standard for determining the validity of patent license limitations or conditions. In 1926 the Supreme Court in *United States v. General Electric Co.*, 272 U.S. 476 laid down the basic standard that has been used for 44 years to determine what kinds of limitations or conditions may be used in patent licenses. The Supreme Court held that a patent owner may license upon any condition that is "normally and reasonably adapted to secure the pecuniary reward" to which the patent entitles him. This is a flexible and reasonable standard that has been interpreted to permit a concern owning a patent to use sound business judgment in determining how it can most effectively obtain a good return on its patent. At the same time it has permitted the Department of Justice to challenge successfully the use of license limitations when they are used as an excuse to restrain trade unreasonably or in any attempt to cartelize an industry.

1. The principal reason why legislation is needed to codify this traditional standard is that the Antitrust Division has indicated that it plans to change the law on a case by case basis to create a rule that will make patent license limitations or conditions presumptively unlawful

Assistant Attorney General Richard McLaren has indicated that he will seek to apply a new and much more rigid test for determining validity of patent license limitations. Under this test he asks two questions: (1) Is the provision *necessary* to the patentee's exploitation of his lawful monopoly? (2) Are *less restrictive alternatives available* to the patentee? If the answer to the first question is "no", or the second is "yes" Justice will probably challenge the restriction. See McLaren, *Patent Licenses and Antitrust Considerations,* 13 Idea 61 (1969). For similar views by other Antitrust Division officials, see Donnem, *The Antitrust Attack on Patent License Provisions,* 14 Antitrust Bull. 749 (1969) ; Stern, *Future Look at Patent Fraud and Antitrust Laws,* 52 J.P.O.S. 3 (1970).

What this new test means in practical terms is that Justice Department will ask the courts to consider patent license limitations to be presumptively unlawful, *shifting the burden of proof to the patentee* to prove both *necessity* and the *unavailability* of less restrictive alternatives. Thus the patentee may in good faith license his patent with limitations that have traditionally been considered as reasonable and lawful in the belief that he is acting reasonably to exploit his patent but the Department of Justice years later may apply 20–20 hindsight to decide the conditions were not *necessary* or that *less restrictive* alternatives were available.

Mr. McLaren's analysis is based upon an analogy to the common law "ancillary restraints" doctrine. But unlike the usual ancillary restraints case, where the only effect of a wrong judgment was to render the restriction unenforceable or to justify an injunction against its enforcement, in the case of a patent license restriction the effect would probably be to render the patent unenforceable because of the misuse doctrine—thereby resulting in the harsh consequence of a *forfeiture* of the patent property.

2. The Department of Justice plan would constitute a major change in existing law—a policy change that should be made, if at all, only by Congress after full hearings and consideration of whether there is a need for such a change and the impact it would have upon the patent system

Now I have great respect for Assistant Attorney General McLaren and for Richard Stern, Chief of the Patent Unit, both of whom are able lawyers. However, with all due respect, the Department of Justice is in reality trying to bypass Congress to make a fundamental change in basic patent-antitrust law because it believes it can secure "judicial legislation" easier than it can obtain Congressional legislation. This is disturbing because it subverts the role of Congress under the Constitution to determine patent policy. It is also unwise because it seeks to make basic policy in the narrow context of the record of particular cases without affording the policy makers with a full understanding of the probable impact of such a change upon the incentives to invest in research and development, the incentive to grant licenses and the incentive to invest in exploitation of new technology.

There are fundamental questions that should be weighed carefully before such a basic policy change is made. Will the inability to use patent license limitations have a significant effect in discouraging the licensing of patents? Will the inability to use patent license limitations severely handicap smaller business concerns who lack capital to exploit their own patents fully but need protection against their larger licensees? Will the inability to use limitations result in licensors charging higher royalties? Such questions are not well suited for determination in adjudicatory proceedings between two parties, and all concerns which will be potentially affected should have the opportunity to present views and evidence concerning the effects of such a policy decision.

3. The Department of Justice has created uncertainty for licensors by indicating it will challenge license limitations long permitted by judicial decisions

By proposing to create a presumption of invalidity for patent license limitations and by indicating that it will seek the overruling of the *General Electric* and other patent antitrust cases the Department of Justice has created major uncertainty for patent licensors. In particular, a major area that is now uncertain is field of use limitations which Justice Department wants to limit significantly but which have been upheld when "normally and reasonably adapted to secure pecuniary reward." Mr. McLaren wants to substitute his "necessity" test and inquiry as to whether there are "less restrictive alternatives" available. Existing case law furnishes a useful guide under the "normally and reasonably adapted" test but there is no guide available under Mr. McLaren's proposed test.

It has been asserted that patent owners can get guidance under the Justice Department's Business Review Letter procedure or the Federal Trade Commission's Advisory Opinion procedure. But with all due respect to both agencies this is largely illusory in this area. The Department of Justice grants clearances only when it considers proposed conduct to be clearly lawful without an extensive factual investigation. Since it would consider license limitations presumptively unlawful it would nearly always give either a negative statement or decline to grant clearance because "necessity" and availability of less restrictive alternatives would usually require an extensive factual inquiry. Similarly, the FTC declines to render Advisory Opinions where an extensive investigation is needed to determine the effects of a proposed course of action. Finally, neither the Department of Justice Clearance nor an FTC Advisory Opinion are binding on other private parties who could sue the licensor for treble damages or assert a misuse defense to an infringement suit.

THE NEED FOR LIGISLATION TO MAKE IT CLEAR THAT LICENSING OF TRADE SECRETS AND TECHNOLOGICAL KNOW-HOW IS LAWFUL

There is a need for a Congressional declaration to clarify the law because of the Supreme Court dicta in *Lear, Inc. v. Adkins*, 395 U.S. 653 (1969) which cast a giant cloud upon the propriety of the long established practice of licensing of trade secrets and technological know-how. Such licensing has been permitted since the English common law and is tremendously important to our economy—running into billions of dollars a year. Trade secret and know-how licensing contributes very significantly to our international balance of payments and a Supreme Court decision that invalidated such licensing would have unfortunate impact.

The dicta of Mr. Justice Black's partial dissent (joined by Justice Douglas and Chief Justice Warren) expressed the view that such licensing is preempted by the Patent Laws. Unfortunately the majority opinion written by Justice Harlan merely reserved the question of whether pending patent applications could be licensed but in such a way that it did not dispel the cloud cast upon trade secret licensing.

The recent opinion by Judge Friendly in the Second Circuit in *Painton & Company, Ltd. v. Bourns, Inc.* (April 27, 1971) is a very sound and well written one upholding the enforcement of agreements licensing trade secrets. If it were followed by the Supreme Court there would probably be little need for Section 301. However, there is no assurance that the Supreme Court will follow this opinion, and since the issue is one of Congressional intent to pre-empt such licensing, it is entirely appropriate for Congress to clearly articulate its intention without further delay. It is also unfair to business concerns to make them continue to negotiate in matters involving such huge sums of money with the uncertainty that will exist until the Supreme Court decides the issues.

Trade secret and know-how licensing is clearly pro-competitive by encouraging the sharing and use of technological data that has been acquired through research and development and business experience. Competition would be hampered if a concern possessing such data must keep it solely for its own use. Since trade secret license agreements are negotiated at arms length by sophisticated businessmen there need be no concern that royalties would be paid for data not possessing real commercial value to the licensee.

Trade secret and know-how licensing has no adverse impact upon the patent system. As Judge Friendly explains in a very lucid manner, there is no basis for a belief that such licensing will significantly lessen incentive to use the patent system. Only upon the basis of one assumption would this be likely—the assumption that the courts will so niggardly construe the patent law that inventors will begin to believe that patents are worthless. Congress should make sure that this does not happen by enactment of the Patent Reform Act and by continued scrutiny of its interpretation.

The Patent System has basically served America well by significantly contributing to our unsurpassed technological progress and standard of living. Anyone who tries to limit it substantially or make basic changes in our licensing law should have a heavy burden of proof that such changes would be beneficial to the American public.

Senator HART. Professor, thank you.

Having heard, I think, three witnesses now, I am beginning to get a little better understanding of what the committee has been plowing through here for 2 days. This is a very broad question, but to the extent you can respond, I think it would be helpful; at least it would be to me.

I got the impression that a reason for the amendments, particularly the amendment 24, was to bring some certainty to the patent field. Now I realize that one of the ways we are going to do that is to put into the statute the words "normally and reasonably adapted the secure pecuniary reward." Now, run around the track with me on that and tell me how that gives any certainty about anything.

Professor WESTON. I think it will give certainty because we have a great deal of case law for the last 44 years interpreting that standard. Therefore, we have something to rely on.

Senator HART. Well, we have a great many antitrust decisions. Yet the antitrust bar says that unreasonable restraint is a very vague standard.

Professor WESTON. It is, but I think it is a desirable one in my opinion.

Senator HART. But a lot of decisions that have interpreted it say that it is.

Professor WESTON. I am not seeking an illusory certainty in the sense that I do not believe absolute certainty is either attainable or desirable in this area. I believe that flexibility has been probably the major reason why the Sherman Act has been as successful as I think it has been. I do not suggest that we need inflexible rules here, but I think we do need clarification. I think we have a situation where the Department has generated uncertainty by apparent plans to make a change without clearly articulating what the change is and without articulating what is going to happen when that change takes place. That is the reason I think that a codification which would give us the existing case law to rely on would be useful.

Now, I do not believe it is going to unduly hamper the Department of Justice in preventing the misuse of patents. For example, we have had the *Hartford Empire* case, the *Line Material* case, the *Gypsum* case and many others, where despite that standard, the Department of Justice has been able to step in and prevent the use of license limitations in patent licensing as an excuse, really, to cartelize an industry. I think that would still continue to be true if this were codified.

Or alternatively, Senator, if Mr. McLaren wants to come forward and propose language which he thinks is more suitable, I think this might be a useful alternative. I think that the committee should go carefully into what the impact of that would be on kinds of practices such as field of use limitations and so forth, and ascertain whether that impact would be adverse on patent licensing or beneficial.

Senator HART. That *Hartford Empire* case, I am told is used as a clear example of the proposition that field of use can be used in an anticompetitive field in an extremely abusive fashion.

Professor WESTON. I concur it was an abuse of field of use limitation. And the GE "normally and reasonably adapted to secure pecuniary reward," test did not prevent the Department of Justice from successfully attacking it there where it had been misused.

Senator HART. The Scott amendment does not raise questions?

Professor WESTON. I heard or saw one statement that gave the impression, I believe it may have been Mr. Ward's, that maybe the *Hartford Empire* case would be overruled by the Scott amendments. I do not believe that can in any conceivable form be accepted.

Senator HART. But before we adopt any change in the law, we have to get answers to questions of this character, do we not?

Professor WESTON. I think it is quite clear that the intent of the Scott amendments is not to permit the kind of abuse that existed in the *Hartford Empire* case. I don't believe the language is reasonably susceptible to the interpretation.

Senator HART. I am reading from amendment 24, from (b)(2), on page 2, beginning at line 3:

> An applicant, patentee or his legal representative may also at his election waive or grant by license or otherwise the whole or any part of his rights and for the whole or any part of the U.S. by exclusive or nonexclusive arrangement with the party or parties of his choice.

Now, is there any obscurity that would compel the court to go to what our intent was?

Professor WESTON. I don't believe that this is at all reasonably susceptible to the interpretation that it would permit the kind of abuse that we had in the *Hartford Empire* case.

I might say also——

Senator HART. Now, wait a minute, professor, and I am very reluctant, because not only am I not a patent lawyer, but I was never a law teacher. But if I had a class in legislative draftsmanship and said, write me a paragraph that is clear, and a fellow turned that in, I would say that is good, that is clear. How can an applicant grant by license or otherwise, the whole or any part, to the whole or any part of the United States, how can you look at that and say that does not give him carte blanche?

Professor WESTON. Senator, that is in the present law.

Senator HART. Well, then, what is the problem if it is in the present law?

Professor WESTON. The problem is not this section, Senator. Let me clarify this.

My statement is not supporting——

Senator HART. The problem may be with me, clearly.

Professor WESTON. My statement, by the way, Senator, is not supporting the precise language of the Scott amendments at all or even these specific proposals. I am really directing mine primarily to section 271(f) I believe it is, which would really adopt, is intended, as I understand it, to adopt primarily the kind of test that I indicated before from the *General Electric* case, the traditional standard. I think that that is the most important provision in my judgment of this proposed amendment.

Senator HART. I was very hopeful that I was beginning to break through to an understanding of the problem here that the committee has. Clearly I have not.

As I take it, when we are talking about field of use, we are talking about licenses that condition, either territorially or in application——

Professor WESTON. Well, territory is a separate kind of restriction from field of use. The territorial one is the one that is explicitly in the present statute. Field of use is not, so that this portion of this section which refers to field of use would be a new amendment.

Now, my own personal approach to this is I would prefer to see the standard stated broadly, as in, I believe it is 271(f), rather than more specifically as in this section. But if I understand the intent of this section, it really is basically to codify existing law. If that is correct, then I would have no objection to it. But I share some concern about the precise language. But I understood that the language is still in a rather fluid state, that the basic policy question is, does Congress desire to codify existing law or does it desire to change the law or leave it as is and permit the Department of Justice to go ahead and try to change the law on a case by case basis in judicial decisions?

Senator HART. When you say existing law, do you mean that the language I read you is presently in the patent title 35?

Professor WESTON. Concerning territorial assignment to the whole or any part of the United States it is in the present patent law.

Senator HART. Well, if it is in the present law, is the objection to the fact that it must be read in connection with and subject to antitrust limitations?

Professor WESTON. Well, concerning territorial limitations, Senator, the only uncertainty that has been created has been by some comments largely in law review articles to the effect that the existing statutory provision was not intended to prevent the granting of licenses limited—exclusive licenses for particular territories. Now, no Department of Justice official, to my knowledge, has ever stated they intend to change that rule, but they have noted the existence of those theories and suggested the possibility that they might study them and consider whether to seek to bring about a change.

So that again, it is an issue which again I think would be desirable for Congress to clarify one way or another.

Senator HART. On the matter of conditioning a license on price, resale price, whatever the patent law calls that, does this language that we say should be, which is taken from the *General Electric* case, and which we want to go into the statute, normally and reasonably adapted to secure pecuniary reward—now, what does that, as you read it, threaten to do, or should we even worry about it?

Professor WESTON. Probably the latter is the case because of the infrequency of the use of this kind of limitation. And also, more importantly, because the courts have already so restricted the use of this kind of limitation that it is virtually meaningless. It has been construed, for example, in——

Senator HART. Well, is this one of the areas where we are petitioned to make clear in the statute that some of those cases are wrong?

Professor WESTON. This would be my understanding. If you adopt——

Senator HART. I would have to be persuaded to a clear understanding before I would buy a change that would make possible what occurred in the *General Electric* case.

Professor WESTON. The *General Electric* case has been limited by the Supreme Court in, for example, the *Line Material* case where they precluded cross-licensing agreements with price fixing clauses in them; in the *Gypsum* case, where they prohibited an industrywide conspiracy, really, to use patent license limitations as an excuse for industrywide price fixing; in subsequent lower court decisions in which they have said even multiple licenses—more than one, apparently—containing price limitations would be unlawful. So that the only existing possible argument concerning their validity—that is, as long as that case law stands—would be a single license. Even that seems to be so infrequently used that I do not think it is a serious problem.

Senator HART. Well, would the Scott amendment permit it?

Professor WESTON. I don't interpret it as such. I do not believe it is susceptible to that interpretation.

Again, I will hedge, sir, on the language of the Scott amendments. I have not really gone into detail on the precise language because of my understanding that it is still in a rather fluid state. I think, though, that it would not be difficult for this committee to make certain, both in the language and in the report on it, that this would not permit such a thing as kinds of price fixing that occurred in the *General Electric* case or *Line Material* or the *Gypsum* cases.

Senator HART. You think it would not?

Professor WESTON. I think it would not.

Senator HART. Yet the language I read came from the *General Electric* case.

Professor WESTON. But we have had the subsequent interpretation.

Senator HART. Well, assuming we are determined to avoid that danger, is it not likely that we could find language more appropriate than this?

Professor WESTON. I think you can readily at least make it explicit that it is not intended to permit that kind of conduct.

Senator HART. Now, I will leave that only to repeat my point. To me, statutory language "normally and reasonably adapted to secure pecuniary reward," would not be my favorite example of clarity with respect to what you can do. Maybe that is because I am not a patent lawyer. But it sure does not sound to me like very much clarity.

Professor WESTON. I think it would be more helpful than starting off with a test that you must show that it is necessary and that there are less restrictive alternatives available when you know that a license that you are negotiating now may be reviewed 17 years later by the Department of Justice with their idea of what's necessary and whether less restrictive alternatives were available 17 years earlier.

Senator HART. Maybe it has other problems, but it is no less clear——

Professor WESTON. One of the problems would be that you cannot use limitations, because I think no one can afford to run the risk of using a presumptively unlawful limitation. The risk is too great because you, in practical effect, forfeit your patent due to the misuse doctrine. So nobody would be able to use it. If that is what Congress feels is a wise choice after clearly considering what impact it would have on the incentive to grant licenses by small business concerns that own patents that may not have the full resources to exploit them and so forth, then, fine. I think it is better for it to be decided in a congressional forum than in the courts on a case by case basis.

Senator HART. What antitrust cases, and I am referring now to your statement on page 6, where you mention the Department of Justice seeking to overrule other patent antitrust cases, at the very top, what are they?

Professor WESTON. None have been filed yet to my knowledge, sir. I am relying upon their written published statements which have not been recanted for this conclusion that this is their plan.

Senator HART. Do we have the statements?

Mr. BRENNAN. Mr. Chairman, some of Mr. McLaren's speeches and Mr. Stern's comments have been supplied to the subcommittee. It might be well at this point—I see Mr. Stern is present—if we could ask the Department to furnish us with a complete compilation of the relevant speeches.

STATEMENT OF RICHARD STERN, CHIEF, PATENT UNIT, ANTITRUST DIVISION, DEPARTMENT OF JUSTICE

Mr. STERN. I would be very glad to supply the committee with the speeches that I consider relevant. I hope if Mr. Weston would find it possible to do so, he could point out the particular speeches or published statements which have not been recanted which indicate a program to overrule some prior course of judicial decision. I am unaware of any speeches to that effect which I have given; I do not think there are any such speeches that Mr. McLaren has given. But I will be glad to look through our files and see what speeches I can find that have any bearing on this question.

Mr. BRENNAN. I am sure it will be helpful to the subcommittee.

Thank you.

Mr. STERN. Mr. Counsel, I would appreciate it if this request could be made in the form of a letter to Mr. McLaren.

Mr. BRENNAN. Certainly.

(The documents referred to were subsequently furnished the committee. See p. 503 of the appendix.)

Senator HART. I would hope we could nail it down for the record, because I have been told that much of the concern that gives rise to the proposed amendments is said to be in response to Department plans, proposals, announcements or statements of one sort or another that they are going to attempt to reverse not alone the *General Electric*, but other cases.

Professor WESTON. One of the other cases I had in mind was the *General Talking Pictures* case which involves field of use limitations.

Senator HART. Do you read that *Talking Pictures* case as permitting field-of-use under any and all circumstances, whether it has anticompetitive factors or not?

Professor WESTON. No, sir, I don't, because I think Hartford Empire, for example, was an indication that it would not.

Here is a quote from one Department of Justice official speech: "If General Electric is overturned on the price-fixing ground, any residual precedential value would be reduced and *General Talking Pictures* would fall with it."

Senator HART. That doesn't mean that all field-of-use licenses—

Professor WESTON. No, it doesn't, but it means that the law would be changed on field of use limitations.

Senator HART. If I ask how, you will say you——

Professor WESTON. I don't know. The rule will have to be changed. That is what creates the uncertainty.

Senator HART. Mr. Brennan?

Mr. BRENNAN. Could you furnish for the record your comments on the Department of Commerce proposal that was made on the first day of the hearings?

Professor WESTON. I have not received a copy of that, but I will be glad to. I have not yet received a copy.

Mr. STERN. Mr. Brennan, might I correct an inadvertent omission that I made in my statement before? I should have indicated that for a number of years, almost since 1926, the Department of Justice has made efforts to have the 1926 General Electric decision overruled; that is the decision which permits price fixing in patent licenses. It has been the consistent policy of the Department of Justice to attempt to have that particular decision, but that decision, I believe, alone, overruled.

Senator HART. There is no reason for you to be embarrassed; I think my question or our discussion indicated that we did understand that there was an effort to overrule GE. We were asking for the other examples.

Thank you very much, Professor.

Professor WESTON. Thank you very much.

Senator HART. We welcome and we will print in the record in full as if given in full the testimony of another lawyer experienced in the field, Mr. Edward S. Irons.

STATEMENT OF EDWARD S. IRONS, ATTORNEY AT LAW, WASHINGTON, D.C.

Mr. IRONS. Thank you, Mr. Chairman. I will not repeat my prepared statement. I have a few brief additional comments which I would like to make if I may, please.

Some months ago, it first came to my attention that the Congress was being importuned on the basis of an alleged crisis in the patent system said to be consequent from uncertainties in the patent law, aggravated by the activities of the Department of Justice, to pass a rather large and significant body of new legislation, not only the amendments 23 and 24, but many aspects of S. 643 itself. I was astounded at this when I first heard it because it was not consistent with my own 20 years of experience in this profession.

I undertook on my own to make a rather careful study of the submissions of the American patent law associations and others calculated to demonstrate the existence of these alleged uncertainties and of the inroads which the Department of Justic is said to intend insofar as the patent system is concerned.

I found, at least in my judgment, sir, that the fact of the matter is that there is no crisis, that there is no more uncertainty in the field of patent law than there is in any other legal field where I and other lawyers are called upon to advise our clients; that the Department of Justice, as far as I can tell, has not actually done anything more than apply more or less routine or established legal concepts, including antitrust concepts, to patent property with predictable results. Competent lawyers, including competent patent lawyers, have no trouble at all, and have not had any for some years, in advising their clients of the procedures which are requisite to stay on the safe side of the line between what is legal and illegal.

The proponents of this legislation know the nature of the advice which can be safely given and which should be given to any client. The circumstance, I think, that has prompted this legislation is not uncertainty at all but a dissatisfaction with the type of advice which must be given to confine the patent concept, the patent monopoly, to the limits which the Constitution itself and the antitrust laws and the other laws designed to guarantee free competition in this country demand that it be confined to. I am not attempting to say that a black and white answer can be given to all patent problems, but such an answer cannot be given to all problems in any legal field. There simply is no crisis of any type which would warrant the interruption with the growth of the law on the conventional case by case basis as it goes on in any other branch of the law.

This atmosphere of crisis, in my judgment, and based on my studies, has been generated by the adoption in many cases, I think, of ultimate or extreme positions. Proponents of this legislation—we have had much discussion here, for example, of field of use licensing—suggest that there is some kind of a black and white issue here, that field of use licensing is somehow going to be abolished, that some kind of legislation is necessary to preserve it and to insure that it is not abolished.

Now, insofar as I am informed, neither the Department of Justice nor anybody else in a responsible position has ever attempted to abolish totally and absolutely field of use licensing. The position, rather, is that like any other contract provision, field of use may be abused. And if it is abused in a way which gives rise to anticompetitive consequences, it should be condemned. There is nothing wrong with this. It is the same type of restriction that people who deal in other kinds of property labor under everyday.

I have heard Professor Weston talk about the alleged test given expression by Mr. McLaren and I have read Professor Weston's paper and his summary of that test on page 3. I am very delighted that the suggestion has been made that the Department of Justice be invited to state its own position on this and that the papers which actually reflect the statements which the gentleman from the Department of Justice made are to be made of record before this committee, because when read exactly, there is no threat implicit in those, either. And the reproduction of this test which appears in Professor Weston's paper is not literally what Mr. McLaren said and when you read what he said, it certainly does not justify the apprehension which has been expressed here.

I would also like to point out that there is a particularly serious danger in accepting the premise that all that is being attempted here is to codify existing law. This, I believe, any reasonable reading of these amendments demonstrates to be inaccurate. For example, we were discussing this business of price fixing in the *General Electric* case, or rather, you were, Senator, with Professor Weston. I am informed that the statement in the Patent Trademark and Copyright Journal for April 15, 1971 is that price fixing is satisfactory and that one purpose of the Scott amendments is to condone it. Perhaps my information is wrong, but I think that it is correct. I mean price fixing in a patent license.

What is going to happen once this legislation is passed is that lawyers, being good lawyers, are going to do their very best to take the position that the real effect of it is to exclude contracts dealing with patent property from antitrust concepts. It is going to generate more litigation, more uncertainty, and more confusion than could possibly exist if no legislation were passed at all.

And there has been some suggestion, and this is a diversion from the main trend of what I wanted to say here, but there has been some suggestion that the Department of Justice wants to reverse established decisions in various areas. Significantly, there has been no evidence that that is true. But, if we could look at S. 643 as a whole, it is perfectly obvious that the intention of that statute is to reverse or modify a great number of important Supreme Court cases which delimit the patent monopoly to a scope consistent with its constitutional purpose. Graham, which enunciated the constitutional patentability standard, *Brenner* v. *Munson* which enunciated the utility standard, *Lear* that you have heard about, which eliminated licensee estoppel, *Scott* v. *Marcalus*, which eliminated assignor estoppel. These are typical but just representative examples of Supreme Court law which S. 643, if passed in its entirety, would overrule.

I want in closing to make one further comment. The Supreme Court has many times commented or perhaps many times is the wrong expression, in *Graham* at least it commented upon the fundamental discrepancy between the standard of invention for patents in the patent office and in the courts. There has been a constant struggle since *Graham* was decided, and notwithstanding the fact that it has been three times reaffirmed in the last 2 years, to suggest that the Supreme Court was wrong and that the constitutional standard of invention does not exist. Commissioner Schuyler, at his nomination confirmation hearings, made it clear that he felt that the court in *Graham* was wrong.

There is no evidence of any change in the patent office attempting to raise the standard of invention to a level which the Constitution demands.

When you put together in one statute a provision like the new provision 103, which is calculated to make bad patents easier to get, with legislation such as amendments 23 and 24, which are calculated to make it possible to enlarge the patent monopoly by private contract, you have by this combination created a situation which, in my opinion and experience, is most seriously contrary to the public interest.

Thank you.

(Prepared statement follows:)

STATEMENT OF EDWARD S. IRONS, LAWYER, WASHINGTON, D.C.

Honorable Chairman and members of the Subcommittee, I am pleased to appear at this hearing to testify with respect to Amendments No. 23 and 24 to S. 643, the pending bill for general revision of the patent laws, Title 35 of the U.S. Code.

Having spent more than 20 years in the practice of law relating particularly to patents, trademarks and their licensing, I am concerned that Amendments No. 23 and 24—as well as certain other provisions of S. 643 such as *e.g.* § 103 lowering the present statutory and constitutional standard of patentable invention and those sections authorizing the investor rather than the inventor to apply for a patent—would, if enacted, tend to greatly weaken and eventually destroy the *federal* patent system that Congress was authorized by the Constitution to establish, which has existed from 1790 until the present.

Last week in *Blonder-Tongue Laboratories* v. *University of Illinois Foundation*, the Supreme Court emphasized that it "fully accepts" congressional judgment to reward inventors through the patent system pursuant to constitutional authorization, but considers strict compliance with statutory and constitutional criteria for patentability necessary to ensure that the monopoly power *prima facie* conferred by any patent, even an invalid one, does not accrue to its owner unmerited competitive advantages to the detriment of the public of the United States, including specifically consumers.

The proponents of Amendments 23 and 24 pay lip service to a strong federal patent system. Their desire is to render *all* patents, including those that do not meet the aforementioned statutory and constitutional criteria, less susceptible to attack on both validity and enforceability (misuse and antitrust) grounds. Their primary interest is hence not in preserving and protecting a *strong federal* patent system under which *public* interest is paramount, the inventor's reward is important but secondary and the investor's interest is, as best, incidental. Rather, the promoters of Amendments 23 and 24 see as *primary* the reward to *investors* willing to finance commercial exploitation of so-called "technological innovations" (including those that do not comply with statutory and constitutional patentability criteria) and would relegate both the public interest in patents and the inventor's reward to secondary status. The pressure today, much of which has been generated in an atmosphere of pseudo-crisis, is for legislation masquerading under the "patent system" label which makes monopoly power over "technological innovation"—*regardless* of patent validity—easy to obtain, easy to enforce and difficult to attack on legal or factual bases to the primary benefit of the investor, the denigration of the inventor and the ultimate detriment of the public, including particularly the consumer.

Amendments 23 and 24 would perform their role in accomplishing this end through the primary mechanism of reducing *federal* power over the *private* "patent" monopoly system they would erect in the partial guise of a "strong patent system".

Amendment 23 would serve the desired ends by eliminating federal supremacy and control over state authorization of *private* monopolies inconsistent with the federal patent grant.

Amendment 24, which to some extent is nourished by Amendment 23, would do so by permitting each patentee to create by *private* contract, at will, a plurality of monopolies and submonopolies not coextensive with the patent grant, many of which are repugnant to the Constitution.

Both Amendments should be rejected—Amendment No. 23 *at least* because of its virtually certain unconstitutionality. Amendment No. 24 *at least* because of its destructive effect upon relevant existing antitrust and patent law.

AMENDMENT NO. 23

According to the "detailed explanation of the Amendment to Section 301", inserted in the Congressional Record at that time that Amendment 23 was introduced, at least a primary purpose of this amendment is to remove from the ambit of the federal patent laws "technical knowledge which by its very nature normally would constitute patentable subject matter", but which consists of "information that is available in the prior art or which, no matter how valuable it may be commercially, lacks the element of unobviousness required for it to be eligible for patent protection".

In other words, *unpatentable* subject matter is to be removed from the ambit of the federal patent laws so the states may recognize arbitrarily established private monopolies covering it.

In 1964 in its decision in *Sears, Roebuck & Co.* v. *Stiffel Co.* 376 U.S. 225 (1964), the Supreme Court observed that "Obviously a State could not, consistently with the Supremacy Clause of the Constitution . . . give a patent on an article which lacked the level of invention required for federal patents." Congress is now asked, by Amendment No. 23, to authorize a state to do exactly that. The Supremacy Clause in Article VI of the Constitution is, I suggest, binding upon Congress equally with the states. It alone *ought* to influence Congress to reject Amendment No. 23.

The aforementioned "detailed explanation" says Amendment No. 23 was recommended in consequence of "recent judicial decisions which cast a shadow of doubt on the propriety of entering into contracts for protection of trade secrets, techniques, know-how and the like, and which suggest that such private contracts are preempted by the patent laws. . .". The writings of Amendment No. 23's proponents identify these "recent judicial decisions" as two in number —(1) the minority concurring opinion of Mr. Justice Black, joined by Mr. Chief Justice Warren and Mr. Justice Douglas, in *Lear, Inc.* v. *Adkins*, 395 U.S. 643 (1969), and (2) the decision of District Judge Constance Baker Motley in *Painton & Co.* v. *Bourns, Inc.* 309 F. Supp. 271 (S.D. N.Y. 1969). If these *be* the impetus for Amendment 23, they are certainly insufficient to justify the drastic action that Congress is asked to take. *Neither represents the present law.* The Second Circuit Court of Appeals reversed the *Painton* decision on April 27, 1971. The majority of the Supreme Court and Mr. Justice White in his special concurring opinion in the *Lear* case, were careful to take a different tack from Justice Black; they left open to a state court on remand the specific question of whether some mode could be found for reaching an accommodation between the federal patent system and so much of the state law of contracts as might permit payment for the alleged trade secret or technical know-how information in issue in *Lear*. There is *at this juncture* no ground for hasty conclusions, legislative or otherwise, that some reasonable area of accommodation consistent with the federal supremacy of the federal patent laws cannot be reached judicially.

Indeed, past experience shows that when trade secrets and technical know-how are not urged to constitute pseudo-patents having the aura of monopoly or "property right", there does exist reasonable ground in equity for accommodation with federal patent law.

The Supreme Court itself in 1917, speaking through Mr. Justice Holmes in *E.I. du Pont de Nemours* v. *Masland*, 244 U.S. 100, rejected the notion that trade secret information is or can be "property", saying that any such assertion is "an unanalyzed expression of certain consequences of the primary fact that the law makes some rudimentary requirements for good faith" in business dealings. Quite independent of the patent system, it *is* public policy on both a state and federal level that fair dealing in business relationships requires one who has benefited from the bargained for services of another to pay for those services. Almost no one would argue that schools which deal in teaching unpatented and unpatentable technology are disentitled to compensation because their pupils could look up the same technology for themselves—but virtually all of us would deny that such schools have a monopoly or property right in what they teach. Disseminators of trade secrets or "know-how" are manifestly in a posture analogous to that of such schools. The dangerous fallacy which underlies Amendment No. 23 and obviously prompted Justice Black's special opinion in *Lear* is the supposition that trade secrets and know-how are private property rights of a character similar to those conferred by the federal government in the grant of a valid patent—a notion that is ***inconsistent*** with a strong federal patent system.

In this connection, there is no substance to the fear, expressed in the aforementioned "detailed explanation of the Amendment to Section 301" to the effect that absent Amendment No. 23 technical agreements between domestic and foreign entities involving transfer of technological information might be outlawed as being preempted by the patent statutes to the detriment of the United States balance of payments position. Technological information conveyed by domestic entities to foreign entities that *could* affect the balance of payments is conveyed for use in foreign countries. Accordingly it is not subject to federal patent law which, pursuant to 35 U.S.C. Section 154 and predecessor statutes, is strictly limited in scope to the United States and its territories. S. 643 does not depart from existing law in this respect, with the result that Amendment 23 could have ***no*** extraterritorial effect. The risk, if any, that contracts between domestic and foreign entities involving transfer of U.S. technological information to foreign countries "might be outlawed", is independent of federal patent policy in the United States and rests upon the patent, trade secret, and contract policies of foreign governments, coupled with federal antitrust policy.

It merits attention by this Subcommittee that Amendment No. 23, if enacted, will predictably be declared unconstitutional by the Supreme Court as soon as a case raising the issue is reached. Congress need only look at the history of prior legislative enactments that were ultimately pronounced unconstitutional, such as the National Industrial Recovery Act of the 1930's, to perceive the measure of chaos that would be created by even brief implementation in the lower courts of a null and void statute.

In addition, it is predictable that the small businessman and the independent inventor—both of whom are the theoretical projected beneficiaries of Amendments 23 and 24—would be hurt rather than helped by Amendment 23. As a practical matter, the offer from an economic weakling of an indeterminate "property right" in the form of a trade secret or know-how relating to unpatented and unpatentable subject matter, which right is viable only because of Section 301 is unlikely to attract much risk capital. Large business enterprises with the economic pressure which their capital resources and size can bring to bear, ***might***, because of their undoubted financial capability to follow through on threats of litigation under Section 301, be able to induce both large and small competitors to accept licenses on state law-created monopoly "property rights" that are ***less than*** patents and because of this be induced to expend their own risk capital to develop such "rights"; lone inventors and small businesses will surely ***not*** be able to obtain the same results, because they cannot apply requisite economic pressure. In any event, the ***public*** will be the loser because it will pay the increased prices of goods consequent from any such strengthening of ***private*** non-federal monopoly power. At the same time the ***federal*** patent system will be weakened in at least two ways: (1) patent rights will be less valuable since it will be easy to establish private monopoly and (2) the struggle to maintain a federal statutory and constitutional quality standard for valid patents will be necessarily undermined.

Since Amendment No. 23 is neither constitutional nor in furtherance of a strong federal patent system, I urge that it has no proper place in S. 643 or any other bill for general revision of the patent laws.

AMENDMENT NO. 24

Amendment No. 24 is concerned with a plurality of devices by which, through private contract, patent owners could at will create new monopolies quite unrelated to the validity of any patent, consisting either of subdivisions of the patent right into submonopolies not necessarily conforming to constitutional and legislative standards for valid patents, or extensions of that right into spheres outside the scope of the patent grant. If enacted, Amendment No. 24 would have the effect of overruling or severely restricting many subsisting decisions of the Supreme Court which rest on both the constitutional patent clause and the constitutional federal supremacy clause. To a rather large extent Amendment No. 23 is vital underpinning for Amendment No. 24, since the former would explicitly place private contractual rights recognized only by state law *at least* on a par with federal patent rights, thereby *a fortiori* denigrating the value of patents *per se* and the latter would validate at least some forms of *privately* created contractual monopoly, legality of which is now open to question in proper cases.

Interestingly, the pressure for legislative definition of the permissible scope of private contract rights applicable to patents is not new; only its direction differs from what Congress looked at over thirty years ago when the Temporary National Economic Committee (TNEC) recommended in its final report that the patent statutes be amended to declare illegal (a) any *condition* in a patent license agreement restricting the licensee in respect of the quantity of any article he may produce, the price at which he may sell, the purpose for which or manner in which he may use the patent or any article produced thereunder, or the geographical area within which he may produce or sell a patented article, and (b), any other restriction in a patent license agreement which would tend substantially to lessen competition or to create a new monopoly, unless it be shown to be necessary to promote the progress of science and the useful arts. A further TNEC recommendation was that compulsory licensing of patents be adopted. Congress at that time, convinced that the evils the recommendations were designed to eradicate could be curbed judicially under existing legislation, chose not to implement the recommendations legislatively.

Today's pressure exerted in a pseudo-crisis atmosphere, to legalize affirmatively the very practices that the TNEC in 1938, also in a crisis atmosphere, wanted Congress to outlaw, is good evidence that case-by-case judicial application of existing legislation *is* doing the necessary job just as Congress thirty years ago wisely foresaw that it would. The plea of Amendment No. 24's proponents that patent owners have practiced the various restrictive licensing practices condemned by the TNEC "for years, [as] common practice"[1] has a somewhat hollow ring. If it is so, it speaks ill of the proverbial "ordinary prudent businessman"—and it has been my experience that he is *most* prudent.

The specific provisions of Amendment No. 24 would effectuate four specific ends:

(1) they would render *per se* legal and exempt from the "rule of reason" test all forms of field of use and geographically restricted licensing of patents [§261(b) and §271(f)(1)];

(2) they would render *per se* legal and exempt from the "rule of reason" test any form of royalty arrangement, however measured, that a patent owner might insist upon, whether or not discriminatory among licensees and whether or not accompanied by arbitrary refusal of a license to some applicants [§261(b)(2) and §271(g)];

(3) they would subject all possible remaining patent license restrictions other than those made *per se* legal as noted in (1) and (2) *supra* to an artificial new "rule of reason" test, governed by patent law rather than antitrust law criteria, including restrictions now constituting settled per se misuse or antitrust violations [§271(f)(2)]; and

(4) the doctrines of assignor and licensee estoppel, which are dubious even under elementary private contract law and which have been effectively laid to rest by the Supreme Court under existing law, are given renewed vitality on the representation that "fair play" is somehow involved [§§261(e) and (f)].

Contrary to representations of Amendment No. 24's proponents, this amendment is *not* an implementation of Recommendation No. XXII of the President's Commission Report. That report recognized a distinction between the patent right—"the right to exclude others from making, using and selling the patented invention"—and conditions or provisions "long associated with the transfer or license of rights under patents which must be distinguished from the exclusive right to make, use and sell conferred by the patent grant", including improvement grantbacks, cross-licenses, package licenses, patent pools, no-contest clauses, and many other matters simply constituting matters of pri-

[1] See the January 28, 1970 letter of Philip G. Cooper, President of the Philadelphia Patent Law Association, to the Honorable John L. McClellan.

vate contract. Under Recommendation XXII of the President's Commission Report *all* patent license restrictions not already illegal *per se* would be subjected to the rule of reason test and the law would provide that the mere grant of a field of use license, unaccompanied by other questionable provisions, is not illegal. In effect the President's Commission Report would have codified the existing *status quo;* Amendment No. 24 turns the existing law with respect to patent licensing topsy-turvy. It renders "certain", by *per se* legalizing, conduct which is today questionable (Points 1 and 2 above) but renders totally *uncertain* the status of licensing restrictions now *per se* illegal (Point 3 above) and the now void estoppel doctrines (Point 4 above). Of particular concern here is the fact that at least some of the presently recognized *per se* misuses and the estoppel doctrines have been relegated by the Supreme Court to their present status because the *federal* supremacy of the *federal* patent laws decreed by the Constitution requires such status. To give a specific example, the Court in *Brulotte* v. *Thys*, 379 U.S. 29, held that *any* device which temporally extends the patent monopoly beyond the term fixed by Congress is a *per se* misuse which, even if condoned by state law, must bow to the federal supremacy of the patent laws. Similarly, the Court's rejection of the state created doctrine of license estoppel in *Lear, Inc.* v. *Adkins*, 395 U.S. 653 (1969)—a result that was foreshadowed by decisions of the court extending back to *at least as early as the 1892 opinion* in *Pope Mfg. Co.* v. *Gormully*, 144 U.S. 244—rested upon the federal supremacy doctrine. *Scott Paper Co.* v. *Marcalus Mfg. Co.*, 326 U.S. 249 (1945), wherein the original owner of a patent (*i.e.*, assignor) was permitted to successfully defend a patent infringement suit brought by his assignee in the circumstance that the challenged product was a copy of a product covered by an expired patent, depends upon the federal supremacy doctrine and its requirement that *all* the subject matter covered by expired patents be dedicated to the common good.

Practically speaking, of course, Amendment No. 24 and its prop, Amendment No. 23, were designed by their proponents to weaken the influence of federal antitrust policy in the patent sphere; it should be noted that, *e.g.*, the U.S. Chamber of Commerce is concerned with "uncertainty" of the existing *antitrust*, rather than patent, law. What proponents of Amendment No. 24 have failed to appreciate is that strengthening of *private* monopoly as an offset to any federally supreme law, including federal antitrust law, *necessarily* also weakens other federally supreme law, including federal patent law and denigrates the limited monopolies the latter authorizes. It cannot be expected, for example, that a sophisticated public will long continue to see merit in a patent system that constitutes a mere excuse for *private* arbitrary levy of a tax upon the ultimate consumer as a means of promoting the investment of risk capital in research. After all, Congress enjoys the power to pass federal tax laws which *will* promote the investment of risk capital in research by direct tax incentives that will fall equally upon all members of the public. It need not accomplish the same end by giving investors carte blanche to impose unequal and arbitrary financial burdens upon consumers of particular patented goods or by immunizing patent licensing from meaningful antitrust attack.

To so relegate promotion of risk capital investment in research to tax legislation would be consistent with the Constitution and its limited authorization of congressional power to establish a patent system, all of our patent laws from 1790 to the present date, the antitrust laws and the relevant pronouncements of the Supreme Court. For example, in *Motion Picture Patents Co.* v. *Universal Film Mfg. Co.*, 243 U.S. 502 (1917), the Court pointed out that "Since Pennock v. Dialogue * * * was decided in 1829, this Court has consistently held that the primary purpose of our patent laws is not the creation of private fortunes for the owners of patents but is 'to promote the progress of science and the useful arts' . * * *" In the same case the Court distinguished "between the rights which are given to the inventor by the patent law * * * and rights which he may create for himself by private contract which, however, are subject to the rules of general, as distinguished from those of patent, law. * * *" Under such "general" law, patents, pursuant to the present 35 U.S.C. 261, "have the attributes of personal property". Like other personal property they are subject to antitrust regulation.

To liken the patent having "the attribute of personal property" to real property, as some of the proponents of Amendment No. 24 who have testified before this subcommittee have done, is just a way of confusing the issue. Yet in defense of legalizing *per se* all geographic and field of use restrictions in patent licenses, it has been argued that patent rights are divisible in the same way that rights in real estate are divisible. As personal and not real property, however, patents must be considered in the same category with airplanes, automobiles, computers and common stock. While rights in these latter items of tangible and intangible property *may* in some instances be divisibie in kind, it is more often the fact that any subproperties so created are totally different from the primary property out of which they originated. A subpatent of limited geographic or field of use scope carved out by a patent owner from his whole patent right *may* be of the same ilk as the whole and may *not* conflict with federal free competition policy. If this is the case, no one, including the Department of Justice, would seek to void a contract which licenses such a subpatent right. In other instances, such subrights created by patent owners, absent examination for compliance with statutory and constitutional patentability criteria, are wholly dissimilar to the patent and constitute mere devices for dividing up and controlling commerce within the United States in particular patented commodities. To prevent by legislative flat any inquiry into these privately created subpatents and their disposition by private contract in the guise of furthering the federal patent system is simply to condone for special interest purposes, an antitrust violation, without promoting in any way either the progress of science and the useful arts or the public interest.

The virtual immunity of all types of royalty schemes from misuse or antitrust attack which would be achieved by enactment of Amendment No. 24 likewise seemingly springs from a failure to accept the *limited* nature of the patent grant as authorized by the Constitution and of all of our patent statutes since 1790. As recently as last week's *Blonder-Tongue* decision the Supreme Court stressed "the far-reaching social and economic consequences of a patent" which have caused the Court to condemn over and over again *all* "attempts to broaden the physical or temporal scope of the patent monopoly". Legislation exempting from judicial scrutiny royalty schemes that expand the patent monopoly beyond the subject matter defined in the patent claim or outside the patent's statutory period of life would run counter to all of this precedent. Similarly, a legislation which permits a patent owner by private contract, to control competition through the imposition of discriminatory royalty rates upon different licensees would neither clarify the law nor strengthen the patent grant, but would certainly impose burdens upon the public in the form of severe restraints upon competition.

So much of Amendment No. 24 as would subject present *per se* rules of misuse and antitrust violation to case-by-case reevaluation under a new and indeterminate patent law-based rule of reason approach serves no useful purpose. To the extent that the "nature of the patent right" is, as the President's Commission suggested in Recommendation XXII "uncertain", this legislative repeal of existing case law—which, by way of example, in the specific case of *per se* illegal tying clauses reaches back over 50 years to *Motion Picture Patents*—can only enhance the uncertainty.

The idea that legislation should be passed to revive in part the doctrines of licensee and assignor estoppel on the pretext that this will promote "fair play" is similarly anomalous. In the first place, it is difficult to perceive that either of these doctrines have ever been justifiable as private contract law. It has always been elemental contract law that failure of consideration is a valid ground on which to render a contract void. It seems to follow that if a patent is in fact invalid, any licensee should be free to challenge it even as the lessee of a defective airplane is free to challenge his lease contract. Just as the airplane lessee need not renounce future benefits if his challenge should prove misplaced, and need not tender payment up to the date of challenge unless the challenge proves misplaced, the patent licensee should not need to act differently in like circumstances. Indeed, the patent licensee *should*, because of the public interest in patent validity, have even *more* freedom to challenge his bargain than the airplane lessee.

In the case of assignor estoppel it is particularly necessary to recognize the practical fact that the vast majority of "assignors" are the actual named inventors of subject matter to be covered in patent applications who, pursuant to employment contracts, must assign to their corporate employers all patent rights in the inventions made during the course of employment. Such individuals who are, at the time of assignment, the servants in law of their corporate assignees have no rights to direct and control the prosecution before the Patent Office by the assignees' attorneys of the assigned patent applications. While they may supply the assignees' attorneys with facts relating to prior art and other bases on which the alleged inventions constitute unpatentable subject matter, they cannot insure that this information will be presented to the Patent Office for consideration incident its evaluation of patentable merit. To decree legislatively that such individuals, in the event that they go into business for themselves in the technological fields of the assigned patents, are estopped to challenge validity is simply not consistent with reality and constitutes a deterrent to individual enterprise on the part of assignor-inventors. The relatively rare cases of patent assignment or "sale" in which the assignor stands on an equal footing with the assignee do not justify legislation so heavily slanted in favor of investors in research (assignees) to the obvious potential detriment of inventor-assignees and the public generally.

I strongly urge that legislation such as that represented by Amendment No. 24 be rejected in the Congress.

SUMMARY STATEMENT WITH RESPECT TO S. 643 GENERALLY

I have noted Senator McClellan's remarks at the opening of these hearings to the effect that "when significant differences of opinion exist as to what patent practices are in the public interest, the Congress should resolve the issue". Congress from 1790 up to the present has hewed firmly to the view that the patent practices which are in the public interest include a strong federal patent system which preempts inconsistent state law, places the public interest paramount, promotes progress in science and the useful arts by requiring a consistently high standard of invention, rewards inventors rather than investors and does so by conferring a temporally and physically limited patent monopoly. Since I believe that the law as it now exists is clear in these respects and that the protestations of uncertainty with which Congress is being bombarded in the present pseudo-crisis are but poorly disguised pleas for a new form of pseudo-patent not contemplated by the Constitution or any patent law Congress has heretofore passed, I urge that the bulk of the pending patent revision bill and particularly that portion encompassing Amendments Nos. 23 and 24 should not be enacted.

In the event that Congress, consistent with Senator McClellan's statement, believes that a new legislative pronouncement concerning "what patent practices are in the public interest" is desirable at this time, I strongly suggest that such legislation should take the form of a careful implementation and codification of the existing law. For example, new Section 103 of the patent act, if there is to be a new one, should carefully codify the standards of patentability enunciated by the Supreme Court in *Graham* v. *John Deere Co.*, 383 U.S. 1 (1966).

If a Section 301 is to be enacted, it should codify the federal supremacy of the patent laws which the Constitution itself requires and the Supreme Court has consistently recognized in many cases over many years including its relatively recent pronouncements in, *e.g.*, *Sears, Roebuck, Lear* and *Blonder-Tongue.*

If legislative provisions relating to patent licensing and misuse are to be adopted they should codify carefully the present rules of *per se* misuse, leaving to conventional antitrust "rule of reason" evaluation in the courts all questions relating to geographic and field of use licensing, royalty structures and royalty bases, discrimination among licensees and the like. Consistently with *Lear* and with *Scott Paper Co.*, licensee and assignor estoppels should be legislatively overruled.

Consistently with the Constitution and with the maintenance of a high constitutional standard of invention, any new statute should continue to require that inventors themselves apply for patent applications and make solemn oath or affirmation to support their applications—a precaution necessary, *inter alia*, to insure that members of corporate research departments conform to the standards of Section 103 by contributing inventions that exceed the ordinary skill of the art within their own peer groups.

I further urge that any more drastic revision of the patent laws, whether in the direction of a lowered standard of invention or a higher one, ought to await a detailed and comprehensive study of the question of whether the patent system as we now know it is performing its constitutionally authorized role of promoting progress in science and the useful arts. Really meaningful evaluation of that question is not possible in hearings such as these where the persons who have requested an opportunity to be heard each have strong personal opinions which may or may not be rooted in fact. Meaningful conclusions in this regard were equally not reached by the President's Commission on the patent system which simply "assumed" that the patent system had been responsible for technological progress in the United States without attempting to evaluate the validity of the assumption. In this connection I want to stress that I do not know what a properly conducted study would show, but I do strongly believe, based on the totality of my own experience in the representation of my clients, that it would augur strongly against any legislative relaxation of the high standards for patentability that statutes since 1790 have required.

Senator HART. Thank you, Mr. Irons. I have not finished reading your prepared testimony but I shall. But listening as I was reading to your informal presentation leaves me with this impression, that in your judgment, it is that the answers which are available to patent lawyers and which are displeasing answers rather than the uncertainty as to answers which should be assigned as a principal reason for the proposals here, is that right?

Mr. IRONS. Exactly.

Senator HART. Help me with this. There is an explicit constitutional grant of authority to the Congress to establish, provide for patents to promote the progress of science and useful arts. In one exchange here this morning, or at least from one witness, I remember hearing the argument that these amendments would foster the sale or marketing of patented products. Now, maybe we would have another basis for enacting legislation of that sort, but if we are limited to simply the grant of authority with respect to the useful arts, would there be a question of constitutionality that could be raised if in fact, its purpose and effect is to enhance the marketing of products?

Mr. IRONS. Well, the argument which you heard this morning, I think, involves a confusion of concepts. I am going to answer your question yes, if that were the primary purpose.

The idea of the patent system in the first place was to get a more prompt disclosure of information which would otherwise be practiced secretly. It has been repeated by the Supreme Court innumerable times that the primary purpose of the patent system is to obtain this disclosure, it is to benefit the public by the disclosure, and that the reward of the inventor is secondary and immaterial. You have to go back into history to understand what the patent system really means and how it was conceived originally. I am going to make a very short statement about this.

Senator HART. Well, you are not wasting your time with me. I am sure you are with everybody else in the room, but I would be glad to hear it.

Mr. IRONS. Well, all right. Many years ago, as long ago as 1850, investors, entrepreneurs, businessmen, began to try to turn the patent system upside down and to say its real purpose was to provide some mechanism so they could make more money, to be blunt about it. The Supreme Court, every time private interest has been put ahead of the public interest and the concept of making disclosures available to the public, has said the primary interest in the patent system is the public interest, it is not to line the pockets of investors. I can cite a half dozen Supreme Court cases that say this without variance.

But the argument never ends and we are constantly being importuned to turn the thing upside down and put the interest of the investor and the corporation, the patent owner, ahead of the interest of the public. And that is just what is going on with this legislation.

There is an old book called Robinson on Patents. It was published in 1890. It is recognized as authoritative and as we must in such cases, go back into history to see what was meant at an earlier day, I will just read one sentence out of it: "The constitutional idea was that of encouraging domestic invention and in the first patent law in 1790 and in all subsequent amendments of that law, the basic idea has been to encourage original invention. The introduction of these inventions into use was wisely left to the incentive of business enterprise." It is in this sense patents are like any other personal property. If you can figure out some way to merchandise a patent and make money out of it consistent with antitrust laws and other laws that regulate commerce and fair dealing, you are free to do it.

But you cannot justify under the constitutional clause patent some kind of legislation which is primarily intended to create an incentive to invest as distinguished from an incentive to invent. If you want to justify legislation which has as its purpose to create an incentive to invest, you must look to the commerce clause or somewhere else.

Senator HART. Well, you began your answer by reminding us that maybe we had mixed our concepts here. To get back to what was implicit in my poorly phrased question, would you regard the Scott amendments as constitutional?

Mr. IRONS. The question is a broad one. To extent that we are talking about amendment 23, which is the preemption amendment, I think it is unconstitutional on its face. I do not think it would survive a summary judgment motion. I do not think it would survive the first challenge. The reasons why are set forth in my statement. I have discussed this.

The others have many ramifications and can't be dealt with summarily. But I will answer the question to this extent: To the extent that any of these amendments permit under the state law of contract the generation of what amounts to a private monopoly at a contribution level, an invention level, if you will, that is lower than the constitutional standard, they are also unconstitutional. And it is precisely for this reason that the licensing of trade secrets, particularly trade secrets which are of little technological significance, gets into trouble. The purpose of the patent system is to give a person who has a contribution to make to science an option. He can keep it secret—I say secret—and he can practice it himself and as long as it is secret, it is his. His other option is to give up his secrecy, to seek a patent, to make the knowledge of the invention available to the public, and so promote the progress of science and the useful arts.

As soon as he walks across the street and grants a license on it and starts disclosing it to somebody else, pursuant to contract or otherwise it is not a secret any more and he is setting up his own little private contractual patent system and you run philosophically and logically into trouble with the whole basis upon which the American patent system is based.

Senator HART. Now I have a question about which I have some knowledge, and it is a relief.

When we passed the Clean Air Act last year, we put in a mandatory licensing feature. I am now departing from the Scott amendment here and turning to the basic revision bill, S. 643. The last page, section 6, strikes the clean air mandatory licensing feature and substitutes a requirement that if the administrator decides that the implementation of the purposes and intent of this act, the Clean Air Act, are being significantly retarded by any section of the patent law, he shall, after consulting with the Department of Commerce, recommend to Congress such modification of the patent law as may be necessary. Now, I am sure this opens up a whole other broad field, highly sensitive to the business of mandatory licensing. But because this codification is before the committee, I feel comfortable in asking you for your views with respect at least to that one section of codification.

Mr. IRONS. I will make this brief response. The first part of the response is that while the Constitution speaks of granting the exclusive right and it has long been recognized by the courts that "exclusive" is a flexible term and if there are circumstances which mandate a compulsory license, it can be legislated or ordered by court.

The second one is that when we have the legislation which has been passed and which obligates the automobile industry to achieve certain standards by 1975, I seriously believe that the Clean Air Act ought to stay like it is and I think that if it doesn't, the automobile industry is going to descend on Congress and demand an immunity from the antitrust laws while they try to comply with the Clean Air Act.

In all honesty, Senator, I have not thought deeply about this and that almost exhausts what I am in a position to say.

Senator HART. You are certainly right about what may be in the minds of the automobile makers.

Mr. Brennan?

Mr. BRENNAN. I have no questions.

Senator HART. Mr. Irons, thank you very much.

Mr. IRONS. Thank you, Senator Hart.

MR. BRENNAN. Senator McClellan, first of all, asked me, Senator Hart, to thank you for presiding today with your customary patience and fairness. Thank you very much.

The record will remain open until June 1.

Senator McClellan also asked me to announce that the Subcommittee would not attempt to mark up the bill until at least July 15. This does not suggest that we plan to start on July 15, but there will be no effort made at least until after that date to mark up the bill.

This concludes the hearings, Mr. Chairman.

Senator HART. We stand adjourned. I thank the gentlemen.

(Whereupon, at 4:15 p.m., the subcommittee was adjourned.)

(Appendix follows:)

APRIL 14, 1971.

Hon. WILLIAM D. RUCKELSHAUS,
Administrator, Environmental Protection Agency,
Washington, D.C.

DEAR MR. RUCKELSHAUS: During the consideration in the 91st Congress of S. 4358, the Clean Air Amendments Act of 1970, the Senate Committee on Public Works incorporated in that legislation section 309 providing in certain situations for mandatory licensing of patents, trade secrets and know-how. This provision was included in the bill without any hearings or without any consideration by the Committee on the Judiciary which has jurisdiction in patent matters. A modified version of this provision appears in section 308 of P.L. 91-604.

During the discussion of this legislation in the Conference Committee, the Secretary of Health, Education and Welfare, on behalf of the Administration indicated with respect to section 309 that "We are not convinced of the need for such a basic change in policy in light of its potential adverse effects and in the absence of known abuses."

Because of my desire not to delay the progress of the Clean Air legislation I did not seek to have the bill referred to the Committee on the Judiciary for a review of section 309. During the meetings of the Conference Committee and the discussion in the Senate of the conference report it was suggested that it would be desirable to have this issue reviewed by the Patents Subcommittee in the 92nd Congress. In order to provide a basis for such a review, I included in S. 643, for the general revision of the patent law, in section 6 of the transitional and supplementary provisions, language repealing section 308 and inserting in lieu thereof a provision that if the Administrator of the Environmental Protection Agency determines that the implementation of the Clean Air Amendments Act is being retarded by any provision of the patent law he shall recommend to the Congress such modification of the patent law as may be necessary.

The Senate Subcommittee on Patents, Trademarks and Copyrights on May 11, and 12 will conduct hearings on various patent issues. A complete enumeration of the various patent issues to be considered during these hearings appears in the Notice of Hearing at pags S 3726 of the Congressional Record of March 24.

It would assist the Subcommittee in determining its position on this issue if we could receive the views of the Environmental Protection Agency on the following matters:

1. Does the Environmental Protection Agency concur in the view of the Secretary of Health, Education and Welfare that there is no current need for mandatory licensing of patent rights?
2. If the Environmental Protection Agency concurs in this view, does the provision contained in S. 643 provide a reasonable basis to assure the implementation of the objectives of the Clean Air Amendments Act of 1970?
3. If there has been a change in the Administration position from that communicated by the Secretary of Health, Education and Welfare, what factual and supporting data is available to establish a current need for the compulsory licensing of patents in order to achieve the purposes of the Clean Air Amendments Act?

I would appreciate receiving a reply to this letter as soon as feasible. After I have had a chance to review your response it may be that the subcommittee will find it necessary to request a representative of your agency to testify during the forthcoming hearings.

With kindest personal regards, I am
Sincerely,

JOHN L. MCCLELLAN, *Chairman.*

ENVIRONMENTAL PROTECTION AGENCY,*
Washington, D.C., June 4, 1971.

Hon. JOHN J. MCCLELLAN,
Chairman, Subcommittee on Patents, Trademarks, and Copyrights, Committee on the Judiciary, U.S. Senate, Washington, D.C.

DEAR MR. CHAIRMAN: This is in response to your recent letter requesting our views on Section 6 of S. 643 which would repeal Section 308, Mandatory Licensing, of the Clean Air Act. We recommend that Section 308, which was added as part of the 1970 air pollution control amendments, not be repealed.

The Senate-passed revision of the 1970 Clean Air Act amendments, S. 4358, provided that holders of patents, trade secrets, and know-how relating to compli-

*This letter was received by the subcommittee on August 17, 1971.

ance with new stationary source performance, hazardous emission, and motor vehicle emission standards would be required under certain conditions, to share this information through the mechanism of mandatory licensing. Determination of the need for mandatory licensing would be made by the Secretary of Health, Education, and Welfare.

The House-passed revision of the 1970 amendments, H.R. 17255, differed in a number of respects from S. 4358. Among these was the absence of a mandatory licensing provision. In an effort to aid in passage of the Clean Air amendments in the second session of the 91st Congress, the Secretary of HEW made a number of recommendations to the House-Senate conference committee. It is our understanding that Secretary Richardson's letter which suggested deletion of the proposed Section 309 (predecessor to the present Section 308) was instrumental in a modification of the provison. As enacted, the provision was restricted solely to patents. The procedure requiring mandatory licensing was changed to provide that the Administrator inform the Attorney General that in the absence of such licensing, new stationary source performance, hazardous emission and motor vehicle emission standards could not be met. The Attorney General would then certify the matter to a district court which, after a hearing, would make the final determination.

Since enactment of the 1970 amendments, and the transfer of all authorities under the Clean Air Act, as amended, to EPA pursuant to reorganization plan 3 of 1970, we have had the opportunity to re-examine this matter. One argument advanced against mandatory licensing is that it would have the effect of decreasing research and entry into the air pollution control field. Our experience to date has been to the contrary. Since enactment of the provision in December 1970, we know of no cutback in air pollution control research nor do we know of any lessening of interest in entering the field on the part of the business community. In fact, our technical staff is visited almost daily by representatives of firms desiring to know how their organizations can become involved in the development of air pollution control systems.

The standards applicable to mandatory licensing under the Clean Air Act are designed to restore and insure protection of the Nation's health at the earliest possible date. Deleting the licensing provisions could have the effect of prolonging the date of the public's need and desire for a healthful air environment.

To what extent mandatory licensing would be necessary is at this point not entirely clear. As a general rule processes and systems covered by patents are made readily available through licensing agreements. However, we do not believe we can rely upon normal practice in such a critical area. The mandatory licensing provision should be kept in reserve for use if needed. In fact, such availability for use may serve as an incentive to voluntary agreements.

We believe it should be pointed out that the mandatory licensing provision offers protection to patent holders. Before a case can be referred to the Attorney General, EPA must first determine that a system or device meeting the requirements of the Standards is not readily available to users and that there are no reasonable alternatives to the system or device. Once a court decides that the above conditions are present, the patent holder would be allowed a reasonable royalty for the license.

For these reasons we urge the subcommittee to retain Section 308.

We are advised by the Office of Management and Budget that there is no objection to the submission of this proposed report.

Sincerely yours,

William D. Ruckelshaus, *Administrator.*

Department of Justice,
June 9, 1971.

Hon. James O. Eastland,
Chairman, Committee on the Judiciary,
U.S. Senate,
Washington, D.C.

Dear Senator: This is in response to your request for the views of the Department of Justice on S. 643, a bill "For the general revision of the Patents Laws, title 35 of the United States Code, and for other purposes."

S. 643 represents an effort to enact the first major revision of our patent system since 1836. The reforms suggested grew out of the Report to the President by the Commission on the Patent System submitted in December of 1966. The Commission found that it was essential (1) to improve the quality and reliability of United States patents, (2) to reduce the time and expense of obtaining patents, (3) to speed public disclosure of scientific and technological information, and (4) to move toward a more harmonious body of international patent laws. The public debate on the many bills introduced in Congress following this report has served to refine the issues and to broaden the general awareness of the many problems involved in this legislative effort.

The Department of Justice supports or has no objection to many of the changes which would be made by S. 643. However, several areas of concern to this Department remain. We therefore urge the adoption of modifications suggested below.

1. When applicants obtain patents from the United States Patent Office through fraud, deceit or inequitable conduct, it is the duty of this Department to protect the public interest that these patents not become a substantial burden upon commerce and to take steps to cancel the improperly procured patent. To minimize the chance of patents being improperly issued and to insure that those which are improperly obtained are cancelled any patent bill should contain safeguards to assist this Department in discerning improper conduct by applicants before the Patent Office and in taking appropriate corrective steps. In this connection, applicants should be required to make maximum disclosure of facts bearing upon the issuance of patents to them. On the one hand, this can be done by reinforcing the duties placed upon applicants to disclose facts known to them which would render their patents invalid. On the other hand, it can be avoided by making available, in *inter partes* proceedings before the Patent Office, discovery rules which will assure that all pertinent facts are placed before the Patent Office tribunals.

To make available in such *inter partes* proceedings all facts which may bear on issues which will affect the issuance of a patent, the discovery means should parallel as closely as possible those provided by the Federal Rules of Civil Procedure. Section 24 of the bill, however, does not provide that a District Court has full authority to issue subpoenas as the Court may deem necessary and appropriate; rather it provides that they are to be issued "in accordance with regulations established by the Commissioner for use in any case in the Patent Office." Nor does the section provide that the Commissioner of Patents has authority to issue subpoenas and orders for production of documents in accordance with statutory authorization.

The Department of Justice strongly opposes Section 24 of the bill because it would make the Federal Rules of Civil Procedure applicable to proceedings in the Patent Office only to the extent that such rules may be consistent with regulations promulgated by the Commissioner. The Department of Justice believes that the Federal Rules of Civil Procedure relating to attendance of witnesses and production of documents should be applicable to contested cases in the Patent Office, as is provided by Section 24 of present law. Section 24 of the bill, in effect, authorizes the Commissioner to make the Federal Rules of Civil Procedure, in whole or in part, inapplicable rather than applicable, abandoning pro tanto established judicial precedent interpreting the rules and substituting unknown and untried procedures with attendant uncertainty.

The Department of Justice would have no objection to an amendment of Section 24 which would incorporate by reference the Federal Rules of Civil Procedure relating to discovery, production of documents, and attendance of witnesses into the Patent Office Rules of Practice and authorizing the Commissioner and any members of the Board of Appeals to issue subpoenas and orders of production in accordance with those rules. Resort to the courts for such assistance would thus be eliminated.

2. A definition for abandonment, consistent with an amendment to Section 102(d)(5), discussed below, is recommended for insertion as Section 100(h):

> "(h) An invention is 'abandoned' when activity with respect thereto has terminated under circumstances establishing an intent not to resume activity with respect thereto. Proof of inactivity with respect to an invention for a period of one year shall constitute prima facie proof of abandonment of the invention. Although an invention may have once been abandoned for a period of time, if activity with respect thereto is later resumed, then it is not abandoned during such subsequent period of activity."

3. For the purpose of eliminating any possible doubt, proposed Section 100 should include a new definition that the term "person" as used in the bill includes those persons identified in 1 U.S.C. 1 *and* the United States. Otherwise the term "person" as used, for example, in proposed Sections 100(d), 191, 192 and 194 may be construed as defined in 1 U.S.C. 1 so as to exclude the Government.

4. Section 102 of the present Patent Code would be modified by proposed Section 102(d) in S. 643 to require "identical" disclosure or description in order for a patent, publication, prior knowledge, prior sale or public use to bar the grant of a patent on an invention in a pending application. Furthermore, the patent or publication which may be prior art, under the bills language, would have to be reasonably available to the public of the United States (Section 102(d)(1)). The Department of Justice believes these proposed changes in Section 102 of the present Code to be undesirable because an invention may be substantially disclosed or described in a prior publication, embodied in a device, or known to other persons even though not "identically" disclosed or described in the prior art. Identity of disclosure or identity of description are most unlikely. The present body of law on equivalence is sufficient to provide guidance for the type of "identity" that should be required in Section 102. Further, the new criterion of reasonable availability to the public of the United States in order for a patent or publication in this or a foreign country to be prior art overlooks the fact that present day library exchange systems, etc., make available publications in this and foreign countries to domestic researchers or interested persons even though the publication might not be considered available to the "public" of the United States in the sense of being on the shelf in numerous libraries throughout the country. The language of Section 102 of the present Code is, therefore, preferable to that of the bill and should be retained.

With respect to Section 102(d)(3), it is recommended that the words "or arts" be inserted after "art," inasmuch as many times subject matter is pertinent to more than a single art as the term is used in connection with classes of patentable subject matter.

With respect to Section 102(d(5), the following language should be substituted for the present language:

> "(5) An invention made in this country by another before the invention was made by the inventor, provided the invention of such other does not stand abandoned at the time of the invention which is the subject of the application; and provided, further, that such other has not suppressed or concealed his invention. However, in establishing priority of invention, an invention which has once been abandoned for a period of time shall not be accorded a date prior to the date of resumption of activity. In determining priority of invention, there shall be considered not only the respective dates of conception and reduction to practice of the invention, but also the reasonable diligence of one who was first to conceive and last to reduce to practice, from a time before conception by the other until his own reduction to practice."

The language set out above is believed preferable since it makes it clear that when an invention has been suppressed or concealed it will not be accorded a patent because public policy abhors suppression and concealment of inventions. However, mere abandonment does not prevent the abandoned invention from at a later point being revived and made the basis of a patent application.

Subsections 3, 4 and 5 of Section 102(d) should be relabeled and redrafted as Paragraphs (e), (f), and (g) of Section 102 since they do not appear to fall properly under subsection (d) of Section 102.

5. Section 103, as revised by S. 643, would provide that in order for prior art to bar the patenting of a claimed invention it must be shown that as a whole the subject matter of the patent was obvious from such prior art, rather than that it "would have been" obvious from such as is presently provided. The change suggests the necessity of showing that there was another person to whom the claimed invention was obvious. If no one other than the claimant was confronted with the problem giving rise to the discovery or invention, it would be impossible to meet this requirement. The present provision is preferable since it clearly bars patentability if a hypothetical person having a certain skill and a knowledge of the prior art would have found the claimed invention obvious.

We recommend the deletion of the last two sentences of Section 103 (at lines 26 to 33 of page 13 of the bill) and retention of the language of the present Section 103, so that the only negative condition for patentability is that patentability shall not be negatived by the manner in which the invention was made. The proposed additional language would unnecessarily complicate Section 103 and is not likely to be beneficial to the courts in arriving at valid conclusions on the issue of obviousness of a patented invention. The determination of obviousness versus nonobviousness of an invention involves so many interrelated factors that it is difficult to provide a check list which would properly relate all these factors to one another and to the issue of obviousness to be decided.

6. The oath required of an applicant by Section 115, as proposed by the bill, could be submitted by an owner or agent of the owner (Sections 111(a), (c)). The Department of Justice does not favor a dilution of the oath requirements of the present Code to the extent proposed by Section 111 of the bill. The present Code calls for an oath by the inventor except under such unusual circumstances as his death (35 U.S.C. 117), the refusal of an inventor to execute an application (35 U.S.C. 118) or in a situation where one joint inventor refuses to join in an application (35 U.S.C. 116). While supporting some of the liberalization of the oath requirement of Section 111 including an initial filing of an application with the signature of an agent of the applicant, it is desirable to continue to require an oath from the inventor, at least within a reasonable time after the filing of the application and in any event, if the inventor is reasonably available, before the issuance of the patent. The inventor's oath has been helpful in the past to pinpoint applications which have been fraudulently filed and to identify specific areas of inquiry in connection with the application. A case in point where the inventor's oath was of substantial assistance to pinpoint a fraud on the Patent Office is *United States* v. *Saf-T-Boom Corporation* (C.A. 8, 1970)—F. 2d—, 167 U.S.P.Q. 195.

The Department of Justice assumes that this provision does not change the requirement of present law that a new oath be filed at the time of any change in the subject matter sought to be patented.

7. Section 123 of the bill adds a new provision, not in the present Code, which would provide that the Commissioner may publish pending applications at the request of applicants. We recommend that proposed Section 123 be amended to make the publication of pending applications more useful to applicants and the public by permitting interferences with published applications both in the Patent Office and in the Courts. Interference-type proceedings in the courts are available to patentees under Section 291 of the present Code and would also be available to patentees under the provisions of the bill. Providing for interferences between patents and published applications will lead to wider use of the publication route for those applicants primarily interested in the defensive use of patents, including the ability to contest interfering subject matter with such patents in the courts.

8. Section 131 pertains to the examination of the patent application by the Patent Office. The bill in Cection 131(a) changes the language of the present statute from "it *appears* that the applicant is entitled to a patent" to "it is *determined* that the applicant is entiled to a patent." It is recommended that the legislative history state that the change has no effect upon existing law.

We recommend that Section 131(b) of the bill be deleted. To set an 18 month time limit within which the examination must be completed cannot serve any useful purpose. The Patent Office is already doing everything possible to expedite the handling and examination of applications.

Proposed Section 131(c) would authorize the Commissioner to require applicants to identify relevant patents, publications or other prior art which the applicant has considered in the preparation of his patent application and to supply an explanation as to why the alleged invention is patentable over such prior art. To assure that there be maximum disclosure of prior art known to an applicant and considered by him, it is recommended that "in preparing" at line 4 of subsection (c) be changed to "in connection with".

An inadvertent failure to comply with this requirement of disclosure of prior art would not be grounds "for holding a patent invalid or unenforceable, or subject the patentee to a charge of misuse." We recommend a modification to make it clear that the burden of showing inadvertence by clear and convincing evidence is on an applicant and that failure of an applicant to meet that burden will leave a presumption of lack of such inadvertence with any resulting patent being invalid or unenforceable. We further recommend that applicants be required to advise the Patent Office promptly of any relevant patents, publications, and other prior art which may become known prior to the issuance of the patent. Finally, the term "inadvertent failure" in proposed Section 131(c), line 9, should be changed to "excusable neglect" because of the greater legal certainty of this terminology and the body of law that has developed defining it.

Bills to revise the Patent Code introduced in the 90th Congress, S. 3892 and S. 1042, contained a proposed Section 131 as follows:

> "In all proceedings in the Patent Office in which the patentability of a claim is in issue, the applicant shall have the burden of persuading the Office that the claim is allowable."

We recommend the inclusion of this provision in the instant legislation.

9. Proposed Section 192 of the bill should make clear that the notification of the Commissioner provided by subsection (a) can take place at any time during the pendency of an application as well as after the issuance of a patent up to one year after issuance. This would permit *inter partes* proceedings with respect to the issues of public use and prior inventorship even before a patent issues. To assure that the proceeding will be an *inter partes* proceeding, subject to all the safeguards, including applicability of any needed discovery, it should be specifically provided that the person who notifies the Commissioner shall be entitled to participate in the proceeding as a party. A suggested substitution for the present language of Section 192 is as follows:

> "(a) At any time while an application for a patent is pending, or within one year after the issuance of a patent, any person may notify the Commissioner that—
>
> > "(1) the invention claimed in such application for patent or patent was in public use or on sale in this country more than one year before the actual filing date in the United States of such application for patent or patent;
> >
> > "(2) the subject matter of a claim of the application for patent or patent is not patentable under the provisions of Section 102(d)(5) of this title because of prior invention; or
> >
> > "(3) the inventor named in such application for patent or patent was not the original inventor of the subject matter claimed.
>
> "(b) If such person within the time specified above makes a prima facie showing, the matter shall be determined by the Board of Appeals, in such proceedings as the Commissioner shall establish and in which proceedings such person shall be entitled to participate as a party."

10. No civil action review in a United States District Court is available from a decision by the Commissioner of Patents under proposed Sections 192 and 193 of the bill. Since the Patent Office is not set up to hear the testimony of witnesses on such issues as public use or sale which may bar a patent application from issuing as a patent under proposed Section 102(d)(4), or in priority of invention contests under proposed Section 193, and since it does not provide for the scope of discovery available under the Federal Rules of Civil Procedure (see our comments on Section 24 of the bill, above), it is recommended that a civil review in United States District Courts under Sections 192 and 193 be available. Such review as to priority of invention contests is presently available by way of civil action under 35 U.S.C. 146. Furthermore, we recommend that a determination of the priority of invention issues, as a matter of public policy, be given statutory preference over a determination of the issues under Section 192 in S. 643. The reason for such preference in determinations is that prior inventorship may preclude a patent from being valid under Section 193 even though the interfering patent application may itself be barred by prior public use or sale pursuant to proposed Section 102(d)(4). This does not preclude the parties, if authorized by the Commissioner, from taking simultaneous testimony on both Section 192 and Section 193 issues.

11. Proposed Section 148 provides that in any appeal from the Board of Appeals to the United States Court of Customs and Patent Appeals, the Patent Office decision shall be given a presumption of correctness.

We recommend against enactment of Section 148 because the existing presumption of regularity of proceedings of administrative tribunals coupled with the presumption of validity of an issued patent under Section 282 should be sufficient guidance for the courts. Anything more would appear to place too great a burden on persons questioning the results of Patent Office investigations into patentability which must necessarily be limited in scope by the time available for considering each application.

12. The revision to Section 183 presented in the bill is a desirable one. In order to make certain that the provision will be construed as intended, it would be well to include in any report of the bill an explanation of the following type:

> "The Amendment of existing law proposed by Section 183 is intended as a limitation on the total period of recovery that may be permitted in one or more suits under Section 183 of the bill or under Section 1498 of title 28, U.S.C. and regardless of any term extension under Section 154(c) of the bill."

13. Section 251 relates to the reissue of defective patents. It is recommended that Section 251(b) be amended by substituting for "oath of the applicant

prescribed by Section 115 of this title shall not be required" the following: "application for reissue may be made and sworn to by the assignee of the entire interest." This proposed change results in retention of the existing oath requirements with respect to reissue applications of Section 251 of the present Code.

14. Section 261 pertaining in part to the assignability of patent rights is at issue in the "Scott Amendments". See Amendments 23 and 24 to S. 643 92nd Congress, 1st Session.

15. We object to Section 271(b) of the bill. This subsection provides that whoever imports into the United Staes a product made in another country by a process patented in the United States is liable as an infringer. Since a process patent for a process invention may well have issued in the foreign country in which the process is carried out (possibly to a different patentee), this provision could involve a double royalty payment and would also serve to block the importation of a product when none of the infringing process has been practiced in the United States. The Department of Justice recommends that Section 271(b) be limited to processes which cannot be patented in the foreign country of origin of the product resulting from the practice of the process.

16. Section 282 sets out the standard of proof and weight of evidence to which a party will be held in challenging the validity of a patent. Section 282(a) of the bill provides that invalidity of a patent for obviousness under Section 103 must be established by "clear and convincing evidence". The high costs of defending patent infringement suits, both by the Government in the Court of Claims and by private litigants in other courts of the United States, causes us to recommend that any strengthening of the presumption of validity of Section 282 of the present law is undesirable. This is in part caused by the fact that the present *ex parte* examination procedures to ascertain the patentability of inventions in the Patent Office are severely handicapped by time and resources. To further strengthen the presumption of validity at this time cannot be justified. Accordingly, the Department of Justice recommends that the standard of preponderance of evidence to show invalidity should be the same in Section 282(a) as in Sections 102 and 103.

17. The coverage of proposed Section 301 is unclear. While purporting to preserve rights other than patent rights, its language indicates that it applies to rights, whether or not subject to this title. Noting that Senator McClellan in introducing the predecessor bill S. 2756, 91st Congress, 1st Session, stated that the purpose of this Section 301 is to restate the "traditional interpretation" that the federal patent law does not pre-empt some vexatious problems of interpretation. We therefore recommend that this proposed section be deleted from the bill. It is noted that Amendment No. 23 to S. 643 pertains to Section 301 of the bill.

18. Section 1542, Sec. 6, would amend Section 308 of the Clean Air Amendments Act of 1970, 84 Stat. 1708 (Public Law 91–604) by striking out Section 308 and substituting for it a provision for recommendations, if necessary, for legislation to the Congress. Section 308 of the Clean Air Amendments Act of 1970 provides that if the Attorney General determines, upon application of the Administrator of the Environmental Protection Agency, that a right under a United States Patent is necessary to enable any person to comply with specified sections of the Act, there are no reasonable alternative methods to accomplish this, and that unavailability of such patent rights may result in a substantial lessening of competition or tendency to create a monopoly in a line of Commerce in any section of the country, then the Attorney General may so certify to a District Court of the United States which may issue an order requiring the person who owns such patent to license it on such reasonable terms and conditions as the Court may determine.

Section 308 provides for specific limited conditions when a court upon a hearing may compel a patentee to license his invention on reasonable terms. To compel such licensing under Section 308 of the Act requires the Attorney General to make certain determinations that particular patent rights are necessary to carry out the intents of the Act, that reasonable alternatives are not available and that failure to have such patent rights available on reasonable terms may result in substantial lessening of competition or tendency to create a monopoly. Recognizing the important public purposes of the Clean Air Amendments Act and the social problems created by air pollution, the Department of Justice recommends retention of Section 308 of the Clean Air Amendments Act.

This supplements the views of the Department of Justice I expressed before the Subcommittee on Patents, Trademarks and Copyrights of your committee on May 11, 1971.

Sincerely yours.

RICHARD W. MCLAREN,
Assistant Attorney General, Antitrust Division.

DEPARTMENT OF JUSTICE,
June 9, 1971.

Hon. JAMES O. EASTLAND,
Chairman, Committee on the Judiciary, U.S. Senate, Washington, D.C.

DEAR SENATOR: We are submitting herewith our comments on Amendments Nos. 23 and 24 proposed for S. 643, 92nd Congress, a bill "For the general revision of the Patent Laws, Title 35 of the United States Code, and for other purposes.

Except for the suggested alternative provisions set forth in this letter, the Department recommends that Sections 261 and 271 of the present statute, Title 35 U.S.C., be retained. The Department in its comments on S. 643 opposed Section 301 of that bill and also opposes the substitute language for Section 301 in Amendment No. 23.

Amendment No. 23 provides that the Patent Code does not preempt federal or state nonpatent protection of intellectual property such as is afforded by the law of trade secrets, contracts, or unfair competition. This provision is contrary to a public policy of free competition and may, indeed, be unconstitutional.

This provision would overrule—or at least draw into question—two 1964 Supreme Court decisions, *Sears, Roebuck & Co.* v. *Stiffel Co.*, 376 U.S. 225 (1964), and *Compco Corp.* v. *Day-Brite Lighting*, 376 U.S. 234 (1964), which held that state unfair competition law could not be used to grant exclusive rights to products which are not patentable under federal law. These decisions have no effect upon the right of the States to impose labeling and other requirements in order to prevent consumer confusion. However, State law may not prevent one company from copying or duplicating unpatented products sold by another company.

The Patent Clause of the Constitution not only grants power to Congress but expresses a limitation beyond which Congress may not go. It may not "enlarge the patent without regard to the innovation, advancement or social benefit gained thereby." *Graham* v. *John Deere Co.*, 383 U.S. 1, 5–6 (1966). Amendment No. 23 would attempt to authorize State laws to protect unpatentable ideas and, indeed, perhaps go beyond the constitutional power conferred even on Congress. Accordingly, such State laws would not only be highly undesirable but also may be unconstitutional.

Of course, if substantial and valuable information is secret, such elements may form the basis for contractual consideration and some reasonable restrictions. However, public information to be protected from use by others must come within the federal law.

To grant what would in effect be patent power to the States would greatly impair our fundamental national policy in favor of free competition (see, e.g., Small Business Act of 1958, 15 U.S.C.A. § 631(a); *Northern Pacific Co.* v. *United States*, 356 U.S. 1, 4 (1957); *United States* v. *Philadelphia Nat'l Bank*, 374 U.S. 321, 372 (1963)), and result in conflicting rules hampering commerce. "[A]s Madison put it in *The Federalist* No. 43, the States 'cannot separately make effectual provision' for either patents or copyrights." *Sears, Roebuck & Co.* v. *Stiffel Co.*, 376 U.S. 225, 228 (1964).

Amendment No. 24 proposes a number of changes for Sections 261 and 271 of S. 643. This proposed amendment would for the first time introduce into the Patent Code specific provisions governing the conveyance of patents, overriding the provisions of general law, including the antitrust laws. The Department of Justice is opposed to these amendments, both in principle and as to drafting, for the reasons set out below.

First, these amendments propose a special antitrust "rule of reason" standard in the area of patent licensing heavily biased toward upholding anticompetitive patent licensing restrictions. The only criterion proposed in § 271(f)(2) for evaluating such restrictions is whether they are ". . . . reasonable . . . to secure to the patent owner the full benefit of his invention and patent grant." This proposed subsection is apparently designed to preserve from impending overruling the 1926 decision of the Supreme Court in *United States* v. *General Electric Co.*, 272 U.S. 476, which sanctioned price fixing in patent licenses, and to prevent the application of certain so-called *per se* antitrust rules which have been developed over the years by the Supreme Court.

Second, specific provisions dealing with the right to license and exact royalties (found mainly in proposed § 271(g)) would permit an extension of the patent monopoly beyond that statutorily granted—both in time and in technology covered. This proposal would make the non-exclusive exchange of patent rights at least presumptively valid, however concentrated the market involved or whatever the effect upon firms excluded from the arrangement. Additionally, this proposal would sanction, without qualification, package licensing (whether or not coerced), exaction of royalties not based on any patented subject matter, extension of the patent monopoly beyond the patent's expiration date, and discriminatory royalties, regardless of anticompetitive intent or effect.

Third, Amendment No. 24 would enunciate a principle that the patent owner's "right to exclude" may be fragmented into any number of pieces—dividing it by territories, customers, and fields-of-use, for example—and marketed in any way, regardless of anticompetitive intent or effect. Proposed § 261(b) defines the patent grant as a "bundle" of several different rights, not the constitutionally based "right to exclude" (35 U.S.C. § 154). The concept that the grant is divisable is elaborated in proposed § 271(f)(1) to give at least presumptive validity to field-of-use restrictions, regardless of anticompetitive intent or effect, and to sanction anticompetitive allocations of customers and markets.

Fourth, proposed §§ 271(e) and (f) would limit challenges to patent validity by patent licensees, now permitted by the Supreme Court opinion *Lear* v. *Adkins*, 395 U.S. 653 (1969). Although we recognize that possible implications of *Lear* could result in unfairness to patentees and disruption of litigation involving questions of patent validity, we oppose this provision as drafted, because it may unduly inhibit justifiable questioning of patent validity and because of its inflexible and arbitrary nature. We have, however, suggested below what we believe to be appropriate alternative proposals.

Unfairness to patentees could flow from the possible implication of *Lear*—with which we disagree as a matter of law—that a patent licensee may be able to continue to enjoy the benefits of a patent license while at the same time challenging the patent's validity. As pointed out by Lear, however, licensees may often be the only individuals with enough economic incentive to challenge a patent, and by this mechanism, the public would be protected from monopolies based upon invalid patents. The language proposed seeks to strike an appropriate balance between these conflicting considerations. It would make clear that nothing inheres in the law of patent conveyancing which negates the usual state contract law dealing with such matters as repudiation, anticipatory breach, and failure of consideration.

We also suggest there be a change to proposed § 271(e), dealing with assignor estoppel, as follows:

ASSIGNOR ESTOPPEL

No assignor of a patent shall contest, directly or indirectly, the validity of the assigned patent, unless and until such assignor shall have first restored to the assignee the consideration received for the assigned patent.

With respect to problems arising under *Lear*, we propose the following language:

LICENSEE ESTOPPEL

Nothing contained in this title shall be deemed to pre-empt the laws of the several states permitting a licensor in any patent licensing agreement to exercise any contractual right to terminate such licensing arrangement, upon the licensee's repudiation of his obligation to pay royalties on the ground that a claim or claims of the licensed patent or patents are invalid, with respect to the claim or claims of the patent or patents so challenged.

Disruption of patent validity litigation could result because, under *Lear*, the validity of patents may apparently be challenged in State court actions brought by licensors for royalties owing to them. As questions involving the validity of patents are most appropriately litigated in the federal court system, our suggested language, which follows, would provide for the removal of such actions to the appropriate district court:

Any civil action commenced in a State court in which a licensee under a patent licensing arrangement asserts the invalidity of any patent, or of any claim or claims of any patent, under which he is licensed, may be removed by any party to the district court of the United States for the district and division embracing the place wherein such action is pending.

The early cartel cases demonstrate that patent licensing may be the source of unnecessarily widespread monopoly power, permitting an industry-wide conspiracy to regulate and limit competition at the expense of the consumer. For example, the glass container industry was at one time almost completely cartelized, with entry blocked and interfirm competition eliminated. See *Hartford Empire Co. v. United States*, 323 U.S. 386 (1945). Titanium oxide patents became the basis for an international cartel. See *United States v. National Lead Co.*, 332 U.S. 319 (1947). Gypsum product prices were imposed on the entire industry by a series of uniform parallel license agreements. See *United States v. United States Gypsum Co.*, 333 U.S. 364 (1948). Other industries where such patent-based monopolies spread far beyond the initial grant include motion pictures, electric light bulbs, radios, and shoe machinery.

The fact that an anticompetitive restriction is not industry-wide and does not involve a whole combination of restrictions, as in many of the cartel cases, does not lessen its pernicious effect. As the Supreme Court held in *International Salt Co. v. United States*, 332 U.S. 392 (1947) (a patent tie-in case, involving a relatively small amount of tied product):

> "The volume of business affected by these contracts cannot be said to be insignificant or insubstantial and the tendency of the arrangement to accomplishment of monopoly seems obvious. Under the law, agreements are forbidden which 'tend to create a monopoly,' and it is immaterial that the tendency is a creeping one rather than one that proceeds at full gallop; nor does the law await arrival at the goal before condemning the direction of the movement."

See also *Klor's Inc. v. Broadway-Hale Stores, Inc.*, 359 U.S. 207, 213–214 (1959).

In summary, Amendments Nos. 23 and 24 will create uncertainty in an area that the courts have been clarifying, expand the patent monopoly beyond its legitimate scope, and change the current law to encourage such anticompetitive and anticonsumer activities as price fixing, market and consumer allocation, and tying.

Except for the alternative proposals suggested herein, the Department of Justice is strongly opposed to enactment of these proposed amendments.

This supplements the view of the Department of Justice I expressed before the Subcommittee on Patents, Trademarks and Copyrights of your committee on May 11, 1971.

Sincerely yours,

RICHARD W. MCLAREN,
Assistant Attorney General, Antitrust Division.

MEMORANDUM OF LAW BY DEPARTMENT OF JUSTICE, MAY 11, 1967

INTRODUCTION

A patent is not a limitless right; its use is not untrammeled. The patent law does not exist in a vacuum. Its goals must be reconciled and kept in harmony with other goals. The purpose of any general patent law revision should not be to immunize this body of law from the effects of other laws, but to maintain all in reconciliation and balance.[1] Of necessity, therefore, there are limits on the patent law, arising mostly as a result of an accommodation with commercial contract and antitrust laws.

Common goals simplify this accommodation; both the patent and antitrust laws seek to spur technological progress. The patent laws do so by giving inventors, as a reward for disclosing their inventions, the right for 17 years to exclude others from making, using, or selling the patented invention. The antitrust laws spur competitive progress by promoting business opportunity. The antitrust laws prevent artificial restraints upon the ability of businessmen to enter into markets and develop lines of business.

Thus, implementation of these two declared public policies in favor of competitive innovation require that the patent monopoly not be extended so as to infringe on the principles of the general law, including the common law of restraint of trade and, since 1890, the federal antitrust laws. See, *e.g.*, *United States v. Masonite Corp.*, 316 U.S. 265, 280 (1942); *Motion Picture Patents Co. v. Universal Film Mfg. Co.*, 243 U.S. 502, 514 (1917). In addition, both the patent and antitrust systems require that all ideas in general circulation be dedicated

[1] Much of the testimony before this Subcommittee assumed that the only parties of interest in a patent license, for example, were the patent owner and the licensee. The balancing of equities was considered only in terms of these two private parties.

Ignored was a third interest—the public interest in a free and open economy, in competitively set prices, in freedom from the exercise of fraudulent, illegally broad or unreasonably oppressive monopoly practices.

to the common good unless they are protected by a valid patent. See, *Lear* v. *Adkins*, 395 U.S. 653 (1969), *Blonder-Tongue Labs* v. *University Foundation*, — U.S. — (May 3, 1971).

The outside limits of the patent monopoly are defined by the Patent Clause (Art I, § 8, cl. 8) of the United States Constitution. This provides that:

> "The Congress shall have 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."[2]

"The clause is both a grant of power and a limitation." *Graham* v. *John Deere Co.*, 383 U.S. 1, 5 (1966).

As a result, contractual expansion of the patent monopoly outside the limits placed on it by the U.S. Constitution, the Patent Code, and the Patent Office is a violation of the patent laws, termed a "misuse."[3] In addition, as with other contracts, the patent licensing contract must comply with commercial contract law, and its use must be in tune with public policies governing commerce among the States, including the principles embodied in the antitrust laws. Accordingly, over many years the courts have been deciding cases of patent misuse and antitrust violation—cases to protect businessmen and consumers from abuse of the 17-year right to exclude others from making, using, and selling.

Proposed S. 643 and proposed Amendments No. 23 and No. 24 would alter this relationship. As we discuss below, S. 643 might be construed to weaken the standards for invention long maintained by the Supreme Court as necessary to justify the grant of a patent. In addition, changes proposed in S. 643 might facilitate fraud and deception on the Patent Office, and could raise the requirements for establishing invalidity of a patent, making it more difficult to ventilate improperly or fraudulently obtained patents. Current proposals for rewriting the patent laws would appear to facilitate the issuance of patents—subordinating questions of validity and possible impropriety in the procurement—rather than to assure that only valid and proper patents are issued and enforced.

Amendment No. 24 might override the general law and create significant exceptions to the antitrust laws in the area of patent conveyancing and licensing. Amendment No. 23 might empower States to grant patent-like protection to subject matter which is unpatentable under federal law.

Both proposed S. 643 and these proposed amendments could, arguably, reverse or overrule a number of Supreme Court decisions and create substantial uncertainty about the continuing authority of many others. Certainly, many will urge such an interpretation before the courts, and extensive litigation will be necessary to settle these matters.

Amendments No. 23 and No. 24, as well as certain changes to S. 643, are extremely broad and general. These proposed short-hand statutory formulae, when applied to the vast variety of specific patent and patent licensing situations, are subject to multiple interpretations, and, as a result, will create much uncertainty and confusion as to many heretofore well-established court precedents dealing with a number of specific patent and patent licensing situations.

In his testimony of May 11, 1971, Assistant Attorney General Richard W. McLaren touched on a number of these important issues, but in the interest of brevity, it was not possible to provide a detailed legal analysis of these many issues at that time.[4] In addition, the Chairman expressed interest at these hearings in what, if any, court decisions this proposed legislation and amendments would affect or overrule. In order to treat these questions, the Department of Justice submits this supplementary Memorandum of Law.

I. S. 643, THE PATENT REVISION BILL

A. Fraud in Patent Procurement

Recent decisions of the Federal Courts have held patents unenforceable against alleged infringers because of, among other things, "unclean hands," "fraud," "material misrepresentations," or an "intentional failure . . . to state material

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[2] This grant of power to the Congress to confer an "exclusive right" to inventors is now implemented by Title 35 of the United States Code. It establishes a Patent Office in the Department of Commerce, provides for proceedings and practice, states what shall be patentable, and provides for a 17-year exclusive right that has the attributes of conveyable personal property.

[3] Coupled with the limitations which the antitrust laws impose on transfer and use of all property rights, including patents, some forms of misuse which also have a significant competitive effect rise to the level of actual antitrust violations.

[4] The Department of Justice has already sent this Subcommittee written comments on S. 643 and Amendments No. 23 and No. 24 thereto, dated June 9, 1971. We will not repeat these comments to the extent they have already dealt with a given issue.

facts," in dealings with the United States Patent Office. The allegedly fradulent acts have included, among others, patenting the invention of another as one's own,[5] deliberate withholding of relevant prior art,[6] and deliberate suppression of relevant test or other factual material.[7]

Certain changes to the Patent Code proposed to be made by S. 643 and the two proposed amendments might facilitate such improper practices, making them easier to perpetrate, more difficult to discover, and less subject to challenge after discovery.

1. *The Oath of Invention and the Duty of Disclosure.* The *ex parte* nature of proceedings before the Patent Office raises particular difficulties in obtaining full and accurate disclosure of information—particularly information harmful to the applicant's position such as prior knowledge, sale, publication, or a prior published description of the alleged invention claimed. The applicant, the inventor, and the attorney or patent agent prosecuting the patent should all, therefore, be held to the highest duty of disclosure. In the words of the Supreme Court in *Precision Instrument Mfg. Co.* v. *Automotive Maintenance Machinery Co.*, 324 U.S. 806, 816–818 (1945):

> A patent by its very nature is affected with a public interest.... a patent is an exception to the general rule against monopolies and to the right to access to a free and open market.... Those who have applications pending with the Patent Office or who are parties to Patent Office proceedings have an *uncompromising duty* to report to it all facts concerning possible fraud or inequitableness underlying the applications in issue.... Only in that way can the Patent Office and the public escape from being classed among the "mute and helpless victims of deception and fraud." [Italic added.]

Another federal agency that relies primarily on *ex parte* disclosures is the Securities and Exchange Commission. As the Court stated in the *Monsanto* case, *supra*, n. 7 at 568, the Patent Office is analogous to the SEC:

> The patent applicant should be held to the same standard of truthful disclosure to the Patent Office that Congress has required of the sellers of securities to the public. Under the securities law, one who sells or offers securities for sale must not omit to state in his registration statement, prospectus, or any other communication directed to the public any material fact necessary to be stated in order to make the communication taken as a whole, not misleading. The same standard of candor should also apply to the patent applicant and when deliberately violated in order to mislead, should result in denial of a patent.

Under proposed §§ 111 and 115, the inventor himself would no longer be required to submit an oath of invention; the owner of the patent could do so instead. If the inventor is reasonably available, however, we believe he should file the oath of invention at some time before the issuance of the patent. The inventor is often the person most knowledgeable as to the background of the invention, and, in many cases, as to the pertinent prior art.

The Department of Commerce proposes permitting the owner of the application to file such an oath, simply as a matter of convenience. The inventor, therefore, would be under no legal obligation to attest to his invention or the truth of statements made in the patent application. This could dilute responsibility for making full disclosure to the Patent Office and render it difficult to hold any individual accountable for willful misrepresentations or deliberate falsifications of fact. We oppose the dilution of the inventor's responsibility to make an appropriate oath of invention.

It has also been suggested in the course of these hearings that if the person actually prosecuting the patent application before the Patent Office—the patent agent or attorney involved—becomes aware of pertinent prior art or public use, he too should be obligated to disclose this to the Patent Office prior to the issuance of the patent. As a matter of practice, the attorney or patent agent prosecuting the patent application is often the one who makes the search for pertinent prior art, and it is he who becomes aware of any prior art or invention that might act as a bar to the patent. Both the applicant and the person

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[5] *Shelco, Inc.* v. *Dow Chemical Co.*, 168 U.S.P.Q. 395 (N.D. Ill. 1970).
[6] *Beckman Instruments, Inc.* v. *Chemtronics, Inc.*, 428 F. 2d 555 (5th Cir. 1970); *Armour & Co.* v. *Swift & Co.*, 168 U.S.P.Q. 269 (N.D. Ill. 1970).
[7] *Monsanto Co.* v. *Rohm & Hass Co.*, 164 U.S.P.Q. 556 (E.D. Pa. 1970); see *American Cyanamid Co.* v. *F.T.C.*, 363 F. 2d 757 (6th Cir. 1966).

primarily responsible for the prosecution of the patent application, therefore, should be required, either by rule or statute, to advise the Patent Office promptly of any relevant prior art or public use which may be or becomes known to either of them prior to the issuance of the patent. To this end, both should file an oath prior to issuance that such has been done.[8]

A provision for such disclosure by the applicant, and presumably, the attorney or patent agent prosecuting his application, is found in proposed § 131(c), under which the Commissioner of Patents may require the applicant to file a patentability brief, containing the "prior art which the applicant has specifically considered in preparing his application for patent." [9] The burden of justifying failure fully to comply with this requirement, if such a patentability brief is requested, should be by clear and convincing evidence and be upon the applicant. Knowledge of and the facts concerning any such inadvertence are peculiarly in the possession of the applicant; it thus is reasonable to put the burden of showing inadvertence on him.

Failure of an applicant to meet that burden should lead to the conclusion that the failure to comply was not inadvertent, thus rendering any resulting patent invalid or unenforceable. The purpose of requiring such a patentability brief is to permit the Patent Office to rely on it and on the veracity of the patent applicant. To immunize the applicant by statute from any penalty for failure to make full disclosure in such a patentability brief provides him a possible loophole. Such a loophole, particularly in an *ex parte* proceeding, limits the beneficial effects of such a disclosure, and might permit it to be a screen for misleading, partial or deceptive disclosures.

2. *Adequacy of Disclosure in "Contested Cases."*

Some proceedings before the Patent Office—such as interferences—are adversary in nature. Our traditional adversary system of litigation, coupled with the pre-trial discovery permitted by the Federal Rules of Civil Procedure, provides for a thorough and fair way of obtaining all the evidence needed to decide a given dispute.

The Department of Commerce recommends, however, permitting the use of the federal discovery rules only "insofar as not inconsistent" with the regulations of the Patent Office. Further hindering the discovery of adequate information before the Patent Office, the Department of Commerce refuses any subpoena power to enforce whatever rules the Patent Office does adopt. We believe existing discovery rules (and appropriate means for enforcement thereof) should not be diluted.

3. *Procedural Barriers to Challenging Patent Validity and Discovering Possible Fraud on the Patent Office.* Part of proposed Amendment No. 24 (proposed §§ 261(e) and (f)) would have the effect of limiting challenges to the validity of a patent, whether based on deliberate fraud or misrepresentations before the Patent Office or on any other grounds. It is largely through such litigation as cited above that the instances of fraud, deliberate misrepresentations, or omission of material facts before the Patent Office have come to light. To muzzle such private litigation—particularly by patent licensees who may often be the only persons having enough economic incentive to challenge a patent—would permit such fraud to go undiscovered, and burden the public—the consumer and competing business—with invalid monopolies.

The Supreme Court in *Lear, Inc.* v. *Adkins*, 395 U.S. 653 (1969), ruled that challenge to a patent's validity by licensees is proper. Just recently, the Supreme Court, in a unanimous opinion, *Blonder-Tongue Labs* v. *University Foundation,*——*U.S.*——(May 3, 1971), reaffirmed the basic policies of *Lear*, stating

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[8] This could be accomplished by adding the following sentence (modified suitably to fit the particular patent bill involved) to the end of § 115:

"Prior to issuance and after notice of allowance, the agent or agents or attorney or attorneys who prepared or prosecuted the application, and the inventor, shall, unless good cause for not doing so is shown, each make oath that he believes to the best of his knowledge, the inventor to be the original and first inventor, that he is aware of no prior art that he reasonably believes to be more pertinent than that considered by the Patent Office, that he is aware of no prior public use or other facts which would bar the issuance of the patent, and that he has made full disclosure to the Patent Office of all facts he reasonably believes to be material to the prosecution of the case."

[9] As we have noted in our letter of June 9, 1971, to assure that there be maximum disclosure of prior art known to an applicant and considered by him, it is recommended that "in preparing" in this phrase be changed to "in connection with."

that certain Supreme Court "authorities encourage authoritative testing of patent validity." [10]

It is the stated purpose of proposed §§ 261(e) and (f), and of the Commerce Department's alternative draft, to limit such authoritative testing of patent validity by private parties. We oppose this effort to overrule or limit the Supreme Court opinion in *Lear* by legislation.[11]

The Department of Justice recognizes, however, that some of the implications of *Lear* may have unwanted or undesirable effects.

a. *Removal to Federal Courts*. One consequence of the Supreme Court's decision in *Lear, Inc.* v. *Adkins, supra*, is that the validity of patents may apparently be challenged in State court actions brought by licensors for royalties owing to them. Since a "federal question" defense to an action arising under States law does not give rise to a right to remove the action to federal court, the result will be litigation of questions of patent validity in courts of the several States.[12]

Congress has recognized that questions involving the validity of patents are most appropriately litigated in the federal court system, and therefore, it has provided, in 28 U.S.C. § 1338, that the federal courts shall have exclusive jurisdiction "of any civil action arising under any act of Congress relating to patents . . . " Moreover, it has provided special procedures in the Patent Code for the giving of notice to the Commissioner of Patents of actions for infringements of patents. 35 U.S.C. § 290.

Accordingly, we propose that, if a challenge is asserted to the validity of a patent in an action pending in a State court, the action shall be removable by any party to the district court for the district or division embracing the place where the action is pending. To accomplish this, we suggest the following language, designed to amend the Judicial Code by inserting a new section, 28 U.S.C. § 1442b:

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[10] In explaining the underlying rationale of *Lear*, the Supreme Court, in *Blonder-Tongue*, cited with approval many of the cases that this proposed legislation and the two amendments thereto might overrule or undercut:

"Although recognizing the patent system's desirable stimulus to invention, we have also viewed the patent as a monopoly which, although sanctioned by law, has the economic consequenecs attending other monopolies. A patent yielding returns for a device that fails to meet the congressionally imposed criteria of patentability is anomalous. This Court has observed:

"A patent by its very nature is affected with a public interest. . . . [It] is an exception to the general rule against monopolies and to the right to access to a free and open market. The far-reaching social and economic consequences of a patent, therefore, give the public a paramount interest in seeing that patent monopolies spring from backgrounds free from fraud or other inequitable conduct and that such monopolies are kept within their legitimate scope. *Precision Instrument Mfg. Co.* v. *Automotive Maintenance Machinery Co.*, 324 U.S. 806, 816 (1945).

"One obvious manifestation of this principle has been the series of decisions in which the Court has condemned attempts to broaden the physical or temporal scope of the patent monopoly. As stated in *Mercoid* v. *Mid-Continent Investment Co.*, 320 U.S. 666 (1944):

"The necessities or convenience of the patentee do not justify any use of the monopoly of the patent to create another monopoly. The fect that the patentee has the power to refuse a license does not enable him to enlarge the monopoly of the patent by the expedient of attaching conditions to its use. *United States* v. *Masonite Corp.*, [316 U.S. 265] 277 [(1942)]. The method by which the monopoly is sought to be extended is immaterial. *United States* v. *Univis Lens Co.*, [316 U.S. 241,] 251–52 [(1942)]. The patent is a privilege. But it is a privilege which is conditioned by a public purpose. It results from invention and is limited to the invention which it defines.

"A second group of authorities encourage authoritative testing of patent validity. In 1952, the Court indicated that a manufacturer of a device need not await the filing of a competitor's patent, but may institute his own suit under the Declaratory Judgment Act. *Kerotest Mfg. Co.* v. *C-O Two Fire Equipment Co., supra*, [342 U.S. 180 (1952)] at 185–186. Other decisions of this type involved removal of restrictions on those who would challenge the validity of patents."

Two terms ago in *Lear, Inc.* v. *Adkins*, we relied on both lines of authority to abrogate the doctrine that in a contract action for unpaid patent royalties the licensee of a patent is estopped from proving "that his licensor was demanding royalties for the use of an idea which was in reality a part of the public domain." 395 U.S., at 656. The principle that "federal law requires that all ideas in general circulation be dedicated to the common good unless they are protected by a valid patent." 395 U.S., at 668. found support in *Sears* and *Compco* and the first line of cases discussed above. The holding that licensee estoppel was no longer tenable was rooted in the second line [of] cases elimiuating obstacles to suit by those disposed to challenge the validity of a patent. 395 U.S., at 663–668. Moreover, as indicated earlier, we relied on practical considerations that patent licensees "may often be the only individuals with enough economic incentive to challenge the patentability of an inventor's discovery." 395 U.S., at 670.

[11] Because of the procedural barriers these proposed amendments raise, and because of their inflexible and arbitrary provisions, the effect of these proposed amendments is to overrule or modify not only the recent Supreme Court decision of *Lear* v. *Adkins*, but also the whole line of cases on which *Lear* was based, including *Pope* v. *Gormully*, 144 U.S. 224, 233–34 (1892); *Westinghouse Electric and Manufacturing Co.* v. *Formica Insulation Co.*, 266 U.S. 342 (1924); *Sola Electric Co.* v. *Jefferson Electric Co.*, 317 U.S. 173 (1942); *Scott Paper Co.* v. *Marcalus Mfg. Co.*, 326 U.S. 249 (1945); and *MacGregor* v. *Westinghouse Electric & Mfg. Co.*, 329 U.S. 402, 416 (1947).

[12] See *Bailey* v. *Logan Square Typographers, Inc.*, 169 U.S.P.Q. 322 (7th Cir. 1971).

Any civil action commenced in a state court in which a licensee under a patent licensing arrangement asserts the invalidity of any patent, or of any claim or claims of any patent, under which he is licensed, may be removed by any party to the district court of the United States for the district and division embracing the place wherein such action is pending.

b. *Permitting the Parties to Provide by Contract for Termination of a Patent License Upon the Licensee's Repudiation of his Obligation to Pay Royalties.* Unfairness could result if the courts should extend *Lear*—which we do not believe they will—and hold that a patent licensee may be able to continue to enjoy the benefits of a patent license while at the same time challenging the patent's validity.

On the other hand, as the Supreme Court recognized in *Lear*, "licensees may often be the only individuals with enough economic incentive to challenge the patentability of an inventor's discovery. If they are muzzled, the public may continually be required to pay tribute to would-be monopolists without need or justification." 395 U.S. at 670.

The alternative proposal made below seeks to strike a balance between the interest of the patentee, who rightly expects that his licensee is dealing in good faith, and the interest of the public in being protected from monopolies based upon invalid or fraudulently procured patents.

A licensee's assertion of patent invalidity—whether based on alleged fraud or other grounds—will generally, if not necessarily, occur in connection with his repudiation of his obligation to pay royalties. Under the contract law of many states, and by agreement in almost every patent license drafted, the repudiation by the license of his obligation to pay royalties gives rise to the option in the patentee to terminate the license agreement, at least with respect to the patents or claims as to which the licensee has refused to pay royalities.

Thus, under the existing state law of contracts, the patentee has available to him a wide choice as to the type of relief which he can seek in the event the validity of the patent is upheld. He can terminate the license and request injunctive relief against further infringement. Or, if he prefers, he can request that the licensee be held to the terms of the license agreement (which may result in greater financial reward to the patentee than injunctive relief). In either event, the question of the validity of the patent would be *res judicata* in any subsequent litigation between patentee and licensee, whether for infringement or in contract for royalties.

There is fear, however, that *Lear* can be interpreted to remove one of the options now available to the patentee—namely, his ability to terminate a license if the patent on which it is based is challenged by the licensee. The proposed legislative solution, § 261 (f), however, would be equally arbitrary. It would appear to force the patentee's license to be terminated by the licensee, if the licensee challenged the validity of the underlying patent, and likewise, regardless of the circumstances or worthlessness of the challenged patent, would force the licensee to pay the royalties due prior to such termination, possibly as a condition for bringing such challenge.[13]

We suggest the following language, amending the Patent Code by adding a new section 35 U.S.C. § 301:

Nothing contained in this title shall be deemed to pre-empt the laws of the several states[14] permitting a licensor in any patent licensing agreement to

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[13] Alternate § 271(f) proposed by the Department of Commerce would not require the payment of royalties owed prior to termination as a condition for asserting invalidity of a licensed patent, but would not relieve the licensee of liability for such royalties accrued for the period prior to such termination.

Thus under both Amendment No. 24 and the Commerce alternative, a patent owner could arguably enforce a license, prior to termination, no matter how worthless the underlying patent or fraudulent its procurement. We strongly oppose such mandatory payment provisions. If a patent is worthless, its license may be worthless, and it would be improper and inequitable to enforce it in any way. Forcing payments for something worthless could act as an arbitrary barrier to challenging a patent's validity violating the policy of *Lear*.

[14] See 28 U.S.C. § 1652 (Rules of Decision Act construed to include case law and statutes).

> exercise any contractual right to terminate such licensing arrangement, upon the licensee's repudiation of his obligation to pay royalties on the ground that a claim or claims of the licensed patent or patents are invalid, with respect to the claim or claims of the patent or patents so challenged.

This suggested section differs from the proposed amendment (§ 261(f)) in several respects.

First, it preserves to the patentee the full range of options for relief if the validity of the patent is upheld. Proposed amendment § 261(f) would limit these options to injunctive and damage relief for infringement and would preclude a successful patentee from holding his licensee to the terms of his license agreement.

Second, it does not require a licensee to terminate a license agreement with respect to patents or claims under which he is licensed but whose invalidity he does not desire to assert in defense to an action for royalties. It does not seem equitable or in the public interest to require a licensee under multiple patents or claims to renounce all benefits under such a license in order to be able to assert the invalidity of one or more of the licensed patents or claims.

Thirdly, while the removal provision provides for Federal determination of patent validity, suggested § 301 would provide that the law of contracts, now a matter of state law, would remain a matter of state law, but that the feared implication of *Lear* would not be adopted by a state court or legislature out of deference to *Lear*.

c. *Assertion of Patent Invalidity by Assignor.* The Department would suggest consideration of the folowing language as an alternate to proposed § 261(e):

> No assignor of a patent shall contest, directly or indirectly, the validity of the assigned patent, unless and until such assignor shall have first restored to the assignee the consideration received for the assigned patent.

This proposed subsection would provide a mechanism for such assignor challenges by requiring an assignor who wished to assert that what he sold his assignee was worthless to act accordingly by returning to the assignee the consideration for the assignment. To deny him the right to assert grounds fo rpatent invalidity reasonably available to him when theassignment was made, as in proposed § 261(e), however, places him in a position other than that he would have under the general law of contracts. Such an anomaly, without special justification, is unnecessary. Furthermore, a large number of "assignors" are corporate employees who, pursuant to employment contracts, must assign to their corporate employers all patent rights in inventions made by them during the course of employment. Such agreements are not arms-length assignments and it is unlikely that the inventor at the time will have made an independent search of the prior art or have taken other legal steps to protect his rights as envisioned by proposed § 261e().

d. *Immunization of "No-Contest" Clauses From Antitrust Scrutiny.*—We oppose the provision proposed by the Department of Commerce (§ 271(f)) since it could be constructed to declare that an agreement not to contest the validity of any licensed claim or patent shall not ". . . serve as the basis for the finding of a misuse or illegal extension of the patent right." It is the stated purpose of this provision to overrule the Seventh Circuit decision in *Bendix* v. *Balax*, 421 F. 2d 809 (1970). We believe that agreements not to challenge the validity of patents can be used to insulate invalid patents from public ventilation, and collusion of this type in the past has led to fraud upon the Patent Office. We therefore oppose any proposal to immunize such agreements from the antitrust laws.

B. Criteria for Obtaining a Patent

1. *Standard of Invention—§103.*—An inventor can obtain a patent only if he has made an invention which sufficiently promotes the progress of science and the useful arts to satisfy the constitutional standard for patentability. As the Supreme Court declared in *Graham* v. *John Deere Co.*, 383 U.S. 1, 5–6 (1966):

> The Congress in the exercise of the patent power may not overreach the restraints imposed by the stated constitutional purpose. Nor may it enlarge the patent monopoly without regard to the inovation, advancement or social benefit gained thereby.

See also *Anderson's-Black Rock, Inc.* v. *Pavement Salvage Co., Inc.*, 396 U.S. 57 (1969).

Before the Patent Code was revised in 1952, it was silent as to any requirement for "invention." The Supreme Court, however, had formulated in 1850 a general condition of patentability in *Hotchkiss* v. *Greenwood,* 52 U.S. (11 How.)

248. The patent involved a mere substitution of materials—porcelain or clay for wood or metal in door knobs—and the Supreme Court held:

> . . . [U]nless more ingenuity and skill . . . were required . . . than were possessed by an ordinary mechanic acquainted with the business, there was an absence of that degree of skill and ingenuity which constitute essential elements of every invention. In other words, the improvement is the work of the skillful mechanic, not that of the inventor. (*Id.* at 267).

This same standard has been applied by the Supreme Court for over a century without deviation.

In *Thompson* v. *Boisselier*, 114 U.S. 1, 11 (1885) the Supreme Court reaffirmed the legal nature and constitutional origin of the question of invention:

> The provision of the Constitution, Art. 1, sec. 8, subdivision 8, is, that the Congress shall have 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 beneficiary must be an inventor and he must have made a discovery. The statute has always carried out this idea. . . . So, it is not enough that a thing shall be new, in the sense that in the shape or form in which it is produced it shall not have been known, and that it shall be useful, but it must, under the Constitution and the statute, amount to an invention or discovery.

In *Hill* v. *Wooster*, 132 U.S. 693, 700–701 (1890), the Supreme Court elaborated on *Boisselier*:

of the subject matter sought to be patented are a prerequisite to patentability.

> . . . This court, however, has repeatedly held that, under the Constitution and the Acts of Congress, a person, to be entitled to a patent, must have invented or discovered some new and useful arts, machine, manufacture or composition of matter, or some new and useful improvement thereof, and that "it is not enough that a thing shall be new, in the sense that in the shape or form in which it is produced it shall not have been before known, and that it shall be useful, but it must, under the Constitution and the Statute, amount to an invention or discovery."

The court has also held invalid patents for trifling advances, as subverting the Constitutional purpose. In *Atlantic Works* v. *Brady*, 107 U.S. 192, 200 (1883) the Court emphasized that:

> . . . It was never the object of those [the patent] laws to grant a monopoly for every trifling device. . . . Such an indiscriminate creation of exclusive privileges tends rather to obstruct than to stimulate invention. . . .

In 1952, Congress codified a statutory standard of invention—§ 103. Essentially, § 103 denied patentability if the subject matter sought to be patented "would have been obvious" to a person having ordinary skill in the art. In *Graham*, at 17, the Supreme Court held this did not change these previously enunciated standards:

> We believe that this legislative history, as well as other sources, shows that the revision [§ 103] was not intended by Congress to change the general level of patentable invention. We conclude that the section was intended merely as a codification of judicial precedents embracing the *Hotchkiss* condition, with congressional directions that inquiries into the obviousness of the subject matter sought to be patented are a prerequisite to patentability.

In addition, *Graham* stressed that in interpreting §103, it is, as in previous precedents, an objective standard of invention that is used.

Under § 103, the scope and content of the prior art are to be determined; differences between the prior art and the claims at issue are to be ascertained; and the level of ordinary skill in the pertinent art resolved. Against this background, the obviousness or nonobviousness of the subject matter is determined. (*Id.* at 17).

Changing § 103, as proposed in S. 643, from a standard of what "would have been obvious" to what "was obvious" could arguably change this objective standard to one involving a determination that there was, in fact, another person to whom the claimed invention was obvious at the time of the invention. The suggestion of the Department of Commerce to add a phrase to make this standard of invention one of what "was obvious at the time the invention was made" would emphasize even more this non-objective approach.

Such a literal interpretation of the "was obvious" standard is unlikely, however, in that it could have the effect in a given case of eliminating inquiry into the actual level of patentable invention. As, in many cases, it would be unlikely that anyone other than the applicant would have been confronted with the specific problem giving rise to the alleged invention, no one could be found to whom the alleged invention "was obvious at the time the invention was made." The patent laws, however, are not to be used "to grant a monopoly for every trifling device" (*Atlantic Works, supra*), and expert testimony would presumably have to be allowed—contrary to a possible literal reading of proposed § 103—to compare the subject matter of the patent and the background skill of the calling to help determine patentability.

What this change in language in § 103 would arguably do, however, is divert the Court's attention from an objective consideration of the improvement over the prior art made by the alleged invention, to consideration of other, less relevant, secondary criteria, such as commercial success, and unfulfilled need. These factors generally relate to the state of the market, and the marketing skill of the patent owner (not necessarily the inventor), and, as such, do not measure the inventors' contribution to the "progress of science and useful arts."

Although the Department of Commerce states these changes in § 103 are not intended to change present law, possible interpretations of these changes could subvert the Constitutional purposes of the patent system and unsettle over 120 years of judicial precedent. The expense of litigation and the confusion to private patent counseling pending a decision that these changes in § 103 are not intended to change the law, argue strongly against any changes in § 103 as it is now written and understood.

2. *Standard of Usefulness*—§ *100(g)*. S. 643 would introduce a definition of the term "useful" into § 100(g) of title 35 to include "utility in . . . research." Present law provides that a patent may be extended to anyone who invents or discovers a new or useful process, machine, etc. The term "useful" is not defined in the present code, but cases have held that the standard of patentable utility is not satisfied by a disclosure of a new chemical which may be useful only in research. (See, *Brenner* v. *Manson*, 383 U.S. 519 (1965), *In re July and Warrant*, 376 F. 2d 906 (C.C.P.A. 1967), *In re Kirk and Petrow*, 376 F. 2d 936 (C.C.P.A. 1967)).

We recommend that the proposed revision of § 100(g) be modified by eliminating the reference to research. If such patents are allowed they could foreclose whole areas of technology from research by others without disclosing anything of direct use to the public in exchange for the patent grant.

In this regard, the "utility" requirement of §§ 101 and 112 of Title 35 stands on much the same footing as the "invention" requirement, now embodied in § 103. In *Atlantic Works* v. *Brady, supra*, the Supreme Court pointed out how the progress of the useful arts advances by a series of small forward steps, each of which follows from similar prior steps and prepares the way for the next. To grant a monopoly over any such slight advance, where no more than ordinary mechanical or engineering skill is shown, "tends to obstruct rather than stimulate invention" (*id.*, at 200) for it chokes off the further piling of step upon step, by putting up a toll-barrier against the utilization of what has gone before to devise what is to come. By the same token, "an indiscriminate creation of exclusive privileges" (*ibid.*) in a given field, in cases where no present utility of the product produced is shown, has the same inhibiting effect. In this sense, the policies of the high standard of invention and the high standard of utility merge—to protect the progress of the useful arts against exclusive grants for that which fails to constitute a substantial contribution to the sum of human knowledge.

As the Supreme Court held in *Brenner* v. *Manson, supra*, at 534–535:

> The basic *quid pro quo* contemplated by the Constitution and the Congress for granting a patent monopoly is the benefit derived by the public from an invention with substantial utility. Unless and until a process is refined and developed to this point—where specific benefit exists in currently available form—there is insufficient justification for permitting an applicant to engross what may prove to be a broad field.

This proposed definition of "utility" would have the direct effect of overruling *Brenner* v. *Manson*. We oppose its enactment.

3. *Standard of Novelty*—§ 102. Prior knowledge, sale, public use, or a prior published description will presently render subject matter unpatentable under 35 U.S.C. § 102. These so-called "statutory bars" lend specificity to § 101's requirement that a patentable invention must be new or novel.

A number of changes in § 102 are proposed that would require "identical" disclosure to bar patentability. Literal identity of disclosure is most unlikely; normally, if there is a prior disclosure or public use, it will be of substantially the same invention. As a result, to require a prior identical disclosure would reward, as a rule, insufficiently novel material. The effect of this change could therefore be to emasculate § 102 and to make it more difficult to demonstrate that a given alleged invention had already been anticipated in the prior art.

It has been argued that "identical" disclosure is now required by the present law. This is not so. In *Deep Welding, Inc.* v. *Sciaky Bros., Inc.*, 417 F.2d 1227, 1234 (7th Cir. 1969), the Court held:

> [E]ven though the disclosures of the prior art may fall short of "complete anticipation," anticipation may be found where achieving complete anticipation only required that one of ordinary skill in the art merely exercised that skill to complete the work....
>
> [I]t is sufficient for anticipation "if the general aspects are the same and the difference in minor matters is only such as would suggest itself to one of ordinary skill in the art."
>
> *Amphenol Corp.* v. *Gen'l Time Corp.*, 397 F.2d 431, 437–438 (7th Cir. 1968).

Similarly, in *Tri-Wall Containers, Inc.* v. *Continental Can Co., Inc.*, 169 U.S.P.Q. 212 (S.D.N.Y. 1971), at 221, the Court stated:

> In determining whether an earlier product constitutes a prior public use of the innovation disclosed in the patent, courts do not insist upon complete identity, rather "It is enough if the two devices are substantially the same . . . or if the advance from one to the other did not amount to invention . . . but it is not enough that the two devices perform the same function and are somewhat similar in construction and mode of operation." 1 Walker, Patents 355–6 (Dellers ed. 1937). *Hall* v. *Macneale*, 107 U.S. 90 (1882); *Sperry Rand Corp.* v. *Bell Telephone Labs, Inc.*, 208 F. Supp. 598, (S.D.N.Y. 1962).

The present body of law on substantial sameness provides guidance for the degree of type of identity required under § 102. The use of the word "identical" would leave it open to argument that this established body of law had been changed. We oppose this change and the uncertainty and confusion it would cause, particularly as the purpose stated by the Department of Commerce is not to change the law in this area.

II. AMENDMENT NO. 24

This proposed amendment would for the first time introduce into the Patent Code specific provisions governing the conveyance of patents. These provisions would override the general law, including the antitrust laws. They could be interpreted to authorize such typical antitrust violations as price fixing, tying arrangements, and market division.

This legislative effort attempts to legalize a number of anticompetitive licensing practices. It is contrary to free enterprise competition which is our fundamental national economic policy, and to the interests of business and consumers alike.

The advantages of carefully and precisely providing for specific fact situations through judicial decision would be frustrated by general statutory provisions not allowing for such flexibility. This amendment will create uncertainty in an area that the courts have been clarifying. It may be interpreted to expand the patent monopoly beyond its legitimate scope, to benefit large, corporate patent holders to the disadvantage of small patent users, and substantially to lessen competition in the exploitation of technology. The resulting extension of monopoly power, we believe, would promote industrial concentration, encourage privately administered prices, and thereby increase inflationary tendencies.

The main justification put forward at the hearings for Amendments No. 23 and No. 24 was an alleged uncertainty of the law. Of at least equal importance, however, was concern as to the positions the Department of Justice has taken with respect to certain anticompetitive patent licensing practices.

It was suggested at the hearings that the Department of Justice is attemping to create new law or policies, thereby changing the law and creating uncertainty as to how fast or in what direction the law will change. However, the Department has not attempted to create new law or policies. The cases it has filed and the principles it has espoused have been laid down in Supreme Court precedents since the turn of the century. Indeed, the positions taken by the

Department comport fully with the advice that competent antitrust counsel have been giving their clients for years.

The fact that the Department of Justice, because of the decision in *United States* v. *Socony-Vacuum Oil Co.*, 310 U.S. 150 (1940) and its progeny, has sought for over 30 years to overturn the Supreme Court decision in *United States* v. *General Electric Co.*, 272 U.S. 476 (1927) (which permitted price fixing in certain patent licensing arrangements) is widely known and can hardly be labeled as a ground for uncertainty. The *General Electric Co.* holding as to price fixing has been seriously eroded by subsequent decisions, and few responsible counsel do or would recommend relying on this aspect of the decision. cision.

A statute necessarily paints with a broad brush. It can, among other things, prohibit certain activities (making them *per se* illegal), or it can permit certain activities (making them *per se* legal). If a statute permits a given activity, without any limitations or exceptions, it arguably permits that activity in all or any circumstances. It appears that this is the kind of certainty that these amendments would provide—rules of *per se* legality that would permit certain commercial practices regardless of any anticompetitive intent or effect, and regardless of their effect on the public.

For example, the Department of Commerce, in its prepared testimony at page 9, states:

> Our proposed section [§ 271(i)] identifies commonly used royalty or pricing practices which, standing alone, parties should be able to include in patent licensing agreements.

Apparently, evidence of use of compulsory packaging provisions and discriminatory pricing practices, which Commerce's proposed § 271(i) (§ 271(g) of Amendment No. 24) would arguably condone, would be neutral facts in any misuse or antitrust proceeding, regardless of anticompetitive intent or effect. Certainly, the statutory language in Commerce's proposed § 271(i)1(b–d), as well as § 271(g)2(B–D) of Amendment No. 24, contains no statutory limitation or suggestion that, for example, royalties that are computed without regard to the actual use of the invention, are limited in their use in any way. Yet the Department of Commerce recognized (page 35 of its May 10, 1971 letter) that such royalty provisions may be used illegally to extend the patent beyond the claimed invention.[15]

If such royalty practices are to be limited, as the Department of Commerce recognizes they have been in the past, to situations in which they do not involve an illegal extension of the patent or a violation of the antitrust laws, then passage of these amendments will cause considerable uncertainty. This ambigous and indefinite language will cause time-consuming, expensive litigation to resolve the fact that these proposed amendments are so limited, as some, but not all, proponents concede. In light of this, since the existing body of case law delineates to a large degree of certainty the boundaries between that which is permissible and that which is not, we strongly recommend against the passage of any such legislation.

Most commercial practices—such as patent licensing—which can involve the antitrust laws are such that they can be perfectly legitimate in some circumstances, but can be unreasonably anticompetitive and hence illegal in other circumstances. In such areas statutory rules as to *per se* legality or illegality may not be appropriate at all and should not be enacted.

The following is an effort to deal with the various specific patent licensing provisions that we believe Amendment No. 24 is designed to effect, and arguably to make *per se* legal, i.e., legal in all and any circumstances regardless of anticompetitive intent or effect.

A. Field of Use Licensing

In our testimony, we discussed §§ 261(b) and 271(f) as they relate to licensing less than all of the patent grant. These sections arguably attempt to immunize from challenge under all circumstances a patent owner's licensing of

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15 The word "solely" does not eliminate the anti-competitive effect of actions permitted in § 271(i) proposed by the Department of Commerce. This word does not detract from the fact that the subsection would permit restraints which are objectionable in themselves. Solely the licensing restraint cited, as the Department of Commerce recognizes, can have an illegal monopolistic effect. If there are such limits on the use of a given patent licensing practice, this limit should be specifically delineated in the statute. Otherwise, the statute may be interpreted to eliminate such already existing limits on a given practice and permit in all circumstances the patent licensing practices dealt with, regardless of their impact on competition or lack of legitimate business justification.

less than all of his patent right, e.g., less than all of the territory, patent term, uses, forms, quantities, or numbers of operations which might be licensed.[16]

Contrary to a number of the prepared statements at the hearings,[17] the Department of Justice does not object to field-of-use restrictions, as a general rule, where they have a legitimate primary purpose, are not unduly broad, and do not have a substantial anticompetitive effect. We will not raise objections even to exclusive field-of-use licensing arrangements where the effect is to encourage rather than to discourage competition, or where the effect is to encourage entry and permit a struggling newcomer to remain in the market long enough to gain a foothold.

On the other hand, field-of-use licensing, used to divide customers or markets, or which in operation injures the public, may well be unlawful. The overall argument against market division and field-of-use restrictions is that in some, but not necessarily all, circumstances such restrictions may allow the patent holder or his licensees to organize the market in such a manner that each of the submarkets is immune from competition. What starts out with a patent owner distributing his goods vertically may end up as a general horizontal agreement, often tacit, among the licensees, all of whom benefit from the particular restrictions imposed.

Those who argue that a patent owner may license in any way less than all of the patent grant regardless of anticompetitive intent or effect, are attempting to revive a theory that was specifically rejected by the Supreme Court in 1917. In *Motion Picture Patents Co.*, v. *Universal Film Mfg. Co.*, 243 U.S. 502, 514, the Court rejected the proposition that "since the patentee may withhold his patent altogether from public use, he must . . . be permitted to impose any conditions which he chooses upon any use which he may allow of it." The Court declared it illegal to license a patented motion picture projector for use only with the unpatented films of a licensee or his designee, stating such gave a patent owner "a potential power for evil over an industry" and that the licensing restriction "would be gravely injurious" to the public interest. 243 U.S. at 519.

Such proponents have, in addition, suggested that the Supreme Court decision of *General Talking Pictures* v. *Western Electric Co.*, 305 U.S. 124 (1938) reaches the conclusion that field-of-use restrictions are *per se* legal without regard to anticompetitive intent or effect. This case held that a license for manufacture and sale of patented sound equipment could be restricted by the patent owner to manufacture and sale for commercial sound reproduction. The holding of *General Talking Pictures*, however, has been limited by a number of later decisions. *Hartford-Empire* v. *United States*, 323 U.S. 386 (1945), declared unlawful a conspiracy to control and regulate the glass bottle making industry by means of license use restrictions. *Ethyl Gasoline Corp.* v. *United States*, 309 U.S. 436 (1940), held illegal license restrictions limiting the people to whom one could redistribute the licensed product. Whatever the remaining value of *General Talking Pictures*, the present law does not sanction all and every field-of-use restriction.

On the other hand, such carving up of the patent right may endanger competition. First, by lumping a whole list of restrictions together, this proposed amendment treats in a crude and uniform way restrictions widely differing in anticompetitive effect. No distinction is drawn between mere discrimination in pricing for different uses or customers, and total prohibition of end product competition; yet in the one case the restriction may be pro-competitive while at the other it may create a monopoly. See Gibbons, *Field Restrictions in Patent Transactions: Economic Discrimination and Restraint of Competition*, 66 Col.

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[16] The Department of Commerce in their proposed § 271(j), would make this fragmentation of the patent into any number of submonopolies explicit. This provision, arguably, could make all such fragmentations *per se* legal, not subject to challenge on any grounds.

[17] *Cairns, p.* 2—"It is apparent from the present attitude of the Anti-Trust section (sic) of the Justice Department as revealed in their testimony before this Subcommittee, as well as in other published statements that it is dedicated to establishing as illegal any limitation in a patent license agreement which amounts to anything less than the complete right to practice all rights granted to the patent owner."

Kirkbride, p. 5—"Since there appears to be some attempts by certain Federal agencies concerned with enforcement of our antitrust laws to curtail or eliminate field-of-use licensing, . . ."

Fonda, p. 2—"Apparently, the Justice Department wants to make people afraid to enter into licenses for less than all the rights of a patent."

L.R. 423, 424–427 (March, 1966). Likewise, Mr. Justice Brennan, concurring in *White Motor Co.* v. *United States*, 372 U.S. 253, 273 (1963), identified customer restrictions as presenting a problem "quite distinct from that of territorial limitations" and "inherently the more dangerons." Proposed Section 271(f), and § 271(j) proposed by the Department of Commerce, would lump these and all other field-of-use restrictions together.

Second, these proposed amendments could arguably make presumptively valid or *per se* legal a number of restrictions traditionally considered antitrust violations. In some circumstances, these amendments might protect market allocation, illegal under such cartel cases as *Hartford-Empire Co.* v. *United States, supra; United States* v. *National Lead Co.*, 322 U.S. 319 (1947); and *United States* v. *United States Gypsum Co.*, 333 U.S. 364 (1948); quantity restrictions, illegal under the doctrine well-established in *United States* v. *Socony-Vacuum Oil Co., supra;* and customer allocation, illegal under *United States* v. *Consolidated Laundries*, 291 F.2d 563 (2d Cir. 1961), and *United States* v. *Addyston Pipe and Steel Co.*, 85 Fed. 271 (6th Cir. 1898), *aff'd*, 175 U.S. 211 (1899).

Such market allocations may be bald efforts to restrain competition. The United States has recently challenged several such arrangements, e.g., *United States* v. *Bristol-Myers Co.*, Civil No. 822–70 (D.C.C., filed March 19, 1970) (bulk sales restrictions on wide spectrum antibiotic); *United States* v. *Fisons Ltd.*, Civil No. 69 C 1530 (N.D. Ill., filed July 23, 1969) (veterinary-human market division of anti-anemia agent); *United States* v. *Ciba Corporation*, Civil No. 791–69 (D.N.J., filed July 9, 1969) (combination product market division of diuretic). Bulk form and trademark restrictions prevent third parties, such as generic drug houses and private label firms, from securing the drugs in bulk form from the licensees or securing the drugs in dosage form under "off-brands" or private label. This limits the nmber of competitors marketing the drug, unjustifiably deprives the licensee of his economic freedom, and thereby restrains competition in the sale of the drug. The result is that prices are stabilized and protected against normal market forces.

B. Extension of the Patent Monopoly

In addition to possible abuses of field-of-use licensing (licensing less than all of the patent grant), it is also possible illegally to extend the scope of the patent monopoly—in time, in technology or products covered, and in the parties restrained. It has been found in numerous court decisions that certain licensing practices, because of their lack of legitimate justification and because of their adverse effect on competition beyond the claims of the patent, are unlawful as constituting misuse of the patent and may give rise to antitrust violations. Thus, it is unlawful to require a licensee to purchase unpatented materials from his licensor (tie-ins);[18] to restrict a licensee's freedom to deal in products or services not within the scope of a patent (tie-outs);[19] to require, as a *condition* of a license under a patent, that the licensee also take a license under other unwanted patents (compulsory package licensing);[20] to insist, as a *condition* of the license, that a licensee pay royalties in an amount not reasonably related to the licensor's sales of products covered by the patent;[21] to place restrictions upon a licensee's sales of unpatented products made by the use of a patented process;[22] and to require a licensee to assign the licensor any patent which may be issued to the licensee after the licensing arrangement is executed.[23] In each of these situations, the patentee is seeking to assert control over more than that which is the subject matter of the patent.

1. *Cross-Licensing, and Pooling.*—Proposed § 271(g)(1) in Amendment No. 24, as well as 271(i)2 proposed by the Department of Commerce, could be construed to make legal all non-exclusive exchanges of patent rights (open patent pools), however concentrated the markets involved or however discriminatory the ex-

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[18] *United States* v. *Loew's Inc.*, 371 U.S. 38 (1962); *International Salt Co.* v. *United States*, 332 U.S. 392 (1947).

[19] *McCullough* v. *Kammerer Corp.*, 166 F.2d 759 (9th Cir. 1948); *National Lockwasher Co.* v. *George K. Garrett Co.*, 137 F.2d 255 (3d Cir. 1943); *Park-In Theatres* v. *Paramount Richards Theatres*, 90 F.Supp. 727 (D.Del.), *aff'd per curiam*, 185 F.2d 407 (3d Cir. 1950).

[20] *American Securit Co.* v. *Shatterproof Glass Corp.*, 268 F.2d 769 (3d Cir. 1959).

[21] *Zenith Radio Corp.* v. *Hazeltine Research, Inc.*, 395 U.S. 100 (1969).

[22] *Cummer-Graham Co.* v. *Straight Side Basket Corp.*, 143 F.2d 646 (5th Cir. 1944); *United States* v. *Ziegler*, Civ. No. 1255–70 (D.D.C. 1970); Blue Book No. 2087.

[23] *United States* v. *Wisconsin Alumni Research Foundation*, 1970 CCH Trade Cas. ¶ 73,015 (consent decree). But see *Transparent Wrap Machine Corp.* v. *Stokes & Smith Co.*, 329 U.S. 627 (1949).

changing firms might be. To preclude examining the effect or overall purpose of such an open patent pool counters the whole thrust of the antitrust laws, stressing form over content. To quote *United States* v. *Krasnov*, 143 F. Supp. 184, 199 (E.D.Pa. 1956), *aff'd per curiam*, 355 U.S. 5 (1957) ;

Mr. Justice Brandeis [in *Standard Oil Co.* v. *United States*, 283 U.S. 163 (1931)] established the rule that a pooling arrangement or cross-licensing between competitors is not illegal in and of itself, but that it may become illegal if it is part of a larger plan to control interstate markets, stating,

> "Such contracts must be scrutinized to ascertain whether the restraints imposed are regulations reasonable under the *circumstances*, or whether their effect is to *suppress* or unduly restrict competition." [Emphasis added in *Krasnov*]

Furthermore, a nonexclusive exchange does not necessarily create a patent pool that, in economic effect, is truly open. For example, if all members of an industry agree to exchange patents that they develop, the incentive to compete in product development may be lessened. In addition, the structure or nature of an industry might require new entrants to join in such an agreement. The proposed amendments are not needed to legalize the simple situations already legal, and might have the damaging effect of preventing attack on the few seriously anticompetitive arrangements that have arisen in the past.

2. *Extending the Patent Monopoly Beyond the 17-year Monopoly Period.*—Proposed § 271(g)2(A) of Amendment No. 24, and § 271(i)1(a) proposed by the Department of Commerce, could be construed to authorize any patent royalty "in any amount, however paid." No court has ever suggested any royalty was illegal because it was extortionate except in a single case where the court originally thought an excessive royalty was being used as a means of resale price maintenance. *American Photocopy Equipment* v. *Rovico*, 359 F. 2d 745 (7th Cir. 1966), held that whether a patentee had charged "exhorbitant" royalties was a triable issue. At page 747, the court said.

> The record before us shows that the license agreements in effect require plaintiff's licensees to fix a minimum selling price far above the price which they would otherwise charge and the royalty policy of plaintiff is in violation of the antitrust laws of the United States, being exhorbitant and oppressive.

As a result. neither of these amendments is needed to protect excessive royalties that are not being used as a means of furthering some other antitrust abuse.

In addition, this proposal could have the effect of modifying the doctrine that post-expiration royalties are illegal. In *Brulotte* v. *Thys Co.*, 379 U.S. 29, 32–33 (1944), the Supreme Court, after considerable discussion, concluded "that a patentee's use of a royalty agreement that projects beyond the expiration date of the patent is unlawful *per se*. If that device were available to patentees, the free market visualized for the postexpiration period would be subject to monopoly influences that have no proper place here." In *Zenith Corp* v. *Hazeltine*, 395 U.S. 100, 136–37 (1969), the Court discussed Brulotte as follows:

> In *Brulotte* v. *Thys Co.*, *supra*, the patentee licensed the use of a patented machine, the license providing for the payment of a royalty for using the invention after, as well as before, the expiration date of the patent. Recognizing that the patentee could lawfully charge a royalty for practicing a patented invention prior to its expiration date and that the payment of this royalty could be postponed beyond that time, we noted that the post-expiration royalties were not for prior use but for current use, and were nothing less than an effort by the patentee to extend the term of his monopoly beyond that granted by low. *Brulotte* thus articulated in a particularized context the principle that a patentee may not use the power of his patent to levy a charge for making, using, or selling products not within the reach of the monopoly granted by the Government.

The language of the proposed provisions goes beyond mere postponement of royalties due for pre-expiration use of the patent. The proposed language would require only that amounts paid after expiration be "based solely upon activities prior to such expiration." Extension of the patent monopoly might therefore be achieved through contract provisions simply stating that later amounts were based upon pre-expiration activities. These could be hollow statements designed to permit collecting royalties for post-expiration use, an illegal extension of the patent monopoly. Or, such statements could provide for a legitimate postponement of royalty payments. The crucial question is under which circumstances post-expiration collection refers to pre-expiration activity, as opposed to post-expiration activity. As the proposed amendments are silent as to this issue, they will simply add confusion by their very existence—causing time-consuming, expensive, and confusing litigation as to what they mean, with no benefit ultimately to be achieved.

3. *Compulsory Package Licensing, and Royalties on any Patented Subject Matter.*—Proposed § 271(g)2(B & C), as well as § 271(i)1(b & c) proposed by the Department of Commerce, arguably authorize in all circumstances collection of royalties "not measured by the subject matter of the patent . . . [and] not computed in a manner that segregates the charge for any particular patent." We oppose these provisions because they could sanction, without qualifications, compulsory package licensing and exaction of royalties not based on any patented subject matter.

Package licensing and tying are objectionable because they often involve the use of leverage of one or more patents to force the licensee to accept licenses of other patents or purchase unpatented items.

Conditioning the license of one patent on licensing of other patents constitutes illegal package licensing (*United States* v. *Loew's Inc.*, 371 U.S. 38 (1962); *Rocform Corp.* v. *Acitelli-Standard Concrete Wall, Inc.*, 367 F.2d 678 (6th Cir. 1966); *American Security Co.* v. *Shatterproof Glass Corp.*, 268 F.2d 769 (3d Cir.), *cert. denied*, 361 U.S. 902 (19599)), as does adjusting royalty provisions in a manner that achieves the same result. In *Hazeltine Research, Inc.* v. *Zenith Corp.*, the district court found that the patentee's demand for a higher royalty on nine patents than for a package containing the nine plus others offended the package licensing doctrine. The Seventh Circuit affirmed and the Supreme Court approved. 239 F. Supp. 51, 77 (N.D. Ill. 1965), affirmed in part and reversed in part, 388 F.2d 25 (7th Cir. 1967), affirmed in part, reversed in part and remanded, 395 U.S. 100, 133–34 (1969).

In *Zenith* the Supreme Court stated, "[i]f convenience of the parties rather than patent power dictates the total-sales royalty provision, there are no misuses of the patents and no forbidden conditions attached to the license" (*id.*, at 138) and "[w]e also think patent misuse inheres in a patentee's insistence on percentage-of-sales royalty, regardless of use, and his rejection of licensee proposals to pay only for actual use." (*id.*, at 139). The decision as a whole emphasizes that the package or other like device must be desired by the licensee rather than result in any way from pressure by the patent owner—whether or not classifiable as "coercion." The provisions of the proposed amendments are not so constructed.[24]

For example, discriminatory royalties have been used to exclude new entrants (e.g., *United States* v. *United Mach. Corp.*, 110 F. Supp. 295 (D. Mass. 1953), affirmed *per curiam*, 347 U.S. 521 (1954)), to force purchase of unpatented goods (e.g., *Barbour Asphalt Corp.* v. *La Fera Grecco Contracting Co.*, 116 F. 2d 211, 214–16 (3d Cir. 1940); see *Motion Picture Patents Co.* v. *Universal Film Mfg. Co.*, 243 U.S. 502 (1917)), and to require package licensing (*American Security Co.* v. *Shatterproof Glass Corp.*, *supra; Hazeltine Research, Inc.* v. *Zenith Corp.*, *supra*). Where royalties are based on a flat fee or on a sliding scale as quantity sold increases, they may foster concentration in industry. Also, discriminatory royalties have been used to destroy competition, as in the case where a patent owner was said to have favored Gulf Coast shrimp firms in order to destroy the industry in the Pacific Northwest. *LaPeyre* v. *F.T.C.*, 366 F. 2d 117 (5th Cir. 1966); *Peelers Co.* v. *Wendt*, 260 F. Supp. 193 (W. D. Wash. 1966); *Laitram Corp.* v. *King Crab, Inc.*, 245 F. Supp. 1019, 244 F. Supp. 9 (D. Alaska 1965). It is often smaller companies which are unable to resist such discrimination, much to their competitive disadvantage.[25]

In addition, giving a blanket authorization to exact royalties not measured by the patent grant or extent of use, which these amendments might do, would change the basic principle that one should not exact royalties for one activity or product, if it is something else that is patented. The Supreme Court in *United States* v. *United Gypsum Co.*, 333 U.S. 364 (1948), criticized a royalty that was

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[24] I addition. this proposed language may permit and make *per se* legal another form of what may be field-of-use licensing—the licensing of particular claims of a patent. If the claims are essentially similar, as they often are, a patent owner could use the device of claim licensing to divide markets or to allocate customers or market lines.

[25] In addition, at least one other decision would be overruled, *Allied Research Products, Inc.* v. *Heatbath Corp.*, 300 F. Supp. 656 (N.D. Ill. 1969). In this case, the right of a patent owner arbitrarily to charge different consideration for similar licenses to different licensees was challenged successfully.

levied on all items whether or not covered by a patent, on the ground that this would discourage manufacturing of unpatented articles. Also possibly reversed by these proposals would be *Rocform Corp.* v. *Acitelli-Standard Concrete Wall, supra,* and *American Securit Co.* v. *Shatterproof Glass Corp., supra.*

4. *Royalty Rate Discrimination.*—§ 271(g)2(D) of Amendment No. 24, and § 271(i)1(d) proposed by the Department of Commerce, state that royalties are not illegal solely because they are "differing from that provided in some other arrangement." We oppose these proposed amendments because they may sanction discriminatory royalties in all circumstances, regardless of anticompetitive intent or effect.

The courts have not held that differing royalties always constitute discrimination, nor have they held that where discriminatory royalties exist they are always illegal. On the other hand, the courts have held that royalty discriminations which are predatorily motivated or which monopolistically restrain competition in other markets are illegal.

C. Special "Rule of Reason" Standard

In addition to making certain patent licensing provisions arguably immune from the antitrust laws (and from the patent law doctrine of "unclean hands," called "patent misuse"), these amendments propose a general standard for weighing the antitrust (or "patent misuse") effects of all other patent licensing or assignment provisions. These amendments are heavily biased toward upholding anticompetitive patent licensing provisions, however, for this proposed statutory standard would enact only one side of the equation; "unclean hands" or anticompetitive abuse are ignored. The only criterion proposed in § 271(f) (2) of Amendment No. 24 for evaluating such restrictions is whether they are" . . . reasonable . . . to secure to the patent owner the full benefit of his invention and patent grant."

If, as the proponents seem to suggest, this provision is not to change existing law, there is no need for its passage, for this generalized 16 word standard, itself not a model of clarity, will cause considerable uncertainty and litigation to establish what it means. The patent owner will, arguably, have to justify what is reasonable to secure him his "full benefit." Also, as this provision could be read to make the benefit to the patent owner the sole test of the lawfulness of restrictive conditions, there will have to be extensive litigation to determine what practices remain an unwarranted misuse of the patent monopoly, and, as well, an unreasonable restraint of competition beyond the patent grant.

At the hearings, Recommendation XXII of the Report of the President's Commission on the Patent System was cited as a justification for enactment of this amendment. But Recommendation XXII itself reveals obscure and confused phraseology. Indeed, the discussion accompanying Recommendation XXII seems to coincide more with our views rather than those of the Department of Commerce. For example, the Commission concludes its comments on Recommendation XXII as follows:

> There are also a number of conditions and provisions long associated with the transfer or license of rights under patents which must be distinguished from the exclusive right to make, use and sell conferred by the patent grant.[28] Among these are improvement grant-backs, cross licenses, package licenses, patent pools, no contest clauses, and many others which are simply matters of private contract, ancillary to the conveyance or license of a patent right. As such, these conditions and provisions must be judged, along with other purely commercial practices, under the antitrust laws and the patent misuse doctrine. The Commission does not recommend immunization of any of these other provisions or conditions from either the antitrust laws or the application of the misuse rule.
>
> This recommendation also makes it clear that a patent may not be used to control commerce in subject matter beyond the scope of the patent. For example, it could not be considered "reasonably necessary" to secure full benefit to the owner of a machine patent that he attempt to control any of the commerce in an unpatented raw material to be used in the machine. Neither could it be held that such an attempt had a direct relation to the machine claims in his patent. By the same standards, the patent owner

[28] This distinction is critical since it points up the difference between rights conferred by the patent grant and rights created by private contract. The latter are subject to the general law, including antitrust law.

could not control commerce in one of the unpatented elements of his combination invention where his claims are to the whole combination.

With all due respect to the Commission, appointed by President Johnson on July 23, 1965, it was not characterized by antitrust expertise—it was a group experienced and interested in patents, not antitrust.[27] Indeed, the rather tentative nature of Recommendation XXII was spelled out by the Co-chairman of the Commission, Judge Simon H. Rifkind, in his testimony before Subcommittee No. 3 of the Committee on the Judiciary of the House of Representative on April 26, 1967. Judge Rifkind testified as follows:

Chairman KASTENMEIER. Judge Rifkind, recommendation No. XXII of the Commission's report, would have written into the statute a formulation of the so-called rules of reason as a guide in determining issues of patent abuse. The bill before us does not follow this recommendation. Would you comment upon that exclusion?

Mr. RIFKIND. This is one of the areas with respect to which I said that I had very small, if any, expertise. My own private view, and perhaps I am being disloyal to my Commission, that this is an area which requires attention but that we did not have the time to go into it in sufficient depth for us to make a first-rate recommendation. I think having it here is good, because it draws attention to it. Not having it in the bill is also good because at this time it is not ripe, in my judgment, for translation into legislative form. You have two systems, the patent system and the antitrust system, which are compatible if carefully put together and yet they appear to have points of conflict. It is true that in recent years every time you want to enforce a patent, you are confronted with an antitrust counterclaim; it has become additionally expensive by reason thereof. You have got to get expensive counsel, because not many lawyers go into that field. It needs attention, Mr. Chairman, serious attention, but we did not have on our Commission a representative from the Department of Justice or the antitrust division as we did from other agencies. So that we really did not have the opportunity, in our debate, to clash ideas with those whose function it is to serve the antitrust policy of the United States. There was a lot of feeling about this and the Commission did vote it but I think it is really an invitation for further study rather than capable of being translated into immediate legislative policy.

1. *A Statutory "Rule of Reason" Approach.*—To the extent these proposed amendments establish a "rule of reason" approach (or give presumptive validity to certain practices), they make it impossible for the courts to establish rules of *per se* legality or illegality. This too could add to greater uncertainty and have unfavorable results. To require a case-by-case evaluation of all economic and other factors would typically raise many factual issues that are either extraordinarily difficult or quite insoluble. It would, therefore, make the application of antitrust law to patent licensing restrictions almost totally unpredictable. Such

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[27] The composition of the Commission was as follows:

Harry Huntt Ransom: Chancellor of the University of Texas.

Simon Rifkind: Formerly a District Judge of the United States District Court of the Southern District of New York and now a partner in the law firm of Paul, Weiss, Rifkind, Wharton & Garrison.

John Bardeen: Professor of physics and electrical engineering at the University of Illinois since 1951; formerly research physicist for the Bell Telephone Laboratories; an inventor.

James W. Birkenstock: Vice President of Commercial Development of IBM Corporation.

Edward J. Brenner: Commissioner of Patents from 1964–1969.

Charles F. Brown: Designee of the National Science Foundation.

Howard W. Clement: Partner in the patent firm of Hume, Clement, Hume & Lee; member of the Chicago and American Patent Law Associations.

Eugene J. Davidson: General Counsel of the Small Business Administration.

John M. Malloy: Deputy Assistant Secretary of Defense for Procurement; designee of the Department of Defense.

Howard K. Nason: President of Monsanto Research Corporation; holder of ten United States patents.

Sidney Neuman: Patent lawyer, former vice president of the Patent Law Association of Chicago.

Bernard M. Oliver: Vice President of Research and Development of the Hewlett-Packard Company.

Horton G. Stever: President of Carnegie-Mellon University since 1965; former Chairman of the Special Committee on Space Technology, National Aeronautics and Space Administration.

Charles B. Thornton: Chairman of the Board and chief executive officer of Litton Industries, Inc.

a "rule of reason" approach calls for long and expensive antitrust litigation, reducing predictability, and introducing so much data as to make rational decision-making so difficult as to lead to arbitrary results. See, Bok, "Section 7 of the Clayton Act and the Merging of Law and Economics," 74 Harv. L. Rev. 226, 287–299 (1960). Secondly, to the extent litigation depends on the power of the litigant to sustain prolonged and costly litigation, the rule of reason tends to entrench the bargaining power of the large licensee or patent owner against the small.

This proposal to overrule *per se* antitrust rules in cases involving patents not only would reverse many years of established law but is totally unwarranted. *Per se* rules arise only in situations where it is quite apparent that the conduct under scrutiny has *no* possible justification. These rules are ultimately established by the Supreme Court, which is very careful and sensitive in the creation and application of such rules. For example, in *Northern Pac. R. Co.* v. *United States*, 356 U.S. 1, 4–5 (1958), the Supreme Court explained the Sherman Act and *per se* rules in the following language:

> The Sherman Act was designed to be a comprehensive charter of economic liberty aimed at preserving free and unfettered competition as the rule of trade. It rests on the premise that the unrestrained interaction of competitive forces will yield the best allocation of our economic resources, the lowest prices, the highest quality and the greatest material progress, while at the same time providing an environment conducive to the preservation of our democratic political and social institutions. But even were that premise open to question, the policy unequivocally laid down by the Act is competition. And to this end it prohibits "Every contract, combination . . . or conspiracy in restraint of trade or commerce among the several States." Although this prohibition is literally all encompassing, the courts have construed it as precluding only those contracts or combinations which "unreasonably" restrain competition. *Standard Oil Co. of New Jersey* v. *United States*, 221 U.S. 1; *Chicago Board of Trade* v. *United States*, 246 U.S. 231.
>
> However, there are certain agreements or practices which because of their pernicious effect on competition and lack of any redeeming virtue are conclusively presumed to be unreasonable and therefore illegal without elaborate inquiry as to the precise harm they have caused or the business excuse for their use. This principle of *per se* unreasonableness not only makes the type of restraints which are proscribed by the Sherman Act more certain to the benefit of everyone concerned, but it also avoids the necessity for an incredibly complicated and prolonged economic investigation into the entire history of the industry involved, as well as related industries, in an effort to determine at large whether a particular restraint has been unreasonable—an inquiry so often wholly fruitless when undertaken. Among the practices which the courts have heretofore deemed to be unlawful in and of themselves are price fixing, *United States* v. *Socony-Vacuum Oil Co.*, 310 U.S. 150, 210; division of markets, *United States* v. *Addyston Pipe & Steel Co.*, 85 F. 271, aff'd, 175 U.S. 211; group boycotts, *Fashion Originators' Guild* v. *Federal Trade Comm'n*, 312 U.S. 457; and tying arrangements, *International Salt Co.* v. *United States*, 332 U.S. 392.

The Supreme Court applied the *per se* rule to a tying arrangement involved in the case. However, as evidence that *per se* rules are not rigid and unreasonable, the Court later affirmed a district court opinion which, in view of special circumstances, made an elaborate investigation of the reasonableness of a tying arrangement. *United States* v. *Jerrold Electronics Corp.*, 187 F. Supp. 545, 556 (E.D. Pa. 1960), affirmed *per curiam*, 365 U.S. 567 (1961). See also *Susser* v. *Carvel Corp.*, 206 F. Supp. 636 (S.D.N.Y. 1962), affirmed, 332 F. 2d 505 (2d Cir. 1964), *cert. dismissed*, 381 U.S. 125 (1965).

There is absolutely no basis for possibly overturning by legislation years of law so reasonably applied with such beneficial results.

2. *The General Electric Case.*—Additionally, this proposed amendment is apparently designed to preserve from impending overruling the old 1926 decision of the Supreme Court in *United States* v. *General Electric Co.*, 272 U.S. 746 (1926). There the Court stated (*id.* at 490) that General Electric could limit the method of sale and the price of light bulbs, "provided the conditions of sale are normally and reasonably adapted to secure pecuniary reward for the patentee's monopoly." Even the language of this specific case is not as restrictive as the

present proposal—securing to the patent owner the "full benefit" (whether or not "pecuniary" or whether or not "for the patentee's monopoly") of his invention.

After *General Electric*, in the *Univis Lens Co.* decision, the Supreme Court announced that the rights granted by a patent must be confined "strictly to the terms of the statutory grant." *United States* v. *Univis Lens Co.*, 316 U.S. 241, 251 (1942). See, also, Gibbons, "Price Fixing in Patent Licenses and the Antitrust Laws". 51 Va. L. Rev. 273 (1965). At the same term the Court in the *Masonite* decision stated that "the promotion of the progress of science and the useful arts is the 'main object'; reward of inventors is secondary and is merely a means to an end." *United States* v. *Masonite Corp.*, 316 U.S. 265, 278 (1942). And in 1948 four of the eight participating justices in *United States* v. *Line Material Co.*, 333 U.S. 287, 315 (1948), concluded that *General Electric* should be overruled. A 1965 effort by the Government to specifically obtain such overruling was thwarted because of a statement at trial that the Government was not seeking an overruling of the *General Electric* decision. *United States* v. *Huck Mfg. Co.*, 227 F. Supp. 791, 803 (E. D. Mich 1964), affirmed, 382 U.S. 197 (1965). Clark, "To Promote the Progress of . . . Useful Arts," 43 N.Y.U.L. Rev. 88, 99 (1968).

The patent owner is sufficiently rewarded by exploiting the patent himself or obtaining royalties. If his discovery is important his reward will be large; if it be unimportant he should not be able to utilize devices to increase the rewards and impose an unjust charge upon the public. *Motion Picture Patents Co.* v. *Universal Film Mfg. Co.*, 243 U.S. 502, 513–14 (1917). See *Zenith Corp.* v. *Hazeltine*, 395 U.S. 100, 135–36 (1969).

A price-fixing agreement is exactly the kind of arrangement to which a licensee might readily agree even if the patent is unimportant—both the patentee and the licensee benefit at the expense of the public. To permit price fixing would only invite many such arrangements and abuses which would far outnumber those situations where price fixing might conceivably be justified to promote any licensing at all. Permitting price fixing might well reduce innovative efforts of others to work around the patent. As Mr. Justice Douglas pointed out in his concurring opinion in *Line Material*, the offering of a price-fixing license is "a powerful inducement for the abandonment of competition, for the cessation of litigation concerning the validity of patents, for the acceptance of patents no matter how dubious, for the abandonment of research in the development of competing patents." 333 U.S. at 319.

Since 1927, price fixing has been a *per se* violation of the Sherman Act, e.g., *United States* v. *Trenton Potteries Co.*, 273 U.S. 392, 397 (1927), a conclusion clearly reaffirmed in *United States* v. *Socony-Vacuum Oil Co.*, *supra*. There is simply no reason why an exception should be made in the case of patents.[28]

The Department of Commerce in its proposed § 271(h) has recognized the problem of trying to retain the price fixing holding of *General Electric*. Their provision provides that the price fixing rule of the *General Electric* case should be changed; also outlawed are tying arrangements and agreements to deal or not deal in unpatented goods—matters which arguably come within the rule indicated in *General Electric*. Such internally contradictory provisions create confusion, because, as the precise arrangement validated in *General Electric* is specifically excluded, the "rule of reason" formula stated there derives no content from the historical circumstances in which the Court itself used such language.

The way the Department of Commerce would provide these limitations to their special "rule of reason" standard would create even more confusion and uncertainty. Their proposal spells out certain conduct as not subject to the special "rule of reason" standard as defined in their proposal. But their letter (page 33) indicated these five enumerated licensing practices are not considered *per se* illegal. Apparently there is to be some undefined third standard by which these five practices are to be judged.[29]

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[28] In a change proposed to Amendment No. 24, the "Tuesday-2" group specifically argues that proposed § 271(f), not different in substance from § 271(f) proposed in Amendment No. 24, should permit price fixing—"It would be entirely reasonable under these circumstances that the licensee be restricted to sell at a price no less than that of the patent owner." 23 P.T.C.J., p. E–7 (April 15, 1971).

[29] The Department of Commerce argues that their proposed special "rule of reason" standard (similar to that proposed in Amendment No. 24) codifies the existing "rule of reason" standard. This position is contradicted by their proposal that these enumerated practices are to be judged by some third standard.

To compound this confusion, some of the conduct enumerated by the Department of Commerce is presently illegal under the antitrust laws—multi-party price fixing, tie-ins, resale restrictions as to territory or customers, exclusive dealing, and joint determination of additional licensees. Some of the conduct specified by the Commerce Department proposal is not presently illegal under existing precedents—the first specification excepts conduct whereby a patentee agrees to fix prices with a single licensee, a practice specifically held legal in *General Electric*, and the third specification excepts all indirect limitations on resale—a prohibition that goes further than *United States* v. *Arnold Schwinn & Co.*, 388 U.S. 365 (1967). The final specification excepts the conduct condemned in *Krasnov*, but authorizes an exclusive license with right to sub-license, a practice whose ramifications have not yet been explored by the Supreme Court. At least here, as opposed to the proposed amendment to § 261(b), the proposal requires a right to sub-license to accompany the exclusive license.

In addition, the Department of Commerce would specifically exclude from "unclean hands" or antitrust challenge license agreements which were reasonable "at the time the license agreement is made"' Such language, arguably, could be used to isolate from challenge agreements, lawful at the time they were made, which subsequently had demonstrably adverse impact upon competition. If this interpretation were accepted, it would overturn the well established antitrust rule that a contractual practice or course of conduct is measured by its effect at the present. Practices which were proper years ago can by a change in circumstances or economic condition become undesirable later. The well recognized antitrust precedent of *United States* v. *Jerrold Elec. Corp.*, *supra*, is illustrative of this. Cf., *United States* v. *E. I. DuPont de Nemours and Co.*, 353 U.S. 586 (1957).

III. AMENDMENT NO. 23

We have already expressed and explained our strong opposition to Amendment No. 23, or to § 301 proposed in S. 643, in both our testimony and in our letter dated June 9, 1971.

The Department of Justice strongly opposes this proposed amendment, or those with the same effect, because it may well be interpreted as overruling *Sears, Roebuck & Co.* v. *Stiffel Co.*, 376 U.S. 225 (1964) and *Compco Corp.* v. *Day-Bright Lighting*, 376 U.S. 234 (1964) to the extent that they hold that state law of unfair competition may not interfere with the public right to copy the subject matter of an invalid or expired design patent. The extent of relief which may properly be granted against copying by the state law of unfair competition, and therefore the outer boundary of such a cause of action, is limited to the prohibition of deception of the public. Such a prohibition can be accomplished by requiring a label identifying the source or some other form of fair warning to the public. Copying an unpatented configuration, when the public is given a fair notice as to source, cannot be prohibited without conflicting with patent and antitrust policies guaranteeing the public free competition in the sale of goods. The *Sears-Compco* decisions hold that state law may not set up a local patent system to prevent one company from copying or duplicating unpatented products sold by another company; we believe this holding is correct and one compelled by federal patent policy.

Nothing the courts have done in the area of preemption warrants legislative action at this time. The appropriate time for legislation, if any, is after such event, not before.

IV. REPEAL OF MANDATORY LICENSING PROVISIONS OF CLEAN AIR ACT AMENDMENTS

Section 6 of S. 643 would amend § 308 of the Clean Air Act Amendments of 1970 by repealing the procedure set forth in that section for the licensing of patents which may be necessary to enable persons to comply with the anti-pollution provisions of that Act. We believe that the provisions of § 308 should be retained, and we therefore oppose enactment of § 6 of S. 643.

At the hearings, there was little, if any, discussion of the specific problems related to the Clean Air Act. Instead, witnesses in favor of § 6 of S. 643 simply made very general statements to the effect that compulsory licensing might decrease invention. They did not address the situation specifically dealt with in those Clean Air Act Amendments—namely, a guaranteed market for whatever anti-pollution device that is developed and patented. They did not consider the alternative apparently sought by the relevant industries affected, which according to one witness, is an exception to the antitrust laws to permit the four major automobile companies to pool research efforts (just the kind of collusion prohibited in the consent decree entered on October 29, 1969 in *United States* v. *Automobile Mfrs. Assn., Inc.*, 1969 Trade Cases, ¶ 72,907 (C.D. Cal)).

If this issue is to be dealt with fairly and fully, the specific problems being dealt with by the compulsory licensing provision should be considered. In two areas, legislatively, the United States Congress has already decided that compulsory, reasonable rate patent licensing was appropriate—as to patents relating to atomic energy (42 U.S.C. §§ 2182–2190), and to certain kinds of foodstuffs and other plant material (Section 44 of P.L. 91–577, the "Plant Variety Protection Act"). In this latter Act of Congress, the public interest in not having a patent monopoly block distribution or use of a given invention was found paramount if "necessary in order to insure an adequate supply of fiber, food, or feed in this country . . ." [30]

The Courts, too, have found that enforcement of the patent monopoly by injunction could be against the public interest. In City of *Milwaukee* v. *Activated Sludge, Inc.*, 69 F. 2d 577 (7th Cir. 1934), the Court of Appeals refused to enjoin the City of Milwaukee from infringing patents covering the operation of a sewage treatment plant. The Court said that to grant an injunction would result in pollution of Lake Michigan, and endangering the health and lives of the local citizenry (*id.* at 593). It therefore ruled that patent rights should be subordinated to the public interest. The Court did allow an accounting to be awarded; this is, of course, the direct analogue of compulsory, reasonable royalty licensing.

Similarly, in *Vitamin Technologists, Inc.* v. *Wisconsin Alumni Research Foundation*, 146 F. 2d 941 (9th Cir. 1944), the Court of Apepals ruled that the public interest was violated when a patentee refused to license, but tried legally to enforce, his drug patent (covering the process of producing vitamin D by ultraviolet radiation). The Court concluded that the patentee could not be allowed to enforce the patent, and went on, also, to refer the matter to the Attorney General of the United States for appropriate action to protect the public interest.

Where an appropriate situation arises, it is not unusual for this country (and most other countries) to provide for compulsory, reasonable royalty licensing of a patent where the public interest requires. We feel that, with the safeguards in § 308, the situation created by the imposition of mandatory antipollution standards by the Government are such to require access to a patented device if not otherwise reasonably available. We do not think research to this end will be restricted by this provision, and we think the suggested alternative of permitting the pooling of research efforts to be against the public interest. This alternative would be anticompetitive in effect, blunting the stimulus of competitive research and permitting possible collusion among competitors beyond that necessary to meet the goals of the Clean Air Act.

DEPARTMENT OF JUSTICE,
Washington, D.C., June 23, 1971.

Hon. JOHN L. MCCLELLAN,
Chairman, Subcommittee on Patents, Trademarks, and Copyrights, Committee on the Judiciary, U.S. Senate, Washington, D.C.

DEAR MR. CHAIRMAN: In reply to your letter of May 18, 1971, we have attached an appendix listing and enclosing the public statements by officials in the Department of Justice relating to patents and know-how.

A number of these speeches have been given on more than one occasion, perhaps in slightly modified form, but as best as we can determine, the enclosed texts represent a complete submittal back to January 20, 1969. We have also indicated where these speeches were reprinted as law review articles, to the extent this has come to our attention.

In our appendix, we have marked three speeches (McLaren, September 26, 1969; Stern, May 14, 1970; Wilson, November 6, 1970) and a portion of a fourth (McLaren, October 16, 1970, pp. 6–8) with an asterisk. We would appreciate your including these in your printed record of the hearings on S. 643,

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[30] In a third area, that of air pollution, the Congress already decided that the needs of the Clean Air Act did require the safeguard of this limited provision—§ 308. To bury this in with S. 643, the general patent revision bill, will force the Congress to accept the whole package, rather than to consider the needs of the Clean Air Act separately from those of general patent revision.

and Amendments No. 23 and 24. To our knowledge, these speeches have not been made generally available in printed form before. They represent our latest views on the subject matter dealt with, and, as we discuss further below, should allay some of the fears and misunderstanding alleged at these hearings. Additionally, we note from Senator Scott's opening statement that several already published law review articles dealing with know-how and *Lear* v. *Adkins* may be included in the printed record. Perhaps, in that event, you may wish to consider including in the printed record one other speech, (Stern, "Antitrust Implications of *Lear* v. *Adkins*," February 19, 1970).

Second, you have asked for a clarification by the Department of Justice of its views on the validity of patent license limitations, with specific reference to what some members of the patent bar have called the "no–yes" test. To answer your question, the Department of Justice and the Antitrust Division have not applied, do not now apply, and do not anticipate applying this so-called "no–yes" test to determine the *legality* of patent licensing limitations. We regret the possible misunderstanding raised at the hearings about this, particularly as Mr. Wilson and I attempted to clarify this in two speeches last year.

My original statement of the so-called "no–yes" test was made on June 5, 1969. I said:

> "In considering whether to attack a particular licensing provision or practice, we ask ourselves two fundamental questions. First, is the particular provision justifiable as necessary to the patentee's exploitation of his lawful monopoly? Second, are less restrictive alternatives which are more likely to foster competition available to the patentee? Where the answer to the first question is no, and the second yes, we will *consider* bringing a case challenging the restriction involved."

This summary formulation was never intended to be used to determine the legality of patent licensing limitations, nor were we prepared to urge this formula on the courts. Rather, this formulation was intended to indicate some of the factors we take into account in determining the kind of patent licensing restrictions we would "consider" prosecuting. Moreover, we necessarily consider other factors in deciding whether to prosecute—such as available manpower, other workload, budgetary factors generally, as well as impact on competition, and amount of commerce affected. As I said on January 29, 1970, "we will continue to scrutinize very carefully patent arrangements that appear to be unduly restrictive, or to unduly expand the scope of the patent grant." That is still true. We will investigate them—but will file suit only if, after such scrutiny, we find the law to have been violated.

Since some did not recognize the close relationship between the "no–yes" test and the ancient rule of "necessary and ancillary restraints," (See *United States* v. *Addyston Pipe and Steel Co.*, 85 Fed. 271 (6th Cir. 1898), aff'd. 175 U.S. 211 (1899); see also *United States* v. *Columbia Pictures Corp.*, 189 F.Supp. 153 (S.D.N.Y. 1960)), we attempted last year to clarify the "no–yes" statement. Last year, therefore, in two speeches (McLaren, October 16, 1970; Wilson, November 6, 1970), we attempted to set forth what we regarded as the proper test of legality, rather than our own standard for investigation. That test is the rule of reason.

The rule of reason in this area embraces three principal elements. First, the restriction or limitation must be ancillary to the lawful main purpose of a contract. Second, the scope and duration of the limitation must not be substantially greater than necessary to achieve that purpose. Third, the limitation must be otherwise reasonable in the circumstances.

This formulation of the rule of reason, I should stress, is short-hand—a generalized statement of a doctrine that has developed over many years. As to any specific patent licensing limitation, there is an extensive body of particular case law bearing thereon. If a patent or antitrust lawyer needs guidance in advising clients, it is to these particular cases he should turn—and to the refinements and principles expressed therein. He is also free, as Mr. Ward pointed out in his testimony, to take advantage of the business advisory and clearance procedures of our Department and the Federal Trade Commission.

Third, you have asked whether the Department of Justice wishes to furnish your Subcommittee with the text of a statutory provision incorporating its policy recommendations as to patent licensing. Except as we have already indicated in our testimony, we believe the present statutory structure as to patent licensing is appropriate and adequate, and we therefore decline to embody our policy recommendations in any new statutory language.

There is no Administration policy as to whether or not to have legislation in this area. Contrary to the Department of Commerce, the Department of Justice believes (except insofar as already indicated) that the present law would be far more appropriate and preferable to having any new legislation, and certainly much more preferable to enacting the Scott amendments or the Commerce alternatives thereto.

Detailed analysis of the cases on patents and antitrust indicates few areas of uncertainty, and with respect to those few areas, the uncertainty which does exist is simply the necessary price for the maintenance of flexibility in dealing with important and complicated issues of public economic policy. Chief Justice Hughes noted some 40 years ago the need for flexibility in dealing with the antitrust laws:

> "As a charter of freedom, the [Sherman Antitrust] [A]ct has a generality and adaptability comparable to that found to be desirable in constitutional provisions. It does not go into detailed definitions which might work injury to legitimate enterprise or through particularization defeat its purposes by providing loopholes for escape. The restrictions the act imposes are not mechanical or artificial. Its general phrases, interpreted to attain its fundamental objects, set up the essential standard of reasonableness." *Appalachian Coals, Inc.* v. *United States*, 288 U.S. 344, 359–360 (1933).

If your Subcommittee finds it desirable to legislate in this area, we would urge it to make a much more precise and particularized study than has been made to date. As to most particularized licensing limitations, there is already an established body of case law. What the proposed amendments are intended to do to any such given line of case law is still uncertain. The commerce affected by patent licensing is in the billions of dollars. The enactment of the proposed, 19 word, generalized "patent rule-of-reason" standard could adversely affect all of this, overruling years of established precedent, unsettling many established commercial relationships, and subjecting the consuming public to unjustified monopoly restrictions and exactions. We believe that whatever principles these amendments embody should be defined and explored, and the effect on given case law of specific statutory language be specifically considered.

If, in deliberating on this matter, your Subcommittee should decide to consider specific statutory language different from that already considered at the hearings, we would most appreciate the opportunity to present our views thereon and any assistance possible. We would hope you would consider the views of all interested legislative and executive agencies, including our own, in dealing with this complex and vitally important subject.

If we can be of any further assistance, please do not hesitate to contact us.

Sincerely,

RICHARD W. MCLAREN,
Assistant Attorney General, Antitrust Division.

PUBLIC STATEMENTS BY OFFICIALS OF THE DEPARTMENT OF JUSTICE RELATING TO PATENTS AND KNOW-HOW [1]

I. FRAUD ON THE PATENT OFFICE

Richard H. Stern, "The Antitrust Consequences of Fradulent Procurement and Enforcement of Patents," May 14, 1970.

Richard H. Stern, "A Future Look at Patent Fraud and Antitrust Laws," September 25, 1969, reprinted in 52 J.P.O.S. 3 (1970).

(Note: This speech was given while Mr. Stern was an official at the Department of Commerce; the contents of this speech were reviewed and cleared by his superiors there rather than by those at the Department of Justice.)

II. PATENT LICENSING GENERALLY

Bruce B. Wilson, "Patent and Know-How License Agreements: Field of Use, Territorial, Price and Quantity Restrictions," November 6, 1970.

Richard H. Stern, "The Antitrust Laws and Restrictive Patent Licensing Provisions," April 20, 1970.

Richard W. McLaren, "Remarks," April 9, 1970, pp. 2–4.

[1] Statements within each subject category are listed in reverse chronological order.

Richard W. McLaren, "Antitrust—the Year Past and the Year Ahead," January 29, 1970, pp. 15–16.
Bruce B. Wilson, "Patents and Antitrust: the Legitimate Bounds of the Lawful Monopoly," November 19, 1969.
Roland W. Donnem, "The Antitrust Attack on Restrictive Patent License Provisions," September 25, 1969, reprinted in 14 Antitrust Bull. 749 (1969).
Richard W. McLaren, "Patent Licenses and Antitrust Considerations," June 5, 1969, reprinted in 13 IDEA 61 (1969).
Richard W. McLaren, "Recent Cases, Current Enforcement Views, and Possible New Antitrust Legislation," March 27, 1969, pp. 3–4.

III. INTERNATIONAL LICENSING

Richard H. Stern, "Territorial Limitations in International Technology Agreements," February 17, 1971.
Richard H. Stern, "The Antitrust Status of Territorial Limitations in International Patent Licensing," January 27, 1971.
(These two speeches have been given on a number of occasions, and can be found in a combined form in 14 IDEA 580 (1971)).
Richard W. McLaren, "Competition in the Foreign Commerce of the United States," October 16, 1970, pp. 6–8.
Walker B. Comegys, "The Application of Antitrust Principles to International Trade and Investment," May 7, 1970, pp. 10–11.
Richard W. McLaren, "Antitrust Policy Today," March 5, 1970, pp. 17–18.

IV. KNOW-HOW

Richard H. Stern, "Antitrust Implications of *Lear* v. *Adkins*, February 19, 1970, reprinted in 15 Antitrust Bull. 663 (1970).
Richard W. McLaren, "Common Law Protection of Unpatented Ideas," September 26, 1969.

THE ANTITRUST CONSEQUENCES OF FRAUDULENT PROCUREMENT AND ENFORCEMENT OF PATENTS

(Address by Richard H. Stern,* Chief, Patent Unit, Antitrust Division, U.S. Department of Justice Before the AMERICAN PATENT LAW ASSOCIATION, ANTITRUST COMMITTEE, Chicago, Illinois, Thursday, May 14, 1970)

The consequences of the fradulent procurement and enforcement of a patent go beyond merely rendering the monopoly grant unenforceable. My topic in this panel discussion is the additional civil and criminal liabilities that a patent owner and those acting in concert with him may sustain when they fraudulently obtain a patent or they attempt to exclude competition by use of a patent that they know is invalid.

CRIMINAL LIABILITY

As you are perhaps aware, in late 1967 an antitrust grand jury indicted two corporations (a patent owner and its exclusive licensee, respectively), and the president and patent lawyer of the licensee corporation, for conspiring to exclude competitors from and limit competition into the bag industry. The means of accomplishing the violation were charged to be threats of infringement suits and an actual such suit, all based on a patent the parties knew was invalid. According to the indictment, the patent was invalid because of the licensee corporation's prior public use which constituted a statutory bar.[1]

The Government subsequently filed a civil complaint, alleging the same violations, and further charging that the corporate defendant which owned the patent had procured it fraudulently. The allegation of fraudulent procurement was based on the applicant's knowledge of the prior public use previously described, and also on the applicant's own public use prior to the critical date.[2] Neither of

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*The views expressed are those of the speaker, and they do not necessarily reflect the position of the Department of Justic.

[1] *United States* v. *Union Camp Corp.*, Crim. No. 4558, E.D. Va. (indictment filed Nov. 30, 1967). See also *Union Camp Corp.* v. *Lewis*, 385 F. 2d 143 (4th Cir. 1967) (Mandamus denied).

[2] *United States* v. *Union Camp Corp.*, Civ. No. 5005A, E.D. Va. (complaint filed, Nov. 4, 1968).

these cases was tried on the merits, because pleas of *nolo contendere* and consent judgments were entered before trial.

Lest any of you become unduly alarmed at the prospect of becoming a criminal defendant merely because some government prosecutor has a difference of opinion with you over the significance of some prior art, or because he second-guesses you on obviousness, permit me to reassure you that things have not gone so far, nor are they likely to. The facts alleged in these cases are that the patent was known to be invalid, because of strong documentary evidence in defendants' possession; that both companies decided to use the patent as a weapon to exclude competitors, in order to preserve monopoly prices; and that there was no doubt in defendants' minds that they were using a specious patent to injure and deceive the public, their competitors, and the federal court. As the Government pointed out in its brief to the Court of Appeals, it was *not* the Government's position that a violation could be premised upon a case of an honest mistake or a bona fide difference of opinion. On the contrary, the only proper basis of such a suit was said to be the enforcement of a claim of patent infringment known to be unjustified, as in the case of a patent that the owner knew to be invalid because of his own prior public use.

Before leaving the subject of criminal liability, I would like to note that there is considerable authority to support the proposition that a conspiracy to procure a patent by means of fraud constitutes, independently of the Sherman Act, a violation of the general federal conspiracy statute (18 U.S.C. § 371). Although the fine under the general conspiracy statute is only one-fifth the maximum under the Sherman Act, the maximum period of imprisonment is five years, rather than one year, and the offense is classed as a felony rather than a misdemeanor. Another significant difference between the two statutes is that the exclusion of competitors from the market by means of the spurious patent is the gravamen of the offense under the Sherman Act, while doubtfully procuring the patent from the Patent Office is the gravamen of the offense under Section 371. The two offenses are thus distinct, although they overlap in some circumstances. Hence, it is possible that a defendant may be punished for one, the other, or both violations.

DAMAGE LIABILITY

Fraudulent procurement and enforcement can create damage liability in several ways. In the bag industry case previously mentioned, several treble damage antitrust suits were filed by allegedly injured competitors—and at least one of these suits was settled for a substantial amount. The damages in these suits appear to have been based primarily on allegations of lost sales or lost profits. Another basis for liability seems to have been plaintiff's legal fees and costs incurred in defending the patent infringement suit.[3]

This does not exhaust the bases on which treble damage liability can be predicated. In the case of a fraudulently procured patent, the monopoly grant would seem to be void *ab initio*, so that there is a total absence (rather than failure) of consideration. Hence, any royalties paid would have been obtained without consideration and under false pretenses, and be subject to refund but the refund would be subject to trebling in an action under Section 4 of the Clayton Act. Similar principles would seem to apply to royalties collected under a known invalid patent. Finally, in this context, it should be noted that expectation or benefit-of-the-bargain damages, over and beyond consequential or reliance damages, are generally recoverable in cases of fraud.[4]

AMPICILLIN CASE

Some of the foregoing considerations are illustrated in the most recent Government antitrust complaint involving alleged fraudulent procurement, filed in March.[5] This civil suit involves ampicillin and other semisynthetic penicillin products, with total annual United States sales approaching $100 million. The complaint alleges that the patent was procured by "various fraudulent acts and inequitable impositions upon the Patent Office." Such acts are said to include

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[3] Cf. *Kobe, Inc.* v. *Dempsey Pump Co.*, 198 F. 2d 416 (10th Cir. 1952), cert. denied, 334 U.S. 837 (1952).
[4] Note, 47 Va. L. Rev. 1209, 1210–12 (1961).
[5] *United States* v. *Bristol-Myers Co.*, Civ. No. 822–70, D. D.C. (complaint filed March 19, 1970).

failure to bring a reference to the attention of the patent examiner, despite defendants' knowledge and belief that such reference was closer than the prior art being considered by the examiner; delaying the publication of an article explaining the significance of this reference, until after issuance of the patent; and reporting in a deceptive and misleading manner the results of experiments conducted upon request of the examiner. It is further alleged that after issuance of the patent defendants used the patent to restrain and suppress competition by collecting substantial royalties "based upon such spurious patent" and by instituting a patent infringement suit under it. The complaint also alleges various other monopolistic and restrictive practices, and alleges the invalidity of another patent on the basis that it was disclosed in the specification of the fraudulently-procured patent, so that there was a statutory bar.

Among oher things, the Government seeks cancellation of the fraudulently procured patent, a declaration of invalidity as to each patent, and a requirement that technical data, including FDA drug application materials, be turned over to all applicants on a royalty-free basis. The Government also seeks to recover damages for allegedly excessive amounts that it has paid for the improperly monopolized drug because of the Government's direct purchases and its domestic and foreign aid support and subsidy programs.

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It is thus seen that fraudulent procurement and enforcement remains a lively antitrust issue. The Department of Justice will continue to investigate fraudulently-procured patent monopolies, particularly in areas having substantial economic impact. Although civil enforcement will tend to predominate, criminal prosecutions may be anticipated in cases where hard-core, highly culpable individual or corporate behavior is discovered. By means of such enforcement efforts, the Department will seek to further its program to protect the integrity of the American patent system and preserve its important function in a free enterprise economy.

Patent and Know-How License Agreements: Field of Use, Territorial, Price and Quantity Restrictions

I very much appreciate the opportunity to participate in this fourth annual New England Antitrust Conference. It is dealing with a subject which is especially timely in view of the present congressional interest in patent law reform.

We will discuss the prospects for the patent bill—including the Scott amendments—in a few moments. First, however, I'd like to review the present realities of patent law licensing, since this will give us a framework to evaluate where we have been and where we are going.

One of the present realities, it seems, is that whenever a Department of Justice spokesman sets forth the Department's position on the application of the antitrust laws to patent licensing arrangements, a certain amount of criticism ensues.

As a matter of fact, after I had been invited to participate in this program and had agreed to do so, I thought of an episode in the life of Snoopy, that hero of Charles Shultz's comic strip, "Peanuts." The episode begins with Snoopy cringing behind a lectern, shielding himself from an assortment of bricks and others missiles. As he does so, he ponders that he came here to give a speech and wonders aloud, "Why is everyone yelling? Why is everyone throwing things? What is going on here?" In the next panel, ominous clouds begin to surround Snoopy, and he exclaims, "Smoke! Teargas! Good Grief!" As the episode ends, with Snoopy completely obscured by the clouds, he notes plaintively, "I hate giving speeches."

Fortunately, the verbal brickbats hurled at the Antitrust Division are far milder than the assortment of missiles which bombarded Snoopy. Consider this restrained comment:

> The Antitrust Division of the Justice Department may be anti-patents; unquestionably they are anti-patent law. They actively promote anarchy in the area of patent licensing.[1]

I imagine you would be surprised if I did not disagree with that statement. Well, I do. We are not anti-patent, and I think we have made our position rather clear. If we haven't, I will have another go at it today.

To begin with, what licensing practices does the Department of Justice consider to be clearly unlawful? I believe that I can identify at least nine. Each

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[1] Wetzel, Legal Trends and Their Effect on Licensing, Les Nouvelles, Vol. 5, No. 3 (May 1970).

of them has an effect on competition which extends beyond the metes and bounds of the claims of the patent.

First, it is clear that it is unlawful to require a licensee to purchase unpatented materials from the licensor. The illegality of such tying clause was established in the *International Salt* case[2] and was reaffirmed in 1963.[3] As a matter of general antitrust law, tying agreements which affect a not insubstantial amount of commerce are unlawful if the selling party enjoys a degree of power over the tying product.[4] When the tying product is patented—in the words of the Supreme Court—

> "The requisite economic power is presumed . . . on the theory that the existence of a valid patent on the tying product, without more, establishes a distinctiveness sufficient to conclude that any tying arrangement involving the patented product would have anticompetitive consequences." [5]

Parenthetically, I leave for your speculation whether the decision with respect to monopolization in *Walker Process*[6] is consistent with the Court's view of tying.

Second, the Department views it as unlawful for a patentee to require a licensee to assign to the patentee any patent which may be issued to the licensee after the patent licensing arrangement is executed.[7] Quite clearly, the legitimate desire for a patentee to be able to practice later-developed commercial embodiments of his invention which may be patented by his licensee can be adequately satisfied by requiring the licensee to grant back a non-exclusive license under any subsequent improvement patent. Moreover, the logical result of such an assignment grant-back provision is to stifle innovation on the part of the licensee.[8]

Third, the Department believes it is unlawful to attempt to restrict a purchaser of a patented product in the resale of that product. This principle goes all the way back to 1873.[9] The patentee can reasonably be expected to exact his monopoly profit at the time of the first sale. He should not be permitted to control the resale of the patented article by a person who has purchased it from him.

Fourth, a patentee may not restrict his licensee's freedom to deal in products or services not within the scope of the patent.[10] If he does so, he is attempting by means other than that of free competition to extend the bounds of his exclusive right to make, use and sell the patented device to the extent where that device might be the only one available to a user of that type of article.

Fifth, the Department believes it to be unlawful for a patentee to agree with his licensee that he will not, without the licensee's consent, grant further licenses to any other person.[11]

Sixth, the Department believes that mandatory package licensing is an unlawful extension of the patent grant.[12]

Seventh, the Department believes that it is unlawful for a patentee to insist, as a *condition* of the license, that his licensee pay royalties in an amount not reasonably related to the licensee's sales of products covered by the patent[13]—for example, upon total sales of products of the general type covered by the licensed patent. This rule, I should point out, does not apply to percentage of

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[2] International Salt Co. v. United States, 332 U.S. 392 (1947).

[3] United States v. Loew's, Inc., 371 U.S. 38 (1962).

[4] Fortner Enterprises, Inc. v. United States Steel Corp., 394 U.S. 495 (1969).

[5] United States v. Loew's, Inc., *supra* note 3, at 45–46.

[6] Walker Process Equip., Inc. v. Food Mach. & Chem. Corp., 382 U.S. 172 (1965).

[7] United States v. Wisconsin Alumni Research Foundation, 1970 CCH Trade Cas. ¶73,015 (consent decree). *But see* Transparent Wrap Machine Corp. v. Stokes & Smith Co., 329 U.S. 627 (1949).

[8] One commentator has characterized a similar statement as a ". . . Freudian conclusion as to what will or will not encourage investment in research." Austern. *Surgeons, Morticians, and Patent Lawyers—The Antitrust Validity of Patent Licensing Restrictions,* Lecture before the Practicing Law Institute Program on Current Antitrust Problems, Dec. 5, 1969. However, if a licensee must immediately give away anything he might invent, the corporate executive charged with reviewing expenditures is going to look long and hard before committing substantial resources to research and development. Accordingly, I would characterize this statement as Aristotelian logic rather than Freudian delusion.

[9] Adams v. Burke, 17 Wall. 453 (U.S. 1873); Hobbie v. Jennison, 149 U.S. 355 (1893); Keeler v. Standard Folding Bed Co., 157 U.S. 659 (1895).

[10] McCullough v. Kammerer Corp., 166 F. 2d 759 (9th Cir. 1948); National Lockwasher Co. v. George K. Garrett Co., 137 F. 2d 255 (3d Cir. 1943); Park-In Theatres v. Paramount Richards Theatres, 90 F. Supp. 727 (D. Del.), *aff'd per curiam,* 185 F. 2d 407 (3d Cir. 1950).

[11] United States v. Krasnov, 143 F. Supp. 184 (E.D. Pa. 1956), *aff'd per curiam,* 355 U.S. 5 (1957); United States v. Besser Mfg. Co., 96 F. Supp. 304 (E.D. Mich. 1951), *aff'd,* 343 U.S. 444 (1952).

[12] American Security Co. v. Shatterproof Glass Corp., 268 F. 2d 769 (3d Cir. 1959).

[13] Zenith Radio Corp. v. Hazeltine Research, Inc., 395 U.S. 100 (1969).

total sales royalties freely negotiated for the convenience of the parties, nor does it apply to minimum or lump-sum royalties.

Eighth, it is pretty clearly unlawful for the owner of a process patent to attempt to place restrictions on his licensee's sales of products made by the use of the patented process.[14] Many articles, though not themselves patented are produced by the use of patented machinery or processes. "Licensors of the patented machines have no right to interfere with free competition in the sale of unpatented products." [15]

And finally, the Department of Justice considers it unlawful for a patentee to require a licensee to adhere to any specified or minimum price with respect to the licensee's sale of licensed products. Although price restrictions on the licensee were approved in the *General Electric* case in 1926,[16] the rule of this case has been consistently eroded. For example, the Court of Appeals for the Third Circuit has held that the grant of multiple licenses containing price restrictions does not come within the purview of the *G.E.* doctrine and, without more, violates Section 1 of the Sherman Act.[17] And twice, the Supreme Court has divided evenly on the question of whether to overrule *G.E.*[18]

I do not believe that it has been demonstrated that the dangerous power to control the price at which a licensee may sell must be added to the benefits of a patent in order to provide adequate incentive for invention, disclosure or licensing. The patentee obtains the full value of his patent when he exacts all the traffic will bear in the way of royalties or by exercising his privilege to be the sole maker or seller. Royalties, or profits from exclusive exploitation, are the marketplace's impersonal way of evaluating the worth of an invention. To be sure, the patent owner might reap even greater rewards were he able to set the prices charged by his licensess. But those additional rewards would reflect not the value of the invention itself but rather the value of price fixing. We see not basis for permitting patentees to engage in this practice, which is forbidden to all others.

The practices which I have thus far outlined are, in the Department's view, unlawful in virtually every context.

Most practices other than these, we believe, have a wider scope for justification under the rule of reason—that is to say, a practice which may be perfectly reasonable if employed in one context may clearly be unreasonable in another. I shall discuss some of these practices in a few moments. But first, let me outline the rule of reason as we see it.

The rule of reason is derived from the ancient doctrine of ancillary restraints, and embraces three principal elements. First, the restriction must be ancillary to carrying out the lawful primary purpose of the agreement. Second, the scope and duration of the restraint must be no broader than is necessary to support that primary purpose. And third, the restriction must be otherwise reasonable under the circumstances.[19]

This rule can be applied—and despite some comments to the contrary, I think sensibly applied—to the myriad of patent licensing arrangements which are not unlawful *per se*. For purposes of illustration, I would like to discuss three types of arrangements in terms of the rule of reason. These are field-of-use licensing, patent pools and international patent and know-how licensing arrangements.

In the last few years, the Department of Justice has filed a number of cases challenging field-of-use restrictions in various contexts.[20] In these cases, we have distinguished between a field-of-use restriction applicable to a licensee who purchases a patented product from the patentee and a field-of-use restriction upon a licensee who manufactures the patented product. In the former case—that of the purchasing licensee—it is doubtful that any but the most compelling circumstances can justify even minimal restrictions upon the use to which the

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[14] Cummer-Graham Co. v. Straight Side Basket Corp., 143 F. 2d 646 (5th Cir. 1944).
[15] 143 F. 2d at 647.
[16] United States v. General Electric Co., 272 U.S. 476 (1926).
[17] Newburgh Moire Co. v. Superior Moire Co., 237 F. 2d 283 (3d Cir. 1961).
[18] United States v. Huck Mfg. Co., 382 U.S. 197 (1965); United States v. Line Material Co., 333 U.S. 287 (1948).
[19] United States v. Bausch & Lomb Optical Co., 45 F. Supp. 387 (S.D.N.Y. 1942), *aff'd as modified*, 321 U.S. 707 (1944); United States v. Addyston Pipe & Steel Co., 85 Fed. 271 (6th Cir. 1898).
[20] United States v. Karl Ziegler, et al., Civil No. 1255–70; United States v. Bristol-Myers Co., et al., Civil No. 822–70; United States v. Fisons, Ltd., et al., Civil No. 69–C–1530; United States v. Glaxo Group, Ltd. and Imperial Chemical Industries, Ltd., Civil No. 558–68.

licensee may put a product which he has purchased. In such cases, the patentee is expected to reap his profits at the time he makes the sale. He cannot expect to control disposition of a product once he has departed with dominion over it.

Field-of-use restrictions upon manufacturing licensees present somewhat more difficult questions. As a general rule, considerable justification can be made for a patentee reserving to himself a well-defined field of use and then offering to license others throughout the remaining fields of use without restrictions on his licensees. If the patentee could not thus protect himself, he might very well decide not to license at all. On the other hand, field-of-use restrictions which divide markets among companies who would otherwise be competitors appear to lack much, if any, justification at all.[21] Such divisions are not usually necessary to promote commercialization of the patent through licensing.

Somewhat akin to field-of-use restrictions are the "bulk sales" restrictions which are particularly common in licenses in the pharmaceutical industry.[22] These restrictions generally prevent a licensee from selling the patented product in other than dosage form. The only justification offered for many of these bulk sales restrictions is that they are designed to prevent the product, in bulk form, from falling into the hands of re-packagers—re-packagers in this context being synonymous with price cutters. On the other hand, some bulk sales restrictions upon manufacturing licenses might very well be justifiable under the rule of reason. For example, such a restriction might be justified on health and safety grounds if the drug were one which was difficult to handle, requiring critical tolerances to put it in dosage form for administration in a safe manner.

Patent pools provide another example of the application of the rule of reason to a particular licensing practice. A non-exclusive exchange of patent rights can be clearly beneficial to the economy when it is employed to remedy a situation in which two or more companies in an industry hold blocking patents. On the other hand, if the practice were to be extended for an indefinite time to all future patents and if, as a result, competition in research and development in the affected industry were in fact retarded, I think you would rather clearly have an antitrust violation.

Finally, the rule of reason is applicable to international patent and know-how licensing arrangements. The recent *Westinghouse-Mitsubishi* complaint,[23] which has attracted so much attention lately, is a good example. It also illustrates the misapprehensions which often surround what are really classically simple cases in the foreign commerce area. One interpretation of the case which I am told is circulating in patent-antitrust circles is that it is aimed at the licensing of know-how wth territorial restrictions, and is designed to obtain new law in this area. Another version is that the case stands for the proposition that if an American company licenses its foreign patents to a foreign company, it must also license any corresponding United States patents to that foreign licensee.

Both of these interpretations are incorrect. What we have in the *Westinghouse* case is not a simple know-how license with territorial restrictions. Neither does it involve a simple license of a foreign patent accompanied by a refusal to license a corresponding domestic patent. Added to the Westinghouse patent-know-how licenses are these considerations—all of which are clearly alleged in the complaint:

1. Not only were patented products subject to territorial restrictions, but so also were a great number of products of the same general type covered by the license agreements—even though such products might not incorporate any of the transferred technology.

2. The agreements—with their territorial restrictions—covered products as to which Mitsubishi did not desire to be licensed—a clear mandatory package-licensing policy.

3. The agreements had been in existence for over forty years—hardly a reasonable length of time by anyone's standards—and yet had years to run.

Thus, this case follows the same general lines as the old *ICI*[24] and *National*

[21] This rule is consistent with such cases as United States v. Birdsboro Steel Foundry & Mach. Co., 139 F. Supp. 244 (W.D. Pa. 1956). In that case, the court made an explicit finding that the companies involved were neither actual nor potential competitors.

[22] E.g., United States 1. Glaxo Group, Ltd., *supra* note 20.

[23] United States v. Westinghouse Elec. Corp., Civil No. 70–852–SAW (N.D. Cal., filed April 22, 1970).

[24] United States v. Imperial Chemical Industries, Ltd., 100 F. Supp. 504 (S.D.N.Y. 1951).

Lead[25] market division cases. Two major manufacturers in different countries—we allege—exchanged patents and technology, in broad fields, with the intent and effect of precluding each from exporting the covered products to the other's country. Such agreements in *ICI* and *National Lead*, also covering broad fields and not confined to patent rights, were held illegal.

Finally, as to territorial restrictions in domestic patent licenses, you are probably aware that at least one commentator has opined that the legislative history of section 261 of the Patent Code shows that it was not intended to legitimate all divisions of territory, without regard to their effect on competition.[26]

I disagree with this view. I think the statute is clear on its face—that is, territorial restrictions are permitted—and, therefore, there is no need to look to the legislative history. This is, I believe, an exception to the general rule of reason.

Much is currently being said of the difficulty—in terms of uncertainty—which the rule of reason is alleged to cause in the area of patent licensing. As I noted at the beginning of this talk, some have ever termed it "anarchy." In considering these allegations of uncertainty and even anarchy, I think it is important to keep in mind the nature of our antitrust laws. They are not in the form of a European code, designed to provide a ready and concrete answer to every problem arising in the law. On the contrary, they are a broad charter of economic liberty and an expression of Congress that competition should be our basic policy. They are designed to be adapted to changing situations and to changing economic conditions.[27]

Despite this, I have the lingering feeling that the hue and cry now being raised results not so much from uncertainty as from the fact that we have made our position quite definite and certain. People know very well where the Department of Justice stands—they just don't like it.

These complaints of uncertainty, however, are now being urged to support the Scott amendments to the bill pending in Congress to revise the patent code. These amendments are based in part upon Recommendation XXII of the President's Commission to study the Patent Laws. The amendments in their present form, I am afraid, would legitimate many of the practices which I discussed earlier as being unlawful, *per se*. Here, we come, I think, to a bit of ancient history. Many lawyers—and the patent bar in particular—are echoing the words of a well-known industrialist who said: "In my opinion it is quite uncertain as to just what we have the right to do and what we are forbidden to do by the Sherman Law.[28] That industrialist happened to be Judge Gary of the United States Steel Corporation testifying before Congress in 1911. So the argument that the Sherman Act breeds uncertainty is hardly a new one.

About a year ago, in another talk on patents and antitrust law,[29] I pointed out that one of the jobs of the lawyer in private practice is to keep his client out of antitrust trouble and that one of the ways to accomplish this was to be cautious as to the type of restriction which you write into licensing agreements. I said that I thought that this was one area in which it was wise for the private lawyer to err on the side of caution. Having operated on the basis of this principle in private practice, I thought at the time that it was a fairly sensible approach. However, I was a little bit shaken when a critic found this approach "overbearing" and "more importantly an overture toward importuning the professional independence of the lawyer, offering a compromise to the lawyers obligation to exercise professional judgment solely on behalf of his client." [30] Seeking some support for my position, I wondered if anyone had had an answer to Judge Gary's complaints of uncertainty in 1911. Going back to the hearings before Congress, I found a witness who testified as follows:

> "I have been asked many times in regard to particular practices or agreements as to whether they were legal or illegal under the Sherman law. One gentleman said to me, "We do not know where we can go." To which I replied, "I think your lawyers or anyone else can tell you where a fairly safe course

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[25] United States v. National Lead Co., 63 F. Supp. 513 (S.D.N.Y. 1945), *aff'd*, 332 U.S. 319 (1947)

[26] Baxter, *Legal Restrictions on Exploitation of the Patent Monopoly*, 76 Yale L.J. 276 (1966).

[27] Northern Pac. Ry. Co. v. United States, 356 U.S. 1 (1958).

[28] Senate Committee on Interstate Commerce, Hearings on Control of Corporations, Persons and Firms Engaged in Interstate Commerce, 62d Cong., p. 724.

[29] *Patents and Antitrust: The Legitimate Bounds of the Patent Monopoly*, an Address before the Pittsburgh Patent Law Association, Nov. 19, 1969.

[30] Wetzel, *supra* note 1, at 84.

lies. If you are walking along a precipice no human being can tell you how near you can go to that precipice without falling over, because you may stumble on a loose stone, you may slip, and go over; but anyone can tell you where you can walk perfectly safely within convenient distance of that precipice." The difficulty which men have felt generally in regard to the Sherman law has been rather that they have wanted to go the limit than that they have wanted to go safely." [31]

That witness was then a Boston lawyer named Louis D. Brandeis.

The supporters of the Scott amendments argue, however, that uncertainty in the area of patent licenses discourages innovation. I know of no empirical evidence whatsoever to support this contention. For example, one commentator suggests that the Justice Department's recent concern with patent licensing arrangements—which he dubs "The Second Patent Crusade" [32]—began in 1965. However, since 1965, non-government expenditures for research and development have increased, in terms of 1968 dollars, from $8.3 billion to $9.4 billion.[33] Moreover, a preliminary report by Professor Oppenheim and Mr. John Scott [34] indicates that the use of the type of licensing arrangements which the government regards as unlawful is far from widespread. Most of these practices, this preliminary report shows, are never used, or are used only seldom or occasionally.

I don't think it can be fairly said, therefore, that the Department of Justice is promoting uncertainty in the area of patent law licensing, or that a demonstrative case can be made for the proposition that the antitrust laws in this field are discouraging innovation.

What, then, of future prospects in the area of patent licensing? It certainly does *not* seem that the present session of Congress will take up the question of patent law reform, including the Scott amendments when it reconvenes in Washington on November 16. Beyond this, I am at the present time unwilling to predict the legislative future of the Scott amendments. Suffice it to say that the amendments, together with the general revision of the patent laws, are receiving much study and thought, both within and without the government.

Common Law Protection of Unpatented Ideas

It was with some trepidation that I accepted your kind invitation to speak here today. The last time I made a speech about patents and antitrust law, the patent bar seemed to regard what I said with about the same hospitality that the farmer views a fox in his chicken coop. One patent lawyer even told me that a patent was getting to be like a mink coat in the Tropics—nice to have, but totally useless. Today, however, you can relax; my topic here does not deal directly with the relationship of patent and antitrust law.

Initially, though, I want to assure you that antitrust is not out to make the patent system meaningless. We recognize that the government grant of patent rights is an important stimulus to research and innovation. The right to exclude others from making, using and selling a patented device is the reward for successful innovation. Our commitment to the philosophy that the patent system encourages "the Progress of Science and the useful Arts" arises from the Constitution itself.

America's commitment to competition, however, is at least as basic as its commitment to the patent system. As the Supreme Court has stated, "Subject to narrow qualifications, it is surely the case that competition is our fundamental national economic policy, supplying as it does the only alternative to cartelization or governmental regimentation of large portions of the economy." [1] The patent system is one of those narrow qualifications," and the constant dialogue between the patent law and the antitrust law is an effort to determine just how narrow or how wide that qualification is.

I am sure that, having heard Mr. Stern yesterday and Mr. Kestenbaum this morning, you are fairly fully briefed on the present state of that dialogue. So

[31] Hearings, *supra* note 26, at 1161.

[32] Hollabaugh, *The Scott Amendments* v. *The Second Patent Crusade*, an Address before the Annual Meeting of the ABA Section of Antitrust Law, August 10, 1970.

[33] National Science Foundation, Publication NSF 69–30.

[34] Oppenheim & Scott, *Empirical Study of Limitations in Domestic Patent and Know-How Licensing: A Preliminary Report.*

[1] United States v. Philadelphia National Bank, 374 U.S. 321, 372 (1963).

I shall turn now to my principal subject—"Common Law Protection of Unpatented Ideas."

Many members of the bar have expressed concern over what they believe to be the logical implication of the Supreme Court's recent decision in *Lear* v. *Adkins*.[2] That implication, they believe, is that a state can give no protection to unpatented ideas.

In the *Lear* case the court stated that there is a "strong federal policy favoring free competition in ideas which do not merit patent protection." The court went on to say that "federal law requires that all ideas in general circulation be dedicated to the common good unless they are protected by a valid patent." The court specifically refused, however, "to define in even a limited way the extent, if any, to which the states may properly act to enforce the contractual rights of inventors of unpatented secret ideas."

However, many have read these passages from *Lear* v. *Adkins* as indicating that, when a proper case comes along, the Court will hold that there can be no state-enforced contractual protection of unpatented or unpatentable ideas. The purpose of my remarks today is to evaluate the merits of this position.

It virtually goes without saying that an idea, a conception, an invention, is valueless unless it is exploited. A discovery, no matter how brilliant, cannot benefit the public unless it is incorporated into products, or produces products, which can be bought and sold in the marketplace. The patent system seeks to encourage not only innovation but also the exploitation of innovation. The price which the public pays for the grant of a patent monopoly is the disclosure by the inventor of his discovery. Even if the inventor does not choose to exploit his own invention, other may take advantage of it after the 17 years of the patent monopoly have run.

Suppose, however, that an inventor does not choose to avail himself of the benefits conferred by the grant of patent rights. No one, of course, can force him to disclose his invention by filing for a patent. He may conclude, for a variety of reasons, that he will reap greater benefits by not seeking a patent upon his discovery. The discovery thus remains known to the inventor alone and assumes the unpatented status of a trade secret.

How the law will treat unpatented trade secrets is one of the things that concerns the bar—and patent lawyers especially—about the presumed implications of *Lear* v. *Adkins*. If the owner of a trade secret cannot protect his secret by contract, how, indeed, can an inventor who does not avail himself of the patent system exploit his idea?

Another area which has been thrown into question by the Court's statements in *Lear* v. *Adkins* is the licensing of the right to make, use, and sell products or to use processes which are embodied in pending patent applications. The patent applications is, of course, confidential. At least some ideas embodied in patent applications are now known to the public generally. But, on the other hand, until an application ripens into a patent, the inventor has no right under the patent laws to exclude others from practising his invention. Whatever rights an applicant has during the period between the filing of his application and the issuance of a patent must be governed by state law—normally the common law—and enforced by state remedies. But does *Lear* v. *Adkins* mean, concerned lawyers ask, that state law can provide no protection for unpatented ideas and thus that no royalties can be collected by an inventor who has contracted to give another the right to use an idea embodied in a pending patent application?

I think that in resolving the questions raised by *Lear* v. *Adkins*, the policy of the antitrust laws can be of assistance. As the court noted, there is an "important public interest in permitting full and free competition in the use of ideas. . . ." The public interest is, of course, fully consistent with the purpose of the antitrust laws. But to look at the court's statement in another way, we might ask ourselves how best can the exploitation of ideas be maximized so that the benefits of innovation and invention can swiftly be made available to the public.

I believe that in answering this question we must keep two considerations in mind. We must avoid a policy of preventing the free use of ideas which are, in reality, a part of the public domain. Second, we must avoid discouraging the exploitation of ideas which are not a part of the public domain.

To illustrate the free use of public ideas point—if an inventor designs a new type of lamp which is not entitled to patent protection and if he markets the lamp he has, in effect, made the idea available to others who may copy it and

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[2] 395 U.S. 693 (1969).

who are free to copy it without incurring liability. I do not believe that state law can properly seek to prevent the free use of an idea which the inventor himself has made public. Of course, states can pass laws aimed at protecting confusion as to source. But that is a little different. Competition benefits when two or more people are marketing identical products, and that is the point I am making. Different considerations intervene where one of the marketers attempts to pass off his product as the manufacture of another.

In addition to staying away from a policy which would prevent the free use of ideas in the public domain, we must also avoid discouraging the exploitation of ideas which have not yet become a part of the public domain. For example, there is a public interest in getting a new invention to the market as soon as possible. Preventing the licensing of patent applications would seem to inhibit this objective. Likewise, there is a public interest in getting to the marketplace products embodying ideas which may be characterized as trade secrets. Preventing the licensing of trade secrets would seem to inhibit this objective.

There is also a public interest in encouraging manufacturers to develop and exploit new techniques of production, which we commonly refer to as know-how. Preventing the licensing of know-how would also seem to inhibit this objective.

On the other hand, we must guard against systems of state law which enable "the heavy hand of tribute to be laid on each slight technological advance in the art."[3] Licenses and licensing restrictions can be used as tools to suppress competition as well as vehicles to exploit new and significant inventions. For example, one competitor should not be forced to pay royalty to another for the use of an idea which the latter has dedicated to the public. As another example, competitors can and do resort to the subterfuge of a license agreement in an attempt to divide markets or customers, or to fix prices. We must seek, therefore, some rational method of determining what unpatented ideas can be the subject of state-enforced contractual licensing agreements and what type of license agreements are permissible.

If a state is to enforce contractual arrangements with respect to unpatented ideas, the first and most important requirement is that the idea really is secret—that is, that it not be generally known either to the public or to the particular industry involved. I believe that there is some indication in *Lear* v. *Adkins* that the Court did not intend to, and would not, totally abolish the long-standing body of law which has grown up around the concept of secret ideas—for example, a secret recipe or formula. In several places in its opinion, the Court referred to "ideas which are in reality a part of the public domain" and "ideas in general circulation." But having said that the idea must remain substantially secret, it is immediately apparent that one class of ideas—those relating to products—cannot be the subject of substantial state law protection once the product is marketed.

Unless the product is the subject of a valid patent, others are free to purchase the product and copy it—if they are able—as long as the consumer is not misled as to the source of manufacture.

The one area with respect to products in which a state can provide some limited protection relates to the theft of blueprints and the like. What should the remedy be when one competitor unlawfully acquires industrial property relating to another's product and proceeds to market an identical product manufactured from his competitor's plans? I suggest that the only proper remedy is to award to the original owner of the idea the damages incurred by him—which may well be the copier's profits—during the period between the theft of the plans and the time when, without the theft, his competitor could have marketed a similar device by buying it on the open market and preparing his own plans for reproducing the purchased product.

In the area of unpatented ideas concerning processes and formulae, state law can play a larger role where the marketing of a product made according to a secret process does not necessarily reveal the nature of the process itself. As long as ideas relating to processes remain secret, I believe that a case can be made that such secrecy can be protected by state law.

A related requirement of ideas to be afforded state protection is that they be valuable. Of course, it is likely that the more secret an idea is, the more valuable it is. The value of an idea can perhaps be measured in two ways: qualitatively by looking to the advance made in the art by the idea—a difficult measurement to make; and quantitatively by looking to how much others are

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[3] Cuno Engineering Corp. v. Automatic Devices Corp., 314 U.S. 84, 92 (1941).

willing to pay for the right to use the idea. The quantitative test, without considering the advance in the art, could lead to unwarranted anticompetitive abuses such as restrictive licensing, and agreements which are in fact coverups to eliminate competition.

Assuming that an inventor has an unpatented idea which is both secret and valuable, what types of licensing agreements should he be free to make?

I believe it is elementary that an inventor should not be permitted to do, in a trade secret or know-how license, that which he could not do if his idea had patent protection. Thus, if a restriction is illegal in a patent license, it stands on no better footing simply because it is embodied in a trade secret license. Applying this principle, the owner of a secret process could not require his licensee to buy his materials from the licensor, or not to use any other process to produce the end product, or to fix the price at which the end product is sold. Also, as in the case of distribution of patented products, the Antitrust Division would likely challenge as illegal a trade secret license provision which divides fields-of-use among licensees who would otherwise compete.

Many lawyers have inserted territorial restrictions in trade secret and know-how licenses in reliance upon the doctrine that such restraints are lawful if they are merely ancillary to the main purpose of a lawful contract, reasonable, necessary to protect the owner of the idea from the unjust use of the idea by the other party, and so on. In evaluating the current legality of such territorial restrictions we will consider, in addition to whether the transferred knowledge is really secret and really valuable, whether the restriction is necessary to enable the licensed firms to enter the field and whether the term of the restriction is reasonable in length under all the circumstances.

I suspect that some members of the Bar think they can avoid the growing body of law condemning anticompetitive restrictions in patent licenses by incorporating similar restrictions in trade secret or know-how licenses. I hasten to dsabuse you of that notion. We will be looking at trade secrets and know-how licensing just as closely as we do similar restrictions in patent licenses, if not more so.

Having said that, it is my view that states can afford some type of contractual protection of unpatented ideas. Accepting that proposition, and assuming that such ideas can be licensed in certain circumstances, what type of legislation is necessary to make this clear in the light of *Lear* v. *Adkins*? As you probably know, the patent revision proposed by Senator McClellan includes a new Section 301 which provides that the Patent Code "shall not be construed to preempt, or otherwise affect in any way, contractual or other rights or applications, not in the nature of patent rights, imposed by state or federal law on particular parties with regard to inventions or discoveries, whether or not subject to . . ." the patent code. In introducing this bill, Senator McClellan said that Section 301 restates the "traditional interpretation" that the federal patent statute does not preempt such rights.

From what I have said previously, I am sure you can conclude that I do not oppose state protection of unpatented ideas in certain situations. I believe, however, that the proposed new Section 301 of the Patent Code could be construed to allow too much state protection of such rights. It almost goes without saying that, if adopted, there would be litigation to determine whether this section overruled the *Sears-Compco* cases[4] and *Lear* v. *Adkins*. Since I believe these decisions are sound, the Antitrust Division will oppose Section 301 as drafted.

We would not object, however, to a more narrowly drafted provision permitting the states to protect inventors' rights in their ideas, provided that those ideas are both really secret and really valuable.

I believe that the accommodation which I have suggested is consistent with both the patent system and the antitrust laws. In addition, it recognizes the existence of a long-standing body of common law which protests private rights to trade secrets and industrial know-how. It protects the choice long available to inventors of disclosing their invention and securing a patent on it, or of keeping their inventions secret and exploiting them through trade secret and know-how licenses.

I should not close without pointing out that the inventor who seeks to exploit his invention by preserving its secrecy runs a substantial risk. If the secret is disclosed by one who has lawfully acquired it, it is, by definition, no longer secret and it passes to the public domain. Likewise, if another inventor reaches

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[4] Sears, Roebuck & Co. v. Stiffel Co., 376 U.S. 225 (1964); Compco Corp. v. Day-Brite Lighting Co., 376 U.S. 234 (1964).

the same idea independently and discloses it, the prior inventor has no right to exclude the second or any other inventor from making, using, or selling products, or from using processes embodying the idea. I suggest, therefore, that inventors and their counsel would be wise in most instances to seek the protection afforded by our federal patent system, for all its perils and troubles.

COMPETITION IN THE FOREIGN COMMERCE OF THE UNITED STATES

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Another area of enforcement concern in foreign commerce involves the division of markets by agreement. Typically, this involves the exclusion of a foreign competitor, depriving the U.S. market of a competitive factor. Not infrequently, patent and know-how licenses are involved. The recent *Westinghouse-Mitsubishi* complaint, which has attracted so much attention lately, is a good example. It also illustrates the misapprehensions which often surround what are really classically simple cases in the foreign commerce area. One interpretation of the case which I am told is circulating in patent-antitrust circles is that it is aimed at the licensing of know-how with territorial restrictions, and is designed to obtain new law in this area. Another version is that the case stands for the proposition that if an American company licenses its foreign patents to a foreign company, it must also license any corresponding United States patents to that foreign licensee.

Both of these interpretations are incorrect. What we have in the *Westinghouse* case is not a simple know-how license with territorial restrictions. Neither does it involve a simple license of a foreign patent accompanied by a refusal to license a corresponding domestic patent. Added to the Westinghouse patent-know-how licenses are these facts—all of which are clearly alleged in the complaint:

1. Not only were patented products subject to territorial restrictions, but so also were a great number of products of the same general type covered by the license agreements—even though such products might not incorporate any of the transferred technology.

2. The agreements—with their territorial restrictions—covered products as to which Mitsubishi did not desire to be licensed—a clear mandatory package-licensing policy.

3. The agreements had been in existence for over forty years—hardly a reasonable length of time by anyone's standards—and yet had years to run.

Thus, this case follows the same general lines as the old *ICI* and *National Lead* market division cases. Two major manufacturers in different countries—we allege—exchanged patents and technology, in broad fields, with the intent and effect of precluding each from exporting the covered products to the other's country. Such agreements in *ICI* and *National Lead,* also covering broad fields and not confined to patent rights, were held illegal.

I have been asked: If *Westinghouse-Mitsubishi* does not forecast a highly restrictive rule on know-how licensing, what is the rule which governs in this area? Actually, I think I have stated my views on this on at least one other occasion. The rule is derived from the doctrine of ancillary restraints, and embraces three principal elements. First, the restriction must be ancillary to carrying out the lawful primary purpose of the agreement. Second, the scope and duration of the restraint must be no broader than is necessary to support that primary purpose. And third, the restriction must be otherwise reasonable under the circumstances. In effect, the rule on know-how licensing is pretty much the same as the rule on patent licensing: Except as to certain well-known restraints which are *per se* unlawful, the standard is the rule of reason.

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NATIONAL AERONAUTICS AND SPACE ADMINISTRATION,
Washington, D.C., May 13, 1971.

HON. JAMES O. EASTLAND,
Chairman, Committee on the Judiciary,
U.S. Senate,
Washington, D.C.

DEAR MR. CHAIRMAN: This is in further reply to your request for the comments of the National Aeronautics and Space Administration on the bill S. 643, "For the general revision of the Patent Laws, title 35 of the United States Code, and for other purposes."

The patent system is recognized by the National Aeronautics and Space Administration as a vital force in the creation, identification, dissemination and use of new technology. The interest of NASA in maintaining the effectiveness of the patent system is underscored in the provisions of the National Aeronautics and Space Act of 1958, which specifically provide for the treatment and protection of inventions, and by Executive Order 10096, which provides for a uniform policy and administration with respect to inventions made by Government employees.

NASA patent policy, based on Section 305 of the Act, and on the 1963 Presidential Statement of Government Patent Policy, is designed to make full use of the patent system in fostering the transfer of technology resultant from the national space program to commercial or non-aerospace fields, thereby further benefitting the economy and enhancing the technological capabilities of the United States to meet the problems facing present and future generations.

In addition to furthering this agency's efforts toward obtaining commercial utilization of aerospace technology generated in its research and development programs in the shortest possible time, NASA's patent program serves to fulfill other worthwhile objectives. Perhaps the first of these is the protection afforded to the Government and to the public to insure the freedom of use of inventions resulting from NASA research programs, without the specter of being forced to pay royalties for the use of the same inventions later developed and patented by private parties. Also, patents have achieved status as a symbol of recognition of technical excellence and creativity. Members of the scientific community frequently evaluate the scientific reputation of a colleague by the number and quality of patents issued to him. Providing this type of employe recognition assists in assuring a competitive working environment for NASA's scientific and technical personnel. And, finally, the patent is an excellent method for disseminating technical information and serves to fulfill our statutory mandate of effecting the widest practicable and appropriate dissemination of information resulting from the space program, Section 203 of the Act. Such dissemination to the scientific community, on the scale afforded by the patent system, provides the additional benefit of assisting in preventing the duplication and waste of research effort.

In reviewing commenting upon the various patent reform bills, commencing with S. 1042, the Patent Reform Act of 1967, we have noted evolutionary change in the thrust and content of the proposed legislation. In commenting on this original bill, we indicated that we believe the major features to be abolishment of the one-year grace period; issuance of a patent to the first to file an application, together with the complete elimination of interference practice; institution of a preliminary application procedure; mandatory publication of applications during pendency; provision for *in rem* invalidity of patent claims; defining prior art more broadly so as to encompass use and sale outside the United States and all disclosure of knowledge in tangible form; streamlining the judicial process for patent infringement litigation; the making of computer programs unpatentable; and the provision for optional deferred examination of applications in the Patent Office. Now, some four years later, it appears that each of these major features has been completely discarded or significantly modified.

The significant changes to existing law presented by S. 643 as well as S. 2756 of the 91st Congress (some of which also appeared in previous bills) include issuance of the patent to the first to file, together with modified interference practice; continuance of one-year grace period; voluntary publication of pending patent applications; provision for filing of a patent application by a party other than the inventor; the extension of the patent term to twenty years, commencing from the date of filing; more clearly defining the test of obviousness of an invention; relaxed provisions regarding joint inventorship; provisions authorizing the requirement of a patentability brief, and the effects thereof; a reexamination period after issuance of the patent; and a section dealing with non-preemption of state and federal laws by the patent law. Our comments below will be limited to those of the above features which we consider to be of particular interest to NASA.

Award of Patent to "First-to-File"

S. 1042, in line with the recommendations of the President's Commission, would have completely eliminated interference contests and the patent would have been awarded to the first applicant to file, regardless of the date of conception. The primary reasons for this fundamental change were said to be the incentives such a system would offer the inventor to file promptly, the benefit to the public of an early disclosure of the invention, and the fact that every other major free-world patent system, save Canada and the Philippines, is based on a first-to-file system. S. 643 preserves a modified interference practice, while at the same time granting the patent to the first applicant to file. We believe such a limited interference proceeding constitutes an acceptable compromise between the strict first-to-file rule of S. 1042, where a true first inventor may be foreclosed, even though he has acted promptly within the spirit of the patent statutes, thereby possibly impairing the integrity of the patent system, and the existing first-to-invent rule whereby an inventor who has not been diligent in pursuing a disclosure through the patent system may nevertheless obtain a patent over a competing applicant with an earlier filing date. Language defining abandonment of an invention, such as is set forth in Section 102(d)(5), would appear to strengthen this concept.

Grace Period

The strongest objection to revision of the patent laws which NASA has noted in the past is to the complete abolishment of the one-year absolute grace period in which an inventor may file his application under the existing patent law. If the grace period were eliminated, as was proposed in S. 1042, it would be extremely difficult to maintain effectively NASA's complementary publication and patent programs. We strongly endorse the retention of the grace period as provided for in S. 643.

Publication

NASA has consistently supported the proposition that mandatory publication of pending patent applications is an effective tool for more rapidly transferring the benefits of the patent system to the general public, and that any patent statute enacted should include such a provision. We would still favor mandatory publication of pending applications between 18 and 24 months from the application's effective filing date, provided the application includes at least one allowed claim so as to justify dissemination of the applicant's disclosure to the public. S. 643, in Section 123, provides only for voluntary publication of pending patent applications.

Term of Patent

Section 154(c) states that the term of a patent whose issuance has been delayed by the imposition of a secrecy order shall be extended for a period equal to that of the delay. This is based on the fact that under S. 643 the period that an application is retained under secrecy prior to its issuance would otherwise be subtracted from the twenty-year term of the patent. In this same context, we would suggest that a new Section 154(d) be included, which would state:

> The term of a patent whose issuance has been delayed by reason of a request of the Administrator of the National Aeronautics and Space Administration that the patent be issued to him on behalf of the United States pursuant to the provisions of Section 305(d) of the National Aeronautics and Space Act of 1958 (42 U.S.C. 2457(d)) shall be extended for a period equal to the delay.

We have found through experience that the delay in issuance of a patent occasioned by a request of the Administrator of NASA that a patent be issued to him may extend anywhere from four months to approximately four years in contested cases. The provisions of Section 305(d) are invoked in some 20 to 25 applications per year. We believe that this fact should be recognized in any legislation which changes the measurement of the term of the patent from issuance to filing date.

Filing by Owner

The owner of an application or his agent, as well as the inventor, may file the patent application, Section 111. This change would approximate the procedure that we have followed for the filing of applications in the name of the Administrator on inventions made under NASA contracts pursuant to Section 305(a) of the National Aeronautics and Space Act of 1958. We believe this is a practical and progressive step in amendment of the patent laws.

Reexamination Chapter

Under Chapter 18 of S. 643, a six-month period is established after the issuance of a patent for any person to cite pertinent publications or patents which may cause the Commissioner to reexamine an issued patent and, if warranted, to cancel claims thereof; and a one-year period to permit any person to notify the Commissioner and present evidence of prior public use or sale, prior inventorship by that person or derivation of the invention from the party providing the notification. We favor such a period for reexamination of a patent since we believe that this will strengthen the presumption of validity or correctness of patents issuing from the United States Patent Office.

Section 305(d) of the National Aeronautics and Space Act

Section 7 of S. 643 provides that the Patent Office Board of Appeals shall:

> (b)(3) Perform the functions specified as being performed by a Board of Patent Interferences in Public Law 593, Eighty-second Congress (ch. 950, 66 Stat. 792, section 1), and in other Acts of Congress and when performing said function shall constitute a Board of Patent Interferences.

In view of the requirements of Sections 305 (d) and (e) of the National Aeronautics and Space Act of 1958 (42 U.S.C. 2457 (d), (e)) relating to duties of the Board of Patent Interferences, it might be preferable for the phrase "Public Law 85-568, 72 Stat. 426" to be appropriately inserted in the above paragraph to cite clearly the application to the National Aeronautics and Space Act. However, the provision as drafted is considered to be sufficient from the standpoint of this agency.

Furthermore, under Section 305(d) of the National Aeronautics and Space Act, questions of title to inventions that may have been made under a NASA contract are required to be heard and determined by the Board of Patent Interferences in accordance with ". . . rules and procedures established for interference cases. . . ." While proposed Section 7 provides that this Board will be replaced by a Board of Appeals, no corollary provision is made to designate the procedure and rules to be substituted for those provided in current Section 305(d). However, in our opinion, the proposed Section 7, taken with Section 5 of the Transitional and Supplementary Provisions (p. 45), adequately protects the interests of NASA since it would maintain intact the body of procedure and precedent built up over the last eleven years for implementing the requirements of Section 305 (d) and (e) of the National Aeronautics and Space Act, while merely substituting the Board of Appeals for the Board of Patent Interferences as the deciding body.

S. 643 contains one addition to S. 2756 of the 91st Congress and that is Section 6 of the "Transitional and Supplementary Provisions," which relates to an amendment to the Clean Air Act Amendments of 1970 wherein the patent provisions of that act would be deleted. It is not known what effect Section 6 would have on the National Aeronautics and Space Administration, and therefore no comment is made at this time as to this proposed amendment.

In conclusion, this agency interposes no objection to the enactment of S. 643; however, we hope the Committee would give consideration to the points set forth above.

The Office of Management and Budget has advised that there is no objection to the submission of this report to the Congress.

Sincerely,

H. DALE GRUBB,
Assistant Administrator for Legislative Affairs.

NATIONAL AERONAUTICS AND SPACE ADMINISTRATION,
Washington, D.C., May 14, 1971.

Hon. JAMES O. EASTLAND,
Chairman, Committee on the Judiciary,
U.S. Senate,
Washington, D.C.

DEAR MR. CHAIRMAN: This is in further reply to your request for the comments of the National Aeronautics and Space Administration on Amendment No. 23 and Amendment No. 24 by Mr. Scott to S. 643, a bill "For the general revision of the Patent Laws, title 35 of the United States Code, and for other purposes."

The Amendment No. 23 proposed to Section 301 is intended to make it clear that the patent laws shall not be construed to preempt the right of the courts under State or Federal law to decide issues with respect to enforcement of contracts involving rights to intellectual property such as trade secrets, technical know-how, and unfair competition.

The Amendment No. 24 stems from Recommendation XXII of the 1966 Report of the President's Commission on the Patent System. The amendments relate to the licensable nature of patent rights which, of course, have antitrust implications.

The Amendments Nos. 23 and 24 are in a quite controversial area, both within the Government and the private sector. In our report to the Committee on S. 643, we interposed no objection to the legislation. However, in the nearly five years since the President's Commission report, it appears that legislation implementing Recommendation XXII has not been drafted which is generally acceptable to the parties of interest. Perhaps acceptable legislation cannot be drafted.

In view of the foregoing, the National Aeronautics and Space Administration would defer to the views of the Federal agencies with primary concern for a determination as to the need for legislation on these matters and the adequacy of the provisions of Amendment No. 23 and Amendment No. 24.

The Office of Management and Budget has advised that there is no objection to the submission of this report to the Congress.

Sincerely,

H. DALE GRUBB,
Assistant Administrator for Legislative Affairs.

SMALL BUSINESS ADMINISTRATION,
OFFICE OF THE ADMINISTRATOR,
Washington, D.C., June 9, 1971.

Hon. JAMES O. EASTLAND,
Chairman, Committee on the Judiciary,
U.S. Senate,
Washington, D.C.

DEAR MR. CHAIRMAN: This letter is written to express the views of the Small Business Administration with respect to S. 643, a bill: "For the general revision of the Patent Laws, title 35 of the United States Code, and for other purposes," and several proposed amendments thereto.

The proposed legislation would substantially revise the patent laws of the United States. The pattern of our present patent system is essentially the same as that created by the 1836 patent statute. In view of the dramatic changes which have occurred in the character of the nation's economy, the tremendous advances in our technology and the development of scientific and technical information, there can be no gainsaying the need for modernization of our patent system.

S. 643 would achieve this objective and thus benefit independent inventors, innovative small business concerns as well as the small business community. The Small Business Administration, therefore, supports its enactment.

The Department of Commerce has recommended to your committee certain amendments to S. 643. Among these amendments are those relating to licensing and other transfers of patent rights (Item P, p. 21 et seq., of the Department's letter).

These proposed amendments are intended to achieve one of the more significant recommendations of the President's Commission on the Patent System—Recommendation XXII. SBA was a member of this Commission and participated in the formation and adoption of this recommendation. We believe its effectuation is required if independent inventors and innovative small business concerns are to be given the protection and encouragement contemplated by the Constitution.

The problems of small businessmen in promoting new ideas and inventions have been extensively chronicled. They are due in no small measure to the uncertainties attendant to the interfacing of the patentee's right flowing from the patent grant and the antitrust laws. Professor John C. Stedman of the University of Wisconsin attributed the reason for this uncertainty to the fact that:

> "Except for an occasional oblique reference to the patent-antitrust issue, as in section 3 of the Clayton Act or section 271 of the Patent Code, Congress has left the matter severely alone. And so it has devolved upon the courts—with the Supreme Court, of course, as the bell-cow—to develop the policy, determine where to draw the line between permitted and prohibited conduct, and decide how hard to hit the transgressor."

The eminent legal authority, former Judge Simon H. Rifkind once declared that the patentee's rights "seem to shrink almost every decision Monday" (i.e., after the Supreme Court hands down its decisions).

Congress should end this judiciary pre-emption and formulate the rules to govern the bounds of permissible patentee conduct in matters relating to licensing and royalties. To this end, we favor the principle urged by Recommendation XXII—a statutory Rule of Reason.

We are fully cognizant of the opposition in some quarters to such statutory prescription—however, we believe that these objections fail to give due weight to the needs of the patentee—particularly those which qualify as small business and at the same time overstate the deleterious impact such legislation would have on our free competitive economy.

While the Small Business Administration does not endorse any specific language to achieve this goal, we do urge that patentees be granted the protection provided by the section 271(h)(i) proposed by the Department of Commerce.

We favor the objectives of the other amendments proposed by the Department of Commerce and urge their incorporation into S. 643.

We have been advised that the Office of Management and Budget has no objection to the submission of this report.

Sincerely,

THOMAS S. KLEPPE, *Administrator.*

THE GENERAL COUNSEL OF THE TREASURY,
Washington, D.C., May 13, 1971.

Hon. JAMES O. EASTLAND,
Chairman, Committee on the Judiciary,
U.S. Senate,
Washington, D.C.

DEAR MR. CHAIRMAN: The Department would like to take this opportunity to express its views on certain sections of S. 643, "For the general revision of the Patent Laws, title 35 of the United States Code, and for other purposes," which is pending before your committee.

The proposed legislation would make numerous revisions in the patent laws contained in title 35 of the United States Code. Proposed section 271(b) of title 35 would provide: "Whoever, without authority, imports into the United States a product made in another country by a process patented in the United States shall be liable as an infringer." Section 281 would give a patentee a remedy by civil action for infringement of his patent, and section 283 would authorize courts having jurisdiction of cases under title 35 to grant injunctions in accordance with the principles of equity to prevent the violation of any right secured by patent, on such terms as the court deems reasonable.

In view of these provisions, it is our expectation that the Bureau of Customs of this Department would not be obliged to make determinations under the patent laws, as revised, to exclude administratively imports from entry, or to detain, seize or forfeit any imported products, except to participate in carrying out an injunction or restraining order of a district court, as the latter deems reasonable to prevent the violation of rights secured by patent. The Department does not anticipate any unusual administrative difficulties in enforcement at ports of entry of injunctive relief or similar restraints on infringing imports.

The proposed legislation does not contain any provision authorizing the Bureau of Customs, subject to an appropriate user fee, to disclose to domestic patent owners information from customs entries covering imports suspected of being products of foreign infringing uses. At the present time, this information is made available on the basis of the "unfair competition" concept of section 337 of the Tariff Act of 1930, as amended (19 U.S.C. 1337). The Bureau's regulations on this matter are contained in 19 CFR 12.39a and 24.12(a)(3). It is not anticipated that the omission of such a provision would result in discontinuance or changes in these procedures.

The Department has been advised by the Office of Management and Budget that there is no objection to the submission of this report to your Committee.

Sincerely yours,

SAMUEL R. PIERCE, Jr.,
General Counsel.

AEROSPACE INDUSTRIES ASSOCIATION OF AMERICA, INC.,
Washington, D.C., May 26, 1971.

HON. JOHN L. MCCLELLAN,
Chairman, Subcommittee on Patents, Trademarks, and Copyrights, Washington, D.C.

DEAR MR. CHAIRMAN: The Aerospace Industries Association of America, Inc., has presented the views of its member companies on proposed legislation which would amend Title 35 of the United States Code dealing with the patent statutes. As we stated previously, this Association supports the United States patent system and recognizes the contributions it has made to the growth of our economy. We appreciate this opportunity to present our views on the latest bill, S.1252, introduced by you for the purpose of amending the patent laws.

The subject bill is an endorsement of the Stockholm Revision of the Paris Convention and would amend the Patent Statutes to accord to inventors' certificates the same rights and effect as an application for patent. Since passage of this bill would give advantages to nationals of countries using a certificate system which advantages are not available to nationals of other States (such as nationals of the United States), the bill should not be enacted.

A patent system and an inventors' certificate system both afford protection for inventions. Both systems may exist in the same country but effectively only a national may opt for a certificate. The requirements and effects of a certificate system contrary to a patent system, result in discrimination against foreign nationals. By its very nature a certificate system is restricted to use by socialistic states while a patent system is not.

An inventors' certificate (or "certificate of authorship"), unlike a patent, gives no right to the inventor to exclude others from the practice of his invention. A certificate is simply a recognition by the State that the inventor did evolve a novel solution of a technical problem.

In countries employing a certificate system, the inventor, by accepting a certificate, and foregoing a patent, conveys to the State exclusive rights in his invention and the State has the responsibility for introduction of the invention. Introduction is required to be accomplished through State enterprises and organizations, with cooperative and public enterprises and organizations (State owned legal entities) having rights to use. For accepting a certificate the inventor receives recommendation compensatory with the effectiveness of the invention in the economy of the State. An upper limit is placed on the amount of compensation to be paid. For important inventions, the holder of a certificate, but not a patent holder, may be accorded additional benefits, such as favorable income tax treatment, academic recognition, better job opportunities, more comfortable housing and other creative comforts.

It is clear that the purpose of a certificate system, and the granting of extra benefits thereunder, is to discourage an inventor from seeking a patent. Also, once an inventor has accepted a certificate and is given these added benefits, should he thereafter seek a patent for a subsequent invention he ceases to enjoy such benefits. There is further discouragement to an inventor attempting to acquire a patent rather than a certificate in that the inventor must pay fees on filing an application for patent and then pay renewal fees if a patent issues. There are no filing costs and no renewal fees connected with a certificate. A patent is granted for a limited number of years but a certificate gives rights in perpetuity to the State. A patent is subject to attack throughout its term but the certificate is vulnerable only within the first year after its publication.

It is apparent that an inventors' certificate provides advantages to a national that clearly are not available to an inventor of another country who seeks protection for his invention. The philosophy governing treatment of inventors of contracting States under the Paris Convention is that a foreign national is to have the same advantages as a national. Since a foreign national is not afforded the same advantages under an inventors' certificate system, the certificate should not be given the same consideration afforded a patent.

Accordingly the endorsement of the Stockholm Revision sought by S.1252 should be refused and inventors' certificates should not be treated as are patent applications and give rise to a right of priority under the same conditions and with the same effect as applications, and an applicant for a certificate should not be afforded the same priority rights as an applicant for a patent.

Yours very truly,

KARL G. HARR, Jr.

AMERICAN BAR ASSOCIATION,
Chicago, Ill., April 22, 1971.

THOMAS C. BRENNAN, Esq.,
Chief Counsel, Subcommittee on Patents, Trademarks, and Copyrights, U.S. Senate, Old Senate Office Building, Washington, D.C.

DEAR MR. BRENNAN: This refers to the Notice of Hearing on Patent Law Revision which appeared in the Congressional Record of March 24, 1971, and confirms telephone conversations we have had concerning topics to be covered by the hearings.

First, as to Senate Amendment 24 to S.643, 92nd Congress, the American Bar Association has not taken a position on the specific provisions of this amendment. The Association has, however, adopted in 1967 a resolution reading as follows:

Resolved, That the American Bar Association approves in principle legislation by which:

(a) The licensable nature of patent rights would be clarified by specifically stating in the patent statute that applications for patents, patents, or any interests therein may be licensed in the whole, or in any specified part, of the field of use to which the subject matter of the claims of the patent are directly applicable;

(b) A patent owner shall not be deemed guilty of a patent misuse merely because he agreed to a contractual provision or imposed a condition on a licensee, which has (1) a direct relation to the disclosure and claims of the patent, and (2) the performance of which is reasonable under the circumstances to secure to the patent owner the full benefit of his invention and patent grant;

(c) It is made clear that the "rule of reason" shall constitute the guideline for determining patent misuse, and be it further

Resolved, That the Section of Patent, Trademark and Copyright Law is authorized to communicate this action to members and committees of Cougress and to others concerned with enactment of legislation to which the subject matter of this resolution is directed.

This resolution contains the essence of Recommendation XXII of the President's Commission on the Patent System established by Executive Order No. 11215 on April 8, 1965, and which presented its report in November, 1966. It is believed evident that the Association can be considered as favoring in principle the substance of the aforementioned Senate Amendment 24, even though the Association has not had an opportunity to act formally with respect to the amendment.

As to Section 308 of the Clean Air Amendments Act of 1970, and Section 6 of the Transitional and Supplementary Provisions of S.643, the Association has a long-established position against compulsory licensing of patents. In 1962, the Association approved a resolution disapproving in principle any requirements that a holder of a patent on a new drug license others for use thereof and provide all technical information required for manufacturing, preparation or propagation of the drug without restriction upon manufacture, use or sale other than payment of a royalty limited to a percentage of the gross selling price of the drug, and specifically disapproved such proposed requirements as contained in S.1552, 87th Congress. After hearings were held in regard to this proposed legislation, Congress decided not to include a compulsory licensing provision. The Association can, therefore, be considered as clearly approving deletion of Section 308 of the Clean Air Amendments Act of 1970.

With respect to S.1252 which provides for granting a right of priority with respect to Inventors' Certificates, the Association approved the following resolution in 1970:

Resolved, That the American Bar Association approves in principle, the Revision of the Paris Convention to qualify Inventors' Certificates with respect to the right of priority under the same conditions and with the same effect as applications for patent.

Specifically, the American Bar Association approves Articles 1–12 of the Revision of the Paris Convention signed at Stockholm, Sweden on July 14, 1967, and be it further

Resolved, That the Section of Patent, Trademark and Copyright Law is authorized to communicate this action to members and committees of Congress and to others concerned with enactment of legislation to which the subject matter of this resolution is directed.

It can be seen from the foregoing that the Association approves, in principle, the subject matter of S.1252.

Relative to adjustment of patent and trademark fees, such as is provided by S.1255, 92nd Congress, the Association does not have an established position at this time. This bill has been referred to appropriate committees of our Section of the Association, and we hope to consider it at the forthcoming Annual Meeting of the Association in July, 1971. Depending on the outcome of that meeting and how much progress our committees make in advance of the meeting, we may be able to establish an Association position fairly promptly.

In view of the importance of the subject matter to be considered at the May 11 and 12 hearings, particularly Senate Amendment 24 to S.643, I request the opportunity to appear before the Subcommittee and present the views of the Association in those areas where the Association has established positions. Our Section has a history of activity with respect to the subject matter of A.24 going back to the Report of the President's Commission on the Patent System. We consider the subject matter to be very important, and believe that our views might be helpful to the Subcommittee in its deliberations.

May I please hear from you concerning this.

Very truly yours,

ANDREW B. BEVERIDGE,
Chairman.

AMERICAN CHEMICAL SOCIETY,
Washington, D.C., June 7, 1971.

Re Patent law revision: Amendments Nos. 23 and 24 by Senator Scott to S. 643.

Hon. JOHN L. MCCLELLAN,
Chairman, Committee on the Judiciary, Subcommittee on Patents, Trademarks, and Copyrights, Senate Office Building, Washington, D.C.

DEAR SENATOR MCCLELLAN: The American Chemical Society, acting through its Board of Directors and its Committee on Patent Matters and Related Legislation, representing over one hundred thousand chemists and chemical engineers, has carefully considered the amendments offered by Senator Scott. We respectfully offer our comments and conclusions.

It seems to us, as chemists and engineers concerned with the practical benefits of science, that misconceptions are growing in nonscientific circles about the role of our patent system in technological development. Within the scientific community, both academic and industrial, the economic realities are contrary to some of the opinions we see. We can only speculate as to the reasons for such divergent conclusions.

For example, we have noted the attack on these amendments as "enriching the patent promoters" at public expense. We believe this represents a failure to comprehend the function of the patent system, which is to serve the public interest by encouraging the generation of inventive technology, the publication of this technology, and its prompt commercialization. If this technology is never invented or never commercialized, that loss will do much greater damage to our economy than the licensing practices which are being critcized.

Chemical technological growth depends on long term, expensive research and development—perhaps to a greater extent than in any other major industrial category. Chemical research and development are in the main conducted with private funds. The field of chemistry has benefited from the patent system and the economy and the fund of public knowledge have been enriched by the store of technology which has been contributed by chemical practitioners in reliance on the patent system. Because of our belief that opponents of the Scott Amendments, and of S. 643, have not adequately considered these views, we undertake to express them to you.

I. INTRODUCTION

The American Chemical Society supports S. 643 in general, as continuing to maintain and improve the legal framework for a strong patent system. As chemists and chemical engineers, in research and in industry—and we speak solely for the fields of chemical technology—our experience leads us to the conclusion that steps which strengthen our national patent system tend also to strengthen our national scientific and economic growth.

The mix of patents issued annually is about twenty-five percent "chemical," a lesser percentage "electrical," and over fifty percent "mechanical." The chemical field is distinguished, at least from the mechanical, by the extraordinarily high research and development costs of the chemical industry.

Chemical inventions fall into two general types, product and process. A new product or combination of products may be the result of several years of experimentation and rejection of unsatisfactory alternatives; yet once discovered and disclosed, it may be easy to copy. Without a patent system, the incentive to do this type of research would diminish.

The other general type of chemical invention has to do with chemical processes. Unlike even complex machines or mechanical devices, a chemical process is usually not discernible by "reverse engineering" from the product. Absent a reliable patent system, chemical process inventions would surely be kept secret. Secrecy does not benefit technological progress.

On the other hand, with reasonable and fair opportunities to license and sell chemical process inventions, disclosure via the patent system is encouraged. In our opinion, the Scott Amendments will enhance the development and the spread of new technology by eliminating present uncertainties and by allowing inventors to license and sell their inventions without fear of court-approved bad faith licenses, or of changes in the law which would invalidate present licensing practices.

We have reached the conclusion that the present trend in the law and present positions of the Department of Justice reflect a misunderstanding of the function of the patent system in our nation's privately-funded scientific and technological efforts. Further, there appears to be little awareness of the actual uses of patent licensing, which in practice achieve utilization of chemical technology that would otherwise remain undeveloped, and transfer technology in such a way that wasteful duplication of research and development effort is avoided. We are convinced that the present trend is, on balance, detrimental to scientific and technological growth. The alleged overriding public benefit from imposing further restrictions on patent licensing has, in our opinion, failed to come to pass. For these reasons, we welcome this opportunity to comment on the amendments offered by Senator Scott.

II. AMENDMENT NO. 23

Accepting the premise that a cloud remains over the issue of whether non-patented subject matter may be the subject of an enforceable contract, we believe that the interests of technological advance require that legislative clarification be enacted.

In the chemical field many industries, large and small, have been built on the acquisition from others of what has come to be called "technical know-how". New businesses have been based on the purchase or license, from the originator of technical know-how, of the skill and experience necessary to succeed in the chemical process industries.

Many millions of dollars are often spent in introduction of new processes and in the design of chemical plants, and substantial economic benefit results from sharing this technical know-how with others, normally by licensing. The foreign licensing of scientific and technical know-how brings into this country many millions of dollars of royalties each year. In 1968, according to the U.S. Department of Commerce, this sum was over a billion dollars for industrial property licenses, with almost all of the patent licenses being accompanied by know-how transfers. In domestic industrial exchange, the licensing of technical know-how results in the ability of new industry to enter into production without the expensive duplication of known technology; we fail to understand how this can have any but a beneficial effect on competition, as well as on industrial growth.

The law, we understand, is unsettled, and the purpose of Amendment No. 23 is to settle it. We understand that the seller of technical know-how, or of an invention on which a patent has not or may not issue, after he has transferred his experience and designs and technology, might not be able to enforce his contract to collect the payment he had bargained for. This cloud over such exchanges has already made itself felt in the chemical process industries. Should the law develop to the point whereby technical know-how and other secret information cannot be sold or licensed without the strong risk of loss of both payment and the know-how, then this sort of transfer will surely diminish. We can think of no realistic balance of public policy considerations which would favor this result. Secrecy, tightened plant and research security measures, and restraints on employee mobility must follow, as well as reduced competition.

Since know-how and secret information would give enforceable rights only against those who receive it in confidence, and while it is still secret, the public loses nothing which it would otherwise have. Anyone who independently develops the secret information has the absolute right to use it and to publish it. But if transfers of technical know-how can be validly undertaken, research efforts are saved for less duplicative areas, and industrial competition is on balance increased. For these reasons the American Chemical Society urges the acceptance of Amendment No. 23, insofar as it pertains to trade secrets and confidential and proprietary information.

III. AMENDMENT NO. 24

We support this Amendment, since it serves to remove some of the doubt which has come to surround some of the established methods of transferring patented technology. As we see it, recent judicial and governmental challenges are based on the economic theory that, by implementing a policy which more strictly circumscribes the uses of patents, free competition is increased and the public is thereby benefited.

We agree that competition is freer in the absence of patents. But within our experience, we believe this conclusion is simplistic. To draw an extreme illustration, competition in a new style of "hula hoop" will be freer. But the unnecessary duplication of expensive research and development effort in complex technological fields, in the absence of incentives to license, can only increase overall costs to the public. The ultimate loss in the absence of such incentives could be that research and development efforts may be reduced and fewer inventions made.

If there is a national interest in maintaining the role of private enterprise in the expansion and development of technology, then this interest must be balanced against the results of a more restrictive patent policy, in determining where the overriding public policy lies.

We suggest that the public and various government departments should be less concerned with whether an inventor can contract for an adequate return on his invention, with the government or the courts intervening to decide what is "adequate", and more concerned with the effect on private technological research and development in fields where research costs are high. There is inadequate reason, in our opinion, for the United States expressly to impose restrictions on the licensing of technology which puts us as a nation at a disadvantage in worldwide technological competition.

Our chemical technological future is at present in delicate balance. With the reduction in governmental support of research, it is again clear that our national scientific progress must depend on private enterprise. An added incentive to private development of technological advances comes from a more flexible patent licensing structure. We admit that we do not know how great this added incentive may be. But we do know, in our own experience, that the present clouds on the transfer of technology by patent license have had a noticeable adverse effect in the chemical arts.

Therefore, we urge the acceptance of Amendment No. 24. The following comments point out some of the ways in which this amendment applies to the development of chemical inventions through licensing.

Section 261(b)(2).—Many inventors in the chemical field, especially those in universities and small firms, do not have the resources needed to develop and market chemical inventions. Yet if the exclusive transfer of patent rights is not allowed, many inventions from this source will never reach commercialization, with resultant loss of the benefits of this technology to the public.

The flexibility whereby a patent may be licensed to more than one licensee for different uses, and the other restrictions sanctioned in this section, appear to us to be logical methods of obtaining maximum technological and commercial development of a patented subject matter. We fail to see that anti-competitive results contrary to the public interest are inherent in "field of use" restrictions, particularly where the fields of use may include, in the chemical arts, such diverse fields (for the same chemical compound, for example) as the plasticizer and the pesticide fields, where the same licensee usually does not have the capability to develop the invention in all fields. In fact, encouragement of the introduction of new technology into diverse fields may well be a factor in increasing competition.

Section 261(e) and *(f)*.—These provisions with respect to contesting the validity of a patent, as offered by Senator Scott, appear to us to present a wise compromise. The public's interest in striking down invalid patents is preserved without unfavorably affecting the parties to a transfer of patent rights. New grounds of invalidity may always be asserted, thus preserving the right to expose invalid patents. Yet the cloud which now accompanies every patent license would be controlled. At present, it appears that any purchaser of a patent may later renege on his part of the bargain with the full approval of the law, while keeping the inventor's property.

The individual inventor and the university scientist are particularly at a disadvantage in any bad faith licensing situation because of the very high cost of patent litigation. Particularly in the chemical field, where secrecy is sometimes a feasible alternative, inability to place reliance on license agreements can be expected to lead to a reluctance to enter into the patent system, with the result that the technology may be lost to the fund of knowledge. We believe that the potential public detriment warrants the enactment of legislation such as is proposed.

Section 271(f) (g).—The American Chemical Society is in favor of legislative enactments which will eliminate doubt as to existing practices, and permit the reasonable use of patent rights in a manner which will support and accelerate technological growth. These sections should, in our opinion, help to achieve that goal, and appear to be in accord with the harmony of the patent and the antitrust laws which is analyzed under Recommendation XII of the Report of the President's Commission on the Patent System.

The American Chemical Society is ready to assist the Congress in its consideration of Patent Law Revision in any way it can.

Sincerely yours,

MELVIN CALVIN.

MEMORANDUM ON THE NEED FOR LEGISLATIVE CLARIFICATION OF THE LAW RELATING TO PATENT LICENSE PROVISIONS

(Submitted on behalf of The American Patent Law Association, Arlington, Va.)

INTRODUCTION

When the patent system is viewed in terms of its constitutional objective of encouraging useful innovation, patent and antitrust concepts may touch but they shouldn't tangle. However, there is mounting evidence of inconsistency and confusion in the courts and a disturbing trend in the Department of Justice concerning the terms that may be incorporated in patent licenses without invoking the sanctions of antitrust.

The importance of this development lies in the fact that the licensing of patents, and the freedom to adapt the license to the business situation facing the patent owner and his prospective licensee, are often indispensable to the full utilization of the patent for the benefit of both the public and the patent owner.

It is the purpose of this Memorandum on behalf of the American Patent Law Association to outline some of the problems of patent license provisions and to suggest areas in need of legislative clarification.

THE ROLE OF PATENTS IN INNOVATION

There are two distinct but important roles of patents in the innovative process, one widely recognized and the other too often ignored. Both are embraced within the constitutional requirement that the patent system "promote the progress of useful arts." [1]

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[1] Article I, Section 8. The Congress shall have 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 first is the incentive to invent, or—more commonly—to support inventive efforts. Of course, a few gifted individuals invent as a reflexive response to a problem or challenge. They may have little regard for the economics or marketability of their inventions but simply invent for the satisfaction of exercising their creative talents. For them the patent system may provide little personal incentive to invent (although patents may afford the only means for bringing their inventions into use for the benefit of the public, as will be developed below).

But the oftimes risky investment in research, development, design, manufacturing and marketing activities in the context of the innovating unit, be it an individual or corporate group, could hardly be justified if the results could always be freely copied by those having no such investments to recover. The innovator of a marketable product needs a *lead time* during which he can deny competitors a free and profitable ride on his investment in the innovation. This is what the patent system gives him in return for disclosing details of the invention in a patent—provided his invention can qualify as sufficiently different from what has been done before to merit a patent.

From this limited lead time of seventeen years sometimes called the patent "monopoly," the patent owner has an opportunity to recover his exenses, earn a profit and possibly invest in other innovative adventures—so long as the public is satisfied his product is worth buying at the price he charges. It is the *prospect of patent coverage* that justifies much investment in research and development leading to new products, new plants, new employment opportunities and genuine progress in the useful arts.

The second role of patents in innovation concerns the ability to market. At the patent's expiration, anyone can use the invention free of the patent. In the meantime, public disclosure of the invention in the patent often stimulates others to invent improvements or make quite different inventions, building on the ideas in the patent.

While public disclosure of the invention in the patent is therefore a contribution in itself, the full range of benefits contemplated by the patent system are not realized until the patented invention is embodied in a product or service available to the public. The right to exclude others from practicing an invention is hollow, indeed, both from the standpoint of the patent owner and the public, if the patent owner lacks the money, talent organization or facilities to bring the invention to market. It is therefore essential that if the patent owner decides to market the invention *he be able to use his patent* to secure what he lacks in the means to market.

This is particularly important where the invention is capable of application outside his regular field of interest or competence. In such event he needs to use his patent in a business arrangement that will give incentive to those of his choosing who are expert in other fields and can handle the special problems of development, manufacturing and marketing.

These two elements, *the incentive to invent* (or support inventive efforts) and *the ability to market*, are the heart of a patent's contribution to "innovation." They are sequential but inseparable, and recognition of this duality will be seen as important in resolving patent-antitrust conflicts in the area of patent licensing.

THE CONTRIBUTION OF PATENTS TO THE ANTITRUST OBJECTIVE

To the extent the patent owner has the exclusive right to prevent others from making, using and selling the invention claimed in the patent, he does, indeed, enjoy a monopoly—albeit a temporary one. But the temporary monopoly of the patent takes nothing from the public, for the patent *by law* covers only that created for the first time by the inventor.

Because a monopoly of any kind is anathema to the antitrust theorist, the monopoly of the patent has given rise to the erroneous idea that patent and antitrust concepts are endlessly opposed. The patent monopoly is regarded as an intrusion on the principle of free and unfettered competition.

In truth, however, the utilization of the temporary patent monopoly brings an entirely new dimension to the free competition sought by the antitrust laws. This new dimension arises from the necessity for competitors to find their own routes to successful products, a process that in its stepwise implementation brings new and better or cheaper products to the market. Indeed, there is no stronger incentive to invent, or to invest in efforts to invent, than a successful, patented product in the hands of a competitor. This can properly be called *innovative* competition—or competition in *value*, as distinguished from price—a form of competition not secured through application of any of the antitrust laws.

PATENTS, PROFITS AND PROPHETS

If the support of inventive efforts leads to grant of a patent, or if a patent is otherwise acquired, the problem of the patent owner is how to use the patent for profit. The patent may cover a manufactured article, a device or machine, a chemical compound or combination of compounds, a process for making something, or a method for doing something. If practicable, the patent owner usually chooses to make and sell the patented product himself or use the process in his own plant.

However, if in his business judgment he decides the best opportunity for profit lies in granting licenses to others, he must proceed with the utmost care. First, he must choose as his licensees only those who, by their good reputations or capabilities, will bring credit to his invention. In licensing his patent for practice by others he is parting with a portion of the exclusive privilege his patent gives him, and licensed activities that would demean the invention would inevitably lessen the value of his remaining rights under the patent.

Second, he must fashion the patent license to the business situation he faces. Obviously, the arrangement must hold prospects of profit for both parties. But in taking into account the business interests involved, the patent owner can properly include in the license only those provisions reasonably related to securing for him the legitimate benefits of the patent grant—which confers the right to exclude others from making, using or selling the patented invention. If the license goes farther, the validity of the arrangement can be called into question because the patent has been employed beyond its lawful scope. The patent owner has, in other words, "misused" his patent.[2]

Patent misuse is a defense against a charge of infringement and may relieve the infringer of liability. Although the patent may be valid, the patent owner loses his right to enforce it so long as the misuse continues and the consequences have not been corrected. If the misuse can be shown to have adversely affected competition, or to have been part of a plan to restrain or monopolize trade, the acts of misuse may rise to a violation of the antitrust laws. The phrase "antitrust laws" includes Sections 1 and 2 of the Sherman Act and Sections 3 and 7 of the Clayton Act, with the Federal Trade Commission Act sometimes included.[3]

While patent misuse is actionable only as a defense to a suit for infringement or a related suit for breach of a license, activities believed to constitute antitrust violations can be enjoined by a court on the basis of action by the Department of Justice, acting in the name of the United States Government, or on the basis of action by injured private parties. The penalties for antitrust violations can range from heavy fines to prison sentences (where a criminal violation is made out), and private parties who have been injured by the illegal acts can sue for treble damages.

Increasingly, the patent owner who licenses his patent needs the gift of prophecy. In tailoring his license to the business situation existing *at the time of licensing*, he and his prospective licensee must foresee not only how the courts and Department of Justice might interpret the license provisions, but also how changing business circumstances might affect such interpretations.

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[2] *Motion Pictures Patent Co. v. Universal Film Mfg. Co.*, 243 U.S. 502 (1917). See also elaboration of theory in *Morton Salt Co. v. Suppiger*, 314 U.S. 488 (1942).

[3] *Sherman Act, Section 1* (15 U.S.C. 1): Contracts, combinations or conspiracies in restraint or interstate or foreign trade or commerce are illegal. *Sherman Act, Section 2* (15 U.S.C. 2): Persons who monopolize, or attempt to monopolize, or conspire to monopolize any part of interstate or foreign trade or commerce are guilty of a misdemeanor. (subjecting them to criminal sanctions). *Clayton Act, Section 3* (15 U.S.C. 14): It is unlawful to sell or lease commodities, whether patented or unpatented, on condition that the purchaser or lessee will not deal in the products of the seller's or lessee's competitors where the effect may be to substantially lessen competition or tend to create a monopoly. *Clayton Act, Section 7* (15 U.S.C. 18): No corporation can acquire the stock or assets (generally interpreted as including patents and interests in patents) of another corporation where the effect may be to substantially lessen competition or tend to create a monopoly. *Federal Trade Commission Act* (15 U.S.C. 41 et seq.): Federal Trade Commission can issue cease and desist orders against unfair methods of competition and against violations of Sections 3 and 7 of Clayton Act but so far has taken little action in matters involving patents.

As will be demonstrated below, the state of the decisional law is unsettled in the extreme. But of equal importance is the threatening posture of the Department of Justice. The recently-announced establishment of a Patent Unit within the Antitrust Division of the Department of Justice underscores concern over some of the policies that seem to be emerging in the patent-antitrust area.[4]

Speaking in Washington on June 5, 1969, Assistant Attorney General McLaren, in charge of the Antitrust Division of the Department of Justice, outlined the guiding philosophy of antitrust enforcement in this area as follows:[5]

"In considering whether to attack a particular licensing provision or practice, we ask ourselves two fundamental questions. First, is the particular provision justifiable as *necessary* to the patentee's exploitation of his lawful monopoly? Second, are less restrictive alternatives *available* to the patentee? Where the answer to the first question is no, and to the second yes, *we will consider bringing a case challenging the restriction involved.*" (Emphasis added.)

The Department of Justice is therefore not only concerned with whether a given practice in a given situation in fact constitutes an antitrust violation, but whether the particular licensing arrangement was "necessary," or whether there might have been other ways of putting the patent to use that would have imposed less "restriction" on the licensee.

More will be said below about use of the word "restriction" in the patent license context. It is important to understand, however, that the Department of Justice is using the term to describe that portion of the patent grant which the patent owner has chosen *not* to license.

If the patent owner can deny access of all others to his invention, it would seem appropriate that he be entitled to control the degree to which he relinquishes his exclusive rights, *so long as the license provisions are within or reasonably ancillary to the patent grant.* No gift of prophecy could possibly anticipate the outcome of a test of a licensing arrangement, made in a given business context at a specific point in time, against the subjective criteria of "necessity" and "availability of alternatives" applied at some future time. One is led to conclude that only the failure of the arrangement would prove its legality.

THE DISPOSITION OF PATENTS AS PERSONAL PROPERTY

It should not be taken as the position of the American Patent Law Association that all the patent license provisions discussed herein should always be permitted to stand in all circumstances. Even the most innocuous terms can be applied in a predatory manner to achieve, through conspiracy or individual action, results that are anticompetitive, clearly beyond the scope of the patent grant and inimical to progress in the useful arts. But to adopt the test proposed by the Department of Justice, or to permit the declaration of *per se* illegality of license provisions which, in their proper application, can bring innovative advances more rapidly into public use and actually create competition in the process, is to defeat the principal objectives of both the patent and antitrust laws.

Considerations of the public interest involved in patent licensing permeates this entire discussion. Another important factor to examine, however, is the nature of the rights of the patent owner. The present statute declares that "patents shall have the attributes of personal property." As will be shown, much of the agitation from antitrust theories today would lead to a clear derogation of this concept.

There is no dispute that a principal attribute of personal property is the owner's right to the benefits of ownership, use and disposition. Of course, the law will impose limitations on the right or apply sanctions against the owner where the public is injured by the exercise of the right. But acts of ownership, use and disposition which are themselves legal will not be interdicted merely because they *may* lead to illegal or undesirable consequences. *The owner of private property enjoys, in effect, a presumption that his acts in exercising his rights of ownership, use and disposition are legal.* He does not have to demonstrate their legality or test them by a rule of reason. The burden of establish-

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[4] *The Wall Street Journal* (Midwest Edition), January 7, 1970, page 16.

[5] Assistant Attorney General Richard W. McLaren, *Patent Licenses and Antitrust Considerations.* Address before The Patent, Trademark and Copyright Research Institute of The George Washington University (June 5, 1969), 161 U.S.P.Q. No. 11, p. 11.

ing that his conduct was illegal or against the public interest is on the party asserting it. Indeed, our society could function in no other way.

Patents are a species of personal property. An important attribute of patent property should therefore be the patent owner's right to the benefits of ownership, use and disposition. Of special concern here is the right of disposition. Certainly, a normal incident of patent ownership should be the right of the patent owner (1) to retain the entire patent property for his own use, or (2) to dispose of all or part of it whenever, wherever and to whomever he chooses. It should not be presumed at the outset that, in exercising his patent right of disposition, the patent owner is going to misuse it. Or, simply because he *might* misuse it, he should not be automatically foreclosed from disposing of his patent on terms that are in themselves perfectly legal. Even one charged with a crime enjoys a legal presumption of innocence; the act of disposing of all or part of a patent right should carry no less favorable a presumption.

Nevertheless, the Department of Justice and some judicial decisions would deny the owner of patent property the same benefits and presumptions accorded owners of other forms of personal property. To implement its bias, the Department avails itself of a ready access to the courts (through bringing suits or filing amicus briefs) in cases it selects as most potentially destructive on their facts to the licensing practices it wishes to outlaw. In addition, the Department is utilizing other forms of attack, such as direct pressure, public announcements by Department representatives on the banquet circuit, threats of suits, and consent decrees, to force its views on patent owners who do not wish to serve as test cases for new antitrust theories.

What is the practical effect of this unfortunate situation on the patent owner trying to put his patent to work?

THE PATENT OWNER'S DILEMMA

A patent is not like a commodity that can be priced and placed on the shelf for sale, like a loaf of bread. In "merchandising" or licensing a patent, many factors must be considered, some arising from the interests of the patent owner and some from interests of the potential licensee. By a process of negotiation, each party represents its interests and strengths in arriving at an arrangement satisfactory to both which is within legal bounds today and, hopefully, will remain so for the life of the agreement.

Among the factors considered, many of which give rise to some form of expression in the license, are the following:

Cost of the development to the patent owner and licensee
Anticipated volume of sales
Patent owner's product line and market position
Need for exclusivity
Territory
Availability of substitutes not under patent
Number of patents involved
Scope of invention v. scope of patent coverage
Ease of circumventing patent
Need for licenses under patents of others
Relative value of invention in different fields of use
Capability of licensee to serve all fields of use
Need for lead time
Need for further technical development
Need for market development
Need for investment in production facilities
Financial responsibility of licensee
Expected savings from use of invention
Need for technical assistance from patent owner
Need for use of trade secrets
Availability to licensee of later improvements by patent owner
Fair royalty
Base for royalty determination
Protection against later licenses at lower royalties
Exchange of licenses in lieu of royalty
Non-exclusive rights to patent owner on improvements by licensee

Right to grant sublicenses
Detectability of infringement
Willingness of patent owner to enforce patent against unlicensed infringers
Willingness of patent owner to defend licensee against infringement suits brought by others
Conditions for terminating the license

Before examining individually certain specific licensing problems, it will serve the better understanding of the impact of antitrust to consider how easily, in the exercise of sound business judgment, a patent owner can fall victim to a whole conglomerate of antitrust problems in licensing his patent. Here is the plight, fictitious but representative, of the A Company:

Company A is small manufacturer of electrical switches based in Los Angeles. Its sales are confined to switches for use in buildings in the Los Angeles area. The company owns a patent on a switch which was developed at a cost of $70,000 and three years' effort. It believes the switch can be adapted for other uses but considers expansion undesirable because of lack of capital, development personnel and manufacturing capacity, as well as the increased costs of marketing in remote areas. It does, however, want to retain the exclusive right to the switch in the building field in the Los Angeles area.

In order to reach other markets, Company A decides to license the patent at a royalty of 5%, giving each licensee the exclusive territory he demands in which to sell and service switches, and limiting each to the sale of switches for use in buildings.

The manufacturer in the Detroit area would like to develop the patented switch concept for use in automobiles. However, in order to recover the estimated $100,000 required for the development, he asks for an exclusive license in the automotive field. A royalty of 2% is established as reasonable in view of the development costs and the low profit margin from large volume sales to automobile manufacturers.

Back in Los Angeles, a competitor of Company A, who manufactures switches for use in aircraft as well as buildings, asks for a non-exclusive license for selling to the building trade and an exclusive license for the aircraft industry. The license for the building trade is refused, because the company wants to retain the exclusive right in its home territory. But the exclusive license for the aircraft field is granted at a 10% royalty rate. This figure contemplates the high profit margin but low sales volume of switches for the aircraft industry.

At this point the company consults its attorney to prepare the various agreements. The attorney is convinced that the business judgment is sound, all terms are reasonable, and the arrangements will move the invention to markets throughout the United States at the earliest possible time, with responsible financial backing and business skill in each of the markets served. But the attorney nevertheless advises that (1) it has jeopardized the enforceability of the patent in all markets, including its own market in Los Angeles, by refusing to license its Los Angeles competitor in the building field after licensing others elsewhere in the same field,[6] (2) it has invited an antitrust suit, because the Justice Department has declared it is looking for a situation where a patent license divides fields of use among companies that would otherwise compete,[5] (3) it has opened itself to private antitrust and treble damage claims from its competitors as well as those of its licensees,[7] and (4) it has provided ingredients of a defense of patent misuse by charging different royalty rates under the same patent.[8,9]

This example illustrates a gamut of licensing problems facing today's patent owners. Company A is small and incapable of extending its market outside its home area. But the magnitude of the invention's contribution is no less because of the patent owner's size. Therefore, if Company A is denied the right to license individually the various fields of use of the invention, and on terms

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[6] *Allied Research Products, Inc. v. Heatbath Corp.*, 161 U.S.P.Q. 527, 530 (N.D. Ill. 1969).
[7] *Clayton Act, Section 4.* 15 U.S.C. 15.
[8] *Peelers Co. v. Wendt,* 260 F.Supp. 193 (W.D. Wash. 1966) ; *LaPeyre v. Federal Trade Commission,* 366 F. 2d 117 (5th Cir. 1966) ; *Laitram Corp. v. King Crab, Inc.,* 245 F.Supp. 1019 (D. Ct. Alaska 1965).
[9] Antitrust and Trade Regulation Report, No. 411, Special Supplement, Part II, May 27, 1969: *White House Task Force Report on Antitrust Policy,* page 22.

that will encourage the licensee to proceed with manufacturing and marketing of a quality product, a significant portion of the patent grant will not be used, and the public will not benefit from the invention in the unlicensed fields not served by Company A.

Moreover, the right to charge different royalty rates for different uses of the invention is important because of the different relative values and sales volumes of the products involved. And if, having licensed the manufacture and sale of building switches in areas not served by Company A, it must then license its backyard competitor, a more prudent course would be to refuse to license anyone in the building field—a decision certainly not in the interests of Company A or the users of switches outside Los Angeles.

THE NEED FOR LEGISLATIVE CLARIFICATION

It is appropriate now to examine certain of the specific license provisions that are under actual or threatened attack. These are:

- Field-of-use licenses
- The right to license (or not to license)
- The freely negotiated royalty
- Royalty differential between non-exclusive licensees
- The royalty base
- Royalty for the package license
- Royalty payment after expiration of patent

In order to appreciate the justifications that demand at least the application of a test of reasonableness before these licensing provisions are categorically rejected as patent misuses or *per se* antitrust violations, brief fact situations will introduce each provision.

1. Field-of-Use License

Company B is a large manufacturer of hardgoods of many types but has limited facilities for chemical research and development, execpt with specific reference to adjunctive supplies for its hardgoods. The company achieves a breakthrough in a chemical process which leads to the development of a new line of materials for use with its hardgoods. It also recognizes vast possibilities for the invention in other fields foreign to its corporate interests and capabilities.

The problem facing Company B is how to make the broadest use of the process without itself departing significantly from its primary business. It recognizes that several areas of application are sufficiently distinct in themselves (paper, pharmaceuticals, novelties, cosmetics) that no single company could exploit the technology to its fullest. It therefore chooses to grant exclusive licenses in a number of fields of use. Several licensees invest considerable money in adapting the basic technology to their particular fields and bring the public new products that differ significantly from the old ones.

In an atmosphere that would discourage or hold illegal the field-of-use license, this program of patent utilization simply would not be possible.

Among the ways a patent owner can divide his patent-given rights, two are most important: by geographical territory and field of use. Although in disfavor with the Department of Justice, the territorial division is specifically sanctioned by statute and enables the patent owner to license his patent in the whole or any part of the United States.[10] It is common to refer to this form of division of the patent right as a territorial "restriction." Since semantics are sometimes important, it should be noted that the territorial division is not a restriction at all but only the grant of rights under the patent for a portion of its territorial scope. The word "restriction" implies an agreement with respect to the rest of the territorial scope, and *no such agreement can properly (or even logically) be implied from the territorial license.*

The license for use or for sale or resale in a specified field of use rests on precisely the same principle as the territorial license. It involves the grant of less than the patent owner's total right to exclude others from any and all uses of his patented invention. As will be noted further below, semantics have become important here.

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[10] 35 U.S.C. 261.

There is no assurance that an invention will be neatly proportioned in its applicable scope to the technical or marketing capabilities or interests of the patent owner, whether the owner be an individual, a small company or a large company. Company B illustrates a situation where exclusive field-of-use licenses can be the single, most effective way of exploiting an invention to the fullest for the benefit of the public as well as the patent owner. In fact, the situation is a classic example of the operation of the patent incentive to encourage investment in innovation, for here the parties making the investment (the licensees) are assured of basic patent protection before they start. They can therefore commit funds more generously and undertake a more comprehensive program of development than might otherwise be the case.

Those who oppose licenses to specific fields of use within the patent grant ignore the fact that such licenses, when translated into marketed products, often provide the public with alternatives that would not otherwise be available—at least until the patent has expired. If a patent owner distributes field-of-use licenses to various producers of different kinds of products, each licensee, in adapting the invention to his particular product line, introduces a new use of the original invention. On the other hand, if the patent owner limits utilization of the patent only to his line of merchandise, the public may not have the opportunity to enjoy the maximum potential of the patented invention. While the patent owner must retain the option to license or not to license, if he chooses to license he should not be absolutely foreclosed from licensing less than his full patent right.

The same principle works in the area of copyrights. A novel is usually published first in hard-cover book form. But prior to publication as a book, it may be serialized in a magazine. The magazine publisher receives an exclusive right only for that limited purpose. Thereafter, the book may be licensed separately for adaptation as a play for the living stage, or for motion pictures, television or other limited uses, including publication of a paperback edition. These licenses of less than the copyright owner's total right, like the field-of-use license, afford the public a variety of options and opportunities to enjoy the work in different formats.

It was pointed out earlier that the benefit to the patent owner from a licensing arrangement must be within or ancillary to the scope of the patent grant. Accordingly, license terms *solely* for the benefit of the licensee, such as giving him the right to restrict the patent owner in his practice of the invention[11] or to veto additional licensees,[12] may understandably encounter difficulties as outside the grant. But, obviously, a license is a two-party negotiated agreement and must offer prospective advantages for the licensee. Legitimate concerns of a licensee which the patent owner may properly consider in negotiating terms of the license include such as the following, all of which can best be served by a field-of-use license:[13]

A prospective licensee may want to commit himself under the license only for a particular product or technological area in which he has a problem, but prefer to avoid commitments in speculative areas where he is unable to make a satisfactory evaluation or has no interest.

The licensee may be able to obtain a lower royalty rate in a field where the patent owner is not using the patent, because in such fields the licensee would not be competing with the patent owner.

A licensee may prefer a sliding scale of royalty payments to ease the expense of his early period of marketing or to reduce the royalty burden as his volume increases. Where the licensee is practicing under more than one but not all the fields of the patent's use, the field-of-use license provides the necessary flexibility in the arrangement.

The licensee may be able to obtain a lower total royalty or lump-sum requirement for a paid-up license if the license is limited as to field.

If the license calls for periodic payment of a minimum royalty to keep the license in force, the licensee may prefer separate licenses for each field so he can cancel individual licenses where he is unable to meet the minimum without disturbing the licenses in his more successful fields.

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[11] *McCullough v. Kammerer Corp.*, 166 F. 2d 759 (9th Cir. 1948).
[12] *United States v. Krasnov*, 143 F.Supp. 184 (E.D. Pa. 1956), affirmed 355 U.S. 5 (1957).
[13] T. L. Bowes: *Forum Contributions*. Idea 12 :1129 (1968-9).

The licensee may prefer separate field licenses so he may later assign the licenses with the business of each field, whereas a single license would be indivisible.

It would seem undeniably within the scope of the patent grant for a patent owner who could rightfully exclude *all* others from practicing his invention for *any* purpose whatsoever to part with a portion of that exclusivity corresponding to a given field of use. It should be readily apparent that *the field-of-use provision, like the permissible territorial limitation, is really not restrictive.* While grant of a license for a particular field could be coupled with a restriction, the typical field license standing alone is nothing more than permission to make, use or sell in a defined segment of technology. It neither expressly nor impliedly authorizes or denies any right of the licensee with respect to any *other* technological area within the patent's scope. The licensee can operate in other fields of the invention on precisely the same basis and subject to the same consequences for infringement as anyone else, without regard for whether or not he is a licensee under some other field covered by the patent.

Here, semantics have become important. The Department of Justice sees no difference between a license containing a positive prohibition against sales in a particular field and a patent license limited to a particular field; it would condemn both as illegal divisions of markets.[14] It regards the fact that in most instances the licensee in fact does not stray into the unlicensed area as evidence of a tacit agreement to divide the market. Here the Department of Justice is reading the facts to prove what it wants to prove, in total disregard of business reality: the licensee usually stays within the licensed field because that is where his interests lie or because he simply doesn't wish to be sued for infringement. Indeed, the patent owner doesn't need his licensee's *agreement* not to infringe. The patent itself is sufficient.

Implicit in the position of the Department of Justice is the necessary presumption that the licensee, absent his license to the limited field, would promptly infringe outside that field. By renting a farmer's oxen, the Department is saying, one by implication agrees not to covet the farmer's wife! Maybe so. But by licensing a field of use, *the licensee makes no promises with respect to other fields within the patent's scope.*

There is a paradox in the Department's position. While it urges that field-of-use patent licenses are just as illegal as efforts at market division where no patents are involved, it would sanction such licenses where the patent owner was *reserving to himself* a portion of the total field covered by the patent.[5] It would seem that if the licensee is *impliedly* agreeing to stay out part of the patent's field in one case, he is doing so in the other. So if business justification exists in one case, the justifying facts should at least be considered in the other.

Moreover, an agreement to divide markets between competitors constitutes a *per se* violation of Section 1 of the Sherman Act.[15] If field-of-use licenses are equated to division of market agreements then they, too, must be *per se* antitrust violations. On what basis, then, can the Department of Justice find some field-of-use licenses justifiable and others not?

Before this broader attack on field-of-use licensing, the primary objection of the Department of Justice in this area seemed to be the field-of-use license in which the field was divided among licensees who would otherwise compete.[5] Such an objection implies the mechanical application of valid antitrust principles but without considering the rationale and justification for the practice in the patent context. A field-of-use licensing program can be well within the scope of the patent grant and should yield to antitrust only if coupled with anticompetitive acts that remove it beyond that scope and into the province of antitrust.

So, too, is a licensing program limiting resale of patented products purchased from the licensor to specified fields or to specified classes of customers. The argument has been made that such practices are analogous to controlling resale *prices* of patented products. On the theory that the first sale of a patented product removes it from the scope of the patent grant, the control of re-

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[14] Bruce B. Wilson, Special Assistant to the Assistant Attorney General, *Patents and Antitrust: The Legitimate Bounds of the Lawful Monopoly.* Address before The Patent Law Association of Pittsburgh, November 19, 1969.

[15] *White Motor Co. v. United States,* 372 U.S. 253 (1963).

sale prices is considered a misuse of the patent.[16] The critical distinction, however, is that *the patent extends to all uses of the patented product*, and hence the analogy to price control is inapposite. Indeed, the patent owner's control over use of his patented product, to the extent he chooses to exercise it, is part of the essence of his right. And no valid reason appears why this right should not follow the product in its first sale by his licensee, assuming notice to the purchaser. The patent right has not yet been exhausted.

The Department of Justice is clearly committed to the destructive extension of antitrust principles in this aspect of patent licensing. On the other hand, President Johnson's White House Task Force on Antitrust Policy, in a report released and commented on favorably by Assistant Attorney General McLaren,[8] recommended that patent owners be denied the right to grant exclusive licenses *except as to specific fields of use.*[9] The patent owner would be required to apply to the Federal Trade Commission for certification that such a license was necessary to the commercial utilization of the invention.

The courts have been more solicitous. In 1938 the Supreme Court expressly sanctioned the field-of-use concept in the *General Talking Pictures* case.[17] Since then, license to *use* in a specified field or to *sell* to customers for use only in specified fields has been widely upheld.[16] Adverse decisions have, of course, resulted where the field-of-use provision was coupled with means which in total import violated antitrust principles.[18,19]

The example of Company B shows the type of problem facing the corporate patent owner. But the situation of the private inventor, research company or university can readily be envisioned as even more difficult, for they must often rely exclusively on licensing to bring their inventions into public use. They must literally sell out to a large company capable of exploiting all the major fields of use of the invention, or in shaping a licensing program run the considerable risk of exposing their patents to the vagaries of court decisions or the pressures of the Department of Justice.

The President's Commission on the Patent System, appointed by President Johnson, singled out such licenses as a particular object of concern. Recommendation XXII of the Commission states:[20]

"The licensable nature of the rights granted by a patent should be clarified by specifically stating in the patent statute that: (1) applications for patents, patents, or any interest therein may be licensed *in the whole or in any specified part, of the field of use* to which the subject matter of the claims of the patent are directly applicable . . ." (Emphasis added.)

This Recommendation has not been included in patent bills submitted by the Administration or by Senator McClellan, apparently because of opposition from the Justice Department.[21]

The patent statute now permits the licensing of a patent or patent application in "the whole or any specified part of the United States." It is submitted that the statute should provide also for the licensing of the patent or patent application for the whole or any specified *use* to which the invention can be applied. It seems clear, as the President's Commission recognized, that the detriment to the public from categorically forbidding either the territorially-limited or field-of-use license far outweighs any risks in sanctioning these established practices.

2. The Right to License (or Not to License)

Company C owns a patent and manufactures and sells products covered by its patent. The company is of modest size and through its relatively small sales organization is unable to reach all the geographical areas in which its product would find a market. From among its dozen competitors it selects four

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16 Raymond C. Nordhaus and Edward F. Jurow: *Patent-Antitrust Law*, at 265, Jural Publishing Co. (1961, Supp. 1968); *The Ansul Co. et al. v. Uniroyal, Inc.*, 163 U.S.P.Q. 517 (N.D. N.Y. 1969).

17 *General Talking Pictures Corp. v. Western Electric Co.*, 305 U.S. 124 (1938).

18 H. Thomas Austern: *Fish Traps, Indians, and Patents: The Antitrust Validity of Patent License Restrictions on Sole Price, Field of Use, Quantity, and Territory*. U. of Pittsburgh Law Rev. 28:181, 188 (1966).

19 J. G. Jackson and E. L. Jackson: *Use Limitations in Patent Licenses*. Idea 12:657 (1968-9).

20 *Report of the President's Commission on the Patent System*, U. S. Government Printing Office (1966).

21 Senator McClellan's statement accompanying introduction of S. 2756. Congressional Record, August 1, 1969, page S. 8952.

whose marketing ability and reach will supplement its own and give adequate coverage of the neglected areas. These companies are anxious to add the product to their lines because they see opportunities, through sales and advertising efforts, for profitable expansion. Similarly, Company C, by licensing these four companies, seeks a return by way of royalties from sales it could not make itself. Although competitors not favored with a license have requested one, Company C had declined because further licensing would so dilute the market as to make it unprofitable for any of the licensees as well as for Company C. The Department of Justice hears from a rejected competitor and presses Company C to license it. The company complies but wishes now it had refused to license anyone.

It would seem unnecessary at this stage of our nation's commercial development to raise the question of the patent owner's right to license or not to license. However, the Department of Justice has in fact exerted pressure on patent owners to grant additional licenses. Moreover, a recommendation of the White House Task Force on Antitrust Policy would require a patent owner granting one license under his patent to grant *all* financially qualified and reputable applicants a license under terms "neither more restrictive nor less favorable" than the first license.[9]

The Task Force engages in an inconsistent dichotomy. It acknowledges that a patent confers on the patentee "the right to exclude others from the field covered by the patent" and declares allegiance to the antitrust "goal" of preventing use of a patent beyond its scope. But then it concludes:[22]

"That goal will be served by denying the patentee the right to confine use of the patent to a preferred group and requiring that *if the patent is licensed it shall be open to competition in its application.*" (Emphasis added.)

If the patent statute gives the right to exclude, it is clearly within the scope of the grant to deny licenses altogether or, equally, to deny additional licenses after the first. But the Task Force would automatically cancel the remaining right of the patent owner not to license solely for the reason that he did license once before. *The Task Force at once acknowledges the proper limitation of antitrust sanctions to matters beyond the patent's grant and the determination to penetrate the grant in the name of antitrust.*

It is revealing that one dissenting member from the Task Force's Report was of the opinion that they had "given too little attention to the patent field" to embark on such recommendations.[23] These, indeed, appear to be accurate observations.[24]

Further evidence of the uncertainty facing the licensing patent owner is a recent court decision. The patent owner had already licensed his patent and put his invention into public use, but the court had this to say in *dictum* about his refusal to grant the defendant a license:[6]

"An owner of a patent cannot assert his rights under the law and Constitution if such owner refuses to make use of a patent, or to license a patent so that it may be of use to the public, *or refuses to license an applicant when it has already granted a license to the applicant's competitor.*" (Emphasis added.)

It is of interest to compare the language with that of a decision of the *same court* (different judge) rendered four months earlier:[25]

"Plaintiff has no duty to grant a license to defendant under the patent in suit, merely because defendant has requested such a license. *A patent owner has the right to grant a license to some, as he chooses, without granting a license to others.*" (Emphasis added.)

The selection of licensees is an important undertaking. As indicated earlier, activities reflecting discredit on the invention, such as a poorly conceived sales approach or inadequate servicing of the product after sale, can in fact harm the rights remaining with the patent owner. The Task Force would meet the problem by requiring compulsory licensing only of parties who are financially responsible and of good reputation. Obviously, this is not enough. It must remain the right of the patent owner to select his partners by criteria in addition to solvency and reputation.

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[22] *Supra* Note 9 at 4.
[23] *Supra* Note 9 at 26.
[24] *Supra* Note 9 at 27.
[25] *Bela Seating Co., Inc. v. Poloron Products, Inc.,* 160 U.S.P.Q. 646 (N.D. Ill. 1968).

When the patent owner negotiates a license, he is committing himself for the life of the license, which typically is for the life of the patent. With the shifting and unpredictable positions of the courts and the continuing threats from the Department of Justice, it is becoming increasingly difficult to plot a reasonable and yet "legal" course in licensing (or not licensing) patents. Legislative intervention to clarify the right to license or not to license is surely in order.

3. The Freely Negotiated Royalty

Patent owner D licensed sixteen companies who were eager to practice the technology of the patent. Royalty and other terms were essentially the same for each licensee, following hard negotiations for the first license. One company declined to accept a license because it regarded the royalty as too high. Several years later it began producing and selling the patented product, and D promptly sued for infringement. The infringer's defense was that D should not be permitted to enforce his patent because the royalty it charged licensees was so exorbitant and oppressive as to violate the antitrust laws. The court agreed, and an extensive and successful licensing program was placed in jeopardy.

That a court would intervene in the business judgments of parties who freely negotiated a given royalty in a licensing arrangement would seem to stretch the imagination. But the above situation is taken from real life. The Court of Appeals for the Seventh Circuit did in fact hold in 1966 that a royalty found to be "exorbitant and oppressive" could be a *per se* violation of the antitrust laws on the theory that prices could effectively be fixed by requiring such a royalty.[26] On remand for determination of whether the royalty here was in fact "exorbitant and oppressive," the District Court concluded it was not.[27] But the proposition stands as precedent, at least in the Seventh Circuit.

Prior to the foregoing decisions the Supreme Court had spoken unequivocally on the right of the patent owner to negotiate any royalty acceptable to a licensee. In 1926 the Court said: [28]

"Conveying less than title to the patent or part of it, the patentee may grant a license to make, use and vend articles under the specifications of his patent for any royalty. . ."

Again, in 1964 the Supreme Court reaffirmed this position: [29]

"A patent empowers the owner to exact royalties as high as he can negotiate with the leverage of the patent monopoly."

A thoroughly reasoned decision in the Ninth Circuit in 1957 reached the same conclusion, stoutly defending the right of a patent owner to set his royalty (while holding against him for patent misuse on other grounds): [30]

"To say that the mere amount of money due and payable for the grant of a license is subject to judicial review would render each and every agreement made subject to court approval."

Where royalty is excessive the problem is usually self-adjusting. It means simply that the parties did not comprehend the nature of the market or underestimated the competition. Once the agreement is signed, both parties want the product sold. If excessive royalty forces the selling price to uncompetitive levels, it would be a rare and shortsighted patent owner who would not be willing to reduce the royalty in exchange for larger sales volume and, ultimately, greater royalty income.

A royalty freely agreed to by the parties in what they initially conceive to be their mutual interests should be left to the parties for further negotiation if their mutual interests are no longer being served. The threat of judicial reformation of royalty provisions or, worse, of judicial determination that a royalty established by mutual agreement is *ex post facto* an antitrust violation should be laid to rest by statute.

4. Royalty Differential Between Non-Exclusive Licensees

Company E produces a patented chemical and sells in bulk to industrial users for reprocessing into other products and in finished form to individual

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[26] *American Photocopy Equipment Co. v. Rovico, Inc.,* 148 U.S.P.Q. 631 (7th Cir. 1966).
[27] *American Photocopy Equipment Co. v. Rovico, Inc.,* 257 F.Supp. 192 (N.D. Ill. 1966); affirmed, 384 F. 2d 813 (7th Cir. 1967).
[28] *United States v. General Electric Co.,* 272 U.S. 476, 489 (1926).
[29] *Brulotte V. Thys Co.,* 379 U.S. 29 (1964); 143 U.S.P.Q. 264, 266 (1964).
[30] *Stearns et al. v. Tinker and Rasor et al.,* 116 U.S.P.Q. 222, 235 (9th Cir. 1957).

customers for their use. Royalty is set in each market to account for the high volume purchases of the industrial user and low volume purchases of the individual customers, both in keeping with competition in each field.

As in the above situation and the earlier examples of Company A and Company B, business realities often demand different royalty rates among licensees under the same patent.

Despite many court decisions clearly holding the patent owner entitled to any royalty or financial arrangement he can negotiate (on the theory that he does not have to license anyone), where two or more licensees paying different royalties under the same patent enter the picture the patent owner's position is less certain. A judicial trend may or may not be indicated in the most recent decisions close to the point, but varying leasing rates for the same patented machines have been held to violate Section 2 of the Sherman Act, Section 5 of the Federal Trade Commission Act, and to be a patent misuse.[8] In those cases different rentals (royalties) were held to be anticompetitive in effect, even though allegedly based on the proportion of labor saved by use of the patented machines.

Moreover, a principal recommendation of President Johnson's White House Task Force on Antitrust Policy would require all subsequent licenses to be on terms "neither more restrictive nor less favorable" than the first license.[9] Mr. McLaren has alluded to this recommendation in public addresses but says he is "not at this time" taking a position of approval or disapproval.[5] A more recent statement by a Department of Justice representative, however, approves different royalty rates for different uses if the patent owner freely licenses all uses.[14]

Despite the compelling business justifications for such arrangements, patent owners are understandably concerned over the uncertainty of differential royalties. This, too, needs legislative clarification.

5. The Royalty Base

Oil well drilling Company F licenses a patent on a method for treating the formation to increase oil production. The method involves use of chemicals already employed in the drilling process for other purposes. It is not feasible for the company to install special equipment to monitor use of the old chemicals for the new purpose. The parties agree that royalty will be determined on the basis of average improvement in oil production each month over a predetermined level.

Ideally, royalty under a patent is based on the number of patented products produced or sold. But frequently the patent covers a process or a part of a machine or composition instead of the final product. In such event the royalty to which the patent owner is entitled may be based on some unpatented, measurable parameter.

In complex situations, however, such as that facing the Company F, a less responsive or even non-responsive basis is appropriate. For example, in the manufacture of television and radio sets involving many patents, royalty based on total sales has been upheld.[31] The rationale advanced by the Supreme Court is the convenience of the parties and the absence of coercion by the patent owner. Other decisions where royalty is paid regardless of whether all of a large number of patents ar used rest on the premise that the licensee is paying for the privilege to use them.[32,33]

While decisions raising the issue are usually reasonable on the facts, litigation on the point has in every case put the party defending the practice to great pains and expense. A simple legislative affirmance of the right to base royalty, fee or purchase price for a patented invention on any mutually agreeable parameter, absent coercion by the patent owner, would alleviate one troublesome aspect of patent litigation.

6. Royalty for the Package License

Municipality G operates a sewage treatment plant. Different conditions of temperature, solids content and other properties of the sewage require different treatments to achieve separation of the solids. The municipality takes a li-

[31] *Zenith Radio Corp. v. Hazeltine Research, Inc.*, 89 S. Ct. 1562 (1969) ; 161 U.S.P.Q. 577.
[32] *Supra* Note 16 at 183.
[33] *Automatic Radio Mfg. Co. v. Hazeltine Research, Inc.*, 339 U.S. 827 (1950).

cense under a group of patents which together offer advantages in treating the municipality's sewage under most of the conditions encountered. Some conditions require practice of one combination of patents, other conditions require another combination. Since all the patents relate to a single ultimate purpose, namely, the treatment of sewage, and since it was not possible to separate the patents as to importance, the license agreement calls for payment of royalties until the last-to-expire of the licensed patents.

There are two central aspects to the licensing of a group or "package" of patents of special interest here. The first is the legality of the package license; the second is the validity of an agreement that states a single royalty for use of any one or more of the licensed patents, such royalty to continue so long as any of the licensed patents are alive.

The owner of a valuable patent is theoretically in a position to coerce a potential licensee into accepting a license under other patents of lesser or no value. It has been held that a party who *seeks* or *voluntarily* accepts a package license does not thereby impose antitrust or patent misuse liability on the patent owner.[31, 33] But where the *patent owner* insists that the license include more patents than the licensee wants, and the patents cover more than a single product, the courts have held the package to constitute an illegal tying arrangement.[34] Where a single product is involved, a mandatory package may be permissible,[35] although ultimately this question will depend on whether tying arrangements are held to be *per se* violations of the antitrust laws or subject to a rule of reason.[36] Fairly clear and objective criteria have thus been spelled out for determining the legality of a package license.

But the second aspect of package licensing is more troublesome. Given the judicial approval for *voluntary* package licensing and the business realities leading to the practice, it would follow that a royalty established during negotiations contemplates the value of the *total package* and carries no implication of the value of the individual patents. In fact, particularly in a situation like that of Municipality G exemplified above, it is manifestly impossible to assign such values. Moreover, in many cases, the patents cover alternate ways of doing the same thing, or features that are mutually exclusive and cannot be used together in a single product.

The problem of royalties does not become acute until some of the patents in the package begin to expire. At that time, assuming the licensee is still practicing under one or more of the patents in the original package, should the royalty be reduced as each patent expires? If so, by how much? If not, is the licensor guilty of extending the monopoly of the expired patents?

The division of the inventions between the various licensed patents,where all relate to the same product or product line or process, is often for the administrative convenience of the Patent Office. And the initial royalty and license are based on the totality of the subject matter to which the licensee desired access. It would therefore seem reasonable in such instances to permit royalty payments to continue so long as any patent in the original package that is being used remains unexpired.

The courts are in conflict. In the Tenth Circuit the practice of permitting royalties to continue has been approved,[37] as it was earlier by the Supreme Court.[33] But in the Third and Sixth Circuits the same practice has been held a patent misuse.[34,38]

The pragmatic effect of the diversity of opinions in the courts leaves the patent owner defenseless against the prospective licensee who negotiates a royalty for a group of patents when he really wants access to only one. After negotiating for the package, he then asks for a license under a single patent and insists on a *pro rata* reduction in royalty under pain of a charge of misuse or illegal tying.

If the parties are unable or disinclined to agree to a royalty breakdown at the inception of the license, absent a package based on coercion, and if at least

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[34] *American Security Co. v. Shatterproof Glass Corp.*, 268 F. 2d 769 (3rd Cir. 1959), *cert. denied*, 361 U.S. 902.

[35] *International Mfg. Co. v. Landon, Inc.*, 336 F. 2d 723 (9th Cir. 1964).

[36] *Northern Pacific Railroad Co., v. United States*, 356 U.S. 1 (1958).

[37] *Well Surveys, Inc. v. Perfo-Log, Inc.*, 396 F. 2d 15 (10th Cir. 1968), *cert. denied*, 393 U.S. 951; *McCullough Tool Co., v. Well Surveys, Inc.*, 343 F. 2d 381 (10th Cir. 1965), *cert. denied*, 383 U.S. 933.

[38] *Rocform Corp. v. Acitelli-Standard Concrete Wall, Inc.*, 367 F. 2d 678 (6th Cir. 1966).

one significant patent is still alive and being practiced, the full royalty should continue as agreed upon. Needless and expensive litigation could be avoided by statutory acknowledgement of this practical resolution of the problem.

7. Royalty Payment After Expiration of Patent

Patent owner H licenses a small, capable company under an important patent. It was anticipated at the negotiations that fairly substantial sums would have to be invested by the licensee to develop the product for market. Accordingly, no initial payment was required by H, but royalties were set at a compensating level. The product was duly developed and marketed, with success. However, unforeseen events caused a financial crisis in the company, and it was unable to maintain its royalty commitments. H agreed to accept payment of *back* royalties over a period of years, which extended beyond expiration of the patent. All royalties were based solely on activities under the patent before it expired.

A 1964 Supreme Court decision in *Brulotte v. Thys Co.* held that a license requiring payment of royalties after expiration of the last-to-expire of a group of licensed patents was an attempt at projecting the patent monopoly and hence a misuse.[29] Uneasiness with the arrangement exemplified above stems from the allegation in Brulotte that payments were simply being spread over an extended period. The Court, however, found "intrinsic evidence" that post-expiration payments were for post-expiration activities. There can be little dispute that the court reached the proper conclusion on its interpretation of the facts.

A patent owner should be free to negotiate the best royalty terms he can get, so long as the royalties are tied to activities taking place *during the life of the patent.* If the licensee under the patent is unable to carry the royalty burden, payments based on use of the patent during its life should be permitted to extend over whatever period the parties agree is tolerable, even though the payments continue after the patent expires.

While the Supreme Court did not expressly rule out installment payment of royalty, the Brulotte case has been interpreted by some to mean that any payment of royalties beyond the patent's expiration would be a misuse. Whether through inadvertence or by design, the Court has left doubt in the minds of many as to the legality of post-expiration installment payments. This question could be settled by legislative approval of post-expiration payment of royalties accrued during the life of the licensed patents.

RESOLUTION OF THE PATENT-ANTITRUST "CONFLICT"

Reference was earlier made to the dual nature of the innovation the patent system is intended to provide. The elements of innovation were seen to be (1) the incentive to invent (or invest in invention), and (2) the ability to market. This duality rests on the premise that a patent has done less than its job if it is not put to work—either by the patent owner or his licensee.

Too often the apparent conflict between the patent and antitrust concepts is resolved by examining whether striking down the patent owner's licensing arrangements would impair the operation of the incentive to *invent.* Professor Donald F. Turner, former Assistant Attorney General, has made precisely this point when he contends that "antitrust does not retard technological progress."[39] As a result, the impact of antitrust on the patent system is only measured by its impact on *one* of the two essential ingredients of innovation.

Certainly there could be an extreme reached in antitrust enforcement where the incentive to *invent* would be clearly affected. But before that point, the innovation fostered by the patent system could be severely impaired through unduly limiting the right of the patent owner to secure the ability to market his invention by licensing his patent.

The need for legislative rapproachement between patents and antitrust was advanced in 1966 by President Johnson's Commission on the Patent System. In its report, an integrated analysis of the entire patent statute was presented and recommendations made for change.[20] Despite its primary mission to examine the state of the patent laws, the Commission saw the problems facing the

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[39] Donald F. Turner: *Patents, Antitrust and Innovation.* Univ. of Pittsburgh Law Rev. 28:151 (1966). See also Gerald Kadish: *Patents and Antitrust: Guides and Caveats.* Idea 13:83 (1969).

patent owner in a menacing antitrust climate and presented the following as its Recommendation XXII:

"The licensable nature of the rights granted by a patent should be clarified by specifically stating in the patent statute that: (1) applications for patents, patents, or any interests therein may be licensed *in the whole, or in any specified part of the field of use* to which the subject matter of the claims of the patent are directly applicable, and (2) a patent owner shall not be deemed guilty of patent misuse merely because he agreed to a contractual provision or imposed a condition on a licensee, which has (a) *a direct relation* to the disclosure and claims of the patent, and (b) the performance of which is *reasonable under the circumstances* to secure to the patent owner the full benefit of his invention and patent grant. This recommendation is intended to make clear that the *'rule of reason'* shall constitute the guideline for determining patent misuse" (Emphasis added.)

It must be noted, however, that this well-reasoned approach by the President's Commission, while conceptually sound, is not without difficulty. It was earlier pointed out that patents, by statute, have the "attributes of personal property." As such, the terms of disposition of patent property, where the terms are in and of themselves legal, should at least carry a *presumption* of reasonableness. But a "rule of reason" would place the patent owner at the procedural disadvantage of first having to *prove* the reasonableness of his license provisions if they were ever challenged. The concept of reasonableness would more fairly be embodied in a *"rule of presumptive reasonableness,"* under which the burden of proving unreasonableness would fall where it belongs—on the party asserting it.

Nevertheless, the Commission demonstrated an underlying appreciation of the patent owner's plight. This is further evident from another observation in the Commission's report. After noting that it did not favor weakening enforcement of the antitrust laws, it noted:

"However, uncertainty exists as to the precise nature of the patent right and there is no clear definition of the patent misuse rule. *This has produced confusion in the public mind and a reluctance by patent owners and others to enter into contracts or other arrangements pertaining to patents or related licenses.*" (Emphasis added.)

* * * * * * *

Whether patents will remain a healthy force for progress or become a vestigial appendage depends in large measure on what patent owners are entitled to do with them. This Memorandum does not contend for the legitimation by statute of practices heretofore generally condemned under antitrust. It does, however, urge resistance to the insistent efforts of the Department of Justice and a tendency in some courts to extend the interdiction of antitrust to practices clearly within the patent grant.

Patents, and matters involving patents, have no constant advocate as does antitrust. The Antitrust Division of the Department of Justice is heard in the courts, where it initiated litigation or submits briefs, and in business, to which it announces areas of patent licensing that will be the subject of future challenge.

In the absence of a counter-force on behalf of the patent system, the recourse of those determined to preserve the patent incentive in its total concept, so inextricably bound to the right to license, is to seek legislation upholding the practices that need support against the unbridled club and clout of antitrust.

SUMMARY

Encouraging innovation is the principal objective of the patent system. Patents do this, *first*, by encouraging invention, or the investment in inventive efforts. Thus, patents provide a lead time for the patent owner against competitors who would copy the invention and enjoy a free ride on the research and development investment. *Second*, patents facilitate the marketing of inventions. Often the useful dimensions of an invention exceed the interests or capabilities of the patent owner to develop, produce or market it. The patent owner must then be able to use his patent to secure what he lacks in the means to market.

The patent is a form of monopoly, albeit a temporary and specially-created one, and therefore is an automatic anathema to some antitrust theorists. Nevertheless, the patent "monopoly" brings a form of innovative competition that no antitrust law can provide. This is, in effect, competition in *value*, as distinguished from price (although the patented product must still compete in price with its available alternatives).

The patent owner is entitled to keep all others from practicing his invention. Or he can sell the patent or license others to use it. A licensing arrangement must hold prospects of profit for both parties and, accordingly, must be adapted to an existing business situation. However, the patent owner is entitled to attach only those terms to his license that are reasonably related to the scope of his patent grant. Otherwise, his patent can be held unenforceable as a patent misuse; or the patent owner can be held in violation of the antitrust laws, subjecting him to severe penalties—including a prison sentence, heavy fines, and treble damages to those his acts have injured. *The need is therefore apparent for reasonable certainty in the laws relating to patent licensing if patents are to be used effectively in bringing new products and processes into maximum use and fostering innovative competition.*

In several important respects, the applicable law is so unsettled as to hamper legitimate licensing activities. This arises from diversities in holdings of our courts. Equally disturbing for the future is the unrealistic attitude of the Department of Justice, due in part to a lack of appreciation of the practical problems of licensing and operating under licenses. Representatives of the Antitrust Division with increasing frequency are threatening actions against patent owners who engage in licensing practices well within the scope of their patent grant and for a proper purpose but which the Division considers opposed in theory to a concept of antitrust.

Patents, by statute, have the "attributes of personal property." The owner of personal property other than patents enjoys, among the attributes of ownership, the right to dispose of all or part of his property whenever, wherever and to whomever he chooses. And in disposing of it he is not called on to prove that what he is doing is legal or even reasonable. The patent owner, in disposing of his patent property, should enjoy the same presumption of legality and reasonableness concerning his transactions.

There is need for legislative clarification in several specific areas of patent licensing. These include:

1. Field-of-Use Licensing

A patent owner is entitled to all uses of his invention. Some uses, such as those beyond his ability or interest to develop and market, he may choose to license to others. Such a license is not restrictive but merely conveys less than the total right belonging to the patent owner. However, the Department of Justice insists that such a license is restrictive, and there is increasing danger that our courts, which heretofore have upheld such practices, will fall victim to this pressure. The President's Commission on the Patent System, appointed by President Johnson, concluded that the field-of-use license, like the license for a particular territory (which is specifically sanctioned by present statute), should receive statutory approval.

2. The Right to License (or Not to License)

Strange as it seems, the right of a patent owner to license parties of his choice has been challenged. A White House Task Force on Antitrust Policy has urged that if a patent owner licenses his patent at all he must license all comers who are financially responsible and of good reputation. At least one court decision has spoken similarly. While the use of patents beyond their proper scope is clearly wrong, and the interdiction of antitrust or the defense of patent misuse becomes appropriate, the insistence that the patent owner must license all qualified parties if he licenses anyone is clearly an unwarranted extension of antitrust philosophy. The lack of appreciation for the facts of business life is endangering the important prerogative of the patent owner to select his licensees.

3. The Freely Negotiated Royalty

A federal court has held that a royalty, acceptable to some sixteen other licensees, was excessive and a *per se* violation of the antitrust laws. While the Supreme Court has repeatedly held that a patent owner is entitled to whatever royalties the parties negotiate, there is now judicial support for questioning the royalty terms of any license. This intervention by a court to determine *ex post facto* that a royalty does not suit the court's idea of reasonableness and amounts to price fixing is more than unwarranted. Moreover, in most instances an arrangement that later proves an undue burden on the licensee will be adjusted for the good business reason that it impairs the sale of the product and the generation of royalties for the patent owner.

4. Royalty Differential Between Non-Exclusive Licensees

A series of court decisions in related cases have held different charges to different licensees to be a *per se* antitrust violation. These decisions may or may not portend a judicial trend against the freedom of the patent owner to charge different royalties to different licensees. This judicial uncertainty is compounded by the report of the aforementioned White House Task Force on Antitrust Policy, on which the Department of Justice has commented with apparent favor. The Task Force would have each license under a patent to be on terms "neither more restrictive nor less favorable" than every other license—even though the licenses be for different products or purposes, and even though the benefits of the license may vary widely among several licensees.

5. The Royalty Base

The complexities in the practice of some product and process patents sometimes make it difficult or impossible to measure the use of the patent for determining royalties. On such occasions the parties agree on some conveniently determinable parameter as a measure of use. It would seem inappropriate for the courts to interfere with such arrangements, and in fact decisions have been generally reasonable. Nevertheless, there is uncertainty which a clear legislative provision would alleviate.

6. Royalty for the Package License

Where a prospective licensee wants to do something that in its totality is covered by a group of patents, some of which may not be used all the time or which may be alternatives to others, the entire group of patents may be licensed. If the patent owner does not coerce his licensee into accepting and paying for unwanted patents, antitrust problems are usually avoided. But in establishing a royalty he may encounter problems. Usually, no breakdown of royalty is made for individual patents because the extent of their use cannot be predicted when the license is negotiated. But when the patents begin expiring the right of the patent owner to continue to receive the full royalty is sometimes questioned. The reduction in value of the remaining patents as each patent expires would in most instances be impossible to determine fairly. If the original agreement contemplating the continuance of royalties until the last significant patent has expired was reached in arms-length bargaining without coercion, it should remain in force as the parties intended.

7. Royalty Payment After Expiration of Patent

A single Supreme Court decision has raised doubts in the minds of some as to the validity of a license calling for payment of royalties after expiration of the patent but for activities carried out while the patent was alive. Installment payment of royalty is usually a concession to the licensee and should not be a source of loss or litigation to the patent owner.

The President's Commission on the Patent System observed the patent owner's plight in the matter of permissible patent license provisions:

> However, uncertainty exists as to the precise nature of the patent right and there is no clear definition of the patent misuse rule. This has produced confusion in the public mind and a reluctance by patent owners and others to enter into contracts or other arrangements pertaining to patents or related licenses.

This, indeed, is true.

The Department of Justice is becoming increasingly active in critical surveillance of patent licensing. While the Department favors a case-by-case development of the law (with the Department initiating or participating in litigation to its own end), such development would inevitably be expensive—both for the patent owner and the public. Moreover, the resulting law could well be misdirected, because it would have its origins in aggravated and unrepresentative fact situations.

The interests of patent owners and the public call for legislative clarification of some of the major problems now in such an uncertain state. Especially, these interests need safeguards against case law making *per se* antitrust violations of some of the practices so important to innovation through patents.

March, 1970.

HOUSTON, TEX., *May 28, 1971.*

Re Scott amendments.

Mr. CRAWFORD C. MARTIN,
Attorney General of Texas,
Austin, Tex.

DEAR CRAWFORD: I have been a participant in the background and history leading to the Scott amendments and as such have followed the recent hearings and correspondence with respect to the Scott amendments. I have had occasion to see your letter of May 3 addressed to The Honorable Philip A. Hart in which you urge him to oppose the Scott amendments.

I find that your attack upon the Scott amendments does not track with the precision that I feel necessary for any value judgment at this interface between patent and antitrust law, the provisions of the Scott amendments and their effects upon the cases which you cite. This conclusion of mine is of course without very much information about the nature of the State of Texas anti-trust actions, but I am familiar with the *Tetracycline* litigation throughout the nation and its history, and I am also familiar with a number of other efforts at antitrust litigation in the patent area. In fact I and my firm have ourselves made some new antitrust law at the patent antitrust interface.

Contrary to the implications of your letter, I am not aware of a single area in which the Scott amendments legitimize patent licensing practices which are not lawful as a matter of the present judicial recitations of the law.

To be sure there are a couple of oft-speaking Department of Justice Antitrust Division lawyers who say Scott's licensing practices are not the law, but the clear weight of present judicial authority supports Scott's licensing practices.

To be sure, the Scott amendment to Section 301 of the Patent Law Revision Bill, goes along with the theme of Senator McClellan's Section 301, reversing the concept of patent law preemption of otherwise unfair competition. This is not directly related to patent licensing. Another feature of the Scott amendments reverses a part of *Lear v. Adkins*, in that it requires a patent assignor to give up the fruits of his assignment before he can attack the validity of the patent that he assigned; and requires a patent licensee to give up the benefits of his license before he can attack the patent under which he enjoys a license. But those provisions in the Scott amendments apparently were not the subject of your letter and I am not addressing myself to those provisions now.

I say again, the Scott amendments seek to render the law on licensing practices more certain (not less certain as your letter recites) and to hold the present state of the law rather than reverse the present state of the law as your letter suggests. I would welcome your directing my attention to any licensing practice not presently lawful that you feel is permitted by the Scott amendments. I will show you authority to the effect that it is lawful.

Further, I do not see how the Scott amendments on lawful licensing practices will work to the detriment of any legitimate State of Texas cause of action.

If we accept as a basic premise, the patent law concept that he who brings something new and nonobvious to society shall be privileged to prevent others from manufacturing, using or selling that same new item for a period of 17 years, then the licensing restraints which the Scott amendments permit—and which the present law now permits—can not add any new detriment to the State of Texas that is not inherent in the basic concept of the patent law. For the licensing contributes to competition rather than reducing competition.

This of course does not suggest anything about the *Tetracycline* situation. If you accept as the basic premise that the *Tetracycline* patents were obtained by fraud on the Patent Office, then any effort to enforce those patents including any licensing effort must of course be viewed as an antitrust violation and the Scott amendments of course do not offer any protection to that activity.

The present state of the antitrust law is such that patent owners quite commonly can not license their patents at all, because to do so is to run the risk of treble damages liabilities in an area where the law is so uncertain that they do not know in what circumstance their license lasting 17 years will remain lawful for 17 years. *This* is a strongly anticompetitive situation—that patent owners are afraid to license *at all*, because to do so is to incur risk of the onerous penalties of antitrust before the license term expires.

The Scott amendments are inevitably not precise in every detail; but they are much more certain than the present state of the law in telling patent owners what they can feel safe in doing in granting 17 year licenses, and in encouraging them to grant licenses rather than hold onto the total patent right to preclude others in order to avoid risk of antitrust exposure.

I think it would be a most unfortunate thing if broad-brush reaction to the Scott amendments, out of the history of such as the *Tetracycline* case to which the Scott amendments do not really apply, should result in the loss of the Scott amendments and in a further increase in anti-competitive results because so much of industry is now scared to death to grant any license whatsoever.

Furthermore, the patent system is now so sterilized that I find myself on not infrequent occasion advising clients not only against licensing, but against investing in development of new products and the market therefor, because in so many areas there is no longer any economic return on that investment. This inevitably means a loss of competition *in research and development*, a loss of competition in the conception and production of *new* products such as tetracycline once was.

Focusing attention of the law so much on the competition with respect to *already existing* products, that we destroy the competition in producing new products like tetracycline, is clearly as mischievous as permitting undue and unwarranted restraint of trade in already existing products as by a fraudulently obtained patent or by unwarranted tying-clause licensing, etc.

I have found it necessary to dictate hastily, and this inevitably results in a rambling dissertation. I would appreciate your response to this letter, particularly I would appreciate your pointing out specifically what Scott amendment you find inhibits a proper claim of the State of Texas in protection of its people. I think I can convince you that there is no provision in the Scott amendments that burdens any proper claim of the State of Texas in protection of its people.

If your review of the issue should satisfy you that your letter to Senator Hart was excessively damning to the Scott Amendments beyond what is real, then of course a corrective letter would be consistent with good public service.

Yours truly,

TOM ARNOLD.

HALFPENNY, HAHN & ROCHE,
Chicago, Ill., May 6, 1971.

SENATOR JOHN L. MCCLELLAN,
Senate Office Building,
Washington, D.C.

DEAR SENATOR: I have been requested by the officers and directors of the Automotive Service Industry Association, a national association of manufacturers, remanufacturers, warehouse distributors, wholesalers of automotive replacement parts and accessories, located throughout the United States, to express the industry's interest in S. 643.

Our members make substantial investment in plants, equipment and research to develop constant improvements on the component parts that we manufacture and sell for not only replacement but for original equipment manufacturers.

We think that the Congress of the United States should set the policy preserving the present incentives which attract people and companies to participate in solving the technological and social problems of our society. In regard to the matter of mandatory patent licensing for improving the quality of the environment, (the issues raised by Section 6 of your bill S. 643), we advised a number of Senatores in regard to our position at the time of the discussion of the Clean Air Amendment Act of 1970, to the effect "that the automotive industry cannot continue research and development expenditures at the present levels in the pollution control field where the sole return from the investment would be royalty payments." We therefore support Section 6 of your bill.

We also support the so-called Scott amendments. These amendments are definitely necessary so that business judgments can be made on the basis of a reasonable knowledge of the factual results. We urge, therefore, that provisions incorporating the principles of the Scott amendments be included in your pending bill relating to the general revisions of the patent laws, S. 643.

If the association or any of its members can be of any assistance, please feel free to call upon us.

Respectfully yours,

HAROLD T. HALFPENNY.

AUTOMOTIVE ORIGINAL EQUIPMENT MANUFACTURERS, INC.,
Warren, Mich. April 30, 1971.

Senator JOHN L. MCCLELLAN,
New Senate Office Building,
Washington, D.C.

DEAR SENATOR MCCLELLAN: We are manufacturers of automotive components and parts for original equipment manufacturers. About 340,000 people are employed in our companies and they work in about 350 plants which are located throughout the United States. We make substantial investments in those plants and people, in equipment and research for the purpose of manufacturing products which we sell. Our research programs are normally conducted with the sale of our products as the principle purpose. Licenses are frequently granted by our companies, however, and we occasionally are required to grant licenses to original equipment manufacturers in order to sell products to them. (e.g., see the attached Appendix I). We frequently take licenses from others (often individual inventors) to help us bring out new products. There are hundreds of other companies in this industry, in addition to our group, most of which operate similarly.

We think that the Congress of the United States should set the policy preserving the present incentives which attract people and companies to participate in solving the technological and social problems of our society. We have in mind such problems as pollution and the increasingly difficult unemployment problems resulting from our burgeoning population. We write to you today, therefore, to express our views on two matters shortly to be considered by your Sub-Committee. The first of these matters is the issue of mandatory patent licensing for improving the quality of the environment, (the issue raised by Section 6 of the transitional and supplemental provisions of your bill S.643); the second of these matters is the so called "Scott Amendments."

With regard to the first matter, we attach a copy of our letter of October 7, 1970 to Senator Baker. As stated in that letter, provisions such as are now found in Section 308 of the Clean Air Amendments Act of 1970 can only lessen the likelihood of achieving the results which we all hope will be obtained by that Bill. Your attention is respectfully invited to the statement contained in that letter to the effect that "Our industry cannot continue research and development expenditures at the present levels in the pollution control field where the sole return from the investment would be royalty payments." We adhere to that view. We support, therefore, Section 6 of your bill mentioned above.

With respect to the second matter mentioned above, the "Scott Amendments," in our view it is the responsibility of the Congress to set the public policy in the United States in this area. We want to continue our research efforts so that new jobs are created and new products are available in the marketplace. This is not only the life blood of our companies, but—we submit—it is the life blood of our country as well. This process is assisted by competitive licensing in the open market. These licenses oftentimes are in specific technological areas. There is no valid reason why licenses of such technology should not be granted with a clear understanding of their ramifications. The guidelines set by the Scott Amendments provide a minimum basis for this clear understanding, and do a great deal to clear the present confusion. If the specific language of these amendments is not clear to someone, we have no objection to suggestions which would contribute to such clarity; we strongly support, however, the present principles of these amendments. Furthermore, we strongly disagree with those who oppose these amendments in their statement that these amendments are not necessary and who argue for a "case by case" development of the law. These Scott-type amendments are definitely necessary so that business judgments can be made on the basis of a reasonable knowledge of the factual result; one cannot build half a factory. We feel that the "case by case" approach interjects totally unnecessary fear and confusion; we are well aware of the fact that litigation in this area is frightfully expensive and almost interminably protracted. As you stated in introducing S.643, in quoting the distinguished jurist who is now our Chief Justice:

". . . a large part of all the litigation in the courts is an exercise in futility and frustration."

We fully agree, and feel the time has come to improve the situation. While litigious lawyers and some teachers may have a financial interest in continuing the present archaic method of determining what the law is, we firmly feel that this is not in the best interests of our country as a whole. We know it is not in the best interest of our industry. We urge, therefore, that provisions incorporating the principles of the Scott Amendments be included in your pending bill relating to the general revision of the patent laws, S.643.

We would be very pleased to submit any additional information, or to testify before your Sub-Committee, should you so desire.

Respectfully submitted,

C. W. Ohly,
President.

Appendix I

In order to obtain free license rights under any patents on inventions made by our suppliers as a result of our bringing problems to them and cooperating with them in the development of structures which we may ultimately buy from them, we request such suppliers to enter into our cooperative development agreement. This cooperative development agreement provides that we shall have a free, non-exclusive license to make, have made, use and sell, in connection with Chrysler products, devices and/or methods embodying any ideas or inventions conceived or acquired as a result of or growing out of the cooperative work. Similarly, the agreement grants a license to Chrysler Corporation on inventions which constitute improvements upon the ideas we convey to them. A large number of our suppliers have signed agreements of this type, which have been directed to specified products, for they realize that we could not work freely with them if we were to be faced with patents they might receive on inventions we stimulated them to make. We are always in a better position to request a supplier to enter into a cooperative development agreement with us if we are advised in advance of commencement of the cooperative development program and given an opportunity to negotiate a cooperative development agreement before work is started.

Automotive Original Equipment Manufacturers, Inc.,
Detroit, Mich., October 7, 1970.

Hon. Howard H. Baker,
U.S. Senate,
Washington, D.C.

Dear Senator Baker: In the view of the Automotive Original Equipment Manufacturers Association, Section 309 of the subject bill should be deleted.

We are manufacturers of automotive components and parts for original equipment manufacturers and employ about 340,000 people in 350 plants throughout the United States. We make substantial investments in those plants and people, in equipment and in research for the purpose of manufacturing products which we can sell. We do not conduct research programs with licensing as the principal purpose. There are hundreds of other companies in this industry, in addition to our group, which have the same objective.

The removal of Section 309, we believe, would facilitate the achievement of the desired results to be obtained from the bill. This removal would preserve the present incentives which attract people to participate in solving the problems of air pollution. Indeed, unless Section 309 is removed, that section will lessen the likelihood of achieving the purposes of the bill. Our industry could not continue research and development expenditures at the present levels in the pollution control field where the sole return from the investment would be royalty payments.

To our knowledge, there is no other statute providing for the compulsory licensing of patents, know-how and trade secrets which result exclusively from privately funded research and development. There is no such provision, for example, in the National Traffic and Motor Vehicle Safety Act, important as that Act is. There never has been any showing whatsoever that compulsory licensing of private know-how, trade secrets, or patents is in the public interest. To maximize the amount of research and development effort required to solve the problems of air pollution or automotive safety, we need the greatest number of people and companies exercising their best efforts. A large number of the technical breakthroughs in the automotive industry are directly attributable to the automotive parts suppliers. More breakthroughs are going to be needed to solve the many problems of air pollution. The best way to assure the continued achievements of the parts suppliers is to continue the incentive provided by the present patent system by removing Section 309.

There is, we submit, no need for Section 309 or any other similar statutory mandatory licensing provision. The major automotive companies license inventions and make their patented products available to other automotive companies. For example, General Motors made collapsible steering columns available to Chrysler and American Motors as soon as this device came into production; GM still supplies to American Motors. In addition, the automotive parts suppliers have always made their patented products available to the entire automotive industry. Furthermore, there is no way that anyone could use a patent to obtain an injunction contrary to the public interest. (City of Milwaukee vs. Activated Sludge, Inc., 69 F2d 577, C.A. 7, 1934).

Not only is there no need for a statutory provision providing for the compulsory licensing of patents, know-how and trade secrets, but the fact is that consistently in the past where public testimony on this important subject has been presented, such provisions have been rejected as unnecessary and undesirable.

Therefore, we strongly urge that Section 309, providing for compulsory licensing, be removed from the subject bill as contrary to the best interests of our country.

We appreciate your careful consideration of the matter and your meeting with our representatives on Tuesday, October

Very truly yours,

GILBERT RICHARDS,
President.

STAFFORD LAW SCHOOL,
Stanford, Calif., May 12, 1971.

HON. PHILIP A. HART,
Chairman, Antitrust and Monopoly Subcommittee,
Judiciary Committee,
U.S. Senate,
Washington D.C.

DEAR SENATOR HART: Thank you for your letter of April 29 inquiring whether I wished to submit a comment on the proposed amendments (#23 and #24) of Senator Scott to S.643. The relationships between the patent laws and the antitrust laws is an issue to which I have devoted a major portion of my professional attention in recent years; hence I am grateful for this opportunity to submit my views. To a much greater extent than is true of most academic commentators on this group of issues, I tend to agree with the repeated assertions of the patent bar to the effect that the courts have unduly sacrificed the objectives of the patent system in the name of antitrust. Nevertheless, I think the Scott amendments are misguided and should not be adopted.

In my view the underlying purpose of both the antitrust laws and the patent laws is to attain a more nearly optimum allocation of economic resources than would occur in the absence of any government intervention in these areas. The patent bar, government antitrust enforcement officials, and the federal judiciary might all accept that statement in the abstract, but the behavior and the arguments of each reveal that there is little perception among any of those groups what the statement means or implies.

In general it is my preference to leave problems of resource allocation to the workings of free and competitive markets and to confine the role of government to the preservation and perfection of such markets. With respect to the processes of innovation, however, there are persuasive reasons to believe that the rewards afforded by competitive markets would be insufficient to attract to the processes of innovation an adequate flow of investment capital. First, the process of innovation is inherently characterized by high risk; and there is some empiric data and some theoretical basis for believing that, given other characteristics of our economy, the flow of resources to atypically high risk activities is less than optimal. But a far more confident basis for expecting a sub-optimal flow of resources to innovation inheres in two other characteristics of the process of invention: the characteristics of inappropriability and indivisibility.

Innovative activities have positive costs, sometimes very high costs. Even when some significant invention is eventually achieved, the inventor faces difficult practical problems in employing it so as to achieve economic returns adequate to recapture, not only the variable costs of employing the invention, but the sunk costs that were essential to bring it to fruition. If others learn of the invention and are able to employ it in competition with the original inventor, competition among them and with him will force the price of the ultimate output to which the invention contributes down to a level just adequate to cover their costs of employing the invention; and the inventor, being precluded by competition from charging higher unit prices, will be prevented from recapturing those sunk costs which initially produced the invention and which its imitators were not required to incur. Since this result is plainly foreseeable, investment in innovative activity will be foreseen as yielding lower rates of return than alternative forms of investment not characterized by difficulty of appropriation and will be disfavored.

Therefore, in the absence of some governmental encouragement, a classic problem of externality is involved in innovation: Private investment in innovation will occur only up to the point where the expected future stream of receipts from the investment of an incremental dollar has a present value of one dollar. If the private value to the innovator were the same as the social value which flows from the last dollar invested in innovation, the level of investment would be appropriate. But that is not the case with respect to investment in innovation: the social value of investment in innovation is equal to the aggregate amount that all those who will thereafter enjoy the goods and services to which it leads would be willing to pay; and in the absence of some legal means by which the inventor can appropriate to himself, by thwarting imitators, the social values that he has created by his invention, he will be unable to capture private gains that are commensurate with the social benefits he has created. This difficulty of appropriation, then, necessitates either some legal devices which enable the inventor to appropriate the fruits of his contribution or, in the alternative, government subsidy to the processes of innovation in amounts sufficient to fill the gap between privately profitable levels of investment in innovation and the higher, socially desirable level of investment.

In the United States we actually use both subsidy and a patent system in an attempt to achieve a more nearly optimum level of investment. If the patent system worked perfectly and enabled inventors to recover through the market returns precisely equal to the benefits they had created, no subsidy would be necessary or appropriate; if any subsidy were provided, an *inappropriately* high level of aggregate investment would result. But the patent system does not work perfectly, and some level of subsidy is appropriate. Whether, in combination, present levels of government subsidy and the patent system achieve too little, too much, or about the right level of aggregate investment activity is a question that no man can answer with any confidence. But one can say with confidence that some approximation of our present patent system plus some amount of government subsidy is far more likely to lead us to optimum levels of investment than is a competitive market system in the absence of either of those governmental devices.

If the patent system generated no adverse effects in its operations, then it would be appropriate to give the inventor an exclusive monopoly position, not merely for 17 years, but forever, in order to bring his private receipts into line with the social utility of his contribution. Wisely, however, we afford monopoly protection only for a limited period of years because the patent system does generate socially undesirable effects of several kinds.

One of the contra-productive features of a patent system is that, once an important and basic invention in a field has been made and a patent has been conferred on the initial inventor, the basic patent deters further improvements by others in that field. One who thereafter develops an improvement is given the right to prevent others from using the improvement, but he is unable to use the improvement himself without simultaneously using the basic underlying invention which is patented by another. The basic patentee therefore enjoys a monopsonistic position with respect to subsequent improvements, and the private profitability of investing in improvement-oriented innovation is thereby diminished.

A second contra-productive feature of the patent system, but one that, for reasons to which I will return, need not be as severe as it is under our present system, results from the characteristic of indivisibility. This characteristic might also be described as the problem of constantly declining average cost of utilizing an existent invention in an ever larger number of applications. It is often the case that an invention, once made, can be used in a wide variety of contexts or commercial applications. Some of these applications will be of great social utility, and therefore of great economic value, and the invention will be indispensable to them; prospective users of the invention in those contexts will be willing to pay very high fees for the right of use. Other applications of the same invention will be of only slight economic value and perhaps the invention will be only marginal to them in the sense that some other technique, involving only slightly higher costs, could be used instead; and the prospective users of the invention in those contexts will be willing to pay only very small fees for the right of use. Once the invention has been brought into existence, however, all costs necessary to bring it to fruition have been incurred; no additional pre-emption of scarce resources is involved in permitting the invention to be used in any application where it has any utility whatsoever. In short, the marginal cost of incremental applications of an existent invention are nearly zero; it is only the inventor's need, if he is to earn a return on his investment, to amortize the sunk costs over the totality of applications that calls for payment of any positive fees for the right of use. To the extent that the patent-holder is able to engage in perfect discrimination, charging high fees to those willing to pay high fees and very low fees to those willing to pay no more, the characteristic of indivisibility poses no insuperable problem; the invention will in fact be used in every application where it is of social value, however small that value may be. In some contexts royalty systems approximating perfect discrimination may be administratively feasible, but in others they will not be. Where they are not feasible, it is necessary for the patentee to charge some more or less uniform fee for use of the invention in each of its possible applications; and under those circumstances the invention will not be used in low utility applications because the magnitude of this average fee will exceed the utility of the invention in those contexts. This disparity between the average fee level and the nearly zero social cost of permitting incremental applications generates a form of economic waste insofar as it precludes applications with low but positive social utilities. To the extent the patent system can be tailored to minimize this effect, it should be so tailored; but naive reactions by courts and enforcement authorities to the phenomenon of differential royalty rates ("discrimination") have blocked their use. Of course, to some extent administrative costs of licensing and royalty collection will preclude perfect discrimination, and some social waste of this sort is inevitable and implicit in the use of the monopoly device as a means of rewarding the flow of resource to innovation.

The patent system's conferral of monopoly protection *for a limited period of years* should be seen as a compromise between an attempt to enable patentees to recapture the value of the benefits they have created while minimizing the persistence over time of these negative consequences of the patent system. Our present 17-year period is probably either a little too long or too short—no one can say with confidence—but perhaps it is as good a guess as any other period.

Thus, when properly viewed, the patent system is not, as it is often alleged to be, in conflict with the antitrust laws which strike at monopoly. The conferral of monopoly in the patent context has precisely the same general purposes as does the antitrust prohibition against monopoly in most others: both are designed to eliminate economic waste and induce an optimum level of resource flow into various sectors of the economy. A patent is merely a particular form of property, created by a special body of laws necessary to confer the usual attributes of property on this form of intangible—laws that are analogous in all important respects to the more familiar laws of the various states which render real property and chattels subject to the exclusive possession and use —indeed to the "monopoly control" if one wishes to put it that way—of their owners.

If nothing more were involved, there could be no possible objection to the Scott amendments. One could say that the owners of this form of property, like the owners of any other form, were entitled to hold it to themselves or to trade it to others on such terms as they and the others might find mutually beneficial. The usual arguments in favor of free exchange would apply with all their usual validity. If the patent owner wanted to parcel out a series of exclusive interests in some parts of his property to others willing to buy such exclusive interests, no persuasive objection could be made. *And if it were the case that all patents were commercially significant and legally unassailable,* then the foregoing premises would apply and the argument for according patentees this kind of freedom in the employment of their property would be very powerful.

But it is the case that all patents issued by the Patent Office actually correspond to significant and new innovative contributions. Patents are sought ex parte; and the capacity of the Patent Office to explore the questions of inventiveness and prior art is imperfect. Some significant fraction of the patents issued are invalid; and although the proportion of patents upheld and struck down in litigation actually reveals very little about the fraction of those issued that are invalid, the results of litigation do suggest that it is substantial. A very significant problem results—another of the patent system's contraproductive features: not only does a dubious patent have all of the bad features of a valid patent and lack all the good ones, but it carries still another social disadvantage. A dubious patent is an extraordinarily effective tool for the formation of an illegal cartel. This *unwanted* aspect of the patent system is in fundamental conflict with the antitrust laws.

The point can best be made by example. Exercising only minor editorial freedom, the facts of the *New Wrinkle* case* can be summarized as follows: Before the patent licenses involved in that case were issued, there were more than 200 manufacturers of wrinkle finish varnishes competing in the manufacture and sale of this type of finish. The New Wrinkle Company obtained patents on a finish of this type and thereafter undertook to license other industry members, issuing licenses that contained minimum price clauses. The dozen leading manufacturers were among the first to sign, and ultimately substantially all of the manufacturers in the industry had taken nearly identical ten-year licenses and were selling at prices fixed by the licensor. Royalties on the licenses were set at 5¢ per gallon, a royalty level that represented between 1 and 2 per cent of the sales price, depending on the type of varnish involved. That little more than an effort at cartelization was involved in that case was made unusually clear by several factors: First, the very large number of licensee-manufacturers prevented reliance on oligopolistic structure and made use of a price clause necessary; second, the royalty rates were revealingly low; third, the licenses contained a provision that the license did not become operative until all of the major manufacturers had subscribed to them; and finally, the history of the situation made clear not only that there were doubts about the validity of the licensed patents as a matter of law, but suggested doubt that the "inventions" covered were sufficiently important commercially to make it impossible for pre-existing finishes to be marketed in effective competition with the patented finish, had manufacturers desired to take that course rather than to subscribe to the licenses.

These features made the cartelization effort of *New Wrinkle* transparently vulnerable to attack, and it was successfully attacked. The lesson to be learned from *New Wrinkle* applies as well to cases not nearly so transparent. Competitiors and potential competitors are often willing to take a licensee under a patent which they know to be of dubious value or legality rather than to attack it or to market an unpatented competing product. Their act of taking licenses bolsters the patent's appearance of legality and commercial importance and reinforces its effect as an entry barrier to unlicensed firms. A low fee, which is called a royalty but which is in substance a fee for the service of

* United States v. New Wrinkle, Inc., 342 U.S. 371 (1952).

cartel administration, is paid to the patentee. If more than a few licensees are involved, a minimum price clause or a clause achieving a division of markets may be included in the license; if the number of licensees is sufficiently few, such explicit restrictions may be dispensed with and reliance may be placed instead either on a secret agreement or upon the mutual perceptions of self-interest that predictably will exist among the very small number of firms. Concentration in the industry may thus be increased by fencing out some number of small competitors; or foreseeable deconcentration of the industry, threatened by potential entrants, may be fended off. Existing competition is lessened. The most probably attackers of any patent that is vulnerable, either to legal challenge or to competition from unpatented substitute products, are the other substantial firms that are familiar with the technology involved. Licensing arrangements, often nominally non-exclusive but tacitly agreed to be limited to some small number of firms, become the means of converting potential attackers of the patent into committed defenders of its legality and commercial importance. Royalties serve the purpose, not of compensating the patent owner for his inventive contribution, but as window dressing and to share expenses of cartel administration.

The critical factor to be recognized in this context is that the holder of a strong and valid patent, like any other monopolist, will maximize his own profits if he transfers his monopoly product—the right to use the invention—to a large number of buyers: he will set a royalty rate high enough to force his licensees, because of their resulting high costs, to set their prices for the end-product equal to the profit-maximizing price; and thus the patentee will capture for himself all of the monopoly profit that is implicit in the demand curve which confronts his licensees. If he selects a number of licensees so few as to result in the creation of an oligopolistic structure at the licensee level, he will have diminished his profit potential by creating a bilateral monopoly situation which will necessitate that he share monopoly profits with his licensees. There is no reason for a holder of a strong and commercially important patent to share monopoly profits with his licensees rather than collecting them himself. And when a patentee conducts his licensing program in such a way as to confer a position of exclusive market power upon his licensee, there is a high probability that the licenses were issued at least in part to fend off attack upon the patents and that cartelization of the industry, rather than the extraction of monopoly profits truly attributable to the patent, is involved.

The only genuine conflict between the patent laws and the antitrust laws occurs at precisely this point. As a practical matter, one rule with respect to the ability of a patentee to confer positions of exclusivity upon licensees must be applied both to the holders of strong and valid patents and to the holders of vulnerable patents, for the two classes cannot be distinguished in advance of expensive and lengthy litigation which may never, in fact, be commenced, If both categories of patentees are allowed to confer positions of exclusivity on licensees, then the antitrust laws will be significantly undermined in order to give primacy to the patent system. If neither category of patentee is permitted to confer a position of exclusivity upon any licensee, the antitrust laws will be enforced far more effectively; and one must then inquire whether any significant loss in effectuation of patent policy has been incurred as a consequence of the inability of holders of valid patents to confer exclusive positions.

This conflict between the two policies is rendered susceptible to sensible resolution by the fact that the ability to confer a position of exclusivity is of far more importance to the holder of a vulnerable patent than it is to the holder of a strong one. The holder of a strong patent usually can demand and collect royalties of a sufficiently high level to enable him to garner substantially the full economic value of his inventive contribution; his position is not significantly advanced by the ability to confer positions of exclusivity. But this is not true of the holder of a weak patent: a prospective licensee in a position to challenge such a patent will not pay high royalties; he will only pay a cartel administration fee and will pay that only in exchange for a position of exclusivity or other restraint on competition. The sensible accommodation, then, of the policies underlying the patent laws and the antitrust laws respectively requires that the ability of patentees to confer positions of market power upon their licensees be curtailed.

In a stumbling and uncertain way, that is the trend of the patent-antitrust cases of the last 15 or 20 years. The doubt that has been cast upon the viability of minimum price clauses, formerly upheld under the doctrine of the 1926 *General Electric* case, is one example of that trend. A price restriction clause confers a position of exclusivity upon a licensee by protecting licensees from competition among one another and from competition from the patentee if, as is usually the case, the fixed price is the price at which the patentee chooses from time to time to sell. The holder of a strong patent does not need a price clause: he will set the royalty level high enough to put his licensees at a significant cost disadvantage as compared with himself; and if he is so much less efficient than are his licensees that the royalty differential does not give him a cost advantage, then it is not in his economic interest to manufacture and sell in any event: he will make higher profits by letting his licensees supply the entire demand and pay the royalties that go with that volume of sales. The trend of decisions toward overruling the *General Electric* doctrine is sound.

Two other licensing patterns by which patentees may confer positions of exclusivity on licensees both constitute agreed division of markets. The division of markets may occur either by allocating a series of fields of application one each to a series of licensees, or by allocating a series of geographic markets one each to a series of licensees. For the reasons stated earlier, it is very difficult to conjure up a case in which adaptation of such licensing arrangements is really in the economic interest of the holder of a strong patent. But the utility of both systems to the process of cartelization under a vulnerable patent is obvious. The explicit conferral of a position of exclusivity upon a licensee, either in a particular field or within a particular geographic area, should be struck down as a violation of Section 1 of the Sherman Act.

The argument, often made, that Section 261 of the present Patent Code authorizes territorial market divisions of this type is unsound. The history of Section 261 plainly shows that its only purpose was to serve as a conveyancing rule that articulated the line between a patent *assignment* on the one hand and a patent *license* on the other; and thus the Section served to distinguish those situations in which the transferee of rights did and did not obtain, as an incident of the transfer, such collateral rights as the ability to commence infringement proceedings and to assert the position of a *bona fide* purchaser for value against outstanding prior equities of which he had no knowledge. The conveyancing rule which Section 261 represents was passed before the Sherman Act was enacted; plainly the enacting Congress never addressed itself to the potential policy conflict between Section 261 and the rule of competition embodied in the antitrust acts. And although the section has been amended subsequent to the enactment of the Sherman Act, the history of those amendments discloses that the policy conflict has not been explicitly considered by subsequent Congresses either. To interpret Section 261 as resolving this policy conflict notwithstanding the fact that the Congress has never considered the policy question would be to allow an important issue of public policy to be resolved by a fortuitous choice of words made over a century ago, notwithstanding the fact that no responsible agency of government has ever really thought about the problem.

Proposed amendment #24 should be rejected by the Congress precisely because they represent an attempt, albeit obscure and devious in its wordings, to alter the trend of judicial decisions and recognize on the part of patentees an unrestrained ability to confer positions of exclusivity upon licensees. It proposes to amend subsection (b) of Section 261 so that it extends to applications as well as to patents themselves; and it enables the patentee to *license* as well as to *assign* on an exclusive territorial basis. If this amendment is adopted, Section 261 would in fact do what it is now often incorrectly asserted to do: it would legalize the creation of sub-monopolies within geographic market divisions; the Section would no longer be what it has been in the past, a conveyancing rule that articulated the line between a license on one hand and an assignment on the other.

The language starting at line 11, page 2, of amendment #24 would increase the durability of cartels formed under dubious patents by making it more difficult for a licensee who has a change of heart to free himself from the cartel. Under present law he may challenge the validity of the patent, thus destroying the cartel if he is successful, without risking loss of his license in the event that his attack is not successful. Subsection (f) would deprive him of that opportunity.

The most objectionable part of the proposed amendment #24 is the language on p. 3, lines 11–15, which authorizes restrictive licenses "reasonable . . . to secure to the patent owner the full benefits of his invention." What this language means is impossible to say with any precision, but clearly its purpose and effect will be to push the courts in the direction of upholding a range of practices which shelter licensees from competition among one another. The language is a rough paraphrase of that which appears in the 1926 *General Electric* opinion; and one must assume it was intended to restore legality to clauses imposing price restrictions. In another version of the Scott amendments, it was proposed to amend 15 USC § 14(a) so as to make price clauses illegal *in the future;* but I note there is no such provision in the form you sent me. If that further change were made in 15 USC § 14, the probable result would be that price clauses, which have been regarded as probably illegal by most antitrust practitioners for over 20 years, are retroactively restored to legality up to the date of the new legislation; and all analogous restrictions, such as quantity restrictions and exclusive positions in a field of application are insulated from antitrust attack whether they appear in past or future licenses. The result, if 15 USC § 14 were not so changed, is less clear. Either result would be most unfortunate, for such clauses provide a powerful device for cartel formation.

At this point I wish to stress a very important distinction. The objection I have argued in the preceding paragraph is to the conferral of positions that shelter licensees from competition among themselves or from the patentee. Price and quantity limits inevitably have that effect and should be illegal in all contexts. But I do not mean to suggest that all field or geographic limitations should be struck down. There is no legitimate objection to the grant of a license limited to a particular field of application or to a particular geographic location except where the licensee is given an *exclusive position* in the designated field or area. There are entirely appropriate and desirable uses of field and geographic restrictions—most importantly, the facilitation of differential royalty rates. A patentee should be permitted to issue a field-restricted license at a particular royalty rate, then to issue a license to field #2 at a different rate, and so forth. But he ought not to be able to assure any licensee that the licensee will be sheltered from competition in the field of his license, either by an express clause limiting the ability of the patentee, or by the *de facto* refusal of the patentee, to issue additional licenses.

Legislation may prove to be necessary to attain the desirable circumstance in which field and geographic divisions, each carrying a different royalty rate, are possible but only if freedom of entry at the specified royalty rate is allowed. Several recent cases, most notably the decision of the Court of Appeals for the Fifth Circuit affirming the Federal Trade Commission's decision in the *Shrimp Peeler* case,* have cast doubt upon the ability of a patentee to issue non-exclusive licenses in several different fields or geographic areas and to charge different royalty rates in each of those different market segments. There is no reason why a patentee should not be permitted to engage in that practice; indeed, there is every rason why he should be permitted to do so. As I mentioned earlier, one of the disadvantages of our basic patent system is that practicalities of administration may force patentees into charging more or less uniform royalty rates with the consequence that applications in particular fields or areas of low but positive utility will be needlessly blocked. That result is unfortunate but more or less inescapable when it is brought about by high administrative costs that attend more elaborate systems of royalty differentiation. But the *Shrimp Peeler* line of decisions adds a totally senseless legal barrier which prevents royalty rate differentiation even when that would be possible from the standpoint of practical administration.

If your subcommittee were disposed to support some socially and economically desirable legislation in the patent-antitrust area, a bill which would both improve the situation of patentees and also effectuate legitimate antitrust policies, and hence would have attractive elements of compromise, would be the following: (1) explicitly authorize patentees to grant *non-exclusive* licenses limited to a particular field or to a particular geographic

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* LaPeyre v. FTC, 366 F.2d 117 (1966).

area, provided that the field or area was not defined so narrowly as to result in a situation of *de facto* exclusivity, and further authorize patentees to impose different royalty rates in each field or geographic area so defined; and (2) further provide that once a patentee has issued a license in a particular field or area, then any other qualified applicant for an identical license must be issued such a license. Legislation along these general lines was spelled out in much greater detail in the "Neal Report", the *Report of the White House Task Force on Antitrust Policy*, of July, 1968.*

A number of other objections might appropriately be lodged against provisions that have appeared in one or another version of the "Scott amendments," but to take up each would greatly lengthen this already awkwardly long letter. I will touch briefly on several of the more important.

It is true that the courts have gone further than is necessary to effectuate the purposes of the antitrust laws in striking down package licensing. The only legitimate objection to package licensing is that it can have the effect of extending the operative life of a soon-to-expire, important patent included in the package because the agreement will extend beyond the expiration of the patent. The authorization of package licensing would be unobjectionable if, at the same time, Congress provided that a licensee under a package license, whether or not explicitly authorized to do so by the agreement, had a right, upon the *expiration of any individual patent in the package*, to demand renegotiation of the royalty rate and to repudiate the license if agreement could not be reached. But the language on p. 4, lines 7-10, which authorizes package licensing, is not so qualified and therefore it should not be enacted.

Proposed $14(a) of title 15 which does not appear in the version you sent me, would freeze into the law the present absurd position of the Supreme Court on "tie-in sales." Contrary to the repeated assertions of the Court, transactions of the type called tie-ins by the Court have many socially useful purposes, such as the imposition of different effective royalty rates on licensees who have different utilities for a licensed invention: and the prevailing rule of *per se* illegality should be abandoned, not codified.

Amendment #23 would enact a sweeping rule of "no pre-emption," the consequences of which are unpredictable and not clearly desirable even where predictable. Presumably the purpose is to overrule the *Sears* and *Compco* decisions as well as the decisions in *Lear*, *Sola Electric* and *MacGregor* holding state doctrines of licensee estoppel pre-empted. While the wisdom of the first two cases is open to reasonable dispute, the result they reach is, in my judgment, probably better than the alternative. Elimination of licensee estoppel is important to the effectuation of antitrust policy, and the watered down statutory substitute for the *Lear* line of cases, provided in proposed amendment #24, is inadequate for reasons previously stated.

I urge your subcommittee to oppose passage of any part of the proposed amendments to S.643.

Respectfully,

WILLIAM F. BAXTER,
Professor of Law.

MORTON, BERNARD, BROWN, ROBERTS & SUTHERLAND,
Washington, D. C., May 19, 1971.

SENATOR JOHN L. MCCLELLAN,
Chairman,
Senate Subcommittee on Patents, Trademarks, and Coyprights,
New Senate Office Building,
Washington, D.C.

DEAR SENATOR MCCLELLAN: I respectfully submit that the Congress should exercise its plenary prerogative to legislate guidelines for the industry of this country in the licensing and protection of patents, trade secrets, and know-how. There is now considerable confusion in the minds of those dealing with intellectual property. Specifically, this is to comment on the matter of the Scott Amendments (SAs).

I am a partner in the Washington, D.C. law firm of Morton, Bernard, Brown, Roberts and Sutherland, specializing in patents, trademarks, copy-

* Published, among other places, in *Antitrust & Trade Regulation Report*, #411, Part II, 5/27/69, Bureau of Nat'l Affairs.

rights, and related antitrust matters. I have been engaged in the licensing of intellectual property rights for the entire period of my engagement in the practice of law, and quite substantially so during the past 6 years in that at any given time, I have had, and continue to have, about 8 to 10 licensing matters before me. I am presently Chairman of the Antitrust Committee of the Patent, Trademark and Copyright Law Section of the Bar Association of the District of Columbia and Chairman of the Legislative Action Committee of the National Council of Patent Law Associations. Attachment "A" presents a copy of my resume as it appears in the 1971 issue of *Martindale Hubbell Law Directory*. The comments made herein, however, are my own.

It occurs to me that many commentators are not expressing any views on specific provisions in the SAs. It seems to me that those not expressing themselves in favor of any of the SAs are so restrained on a broad philosophical basis, an untenable basis, rather than on a basis showing some problem with any given provision in the SAs, which are based on experience. They appear to base their philosophical approach on the following basic assumptions:

(1) the Antitrust and Patent Laws are to encourage innovation, and

(2) the Sherman Act should provide flexibility in a "Rule of Reason" approach.

There is no quarrel with bare assumption (1) except that it does not go far enough. A means of encouraging innovation is *to provide for the free-flow of intellectual property in commerce*, for instance by way of assignment or licensing. Moreover, the availability of assignment or licensing prospects is significantly more important to the "small man" lacking the required funds to develop an innovation for commercial use.

The SAs have evolved as a result of *the experiences* of those engaged in the flow of intellectual property in commerce. They draw on Recommendation XXII of the President's Commission of 1966 for both principle and language. They contain specific provisions delineating some "lighted" roads, sanctioned by existing law, on which the motorist of intellectual property can travel with a *relative* degree of *safety* on his licensing ventures.

One leading speaker pointed up very well the problem leading to the SAs, during his presentation at a committee meeting of the American Bar Association held in St. Louis last summer, when he stated:

"I must also say that except for the *per se* type violations, the entire field of antitrust is filled with uncertainties. The line of demarcation between the permissible and the prohibited is constantly subject to change. This is so for two major reasons: (1) the Sherman Act, like the Constitution, is stated in broad language and the courts . . . 'are free to adopt and shape policies limited only by the most general statement of purpose': and (2) the scope and nature of the American industrial economy, i.e., the factual setting in which antitrust problems arise, are constantly changing with the result that the courts are required to apply the general language of the Sherman Act to new and different situations.

"This does not mean, however, that Congress, if it chooses to do so, cannot spell out in the Patent Laws the licensing practices which the patent owner may or may not engage in. For example, without any noticeable adverse impact on competition, the existing Patent Laws have, for many years, expressly sanctioned domestic territorial licensing on an exclusive basis. . . . In short, I support the general proposition that Congress, to the extent it can reasonably be done, *should remove uncertainties in the law of licensing*." (Emphasis added.)

Moreover, in a case wherein the government was urging a change in the policy of title to inventions made by employees, even the Supreme Court stated:

"The courts ought not to declare any such policy; its formulation *belongs solely to the Congress.* * * * These are not legal questions, which the courts are competent to answer. They are *practical questions*, and the decision as to what will accomplish the greatest good for the inventor, the government, and the public rests with the Congress. *We should not read into the patent laws limitations and conditions which the Legislature has not expressed.*" *U.S. v. Dubilier Condenser Corp.*, 289 U.S. 178, 198, 53 S.Ct. 554, 561 (1933). (Emphasis added.)

It is only by considering all the practical issues in a given matter, but as to which there is no record before a court, that the proper determination of the public policy can be made. Much was said at your hearings on the SAs from a theoretical standpoint while ignoring the practical aspects.

Assumption (2), *i.e.*, the Sherman Act should provide flexibility in a "Rule of Reason" approach, fails to recognize that (1) the Sherman Act itself was a codification of common law principles *at the time* (1890) of its enactment and (2) the commerce of intellectual property has undergone a colossal change since the enactment of the Sherman Bill. Indeed, this commerce is not only complicated by the subject matter of the innovations and by the complexity of the new avenues of commerce the innovations have created and continue to create, but also by the scope of the involvement of this commerce which extends to all parts of the globe.

The delineation of some "lighted" roads as provided in the SAs is long overdue, particularly when you consider the character of the subject matter in commerce at the time of the Hearings on the Sherman Bill. The SAs do not purport to sanctify *all* actions, but "merely" to declare what actions will be per se not illegal.

One factor should be emphasized, *i.e.*, the state of technological development was relatively primitive at the time of the passage of the Sherman Act. Nor did some people envisage development of today's level; for instance one Senator around this time was reported as proposing that the Patent Office be closed down since all inventions had been made.

The relative simplicity of the state of technological development at the time the Sherman Act was enacted is further exemplified by a report in 31 *Congressional Record* 3151 of the Senate hearings held on the Sherman Bill when Senator Kenna, in trying to understand Section 2 of the Bill, put it this way:

"Mr. Kenna. Suppose a citizen of Kentucky is dealing in shorthorn cattle and by virtue of superior skill in that particular product it turns out that he is the only one in the United States to whom an order comes from Mexico for cattle of that stock for a considerable period, so that he is conceded to have a monopoly of that trade with Mexico; is it intended by the committee that the bill shall make that man a culprit"

Thus, the implications of the Sherman Bill were being evaluated in terms of livestock, as further shown *infra*, and the Bill was directed to the codification on the common law at that time.

"Mr. Edmunds. It is not intended by it and the bill does not do it. Anybody knows the meaning of the word 'monopoly', as the courts apply it, would not apply it to such a person at all; and I am sure my friend must understand that."

Id. at 3152:

"Mr. Hoar. I put in the committee, if I may be permitted to say so (I suppose there is no impropriety in it), the precise question which has been put by the Senator from West Virginia, and I had that precise difficulty in the first place with this bill, but I was answered, and I think all the other members of the committee agreed in the answer, that 'monopoly' is a technical term known to the common law, and that it signifies—I do not mean to say that they stated what the signification was, but I became satisfied that they were right and that the word 'monopoly' is a merely technical term which has a clear and legal signification, and it is this: It is the sole engrossing to a man's self by means which prevent other men from engaging in fair competition with him.

"Of course a monopoly granted by the King was a direct inhibition of all other persons to engage in that business or calling or to acquire that particular article, except the man who had a monopoly granted him by the sovereign power. I suppose, therefore, that the courts of the United States would say in the case put by the Senator from West Virginia that a man who merely by superior skill and intelligence, a breeder of horses or raiser of cattle, or manufacturer or artisan of any kind, got the whole business because nobody could do it as well as he could was not a monopolist, but that it involved something like the use of means which made it impossible for other persons to engage in fair competition, like the engrossing, the buying up of all other persons engaged in the same business."

The historical aspect points-up that the field of intellectual property was "small potatoes", commercially speaking, at the time of the enactment of the Sherman Act and continued to be so until about 1940. Also, the general

Antitrust concepts being asserted today are not new, but many of the specific concepts are.

The field is now, however, "big potatoes." This is shown by the tremendous increase in the rate of patents issued since 1950, a increase to 10,000 from 6,000 in the number of attorneys registered to practice before the Patent Office over the last couple of years; the amount of money being directed to R&D today; the appearance of more and more products of manufacture on the market; the amount of litigation in the intellectual property field; and the jump-up of Antitrust matters in our practices. With this tremendous rate of increase in activity, it is no surprise that the Justice Department organized a special Patent Unit to concern itself solely with Patent-type matters.

Lionel Kestenbaum, who was with the Justice Department at the time of an APLA meeting in St. Louis a couple of years ago noted that an effort was in the process of being made by Justice toward the patent area in 1948, but it was diverted because of greater demands in other areas.

The "opening shot" of the present Patent Antitrust era can be viewed as having started in 1966. For instance:

1. In *Chemical Week* (11-19-66): "Spotlight Turns to Patents

"Chemical process companies engrossed in patent technology may soon receive letters from the Justice Department, demanding information on their patents, patent licenses, cross-licenses and pooling arrangements."

2. In *Chemical Week* (1-7-67): 'Antitrust: Busy Scene

"In 1967, antitrust moves affecting the chemical process industries will center on three areas—conglomerate mergers, advertising and patents. The Justice Department and the Federal Trade Commission are busy molding new policies whose impact would be felt by U.S. businessmen for years to come."

3. In *F.D.C. Reports** (1-12-70): "Announces formation of 'Patent Unit'

"Mr. Stern emphasized that he and his unit are not 'anti-patent.' The patent-antitrusters, Stern told 'The Pink Sheet,' believe in the importance of the patent system to a free enterprise society, and the whole purpose of the (patent-antitrust) program is to protect the integrity of the patent sysem against abuses."

Statements made by the Department of Justice must be considered in perspective. Having perspective in the Antitrust area today tells us the following:

(1) The field of Intellectual property rights is now a "big part of America's business."

(2) Since it is a "big part of America's business," it will be constantly scrutinized by the Courts, the Department of Justice, The Federal Trade Commission, and competitors.

(3) Since many Courts, different Governmental Agencies, and a myrlad of competitors will be in the act of scrutinizing, some *guidelines* are called for to insure some *uniformity* in standards, provide a clearer understanding of what practices are acceptable, and that such practices will not be "chameleon" in character.

Our prime concern is to insure that the public continue to stimulate the introduction or use of innovations. One way of promoting this introduction is to provide for the flow of intellectual property in commerce; property or innovation which was not there earlier, i.e., which was never in the public domain. The SAs are directed to this point in that they provide some "lighted" roads, already sanctioned by existing law, on which the motorist of intellectual property can travel with a relative degree of safety when on a licensing venture.

As earlier noted, it is not intended that they create any exemption from the antitrust law for any conduct that could be shown in fact in a given case to have created an unreasonable restraint of trade or a substantial lessening of competition or formed a part of a conspiracy to monopolize, but by appropriate statutory provisions, to prevent certain patent utilization practices found in arrangements of assignment, license, or waiver of patent rights from becoming *per se* misuse or illegal. In most cases in which responsible parties follow these practices, it is believed that the results are positively in the public interest, and promote competition.

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*A specialized weekly for executives in the drug, cosmetic and related industries published by F-D-C Reports, Inc., Washington, D. C.

Just as the Sherman Bill itself was directed to the codification of the law at that time, so too are the SAs directed to the codification of law to meet the colossal change since 1890 which has taken place in the character of the commerce of intellectual property. Thus, the SAs are not "all encompassing" but merely delineate some "lighted" roads to help the free-flow of intellectual property in commerce.

I respectfully request that this letter be made a part of the record of the hearings held by you on Scott Amendments Nos. 23 and 24 to S.643.

Respectfully submitted,

EUGENE L. BERNARD.

Attachment A

Eugene L. Bernard, born Youngstown, Ohio, 1928; admitted to bar, 1954, District of Columbia; practice before U.S. Patent Office. Preparatory education, Ohio State University (A.B., 1949); legal education, George Washington University (J.D., 1951). *Fraternity*: Delta Theta Phi. Author: "The Technical Employee—His Mobility." *Bulletin D'Informations*, June, 1969, Association Belge Des Juristes D'Enterprise, Bruxelles. Member, National Panel of Arbitrators, American Arbitration Association. *Member*: Bar Association of the District of Columbia (Member of Council, 1965-1970. Chairman, 1968-1969 and Chairman, Antitrust Committee, 1970—, Patent, Trademark and Copyright Law Section; Member, Board of Directors, 1969-1970); American Bar Association (Chairman, Committee on Patents, 1961-1962. Administrative Law Section): Patent Lawyers Club of Washington, D.C. (Treasurer, 1959-1960; Vice President, 1960-1961; President, 1961-1962); American Patent Law Association (Chairman: Public Relations Committee, 1964-1966; Sub-Committee on Antitrust Aspects of Patent Know-How Licensing, 1967-1968).

STATEMENT IN OPPOSITION TO SCOTT AMENDMENTS TO S. 643 AND OPPOSING LOWERING OF STANDARD OF PATENTABILITY

By

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Responsive to the invitation of Senator Hart, the following analysis of the "Scott Amendments" to S. 643 and the standard of patentability is respectfully submitted for the Subcommittee's consideration.

The "Scott Amendments" challenge the Subcommittee to a high exercise of its responsibilities. For such amendments, while they would powerfully aid private interests, at the same time involve areas of law of such complexity that understanding by the general public is all but precluded. As a result the Subcommittee is unable to receive the benefits of a broad based discussion by the general public, which matters of such import would ordinarily generate.

GENERAL CONSIDERATIONS

Before turning to a detailed analysis of the Scott Amendments, there are some general considerations that cut across the entire field. These concern whether there is a general need for increased patent protection and the work of the President's Commission on the Patent System, the problem of greater certainty in patent licensing provisions and its relations to the standard of patentability, the relation of market structure to patent licensing arrangements and finally, legislative recommendations which would make possible a more informed base for policy in this important area.

A. *The Inadequate Case for Increased Patent Protection and the President's Commission on the Patent System*

The Scott Amendments would strongly increase patent protection at the expense of antitrust considerations. Under these circumstances it would be only appropriate for Congress to insist that the proponents of vastly increased patent protection should, by clear and convincing evidence, demonstrate (1) that the existing system is failing to provide sufficient incentive for invention and innovation, and (2) that the proposed amendments would appropriately increase the incentive for inventors and investors in research at the times they are making their decisions whether to invent or spend money on research.

As I review the literature I find it striking how under-developed the basic data is on which any case for such a policy change must rest. Justice Harlan noted only two years ago in reference to royalty arrangements—with which the proposed amendments also deal—how little discussion there had been of the problems involved either by lawyers or economists. *Zenith Radio Corp. v. Hazeltine Research, Inc.*, 395 U.S. 100, 145 (1969) (dissenting opinion). The best recent article on the general subject with which these amendments deal is purely analytic, containing no empirical data. Baxter, *Legal Restrictions on Exploitation of the Patent Monopoly: An Economic Analysis*, 76 Yale L. J. 267 (1966). Professor Machlup in his 1958 Report to the Senate Subcommittee on Patents, Trademarks and Copyrights also noted the absence of empirical evidence. *Study No. 15, Subcommittee on Patents, Trademarks and Copyrights*, Senate Judiciary Comm. (85th Cong., 2d Sess.) 63-65, 74-80. To the same effect on the lack of empirical data are the views of Professor Kaysen and former Assistant Attorney General Turner. See Kaysen and Turner, *Antitrust Policy* 161-162 (1959), and Turner, *Patents, Antitrust and Innovation*, 28 U. of Pitt. L. Rev. 151, 153 (1966). Indeed, such indications as there are would seem to be to the contrary, for the reason stated by Kaysen and Turner: if courts have in recent years, as patent proponents claim, raised the standard of patentability and diminished the licensing rights of patent holders, one might expect to have seen a measurable decline in invention and innovation. Since no such effect has been observed, one might be inclined "to suspect that the rewards offered at present still exceed the supply price." Kaysen & Turner, *supra*, 162. Professor Machlup has also expressed the opinion that restrictive arrangements do *not* serve as an incentive to invention or investment in research. Machlup, *supra*.

In short, the most basic need, if there is to be any significant legislation affecting patent-antitrust policy, is for empirical evidence on how the present system is working, and particularly empirical investigation of the extent and effectiveness as incentives of particular patent restrictions. By necessity this should precede, rather than follow, amendments to the Patent Code affecting the basic patent-antitrust adjustment. Accordingly the only legislative change I would now propose is one that would facilitate the gathering of additional data on how the present system is working, both with respect to encouragement of invention and effects on competition and competitive markets.

Even if it should be decided after such an investigation that added incentives were needed, it is not at all clear that they should be of the type proposed in the Scott Amendments. They might even more appropriately be liberalized tax write-offs for R and D expenditures. This kind of provision has the virtue of being supported by the general revenues rather than consumers of the articles involved, which may be vital to health or safety. Moreover, the write-off could be limited to fields where it might be desirable to encourage greater invention, rather than being a simple undifferentiated increase in invention reward, whether for a more effective automotive brake or an electric rocking chair. See Mansfield, *The Economics of Technological Change* 218, n. 34 (1968).

Another important alternative to be considered if deficient innovation is the problem is reservation by law of some portion of the patent reward for the employee-inventor instead of permitting him to assign away in advance all of his rights to patents he invents. After all the employee-inventor is probably the prime source of invention in present society. Such a system indeed exists to some extent in West Germany. See *Mansfield, supra*, 211.

In addition to stimulating invention, there is also the problem of ensuring use of desirable patents, as Scott Amendment proponents have urged in defending field of use restrictions. Why do such proponents not urge statutory changes to require compulsory licensing of unused patents at reasonable royalties? Particularly so, when the United States is the only major capitalist country that permits total suppression of use. See Kahn, *The Role of Patents* in Miller, ed., *Competition, Cartels and Their Regulation* 332 (1962).

That proposals such as these are not under serious consideration unmasks the proponents of the Scott Amendments. Talk of increased incentive to stimulate invention and patent use is a cover for simply increasing at the public expense the monopoly toll that those holding patent rights would be permitted to extract.

The President's Commission on the Patent System

The 1966 Report of the President's Commission on the Patent System has been seized upon by Scott Amendment proponents as somehow supplying the missing data showing need for greater patent reward. Indeed, the 1966 Report forms a central arch in the proponents' case. It is vital, therefore to recognize how slender is the reed of support which the Commission Report provides for the Scott Amendments.

The Report of the President's Commission contains no factual evidence whatever showing that additional patent licensing restrictions are needed for continued or improved invention, nor does the Report supply information concerning the expected costs of additional licensing restrictions. Now this is hardly surprising since, as the Commission's Chairman, Judge Simon Rifkind, made clear in his testimony to Congress, the Commision worked under a severe time constraint that precluded any substantial study of the relation of the patent system to the antitrust laws. The following testimony from House Subcommittee hearings makes this clear:

"Mr. RIFKIND: . . . our first assignment was to mark out the boundaries of a doable task . . . I mean something that could be accomplished within the space of a year . . .

* * *

"Chairman KASTEMEIER: . . . What are the areas affecting patents that you really did not consider?

"Mr. RIFKIND: There were really quite a number . . . we had . . . a long list of problems which—from which we withheld any attention. We abandoned then, either at the first glance or because we could not arrive at any sensible solution or contribution in the area. The whole subject of *the relationship of the patent system to the antitrust field,* we touched on, but we did not really go into depth in this very important area." (Emphasis added.)

Hearings on H.R. 5924, H.R. 13951 and Related Bills, before Subcom. No. 3 of House Comm. on Judiciary, (April 26, 1967) pp. 169 and 182.

Repeatedly, Scott Amendment proponents have referred in tones of solemn respect to Recommendation XXII of the Report, the sole recommendation concerning patents and antitrust. From this recommendation, they not only draw literal support for two of the Scott Amendments, but moral support for all the others. "The legislative branch should now take the lead," intones the brief prepared by members of the A.B.A. Patent Section, "fortified . . . by Recommendation XXII of the Presidential Commission . . ." Antitrust & Trade Reg. Rep. (No. 506) p. E-3 (March 30, 1971).

In all of this I have been unable to find any disclosure of the strict disclaimer made as to Recommendation XXII by the Chairman of the Presidential Commission in his testimony before Congress:

"Mr. RIFKIND [Recommendmation No. XXII, dealing with patents and antitrust] is one of the areas with respect to which I said that I had very small, if any expertise . . . *We did not have the time to go into it in sufficient depth for us really to make a first-rate recommendation.* . . . we did not have on our Commission a representative from the Department of Justice or the antitrust division as we did from other agencies. So that we really did not have the opportunity, in our debate to clash ideas with those whose function it is to serve the antitrust policy of the United States." Id. at 184. (Emphasis added).

B. The Problem of Greater Certainty in Patent Licensing Provisions—Relation to Standard of Patentability

The principal argument of the patent lawyer for the Scott Amendment is the need to make the legality of licensing arrangements more certain and predictable. They assert an inability to advise with confidence on the enforecability of field of use, royalty and other licensing restrictions. The Justice Department and others express disagreement on the extent of uncertainty. To an extent, these arguments do not meet.

The problem is not really one of uncertainty, but as to where the areas of uncertainty are located. It is a truism that all fields of law are uncertain at their periphery. Patent lawyers know very well how to draw up a licensing agreement that will *not* be legally uncertain. The problem is that they (or their clients) wish to include more patent restrictions than such an agreement which is free of uncertainties would contain. Passage of the Scott Amendments will not remove uncertainty from licensing. It will simply shift the periphery of uncertainty.

To be specific, proposed Section 271(f) would preclude a court from finding misuse or illegal extension of patent rights where a patent license excludes or restricts conduct "in a manner that is reasonable under the circumstances to secure to the patent owner the full benefit of his invention." This provision is designed explicitly to prevent courts from developing *per se* rules in this area. Now it is as clear as a torch in the night that *per se* rules tend to make the law more certain, while a rule of reason, by requiring *ad hoc* case to case determinations, reduces certainty. If a patent lawyer cannot predict, as the A.B.A. Patent Section Brief claims, when a court will find a royalty payment to be "exorbitant and oppressive," equally he cannot predict when it will find a restriction "reasonable under the circumstances to secure . . . the full benefits of . . . invention." The difference is simply that the first uncertainty tends to decrease the outer limits of patent reward and hence is objectionable while the second uncertainty expands the outer limits of patent reward and hence is desirable.

If other example is needed, one need only refer to the uncertainty as to basic patent validity. Patent lawyers are well aware of the devastating casualty rates among patents that are litigated in the courts. Thus, into hundreds, perhaps thousands of licensing arrangements, there is built the uncertainty of future judicial declaration of patent invalidity. One method of reducing this uncertainty would be to raise drastically the standard of patentability administered by the Patent Office, or perhaps to create a special class of petty patents issued for a short term of years for patents of questionable invention. It comes as no surprise that this is not the proposal of the patent lawyers. Rather, they propose to make it harder for parties to contest the validity of patents in the courts and I have heard nothing to indicate that they do not also favor lowering the general standard of patentability as provided in S. 643. This is change is the right direction, as they view it.

It must also be added that there is some exageration in the claim of uncertainty since to a considerable extent the claim is based not on settled law, but on dictum in a few lower court decisions, and often on no more than mere statements in speeches by Department of Justice officials. See Brief Prepared by Members of A.B.A. Patent Law Section, Antitrust & Trade Reg. Rep. (No. 506) E-3-4 (March 30, 1970).

All of this is not to be too harsh on the patent lawyers. What I think is revealed by the basic inconsistency of their position is that they essentially represent private interests, patent owners and licensees. Of course, these two groups often meet at arms-length, but peculiarly in patent licensing, restrictions inure to the benefit of both parties to the agreement. The licensee agrees to the patent owner's terms and receives in exchange a competition-free submarket. Although both parties are better off, the public is apt to be worse off. Patent lawyers are not retained, however, to represent the public's interest in the matter in patent licensing arrangements. Thus, their neglect of the public interest aspects of the problem is understandable. The Congress must take a broader view.

My own thoughts in this area are that to the extent there is unacceptable uncertainty, it is based on the widespread disagreement between the actions of the Patent Office and the courts. Greater certainty could thus be achieved by either lowering court standards or raising Patent Office standards. I favor the latter. The standard of patentability now is surely not excessively high when patents such as the following were only finally invalidated at the Supreme Court level: rubber caps on wood pencils, on oval rather than a cylindrical roll for toilet paper, rubber handlebar grips for bicycles and a flat cord (in place of a round cord) for the loop at the end of suspenders. Dewey, *Monopoly in Economics and Law* 174 (1959). Thus, I would urge that those provisions of S. 643 that would lower patentability standards further not be adopted. Further, I would urge that Congress insist on an upgrading of Patent Office standards such that an applicant receiving a patent would be able to predict with much greater certainty that a court will later agree with the Patent Examiner.

C. The Unconsidered Relation of Market Structure to Patent Licensing Arrangements

The proponents of the Scott Amendments refer with solicitude to "the little man from Little Rock"—the small patent owner who cannot market his patents unless he is free to enter into the highly restrictive and exclusionary licensing arrangements authorized by the Scott Amendments. For his protection, therefore, all patent owners, large or small, are to be vested with increased powers. What if our little man is on the receiving end of the restriction, and finds his competitive opportunities constricted by a large patent owner? Or suppose he is only a little consumer? It seems apparent that not little men, but patent rights are to be protected, whether those involved are pygmies or giants. Indeed, the situation is not even one of equality for the little man. Many of the Scott Amendments positively favor the large enterprise as against the small. This is seen particularly in Section 261 (e) and (f) which raise the financial barriers to patent challenge. Thus, the Scott Amendments appear to offer very little to our "little man from Little Rock." Moreover, the approach of the Scott Amendments ignores the whole development of antitrust law over the last decade.

Reflecting three decades of economic research, both empirical and theoretical, the law has increasingly recognized in the last ten years the special competitive threat posed by concentrated markets and the existence of a national antitrust policy to prevent further concentration in such markets. I have traced this development at some length. See Brodley, *Oligopoly Power Under the Sherman and Clayton Acts: From Economic Theory to Legal Policy,* 19 Stanford L. Rev. 285 (1967). This general approach has been applied to patents. Patent restrictions significantly buttressing the market power of large firms in concentrated markets have been held illegal. See *United States* v. *United Shoe Machinery Corp.*, 110 F. Supp 295, *affd. per curiam* 347 U.S. 521 (1954). Contrariwise, patent restrictions which serve to strengthen a small firm seeking to enter a concentrated market have been upheld. *United States* v. *Jerrold Electronics Corp.*, 187 F. Supp. 545 (E.D. Pa. 1960), *affd. per curiam* 365 U.S. 567 (1961).

Notwithstanding this development, the proposed antitrust amendments treat patent owners and licensees as undifferentiated categories. Seemingly ignored is the fact that the threat of injury to competition from a particular type of patent restriction can vary remarkably depending upon the structure of the market. This is a further reason why addition study is needed. It is urgently worth exploring whether a workable patent-antitrust policy can be developed that would take market structure into account, and specifically whether a policy can be formulated to effectively discriminate between the imposition of a restriction that entrenches the power of already dominant firms in oligopoly markets, as distinct from one which strengthens the ability of a smaller firm to challenge dominant firms in such markets. (The President's Commission on the Patent System in its 1966 Report ignored altogether the possibility of this approach.)

D. The Legislation That Should Be Enacted Now

In view of the considerations outlined above, and further developed in the body of this paper, I recommend no new legislation in the patent-antitrust area except that which would facilitate additional fact gathering. This is in no way to assert that Congress does not have the right to settle disputed policy issues. It is to recognize that legislative changes in this field have a permanence and durability that requires an adequate factual foundation. Of course, there are bound to be cases arising from time to time in the courts. Thus, there may be some judicial developments. It is to express no general preference for judicial law making to say that based on our present knowledge in the patent-antitrust area, this is a preferable course for the present. When general legislative action is premature, case by case determination is preferable in the accepted common law tradition. I have two recommendations to provide a better basis for policy making in this area:

First, as recommended by the 1968 White House Antitrust Task Force, I would recommend legislation, which would require the public filing of every patent license arrangement. *Report of the White House Task Force on Antitrust Policy D-1 (1968)*. If the enforcement of licensee restrictions is to be significantly changed, it seems vital first to find out a great deal more than we know about the nature and extent of the licensee restrictions now in use, and the ways in which two or more restrictions may be combined.

Second, I suggest the creation of a new task force or study group, adequately funded and staffed with experts in both the patent and antitrust fields, including economists, to study patent-antitrust policy and to develop the data necessary for a reasoned policy choice as between the encouragement of invention and patent disclosure and the protection of competition. Among other things it might be possible to make a cost-benefit analysis as to particular restrictions and expected gains and losses in both the patent and antitrust areas. Such a study would remedy the present policy disarray in which a White House task force on antitrust policy composed of antitrust experts was accused by one member of making recommendations about patents without having fully studied the patent system, *Report of the White House Task Force on Antitrust Policy* (Separate Statement of Richard E. Sherwood) (1968), while a Presidential commission on patent policy, which excluded antitrust experts, failed to give any systematic consideration to the complexities of antitrust policy.

Discussions of Specific Provisions of Scott Amendments

A. Challenging Patent Validity: Sections 261 (e) and (f)

These provisions, which restrict the freedom of both assignors and licensees to challenge the validity of patents, strike one on first reading as providing for no more than ordinary commercial good faith. Analysis destroys such impression.

There is a fundamental difference between patents and ordinary commercial contracts. The typical commercial contract is almost invariably based on a lawful foundation—the consideration is lawful. Patents litigated in the courts are more likely than not to turn out to be based on an *unlawful* foundation—an invalid patent or illegal extension of the patent right. Worse still, in the ordinary commercial contract whatever costs may arise from the invalid contract are likely to be borne only by the parties. The invalid patent on the other hand imposes its costs not only on the parties but on the public in the form of higher prices through restrictions on competition or technology.

The realistic situation, therefore, is that having given the patent owner a monopoly at the public expense, the government must be diligent to prevent abuse of that monopoly right. Reliance on the comercial self-interest of private parties to test patent validity is the prime vehicle of patent enforcement. There is nothing at all novel about this method of protecting the public interest through private action. Why after all does Congress allow the private antitrust plaintiff to receive the windfall of triple damages? Why is the protesting party before an administrative agency able to assert public interest considerations that are not personal to him? Why does the Securities and Exchange Act give shareholders the right to initiate actions for short-swing transactions by corporate insiders although the transaction may have caused them no injury?

The answer to all of these questions is the same. Where the public interest is deeply concerned and where full vindication of the public interest cannot be or is not achieved by public enforcement alone, public policy permits the harnessing of private interests for the public benefit. And this is precisely what Chief Justice Stone said in the leading patent decision, *Scott Paper Co.* v. *Marcalus Mfg. Co.*, 326 U.S. 249 (1945) in which the Court held that the assignor of a patent was not stopped from challenging its validity. Chief Justice Stone said, ". . . interest in private good faith is not a universal touchstone which can be made the means of sacrificing a public interest . . . namely, that the invention of an expired patent is dedicated to the public . . ." (326 U.S. at 257).

Can anyone seriously argue that public enforcement alone is adequate? Over the six year period, 1948 through 1954, the majority of all patents challenged in the federal courts were declared invalid! In the district courts the patent invalidity percentage was 53.5%; in the court of appeals, 63% and in the Supreme Court, 71%. The percentage of patents during the same period which were held valid was less than the remainder. Indeed, during this period only 32% of the patents challenged in the district court were held valid, and in the court of appeals only 18%! *Dewey, Monopoly in Economics and Law* 175 (1959). More recent data gives the same picture. A 1966 source states that the patents have been held valid in only 28% of litigated cases. Rossman, J., *Book Review*, 48 J. Of Patent Off. Soc. 132, 134 (1966), and Mr. Schuyler of the Patent Office estimated in 1969 that 72% of all patents litigated in the court of appeal have been held invalid. *Hearings on the Nomination of Earl Schuyler, Jr.*, Subcom. on Patents, Senate Committee on Judiciary, 91st Congress, 1st Session (May 2, 1969), cited by Jones M., "The Impact of the Patent and Antitrust Laws on Consumers" (Address, Nov. 6, 1970).

The situation can be described as nothing less than shocking. The public is suffering monopoly conditions in hundreds, perhaps thousands of patented articles which rest on no invention a court would uphold as patentable. Proposed Sections 261 (e) and (f) would undermine the situation even further by diminishing the ability of assignors and licensees to challenge (this network of) invalid patents. Under these circumstances it seems unthinkable for Congress to weaken in any way the forces, inadequate at best, which provide a source of challenge for invalid patents unless Congress is prepared at the same time to drastically raise the standards of patentability in the Patent Office.

There is another aspect of these sections which has escape notice. They cut much more sharply against small business than big. Thu, a requirement than an assignor must restore all consideration received before challenging a patent will not block attack by a large enterprise with ample funds. The requirement will have its restrictive impact on the small assignor, and combined with the tremendous expense of patent litigation can effectively choke off such patent challenges by *small companies*. A small company licensee will similarly be less able to take the gamble of renouncing all future benefits under the license, which is made a condition to license challenge under Section 261 (f). The small licensee may be convinced of patent invalidity, but if his financial means are limited, he cannot be certain of his ability to sustain to final court decision the horrendous costs of patent litigation. The result is apt to be that he will simply not challenge the invalid patent when he must, in effect, burn his bridges in advance. The requirements of Sections 261 (e) and (f) impose far less constraint on the large enterprise. Convinced of patent invalidity, the large enterprise can indeed make a long term financial committment to the litigation. Thus, the most accurate description of Sections 261 (e) and (f) is that they will serve to diminish patent challenge most especially by *small* patent holders and *small* licensees.

For these reasons I oppose altogether Sections 261 (e) and (f) as harmful to the public interest. I agree, however, with the proposal of the Department of Justice which would permit removal to the federal courts of state court actions in which the validity of a patent is challenged. This makes for more orderly development of patent law, is conservative of judicial time and helps to avoid federal-state conflict.

B. Splitting the Patent Atom: Fractionalization of all Patent Rights Under Section 261(b)

Section 261(b), carefully analized, is a grant of rights to patent owners of breath-taking sweep. Viewed as a whole, Section 261(b) would sanction without apparent limitation restrictions by patent owners on licensees as to (1) territory, (2) customers, (3) uses, (4) purpose, and (5) quantities sold. A judicious combination of these devices, and in instances even a single one of them, would make it possible for the patent owner to develop a cartel-like structure in the licensee market. Each licensee, for example, could be assigned rights to a distinct geographical territory and all possibilities of cross-selling then removed by quantity limitations and customer and use restrictions. (Similar comments can also be made as to proposed Section 271(f)(1), which to an undefined extent overlaps Section 261(b) and proceeds on the same underlying assumption.)

This proposed section rests on a basic misconception—that since a patent owner has the right to exclude all others from use of the patent, it adds nothing to the basic patent restriction to permit fractionalization of the patent right in any size, shape or form. The misconception stems from neglecting the fact that each additional licensing agreement or assignment binds a separate *actor*, limiting both his actual and potential competitive effort. When it is remembered that the patent owner may himself be a competitor of his license, the full anticompetitive consequences become apparent. Section 261(b) dos nothing less than permit a patent holder to create a full blown cartel in petitive potential reaches a maximum in the case where patent owner and his an end product market as between himself and his competitors. The anticompetitive potential reaches a maximum in the case whene patent owner and his licensees are the leading firms in a highly concentrated market with high entry barriers. (Situations involving small patent holders unable to market their patent except through restrictive devices raise totally distinct problems—see discussion below.)

It is unlikely that licensees will have serious objections to the system. Patent owner has brought them in as limited partners so to speak in the cartel arrangement. Having conferred on them some of the benefits of monopoly, he may readily obtain their cooperation. All of this tends to lower their incentive to develop competing technology or challenge the patents as invalid. It also carries the additional risk of involving the competitive firms in cooperative arrangements that may spill over into other areas of their operations. The victim of the arrangement is the consumer and the free market.

Proposed Section 261(b) goes beyond existing law in that where under *General Talking Pictures Corp.* v. *Western Electric*, 305 U.S. 124 (1938) a particular field of use restriction might be upheld, the proposed Section would permit combination of several such restrictions. That is to say restrictions on territory, uses, customers and quantity might all be combined in a single license. The proposed Section is particularly unfortunate in view of the underdeveloped nature of the cases and critical comment in the area. Although the 1966 Report of the President's Commission on the Patent System contained a brief recommendation for a clarifying amendment to the Patent Code, authorizing field of use licensing, this is neither spelled out in detail nor justified by any supporting data or reasoned analysis. See *Rep. Pres. Comm. on Patent System* 36–38 (1966).

It is perhaps instructive that in the analogous non-patent area of distributor restrictions, where there has been a much more solid development of antitrust analysis, the complexity of the problems raised has been recognized, including the fact that different kinds of restrictions on fields of use raise differing questions and risks. Thus, Justice Brennan concurring in *White Motor Co.* v. *United States*, 372 U.S. at 273 (1963), identified customer restrictions as presenting a problem "quite distinct from that of territorial limitations" and "inherently the more dangerous." Proposed Section 261(b) would lump these and all other field of use restrictions together. Additionally, in the non-patent areas there has been increasing sensitivity to the differing impact of vertical restrictions depending upon the status of the firms involved (new entrant, failing company) and the structure of the market. See *Sandura Co.* v. *FTC*, 339 F.2d 847 (6th Cir. 1964). Such considerations were also mentioned, although perhaps not adequately resolved, in *United States* v. *Arnold Schwinn & Co.*, 388 U.S. 365, 374 (1967). Proposed Section 261(b) neglects the dimension of market structure altogether.

It is therefore fully consistent with the general development of antitrust law to recognize that field of use and territorial restrictions can sometimes be beneficial, particularly as applied to smaller companies. They may be the only means by which a small patent owner seeking to compete with larger firms may have to induce distributors to enter into a licensing arrangement. Recognition of such special factors, in which a field of use or territorial restriction might in fact be pro-competitive, is not barred, but indeed has received renewed impetus from recent judicial decisions. *United States* v. *Arnold Schwin & Co., supra.* (new entrants and failing companies): *Brown Shoe Co.* v. *United States*, 370 U.S. 294, 330 (1962) (small company breaking into a new market or staying in business); *United States* v. *Jerrold Electronics Corp.*, 187 F. Supp. 545 (E.D. Pa. 1960), *affd. per curiam*, 365 U.S. 567 (1961) (new entrant): *Fortner Enterprises, Inc.* v. *United States Steel Corp.* 394 U.S. 495, 506 (1969) ("legitimate purpose" served). However, the fact that under some circumstances a restriction may be desirable, particularly in the case of smaller companies, is no argument for validating the restriction across the board. What is needed is a discriminating approach which would give special attention to the problems of small firms. This Section 261(b) utterly fails to do and thus would move the patent law in a direction directly contrary to the case law development in the antitrust field.

Congressional authorization of unrestricted field of use and territorial restrictions would be particularly unfortunate in view of the fact that it is only recently that the full potential of restrictive distribution arrangements has been recognized. Following the analysis of the economists, Chamberlain and Bain, it is now recognized that high product differentiation can effectively insulate a product, within limits, from the discipline of *inter*brand competition, thus necessitating effective *intra*band competition if the public is not to be exploited by a degree of monopoly pricing. This has been recognized not only under United States law but in the developing antitrust laws of the European Common Market. See *Establissements Consten and Grundig* v. *EEC Commission*, Court of Justice of the European Communities, CCH C.M. Rep. § 8046 (1966).

In short, while antitrust law has developed greater hostility to field of use and territorial arrangements (unless they serve a demonstrably pro-competitive purpose), the proposed amendment to Section 261(b) would have Congress underwrite the validity of restrictive patent licenses; however concentrated the market. It seem anomalous that although few would argue in favor of licensee price fixing by patent owners, division of the market by patent owners as between licensee competitors is to receive a new grant of immunity. Yet both types of restraint would seem similarly to deprive the consumer of the benefits of free competition at the licensee level.

For these reasons I do not think Congress should act to affirm the legality of field use and territorial arrangements. The fact is that the splitting of the patent atom, like the splitting of the physical atom, is capable of releasing destructive forces.

C. Permissible Licensing Practices and the New Rule of Reason: Proposed Section 271(f)

Section 271(f) contains two subprovisions. The first appears to be similar in nature to Section 261(b) discussed above in that it validates without restriction any fractionalization of the patent right. It is undesirable legislation for the reasons previously discussed. In addition, it creates a puzzling interpretive problem as to the extent of overlap and non-overlap between the two Sections.

The second subprovision of Section 271(f) would introduce a mandatory "rule of reason" standard into the patent-antitrust area .Turning its back on recent legal and economic insight, the Section provides that in the future all restrictive licensing arrangements are, standing by themselves, to be judged by whether they are "reasonable under the circumstances to secure to the patent owner the full benefit of his invention and patent grant." The lineage of this language may be traced to the much criticized case, *United States* v. *General Electric Co.*, *supra:* ". . . the patentee may grant a license . . . upon any condition the performance of which is reasonably within the reward which the patentee . . . is entitled to secure." 272 U.S. at 489. In any event the Section introduces the concept of "full benefits of . . . invention" without defining what these benefits might properly include or what means may be employed to get them.

The proposed section stems from the recommendation of The President's Commission on the Patent System. As indicated above, this was an area where the Commission did not undertake any substantial study, and there was no informed antitrust input. The recommendation, as so much else in the Scott Amendments, is an attempt to turn the clock back to an earlier era of antitrust enforcement, to a time when economic concepts we now take for granted, had not been identified. The recommendation is in the teeth of modern antitrust evolution, which has been in the direction of permitting courts to make a reasoned choice concerning the type of legal rule best adapted to the situation at hand. Under such approach the court's choice, based on the economic characteristics of the particular restrictive practice and the cost of litigation, can vary between (1) a rule of reason, (2) a presumptive rule of law subject to defenses, or (3) a per se rule. The proposed statute would compel a court to follow the first approach.

Thereby does the proposed Section turn its back on years of economic and legal scholarship and judicial evolution, and send patent-antitrust law off on a radically different course from the rest of antitrust law. Specifically, the Section ignores the following considerations: *First*, the rule of reason approach in antitrust is not always an unmixed blessing. It makes for protracted and monumentally expensive antitrust litigation. It enormously reduces predictability of legal decision, thus making business planning much more uncertain.

It may introduce so many facts and data as to render rational decision making beyond human capacity, thus leading to arbitrary results. All of this for the reasons President Bok has so convincingly stated. Bok, Section 7 of the *Clayton Act and the Merging of Law and Economics*, 74 Harv. L. Rev. 226, 287–299 (1960). *Second,* under these circumstances, and given limited budgets by enforcement agencies and private parties and the particularly high cost of litigations involving patents, the rule of reason approach can be simply a sophisticated method for achieving a high degree on non-enforcement of the antitrust laws. *Third,* to a remarkable extent the potency of the threat of patent-antitrust litigation *by private parties* is dependent not so much upon the strength of the possible antitrust or patent misuse case as upon the simple power of the litigant to sustain prolonged and costly litigation. Thus the rule of reason approach tends to entrench the bargaining power of the large licensee or patent owner as against the small. Here it runs directly contrary to enlightened antitrust policy, sometimes recognized in the cases, which seeks to aid the smaller firm in challenging market leaders. *Brown Shoe Co.* v. *United States,* 370 U.S. 294 at 330 (1962) ; see Brodley, *supra.* 19 Stan. L. Rev. 285, 301, 340 (1967).

Suggested amendments to Section 271(f) which would exclude from the rule of reason approach a narrow list or proscribed practices, such as price fixing, tying and collective refusals to deal, would if anything, make the provision even more undesirable and inflexible. They would serve to freeze the concept of anticompetitive restriction at a single moment in time, for the enumeration would be construed as a legislative finding that these alone are the seriously anticompetitive practices. Excluded might be practices which would turn out to pose even more serious anticompetitive dangers, for example closed patent pools, exclusive cross-licensing arrangements, joint patent holding companies and acquisitions of patent assets, however extensive. This would be precisely the approach that United States law has wisely declined to follow in the general antitrust area.

Thus, it can be seen that proposed Section 271(f) in any form is a rigid and doctrinaire approach to a complex problem. It cripples the courts' ability to carry out their mandate to achieve a harmonious accord between patent and antitrust policies, giving due consideration to such factors as burdens of expense in litigation, judicial administration and predictability of decision. Instead courts are bound to a full rule of reason hearing in all cases, whatever the burden of such proceedings and however intractable they promise to be. Such an approach seems totally to ignore the probability that our knowledge of the effects of various restrictive practices and their effects on patent incentive and competitive markets may grow; that in the future, case adjudication, scholarly investigation and empirical experience may justify additional general rules, presumptive or even in some instances per se.

In short, the proposed Section is an unfortunate regression to an earlier and less informed era of patent-antitrust policy.

D. Royalty Arrangements: Proposed New Section 271(g)

Proposed Section 271(g) would establish a broad avenue of immunity around patent pooling, patent interchanges and royalty arrangements. The Section contains two subprovisions, the first dealing with non-exclusive exchange of patent rights and the second with royalties.

1. *Non-Exclusive Patent Exchange*

Provision (1) of Section 271(g) declares that non-exclusive patent exchanges are, standing by themselves, *per se* lawful. This result holds however concentrated are the markets involved and however discriminatory the exchanging firms might be in selecting those with whom they will interchange patents. Exchange of patent rights would seem also to comprehend future patent rights and grant-backs of new inventions. Thus, two dominant or even duopoly firms might exchange competing patents on a non-exclusive basis and thereafter, each, acting unilaterally, decline to license any firms that sought to compete with them, thereby creating a two firm cartel. Inclusion of future patent rights and grant-back provisions on patented improvements would ensure a continuing union of patent technology between the two firms. If new patents were being filed, the patent duopoly might continue indefinitely into the future. Of course if they were to *agree* not to license others, they would be in violation of the Sherman Act, and Section 271(g) does not change this result. But why in the world would they need to enter into an agreement to pursue a course of action so decidedly in their mutual interest? The evil is compounded if one imagines such a patent interchange combined with a field of use agreement such that the two firms not only exchange patents and exclude others, but avoid competition between thmselves.

Other possible abuses suggest themselves. Suppose one firm provides the dominant market for patents of a particular technology. And suppose a small company has two valuable patents, one of which it wishes to license and the other to use itself in competition with the large firm. Section 271(g) immunizes a refusal by the large firm to take a license on the first product unless it also receives a license on the second.. The result could be to block the small firm from even attempting to compete in the second market. In other words Section 271(g) authorizes in effect a tying purchase: I will take a license from you on one patent if and only if you agree to license a second one to me.

2. *Royalty Arrangements*

Provision (2) of Section 271(g) confers on patent owners broad, open ended royalty rights. The royalty provisions of Section 271(g) discussed specifically below, appear to overrule such portions of *Zenith Radio Corp.* v. *Hazeltine Research, Inc.*, 395 U.S. 100 (1969) as concern patent-misuse (Part III of opinion), and to freeze the law in this area as it existed in an earlier and cruder form. Such freezing of law development seems to me most undesirable at this time. For as Justice Harlan noted in his *Zenith* dissent, "there has as yet been little discussion of these matters by lawyers and economists." To be sure, Justice Harlan, dissenting, offered this as a reason to "adhere for the present" to an older rule of law, but his comment applies with redoubled force against statutory enactments in this area. This is particularly so since, as Justice Harlan suggested, Professor Baxter's recent economic analysis in Yale Law Review has identified the possibility of a significant injury to competition resulting from end product royalty arrangements. 395 U.S. at 145, citing Baxter, *supra*, 76 Yale L.J. 267 (1966).

The first and second subprovisions of Section 271(g)(2) authorize royalties based on licensee end product sales, the only limitation being that payments may not be made with respect to activities after the patent has expired. This would reverse that part of *Zenith* holding that patent royalties may not be based on products not incorporating the patent. As Professor Baxter has pointed out, this permits the patent owner to take away the licensee's incentive to discover substitutes for the patent. This for the reason that even should he licensee discover an entirely new and cheaper technology not utilizing the patent at all, still he must continue to pay royalties so long as he sells the end product. Moreover, he is apt to find that it is not feasible for him to license his patent to others since the potential licensees for any new invention are likely to heavily include present licensees of an existing patent owner. Yet these licensees themselves remain liable to the existing patent owner to pay royalties on end product sales even though thy should substitute entirely the use of the new patent for the old. That is to say, a new invention would have to represent such a breakthrough as to justify potential licensees' paying a double royalty.

The anticompetitive potential of the first two subprovisions of Section 271(g)(2) are compounded by the third. This expressly sanctions the package licensing or "block booking" of a whole inventory of patents. In *Zenith Radio Corp.*, *supra* 395 U.S. at 139, the Supreme Court attempted to draw the line between legality and illegality in package licensing on the basis of whether the licensee enters into a package licensing arrangement because he finds it desirable or convenient or whether he does so because he has been forced into it by the patent owner. This entire approach would be reversed and "block booking" of patents would receive a per se validation.

Moreover, when package licensing is combined with royalty payment provisions based on end product sales, as permitted by the first and second subprovisions, the restrictive possibilities intensify. Now the licensee is inhibited from developing inventions not only as to patented components of his existing end products, but also as to patented components of products he may manufacture in the future, to the extent such components are included in the license package. Again, he is obligated to pay royalties on the patented components of such end products whether or not he actually uses the components. And as before, competitors and potential competitors of the patent owner are foreclosed, but the foreclosure now is greater for it extends not only to licensees' existing product line, but also to a whole inventory of future products that may be made by the licensee.

The fourth subprovision, which permits discriminatory arrangements by patent holders as between licensees, may under some circumstances not be harmful if confined to patent royalties paid directly on the licensed patent as distinct from end products or patent packages. So confined it seems to give the patent holder the right to charge what the patent is worth to various licensees and so to reap the value placed by the market directly on the patent as such. Nevertheless, the subprovision carries opportunities for severe abuse, particularly where the patent holder is a competitor of the licensee in the end product market. For example, the patent holder could inhibit competition by requiring payment of steeply rising royalties by the licensees whose competition he fears, and thus effectively confine the market share of each such competitor. If demand rose beyond patent owner's ability to serve the market he has reserved for himself, he could then amend the license agreements to reduce royalty payments. Of course, a licensee need not enter into any such licensing arrangement, but what is the choice—an immediate foothold today as against the unquantifiable hope of inventing around or bypassing the patent tomorrow.

E. Restricting the Use of Ideas: Section 301

Section 301, both as contained in the Scott Amendments and in S. 643, represents an over-simplified and most unfortunate resolution of a complex problem. Limits on the free exchange and use of ideas are presently imposed by both the patent law and non-patent legal doctrine such as trade secrets, unfair competition and to an extent general contract law. In general, a free society does not consider restriction on use of ideas to be a good thing in itself. Restrictions are imposed only for strong, public interest considerations. These vary depending on the interest to be served. But there is also an overlap and interrelation. The same idea may be a candidate for more than one type of legal restriction. The matter is further complicated by dual jurisdiction since protection of most non-patent ideas has since *Erie* v. *Tompkins* been vested in the state courts, while patent protection resides exclusively in the federal courts.

While I do not purport to be wise enough to specify what precisely should be the range of protection given to the various categories of ideas and their expression, it would seem clear that the system should be coordinated. Protection or non-protection of an idea under one legal doctrine can often have ramifications for idea protection under other doctrines. The vice of proposed Section 301 is that it cuts the field in two, severing patent protection of ideas from any coordination with non-patent idea protection. More explicitly, Section 301 would overrule *Lear, Incorporated* v. *Adkins*, 395 U.S. 653 (1969) in so far as that case held that "the technical requirements of contract doctrine must give way before the demands of the public interest . . ." in patent enforcement. *Id* at 670. Section 301 also calls into question the decisions in *Sears Roebuck & Co.* v. *Stiffel*, 376 U.S. 225 (1964) and *Comco Corp.* v. *Day-Brite Lighting, Inc.* 376 U.S. 234 (1964) in which the Supreme Court striving for a coherent national policy, declined to permit patent holders who had been stripped of their federal patent rights to invoke state law to exclude competitors from copying the very articles as to which their patents had been invalidated.

No one would pretend that the questions are simple or that *Lear*, *Sears* and *Compco* represent the final solution. But that state law protection against copying of invalid patents as in *Sears* and *Compco* or contractual enforcement of invalid patents as in *Lear* should be allowed to develop in isolation to federal patent law and policy is an irresponsible and perhaps unconstitutional abdication of federal responsibility.

As indicated above, the coordination of federal patent policy with various areas of idea protection raise differing problems. Thus, the question of deceptive palming off, raised by unfair competition statutes, raises the question of adequate identification of goods, as Justice Harlan carefully noted in his concurring opinion in *Compco*. The public would seem to have no interest in preventing one manufacturer from making non-patented goods that look like those of another if the goods are adequately labelled and marked. Indeed, the public interest may lie in the other direction, in reducing excessive product differentiation. The protection of trade secrets and know-how raise questions of an entirely different nature. As in the case of patents, such rights are protected in order to encourage them, but not without limit and not to the extent that the trade secret right would undermine the Congressional limits on patent protection.

The entire subject is a question for careful development and coordination. And in this connection it is encouraging to see Justice Harlan, a strong advocate of such a coordinated viewpoint, emerging as the spokesman for the Court, as he was in *Lear*. This balanced viewpoint should be further enhanced by recent changes in the Court. Regrettably, Section 301 would draw to a close the attempt to bring conflicting state and federal policies affecting patent rights and idea protection into reasonable accord.

NEW YORK, N.Y., *April 16, 1971.*

Hon. PHILIP A. HART,
Chairman, Antitrust and Monopoly Subcommittee,
U.S. Senate, Washington, D.C.

DEAR SENATOR HART: I am in receipt of your letter of April 1 asking my comments on the so-called Scott Amendments to the Patent Code.

I am pleased to comply with your request and, since I covered this same ground with Honorable Richard W. McLaren, Assistant Attorney General at the Antitrust Division, a few months ago, I am giving you my views in the form of the enclosed copy of my letter to Mr. McLaren dated November 9, 1970.

Sincerely,

HERBERT BROWNELL.

NEW YORK, N.Y., *November 9, 1970.*

Hon. RICHARD W. MCLAREN,
Assistant Attorney General, Antitrust Division,
U.S. Department of Justice, Washington, D.C.

DEAR MR. MCLAREN: I have reviewed the "Scott Amendments," the alternative amendments enclosed in your letter of October 27, 1970 and much of the literature concerning proposed amendments to the patent code and do not believe any legislation is desirable at this time. The basic arguments for legislation at this time are (1) an alleged wide spread confusion as to the state of the law in this area and (2) an alleged need to increase profits available to patent owners to support a desirable level of research and development. However, detailed an analysis of the case law with respect to patents and antitrust indicates few areas of uncertainty, and with respect to those few areas, the uncertainty which exists is simply the necessary price for the maintenance of flexibility in dealing with important and complicated issues of public policy. As Chief Judge Hughes pointed out almost four decades ago:

> "As a charter of freedom, the act has a generality and adaptability comparable to that found to be desirable in constitutional provisions. It does not go into detailed definitions which might either work injury to legitimate enterprise or through particularization defeat its purposes by providing loopholes for escape. The restrictions the act imposes are not mechanical or artificial. Its general phrases, interpreted to attain its fundamental objects, set up the essential standard of reasonableness. They call for vigilance in the detection and frustration of all efforts unduly to restrain the free course of interstate commerce, but they do not seek to establish a mere delusive liberty either by making impossible the normal and fair expansion of that commerce or the adoption of reasonable measures to protect it from injurious and destructive practices and to promote competition upon a sound basis."

Insofar as the alleged need for increased profits to patent owners is concerned, I know of no factual basis for the asserted need and agree with Professor Machlup's conclusions in his classic study of the area to the effect that the available empirical evidence is insufficient to come to any sound conclusion as to the effect of the patent system on "the progress of the technical arts and the productivity of the economy." A detailed factual investigation of this contention is long overdue; however, no factual basis for new legislation presently exists.

The amendments enclosed in your letter appear to me to be unnecessary in view of the present status of the law or to represent changes in the law without sound basis in public policy.

I. The proposed amendment to § 261(b) authorizes exclusive licenses as well as assignments. Under *Krasnov* an exclusive license which is not an assignment might be illegal and while I have no strong views on the issue, I see no reason why that issue should not be decided by the courts based on a fully developed factual record rather than by legislation.

The proposed amendment also authorizes licenses of "any part" of a patentee's rights. This would clearly authorize field of use licenses which are presently legal under *General Talking Pictures*. However, *General Talking Pictures* relied heavily on *General Electric* and may not survive the generally expected overruling of *General Electric*. *Schwinn* and *Sealy* also indicate *General Talking Pictures* may ultimately be overruled by the Supreme Court although the lower courts still apply *General Talking Pictures* consistently. The issues involved are complex and interrelated with issues in other areas of antiturst concern; I believe they should be decided by the courts on the basis of fully developed records and detailed analysis of the relationship between general antitrust doctrines and the alleged necessity for an exception in the area of patent licensing.

II. The proposed amendment to § 271(f) changes the procedure for litigating the validity of any patent claim by transferring to federal courts all cases in which such issues arise in state courts. State courts have traditionally dealt with such issues—e.g. the *Lear* case came up through the state courts—and I see no reason for adding to the already overburdened federal courts the additional burden imposed by this proposal.

The proposal also lays down a rigid rule that in all cases in which a claim of patent invalidity is made, the patentee may terminate the license as to all claims which are attacked and (1) have the court determine a reasonable royalty for the remaining claims and (2) collect for the consideration due prior to the assertion of liability. However, the issue as to whether the invalidity of one claim vitiates the validity of the entire license is one that should be decided on the facts of each case and a court should be free to decide in a particular case that no consideration at all is owed the patentee. The proposed rule would as a practical matter probably deter many licensees from attacking the validity of patents or claims and thereby undercut the "important public interest in permitting full and free competition in the use of ideas which are in reality a part of the public domain." *Lear* at p. 670

Finally, the proposed amendment to § 271(f) declares that an agreement not to contest the validity of any licensed claim or patent "shall . . . not serve as a basis for a finding of misuse." This is directly contrary to the Seventh Circuit decision in *Bendix* v. *Balax*, 421 F.2d 809 (CA 7, 1970), and to the rationale of the Supreme Court holding in *Lear*.

The proposed amendment to § 221(g) prevents an assignor from attacking the validity of a patent without first restoring to the assignee the consideration received for the assigned patent. This would deter attacks on the validity of patents by persons in the best position to do so and therefore directly contrary to the public policy underlying *Lear*, *Compco* and *Stiffel*. Indeed it is contrary to the *Sola-Katzinger-MacGregor* line of cases, all of which held patentees could not collect royalties from licensees where the licensees could show the patents involved were invalid and the licenses involved therefore violated the antitrust law, as well as the misuse line of cases which held patentees could not collect royalties for use of even valid patents where the patents had been "misused."

III. The proposed amendment to § 271(h) is to some extent unnecessary and to some extent unsound. On the one hand, it adopts a general rule authorizing any restriction which is "reasonable . . . to secure the patent owner the full benefits of his . . . patent grant", which is the general rule laid down in *General Electric*; this is simply a restatement of the rule of reason in the patent area and therefore unnecessary. However, the general rule is also applied to allowing a patent owner the benefits of "his invention." If "his invention" and "patent grant" are synonymous, the addition is surplus; if "his invention" means more than "patent grant" the rule is either unnecesary since the rule of reason applies outside the patent area, or unwise since patentees should have no greater rights to restrain competition unduly than any other owner of property.

The proposed amendment to § 271(h) also spells out certain conduct as not subject to the general rule of reason. Some of this conduct is already illegal under the antitrust laws so the specification is unnecessary—multiparty price fixing, tie-ins, resale restrictions as to territory or customers, exclusive dealing, joint determination of additional licensees. Some of the conduct specified by the section is not clearly illegal under existing precedents—the first specification prohibits a patentee from fixing the prices of a single licensee, a practice specifically held legal in *General Electric*, and the third specification prohibits all indirect limitations on resale, a prohibition that goes further than *Schwinn*. The final specification prohibits the conduct condemned in *Besser* and *Krasnov* but authorizes an exclusive license with right to sub-license, a practice whose ramifications have not yet been explored by the Supreme Court. At least here, as opposed to the proposed amendment to §261(b), the proposal requires a right to sub-license to accompany the exclusive license. The difficulty I have with the proposal is that it clearly recognizes that some patent licensing practices should be illegal per se while others should be judged under a rule of reason—which is the general approach the courts have adopted without legislation—and then goes on to change the specific rules the courts have worked out in balancing the various policy and factual elements involved without any consistent rationale for overruling the court developed rules or any rationale at all for depriving the courts of the power to continue to develop specific rules in the area on the basis of more refined analysis or more detailed factual records.

IV. The proposed amendments to § 271(i) are unnecessary and will simply create additional confusion in this area; if they are intended to change the law, which they do not purport to do, they would be unsound as a matter of public policy.

(i) The first proposal authorizes any royalty in "any amount, however paid or measured" except for royalties based on activities after a patent has expired. No court has ever suggested any royalty was illegal because it was extortionate except in a single case where the court originally thought an excessive royalty was being used as a means of resale price maintenance; thus, no amendment is needed to protect "excessive" royalties not being used as a means of furthering some other antitrust abuse. *Brulotte* held post expiration royalties illegal, a doctrine the proposal does not purport to overrule. *Brulotte* did not hold illegal collection of royalties after a patent expires if the royalties clearly relate to pre-expiration use; the crucial question is when post expiration collection refers to pre-expiration activity, and the proposed amendment will simply add confusion here by its very existence. Insofar as bases on which to measure royalties are concerned, the only times the courts have indicated any antitrust illegality was involved were when bases were used which created tie-in situations or deterred competition with the patents involved, situations which the proposed amendments to § 271(a) and 15 USC § 1 declare should continue to be illegal. Here again, therefore, the mere existence of the amendment will simply create time consuming, expensive and confusing litigation as to what it means, with no benefit ultimately to be achieved.

(ii) The second proposed amendment states that royalties are not illegal merely because they are not measured by the patent grant or extent of use. The courts have never suggested such royalty arrangements are illegal, except when used to create tie-ins, to deter competition with the patented product or process involved, or to collect royalties for post expiration use. The proposed amendments to § 271 and 15 USC § 1 agree these practices should continue to be held illegal and, therefore, the proposed amendment is unnecessary and confusing.

(iii) The third amendment states that royalties are not illegal simply because they are not segregated by patent or claim. Here again, the courts have condemned such arrangements only when used to create tie-ins or post termination royalties, so the amendment is unnecessary and confusing.

(iv) The final proposed amendment to § 271(i) states that royalties are not illegal solely because they "differ from that provided in some other arrangement." The courts have not held that differing royalties always constitute discrimination, nor have they held that where discriminatory royalties exist they are always illegal. The courts have held that royalty discriminations which create or maintain monopoly positions or which substantially restrain competition in other markets are illegal, and the proposed amendment does not change those rules. The proposal is thus unnecessary, and if adopted, will result in needless confusion and useless litigation.

(v) The proposed amendment to § 271(j) authorizes (1) licenses of less than 17 years and for areas less than the United States, licenses no court has ever suggested were illegal and (2) licenses which allocate fields of use, customers, etc., which as indicated above under II are presently legal under *General Talking Pictures* but which the courts may ultimately hold illegal as inconsistent with the general antitrust analysis of such cases as *Motion Picture Patents*, *Masonite*, *Sealy* and *Schwinn*. The discussion under II above is thus applicable here. The courts may eventually hold such practices to be illegal per se, or illegal only when used by dominant firms in an industry, or illegal only when abused in particular market situations.

(vi) The proposed amendment to 15 U.S.C. § 1 would declare the price fixing, tie-ins and agreements not to compete with patented products or processes are illegal per se. These practices have long been held to be illegal per se, so the amendment is unnecessary.

(vii) This proposed amendment would declare that the patent code should not be declared to preempt state law with respect to matters "not in the nature of patent rights." In *Stiffel* and *Compco*, the Supreme Court held that state law could not prohibit copying products, but copying products is "in the nature of patent rights" so the proposed amendment would not overrule *Stiffel* or *Compco*, which applied the preemption doctrine to such copying. In both *Stiffel* and *Compco*, the Supreme Court stated that the States could prohibit copying trademarks, labels or distinctive packaging to prevent misleading purchasers as to the source of goods. Neither *Stiffel* nor *Compco* involved trade secrets or know how. *Lear* did involve trade secrets and know how, and the Supreme Court refused to decide the issue due to its "difficulty and importance" until the state courts had "after fully focussed inquiry, determined the extent to which they will respect the contractual rights of inventors [of unpatented secret ideas] in the future." There is district court dicta in *Painton* which I believe is unsound, but that case is now on appeal in the Second Circuit. Thus, nothing the courts have done in the area of preemption warrants legislative action at this time. Moreover, if legislative action were warranted, the proposed amendment would not avoid preemption based on the patent clause in the Constitution and the Sherman and Clayton Acts, as opposed to preemption based on the patent code.

Sincerely yours,

HERBERT BROWNELL.

BURKE RESEARCH CO.,
Pompano Beach, Fla., May 20, 1971.

Hon. JOHN L. MCCLELLAN,
Chairman, Subcommittee on Patents, Trademarks, and Copyrights, Committee on the Judiciary, U.S. Senate, Old Senate Office Building, Washington, D.C.

(Attention: Thomas C. Brennan, Esquire, Chief Counsel.)

DEAR SENATOR MCCLELLAN: In connection with Senate Bill S. 643 for the general revision of the Patent Laws Title 35 of the United States Code, etc., I was kindly informed by your Chief Counsel over the telephone on May 11, 1971 that it would not be possible to hear all of the persons and organizations who had requested to appear at the hearing on said Bill before your subcommittee, and that the subcommittee would print written comments on the Bill if submitted before June 1, 1971.

Pursuant to that advice I enclose for inclusion in the hearing record and for consideration by the members of your subcommittee the accompanying statement giving my views, as an independent inventor, relative to said Bill, and stand ready to answer any questions any member may have in this connection, that may be of use to the committee.

Sincerely yours,

OLIVER W. BURKE. Jr.

STATEMENT

STATEMENT TO THE SUBCOMMITTEE ON PATENTS, TRADEMARKS, AND COPYRIGHTS, COMMITTEE ON THE JUDICIARY, U.S. SENATE

(By Oliver W. Burke, Jr.)[1]

Mr. Chairman and Members of the Committee: the present statement is an amplification of remarks made by the author in an address just delivered at the 48th Annual Meeting of the American Institute of Chemists held in Bir-

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[1] Former Deputy Director of the Office of Rubber Reserve, Reconstruction Finance Corporation, administering the National Synthetic Rubber Research and Development Program; holder of Doctorate degrees in Chemistry and Economics; proprietor of Burke Research Company, an unincorporated private small business enterprise, which is financially sustained by originating, developing, patenting, licensing and selling of inventions to the rubber and chemical industry.

mingham, Alabama, on May 15, 1971. I trust the views expressed in the following ten points may be found to merit serious consideration by the Subcommittee members.

I. THE ROLE OF INDEPENDENT INVENTOR

About 70% of United States patents are issued to assignees; about 30% of them are issued to inventor-applicants. This means that *nearly one-third* of all U.S. patents are taken out by independent inventors. Despite this fact, the Subcommittee will note that the independent inventors were not represented on the President's Commission on the Patent System, the public members of which were selected from the category of University Officials, Attorneys and Judges, and Corporate Officers.

The Subcommittee has evidently appreciated the role of individual inventors and small business because in the successive bills introduced since 1967 a number of the proposals which would have been highly detrimental to inventors and especially to individual inventors connected with small business, have been eliminated. Therefore my present statement is directed to certain salient proposals of S. 643 (together with Amendment No. 24 thereto, and S. 1255 concerning fees) which appear to me, respectively, to be desirable or undesirable from the standpoint of private enterprise and the country as a whole.

II. PROPOSED AMENDMENTS TO SECTIONS 102 AND 103

The basic philosophy of our Patent system requires that an inventor be accorded a patent fully commensurate with the invention disclosed as the *quid per quo* therefore. Title 35 USC 101 and 102 now recognize this fact. Section 101 now provides "whoever invents" an invention "may obtain a patent therefor subject to the conditions and requirements of this title." Sections 102 and 103 specify *positively* that a person *"shall be entitled to a patent"* unless certain provable facts appear. This law gives incentive to an inventor by *assuring* him that when he files an application in the Patent Office, he has a right to a patent unless the Examiner shows one of the provable negating facts to exist.

This present law has worked adequately in nearly all cases, most of which are never litigated. It is axiomatic that only a very small percentage of commercially useful patents are ever involved in litigation before the courts, and that only a still smaller proportion of these contested patents ever reach the higher courts; and that those which are litigated, and especially those which do reach the higher courts, are the "hard cases which make bad law." Reformers always stand ready to seize upon pronouncements made in connection with such few litigated cases as a reason for urging introduction of unwise changes into a generally satisfactory law.

The proposed revisions of Section 102 (S. 643, page 12, lines 15–18) are of this sort. Because the courts in certain borderline cases have questioned whether the standard of invention therein applied was sufficiently high, immediately someone (the reformer) proposes placing a greater burden on all inventors seeking patents, as a supposed way to handle the situation. Actually the review by the court, of the border-line cases, was and is the best way to rectify any instance of the Patent Office *not* carrying out adequately the examination required by the statute.

Furthermore, the Patent Office Examiner wears four hats: (1) he is the confessor to whom the applicant discloses his invention. (2) He is then an investigator who, informed and guided by the applicant's disclosure, searches for all pertinent art he can find which may negate patentability. (3) He is then the prosecutor who opposes issuance of a patent for the claimed invention by rejecting the claims on any ground he thinks to be tenable or possibly tenable. (4) And finally, he sits as a judge to decide whether the applicant's affirmative response is sufficient to overcome the grounds of rejection he has himself asserted. Whenever a person is "both prosecutor and judge" a pleader's response must be particularly convincing to cause the "judge" to doubt the contention he himself has raised as "prosecutor." Under such circumstances, to require more of an inventor is not warranted.

Under the present law, the inventor at least has an affirmative promise of the statute that he will be accorded a patent unless a positive fact to negate his right thereto is shown to exist by the Examiner. The proposed amended Section 102 in effect would require the *inventor to establish a negative fact* by "a preponderance of proof," viz: that *none* of the conditions (a) through

(d) (5) of the section exists. Obviously this sort of requirement would put an excessive burden on the applicant and an excessive power of decision in the hands of an arbitrary examiner, and would probably deprive the public of invention disclosures in many cases, contrary to the public interest in obtaining publication of such disclosures for a fair *quid pro quo* measured by a commensurate patent grant. The purpose of the patent laws is and should be to issue patents for inventions, not to impede the obtaining thereof. This purpose is adhered to by the proposed amendment to Section 103 (S. 643, page 13, lines 28–30). The proposed amendment to Section 102 (S. 643, page 12, lines 15–17) would increase the costs and obstacles to be overcome in obtaining a patent, and to such extent would impede the disclosure of invention which is necessary to effectuate the purpose of Section 8 of Article I of the Constitution "to promote the progress of . . . useful arts."

For these reasons I support the amendment of Section 103 at page 13, lines 28–30 of the bill, and strongly oppose the amendment of Section 102 at page 12, lines 15–18 of the Bill.

III. SECTION 102(d)(3) AND 102(d)(5)

Sections 102(d)(3) and 102(d)(5) at S. 643, page 13, lines 3–6 and 12, are contrary to the intent of Section 8 of Article I of the Constitution that the inventor, i.e. the first independent inventor to comply with the patent laws by diligently filing an application disclosing his invention, shall be awarded a patent. Under the proposed Sections 102(d)(3) and 102(d)(5) of S. 643, an inventor could supress or conceal his invention and keep it secret from the public, disclosing it only to persons in the art in privity with him with the intent of never disclosing the invention to the public, and could still urge the so concealed or suppressed trade secret as a bar to a patent to an independent inventor who did comply with the spirit of the patent law. This certainly is not the aim of the patent clause of the Constitution. The present law, Title 35 Section 102 (a) and (g), is consistant with the public policy of the patent clause, Section 8 of Article I of the Constitution, and I am opposed to the proposed revisions thereof for the above reasons.

IV. SECTION 131(b)

The proposal to "legislate" that the Patent Office shall normally "dispose" of applications within 18 months of their filing date is unrealistic and unwise. Broad or complicated inventions usually take longer to examine and prosecute than narrow or simple ones. Also the length of time required to prosecute an application to obtain protection commensurate with the invention disclosed, is greatly influenced by the personality of the Examiner, i.e. whether he unreasonably adheres to his position as a prosecutor-advocate (see II, above) or is able to abandon such position in the face of evidence or argument showing it to lack an unequivocal foundation.

If any enactment of specific instructions to the Commissioner is deemed necessary (ordinarily not the province of a statute), the proposed Section 103 (b) should be terminated by a period after "applications" (S. 643, page 21, line 3) and the unrealistic phrase "so as to normally dispose of applications within 18 months of their filing date" (which also puts too much emphasis on closing out the prosecution regardless of whether the invention has been given a full, proper and unbiased examination) should be eliminated.

V. SECTION 131(c)

In filing an application the inventor by oath or solemn declaration avers that he believes the subject matter of his claims to be patentable. This should suffice unless the Examiner, as one skilled in the art and with the added advantage of the guidance of the applicant's disclosure, can find prior art disclosing or making obvious the invention. However, if applicants are to be required to supply to the Examiner the prior art considered in preparing the application, so that the Examiner can consider the same, simple fairness to the applicant and to any court later called on to review the patent requires such consideration to be made of record in the application and the patent resulting therefrom. To so provide, if Section 131 (c) is to be adopted, it should be amended, as by inserting after the first sentence thereof (i.e. in S. 643 at page 21, line 13) a provision "All references so submitted or cited shall be made of record as 'References cited in the file of this patent' and be so listed in the patent document."

VI. SECTION 154

The present law insures full examination before the issuance of a patent, and hence the issuance of a patent with claims which inform the inventor and the art, as to the scope of protection accorded. Different types of inventions present different problems in prosecution. A large corporation seeking a "defensive patent" can sacrifice part of the protection to which it is entitled, in order to obtain issuance of the patent. But an individual inventor, if he is to sell or license his patent to others, can ill afford to sacrifice any part of the protection to which he is entitled, because to do so may seriously reduce or destroy the value of what he has to sell. Therefore, if necessary to obtain what he believes to be adequate protection for his invention, the individual inventor is forced to present and insist upon claims fully covering the novelty of his invention, and the broader and more basic the invention, the more are such claims both essential and difficult to obtain. Hence, to obtain the necessary protection, the individual inventor may have to prosecute appeals, or file continuing applications, or contest interferences, which would not plague one seeking only a "defensive patent."

Moreover, the broad and basic invention is the one which contributes the most to the public in promoting progress in the useful arts, and it obviously is unfair to require an inventor to forego the protection he needs or, in the alternative, to sacrifice that part of the term of the patent which is consumed in obtaining adequate protection. I therefore believe that I speak for all individual inventors in supporting retention of the present law 35 USC 154, and opposing the modification thereof (20-year from filing term) proposed in Sections 154 (a) and (b) of S. 643.

VII. SECTION 191 AND 192

As set forth, these sections of S. 643 are permissive only, and smack of star-chamber tactics in the provisions of *Section 191(b)* to not disclose the identity of the informer. To simply notify the Commissioner of Patents of the identity of the allegedly pertinent prior art is one thing, but if the informer submits arguments, or affidavits, or other materials seeking to interpret, or to sway the Commissioner's interpretation, of the documents, these materials and the identity of the persons submitting the same should be disclosed to the patentee so that he can answer the same.

Also *Section 192* does not expressly preserve the right to confront the adverse claimant. and with Section 102(d)(5) in its proposed form, would enable an adversary to interpose a suppressed or concealed invention or trade secret, never disclosed by him publicly or through the issuance of a patent, to negate the right of the first diligent inventor who has compiled with the spirit of the patent law by disclosing the invention in exchange for the rights to be secured to him by patent.

If the purpose of these sections is to transfer to the expert scrutiny of the Patent Office questions of patentability heretofore tried in the courts in infringement and declaratory judgment proceedings, such proposal might have merit from the standpoint especially of the patentee, but in such connection there should not be any permissiveness, or any 6-month or 1-year periods as in proposed Sections 191 and 192. Instead the courts under proposed 35 USC 282 should be limited in jurisdiction to a determination of whether or not the claims of the patent have been infringed by the defendant, and it should be provided that any defendant wishing to attack the validity of the patent shall be required to institute a proceeding so to do in the Patent Office, with a suspension of the infringement suit during the trial of such proceedings on such terms as may be deemed just by the court, the proceedings in the Patent Office providing for amendment of the patent to confine its claims to the patentee's own invention, and for appropriate review of the decision by the Court of Customs and Patent Appeals, if desired.

VIII. SECTION 193

As an individual inventor, I have been involved in "interferences" in the U.S. Patent Office, and also in "conflict proceedings" in the Canadian Patent Office. In the latter, on declaration of a "conflict" the parties submit their proofs in affidavit and exhibit form, in duplicate, and the Patent Office renders a decision of priority based thereon, and delivers to each party therewith the duplicate copy of the opponents proofs and identification of the opponents application. A party dissatisfied with the decision may commence proceedings in the Exchequer Court for the determination of the respective rights of the parties. Such proceeding is expeditious, and usually the Patent Office decision is correct and no Exchequer suit is filed. The costs and delays of taking of testimony, preparation of briefs, oral arguments, etc., in the Patent Office are avoided, yet the applicant's rights are protected by the provisions for court procedure in the rare case in which the losing party may believe the Patent Office decision to be contrary to the evidence, or may challenge the veracity of his opponent's proofs. The public is not confused by the premature issuance of a patent to one party, subject to revocation, and the rights of the first diligent inventor, with respect to his invention domestically and in other countries, are not prejudiced by premature publication.

The proposed Section 193 would have the disadvantages of premature publication, and would merely penalize *both* applicants, as regards enjoyment of the full terms and benefits of their patents. The party whose patent is prematurely issued subject to the priority contest could hardly expect to be able to interest third parties in assuming the costs of undertaking manufacture under such circumstances until after the conclusion of the contest. Hence his period of enjoyment of his patent, even if he were successful in the contest, would in effect be curtailed. And the public interest in having the subject matter manufactured would be left unsatisfied accordingly.

From the standpoint of the individual inventor, therefore, I would favor adoption of a "conflict" procedure similar to that employed in Canada. And in the interest of early disclosure to the public and early conclusion of the patent term, I would favor issuance of the patent to the party accorded priority by the Patent Office, such issuance to start the patent term as to such claims, with provision in the law that, since the public has notice of the claims so issued, if in a court proceeding the other party to the priority contest should ultimately be awarded priority and obtain those published claims, then he would acquire for them the patent term running from the date they were first published in the issued patent. In this way, I believe, the public interests, and those of the inventors, would be most fully served.

IX. SECTIONS 12 AND 14 (AND SENATE BILL S. 1255)

The Patent Office is only one of the Government agencies concerned with promotion of the useful arts. Others include, e. g., the Department of Agriculture, the Bureau of Foreign and Domestic Commerce, the Bureau of Mines, and the Bureau of Fisheries, to name but a few.

None of these agencies except the Patent Office has to my knowledge ever been subjected to the claim that it should be self-supporting in any particular degree from revenues collected from those engaged in the field of endeavor being promoted by the agency concerned.

Th inventors of agricultural machinery, fertilizers, soil conditioners, improved plant species, and other aids to agriculture, for example, have done more to enable a small proportion of the population to feed the whole than any other group. Why, therefore, should such inventors, and other inventors promoting the efficiency of those engaged in other useful arts, be penalized by making them pay a high percentage of the cost of operating the Patent Office, when the farmers, the miners, the fishermen, etc., are not required to so underwrite the costs of the agencies trying to promote the usful arts in their fields. It should be recognized that the inventors are one of the country's most valuable assets, aiding progress in all fields of useful arts, and that they should not be required to bear any larger part of the cost of Government operations preformed for the common benefit in their field than should those otherwise engaged in activities useful to the country.

Again, the provision of Section 12 for "research" in storage and retrieval of information, while obviously a worthy endeavor which I favor, if successful will benefit the entire country, not just the inventors, wherefore the cost thereof should be borne equally by the public at large, and not in special part by inventors.

I would suggest therefore, that there is no justification for the increase of fees that would be required by S. 1255; that it should be recognized that the endeavors of inventors in making inventions and disclosing them to the public in exchange for a limited period of exclusive use is a public service; and that Section 41 (c) of the Bill (S. 643, page 10, line 40 to page 11, line 4) should be deleted as contrary to public policy.

X. SECTION 121 (AND 103)

The present law provides that when "restriction of species" is required in an application also containing a claim generic to the species, the generic claim shall be examinable with the elected species, and if allowed will afford a basis for restoring to the application the claims to other species within the genus. The courts have ruled that the breadth of a generic claim which is clear in terminology and scope, does not render it indefinite. However, there has been a tendency in practice for an Examiner who does not wish, or feel competent, to extend his search to all subclasses in which a species of the genus might be found, to try to avoid the need for making a full search by rejecting the generic claim on trumped up grounds, or to "off the record" take the position "We just don't allow claims of such broad scope in our examining group." Obviously this sort of practice is not following the directive of Congress, but is an attempt by the particular Examiner to evade so doing. To eliminate this unlawful practice as far as possible, the second sentence of proposed Section 103, at S. 643, page 13, lines 26 to 30, should be amended to read as follows (insertion underlined):

> "Patentability shall not be negatived by the manner in which the invention was made, nor because the invention *is broad in scope*, or has simplicity, or is the last step in an evolutionary development, nor because it is not revolutionary, basic, scientific or technical in character."

To the extent that such amendment would insure a proper action on a generic claim and an allowance thereof when not anticipated or made obvious by the prior art, it could be expected that the need to file a multiplicity of divisional applications for various sub-genera or species would be minimized, thus reducing the burden of such repeated applications on the Patent Office, and the number of patent documents required to effect protection commensurate with the scope of the inventor's contribution, thereby reducing unnecessary increase in the volume of material to be searched in future cases.

XI. IN CLOSING

My above opinions are based upon over twenty years of personal experience in the solicitation, in active participation with patent counsel, of patents in this country and in foreign countries which have formed, and do form, the foundation of my small business enterprise. Such experience has included many conferences with Examiners concerning the prosecution of my applications, and the making, in person, of searches in the Patent Office files to determine what has been done to solve particular problems in the art in which I am working, and in what respects the prior art has provided no solutions thereof. I therefore believe that I can speak with some authority on the ten points above set forth, and trust that my efforts will be of aid to the committee in its endeavor to make such changes, and only such changes, in the patent laws as are consistent with the objective of the constitutional provision therefor.

Yours sincerely,

OLIVER W. BURKE, JR.

MAY 3, 1971.

Hon. JOHN L. MCCLELLAN,
Chairman, U.S. Senate, Committee on the Judiciary,
Washington, D.C.

DEAR SENATOR MCCLELLAN: Thank you very much for your letter of April 14, 1971, to our President, Mr. John J. Riccardo. Mr. Riccardo has asked me to write to you setting forth Chrysler Corporation's views on the matter.

It is our feeling that any change in our Patent Laws, as controversial as the mandatory licensing of U.S. patents, should have been the subject of hearings before your Patent, Trademark, Copyright Subcommittee of the Committee on the Judiciary before being legislated into law. Furthermore, if mandatory licensing of U.S. patents is to become a part of the law of our land, such a provision should be included in our Patent Laws, that is, Title 35 of the U.S. Code, rather than as an amendatory provision to the Clean Air Act. The criteria for determining the granting of mandatory licenses under our U.S. patents should be clearly set forth in our U.S. Patent Laws and not in one or more different acts that are designed to determine the functions of the various governmental agencies involved. We hope your proposal as to mandatory licensing will be supported by the Congress.

It is very difficult for us to discuss the patent licensing provision of the Clean Air Amendments Act of 1970 without giving you our views on this Act as a whole. It seems to us that any decision in regard to the patent licensing provision should be made within the context of an overall philosophy as to the most desirable approach for advancing the national interest in clean air in a manner that is most consistent with maximum utilization of the nation's resources to achieve maximum benefit.

We believe there are a number of inconsistencies in the approaches taken by various agencies of the Government in dealing with the entire matter of vehicle emissions and that, as a result of these inconsistencies, the people of this country are going to have to pay a price for vehicle emission reduction out of all proportion to any benefits to be obtained. Further, we believe these inconsistencies have the effect of delaying rather than advancing solutions to the problem.

The patent licensing provision to which you refer seems to us to represent, in part, a philosophy that normal competitive patent provisions should not apply in an area of public interest of this kind. On the other hand, the heart of the Consent Decree, which the Department of Justice required as a basis for settlement of the suits it started against the automobile manufacturers, is premised on the assumption that it is imperative to retain normal competitive practices among manufacturers. As a result, it restricts exchanges of information between the manufacturers who are working to solve the problem.

A similar dichotomy is found when you compare the role of the Environmental Protection Agency, which presumably was established so that persons of expertise could supervise advances in clean air and determine where, how and at what rate regulations should be promulgated, with the provisions of the Clean Air Amendments Act, which essentially takes all authority away from such Agency by specifying that vehicle emissions have to achieve a certain percentage limitation by a certain date, even though there is no scientific basis for arriving at these percentage limitations.

There is no doubt in our minds that the effect of these various inconsistencies emanating from the Government, along with others which there is no need to list here, are making the vehicle manufacturers' task of achieving sensible emission control results extremely difficult and inordinately expensive to the public.

Within this context, the patent licensing provision seems to reflect only another example of lack of clarity of national goals, priorities and methods for achievement in this area. It would seem to us that two approaches could be taken. One would simply say that we wish to apply the maximum incentive to have any firm achieve the standards set forth in the Clean Air Amendments Act. On this basis it could be argued that nothing could be a greater incentive than to say that if one company achieved the goals set forth in the Act and the others did not, that the other companies would have to go out of the automobile business and there would only be one producer. Obviously, this is not a feasible alternative, even though it is logically consistent with the Department of Justice position espoused in the Consent Decree.

Consequently, we assume that the patent licensing provision was inserted in order to arrive at a fairly unsatisfactory compromise by saying that if someone did discover a device that would allow him to benefit significantly from his discovery, he would have to share it with all vehicle manufacturers so as to make certain that no one could achieve a monopoly position or that no inventor, by charging too high a royalty for his invention, could cause a substantial increase in the price of motor vehicles. Frankly, we cannot help but believe that the concern expressed for the price the public will have to pay by requiring compulsory licensing is very minor when compared with the complete lack of concern for the price the public will have to pay expressed in the unrealistic and scientifically unsupportable vehicle emission standards set forth in other sections of the bill.

It seems to us we can follow traditional competitive processes, including those embodied in our patent laws, or we can decide that this is a problem of such national importance that it should be approached on the same basis as the atomic bomb project in World War II, the moon shot and other similar projects. None of these cost the public any more than the price they will have to pay as a result of the provisions of the Clean Air Amendments Act.

We, at Chrysler, frankly have favored the latter approach. We believe, when we are talking of possible costs to motorists of $3 to $5 billion a year, that this has become a project of such scope that maximum cross-fertilization of thinking between industry, Government and the academic community should be encouraged. We believe, when we are discussing a use of the nation's resources, a cost to the public and a decision as to national priorities of this magnitude, that it is ridiculous to try to approach it on the basis of a Federal law, which simply states that it is a problem for the vehicle manufacturers to solve, and which then attempts to come up with some minor compromise of the type contained in the patent licensing provision of the Act.

I hope this letter has been somewhat responsive to yours. While we realize that it does not deal solely with the patent issue, we hope it does make clear why we believe this issue cannot be dealt with separately from the overall context of the problem.

Sincerely yours,

PAUL A. HEINEN.

JACKSON, MISS., *April 12, 1971.*

HON. JOHN L. MCCLELLAN,
Chairman, Senate Subcommittee on Patents, Washington, D.C.

DEAR SIR: I have studied your S. 643 bill. I certainly believe that the forced licensing provision in the Clean Air Bill was ill-advised and I hope Congress enacts your amendment to it. I worked on construction a good many years and know about air pollution there at first hand. I worked at a refinery in 1923 and saw my first resinous wood paper mill two years later. I am surprised at the pollution hubbub. The change in controlling industrial pollution is almost beyond belief. But, of course, we can do better. However, we will need new technology. It will only come when inventors have conceived the new machines and methods and engineers have developed them to supply the new technology. It seems that Congress might better have offered some incentive instead of penalizing them.

I agree with the changes in the bill except for 148-and-154(b). I also agree with the amendments offered by Senator Scott, for the same reason that I disagree with 148 of S. 643. The question is judicial discrimination against the inventor or patent.

The proceeding set-up in sect. 144 is an appeal. The proceeding set-up in sect. 145 is a trial De Novo. Nothing is better established in American Law than the distinction between the two. In the appeal the ruling of fact appealed from is always presumed to be correct. But the trial De Novo is a new trial *and no* presumption of correctness is present. What 148 would do is to set up an entirely new doctrine of law to use against inventors. But it is even worse. In the action in 148, the Patent Office is the defendant in the action. Surely it is beyond belief to allow the opinion of one of the parties to have the force of law in a suit. It is an example of judicial discrimination. Sec. 154(b), no doubt, is well meant but I don't think it is feasible now. It would make the patent expire twenty years after the first application—which would be fine under ideal conditions. But the Patent Office is often behind in its work and even without this, delays often occur which the inventor cannot help. Moreover, I am inclined to think too much speed increases the chance for error. The cases show that many good patents were held up several years in the Patent Office for no good reason. (The False Teeth Case, for example). I feel the change may be another handicap for inventors.

The Scott amendment for statute 261 would simply restore to the patent some of its property rights which it had and give the patentee the same rights that owners of other property enjoy in Courts. The estoppel comes from the English law on deeds, which prevents one from giving a deed and contending that he never owned the land. Thus a man sold land belonging to his uncle, giving a deed. The uncle died, willing him the land. The Courts would not let him prove that the deed was invalid because he did not own the land when he gave the deed. In the Scott Paper Case, the Supreme Court allowed an officer of a corporation to prove his own fraud against his own stockholders (his wards), and infringe his own patent in the *hope* that the public would benefit if he were allowed to profit by his own wrongdoing. The amendment would prevent this.

Subsection (f) is a corollary to (e). It prevents a licensee from claiming the right to use a patent under a license, and denying that the patent is valid at the same time. It is supposed to have come from the general rule, that (a) cannot claim to have possession of a thing from (b), and in the same action claim (b) had no right of possession to give. (ex A tenant claiming possession under a lease and in the same action claiming that the leasor had no title.) To me the whole theory of judicial discrimination seems out of order in our American system.

The second part of subsection (f) and (g) refers to so-called misuse which perhaps is the most controversial subject in present patent law.

It should be remembered that so-called "misuse" is wholly a judicial doctrine without any congressional authority. It rests upon the theory that Courts have a right to go beyond Congress in matters of public policy for the public good. To some of us, it looks like judicial blackmail. Statute 284 provides that in a patent action, where the Court finds infringement and validity, it shall award the patentee damages not in any case, less "than a reasonable royalty for the use of the invention by infringer." But in "misuse" cases the Courts simply refuse to enforce the patent rights at all or award *any damages*. It makes no difference that the patentee has done nothing not allowable under the laws of Congress. He need only to have commercialized his invention in a way that the Court dislikes.

Most of the "misuse" doctrines have been brought out by the Department of Justice and are related to the ways of putting patents into commercial use. A large number are intended to force tbe patentee to do this in so cumbersome a way as to destroy the commercial value of the patent. An example was a drug for treating a disease in laying chickens. It had to be dissolved in the drinking water. The Patent Office required it to be claimed dissolved in the water. The Courts held that because the patentee sold the drug to the chicken owners and allowed them to put it in the water, instead of forcing them to buy both the water and the drug from him, he had "misused" his patent, and refused to enforce it! This is the kind of logic behind much of the "misuse" law.

(f) (g) I assume the amendments are intended to protect package licensing. In some industries, like T.V., many different patents must be used in one article. Some companies have many patents. It would be difficult to make terms and keep account for each of these individual patents. So a producer who wants to make a certain article contracts with some developing company to use any of its patents it finds it needs for a lump-sum. This seems to be the only convenient way such inventions could be commercialized, but the Department of Justice has been against the practice.

Statute 103

I, of course, agree with the amendments to 103 so far as they go. They have been due ever since the Courts started to rule the statute as an endorsement of the construction that the Cuno Decision gave to the Hotchkiss Case. But I note that all but the one regarding combinations of old elements are negative, and I wish some affirmative provision had been made which would have allowed for the use of tangible evidence, like the presence of a new function or application of a new principle of natural law. Chief Justice John Marshall ruled that the presence of a new function (or effect) was affirmative evidence of the presence of invention in Davis-V-Palmer—in 1827. (7-FC-159-Case 3645). It was always accepted as such until the Cuno Decision, where Justice Douglas thought Hotchkiss, where no new function or effect was present, overruled it. (The context shows Justice Douglas did not know the difference between a functional and non-functional result.) It was carried on by the Court of Customs and Patent Appeals until the John Deere Case.

Of course, the amendment on the combination claims will be a great step ahead if the Courts follow it. I have already expressed myself on the judicial attitude there. It is incredible that the Courts should be so lacking in mechanical aptitude. Mr. Cyril A. Soans, a retired patent attorney, has written a very recent book. It sounds somewhat like a reformed drunkard's description of the evil of drink. He is especially critical of the way the Courts have construed statute 103—which he helped write. As a general thing, I agree with him that the statute is entirely unrealistic and simply has been used to set up supposition as fact. Insofar as I ever knew, there is no valid reason for supposing the knowing about machines that won't work will suggest how to make one that will. History of invention bears this out. Eli Whitney had never seen cotton until shortly before he began to work on his gin. Morse taught commercial art and knew nothing about electricity until he started to work on the telegraph. Neither did Bell, who was a teacher, know about electricity until he started to work on the telephone. But to go on would make this letter too long.

With respect and best wishes,

Respectfully,

LOGAN R. CROUCH.

PATENT, TRADEMARK AND COPYRIGHT LAW SECTION,
THE BAR ASSOCIATION OF THE DISTRICT OF COLUMBIA,
Washington, D.C., May 26, 1971.

Re May 1971 PT&C Subcommittee Hearings.

Hon. JOHN L. MCCLELLAN
U.S. Senate,
Washington, D.C.

DEAR SENATOR MCCLELLAN: We appreciate very much the opportunity to provide this written statement relative to matters of great importance to our nation's business, economic and technological well being. Our objective in this statement is to be brief and to the point with respect to the proposed legislation which was the subject of the hearings.

Re Scott Amendments A.23 & A.24: The Bar Association of the District of Columbia has already taken a position favoring the Amendments in substantially the same form as introduced in the 91st Congress. We now reiterate this position of favoring the enactment of legislation set forth in the principles of the Scott Amendments.

A basic principle of the Scott Amendments is that expressed in Recommendation XXII of the President's Commission of 1966; i.e.—

(a) To prevent, by appropriate statutory provisions, certain patent utilization practices relating to asignment, license, or waiver of patent rights from becoming per se illegal or a misuse; but

(b) Not to create any exemption from the antitrust law for any conduct that could be shown in fact to have created an unreasonable restraint of trade or a substantial lessening of competition or formed a part of a conspiracy to monopolize.

We are also aware of consideration that has been, and continues to be, given to possibly revising the specific language of the Amendments so as to embody with even greater clarity and certainty the basic principles set forth in the proposed legislation. We support all efforts toward this goal, and are prepared to assist and work closely with your staff at any time and as called upon to do so.

Re S. 1252 (Inventor's Certificate): We support the enactment of the proposed legislation. The International Affairs Committee of this Section reported that the disclosure content of an inventor's certificate should be reliable. The report also expressed a considered opinion that the subject matter thereof may well receive a more rigorous examination within countries sustaining inventors' certificates than is provided currently within certain registration countries relative to their patent applications. Accordingly, and as indicated previously, we support favorable action with respect to this Bill.

Re S. 643—Section 6 (Mandatory Licensing): We support the proposed legislation to strike out Section 308 from the recent amendment to the Clean Air Act because its very existence does a disservice to the incentive to invent under our patent system. There is no need for the substance of a Section 308—and, accordingly, striking out this Section will eliminate all "negatives" and restore all of the "positives" under our patent system.

Re S. 1255 (Fees): We are opposed in principle to any increase in fees. Nevertheless, and although disappointed, we recognize the practical necessity for an increase in fees. We urge that deterrents to the filing of patent applications be minimized—and, in this connection, urge no change in the application filing fee.

We support the proposal for a fixed issue fee. This just makes good sense from the standpoint of easing administrative burden within the Patent Office as well as for applicants and their respective attorneys.

Thanks again for the opportunity to provide this written statement. Your continued interest in, and understanding of, the U.S. patent system is most assuring and greatly appreciated.

Very truly yours,

JULIUS JANCIN, JR.

THE DOW CHEMICAL COMPANY,
Midland, Mich., May 13, 1971.

Senator JOHN L. MCCLELLAN,
Senate Office Building,
Washington, D.C.

DEAR SENATOR MCCLELLAN: I am writing this letter for the purpose of expressing views on certain portions of the amendments to S. 643 introduced by Senator Scott as Amendments Nos. 23 and 24. It is our belief that insufficient consideration has been given by the opponents of the Scott Amendments to the particular needs of the chemical industry with respect to the licensing practices embraced by these amendments. These comments will, however, be selective to those portions of the Scott Amendments which in our opinion merit the special concern of your subcommittee and the Congress. They will indicate our strength support for those portions of Amendment No. 24 relating to Section 261 and for Amendment No. 23 relating to Section 301 of S. 643.

SECTION 261(b)(2): FIELD-OF-USE LICENSING IN CHEMICAL INDUSTRY

While we feel there is ample justification on general principles for securing the rights of a patentee to license his patents by any fractionation of his total grant, which would include the right to license by territory, fields of use, quantity, and the like, the chemical industry presents a special and compelling situation in regard to field-of-use licensing. It is peculiarly the nature of the chemical industry that chemical inventions usually possess prospects for uses totally beyond the knowledge and capabilities of the inventors to perceive. The reason is that the properties of chemicals in different environments and combinations offer opportunities for use that can only be foreseen by those having special interests and aptitude in fields that utilize those properties. In most instances, the properties of a new compound are only determined with respect to certain basic parameters related to the use contemplated by its inventors. It is this parochial view of chemical inventions, necessarily limited by the interests of the inventors, that makes the chemical field fertile for subsequent inventions by others. But those others need an incentive, as did the original inventor, for investment in the development of the new uses or new combinations.

Faced with this prospect, it is clear that in the chemical industry a license by field of use offers a way for subsequent inventors in different fields to make the most of new compounds and to secure their investment insofar as possible by working under the shelter of exclusive field-of-use licenses under the compound patent.

Opponents of the Scott Amendments and of the concept of field-of-use licenses have somewhat softened their opposition in the face of the overwhelming logic of this form of licensing. But, unfortunately, there remains influential sentiment that would surround the exclusive field-of-use license with such restrictions as would, in fact, discourage such licensing or make it difficult or impossible to implement. For example, some insist that such licenses only be granted on a showing that exclusivity is necessary to secure the funds for investment in the development. The burden of such a showing would be unrealistic in the real life of business, where opportunities must be moved upon rapidly and free of the uncertainties that would accompany attempts to comply with such requirements.

An example of the short-sighted predilection against exclusive field-of-use licensing is the statement by a representative of the Antitrust Division, published in the May, 1970 issue of the Michigan State Bar Journal, in which the author states:

"It appears most unlikely that it could be established that exclusive field-of-use licensing is necessary for there to be any license at all . . . It is usually desirable to license others in order to promote the widespread sale of the patented product and thus stimulate demand . . . Therefore, the burden of providing absolute economic necessity for an exclusive field-of-use restriction should not rest heavily upon the defendant."

This language clearly does not contemplate the realities of chemical inventions, where exclusive licensing by field of use often is followed by considerable investment in development before a product is available for market. If the patent system functions to provide incentives for the inventor in the first instance, it is certainly applicable to the efforts of further development necessary before additional fields of use for the patented chemical compound can be exploited.

The same author exemplifies the evils of exclusive field-of-use licenses by referring to the grant of rights by a patent owner to develop and sell a product for animal use, while retaining the right to develop and sell the patented chemical compound for human consumption. This argument, again, does not contemplate the reality that the capabilities and interests for human and for veterinary use seldom are found in the same company, even though the underlying technology may be closely related. It would, indeed, be unforgivable to preclude a veterinary drug manufacturer who synthesizes and patents a chemical compound from granting an exclusive license which would make it economically feasible for a manufacturer of drugs for human consumption to carry the development into that field.

Indeed, we have a good example of this type of problem in a recent license agreement with another chemical manufacturer. The company approached Dow with a proposal for an exclusive field-of-use license that would enable them to undertake development of a strong, light-weight substitute for the conventional plaster cast building on a Dow patented invention .The uncertainties of ultimate success, the extensive and costly development involved, and the necessity (if the development was successful) for a program of education of medical personnel who would be using the new cast all combined to make it perfectly clear that an exclusive field-of-use license was justified.

While sometimes giving grudging support to the exclusive field-of-use concept, opponents of these amendments view the grant of a *non*exclusive license to a field of use with even greater skepticism. They forget entirely that one or two or three licenses depart only fractionally from the concept of the exclusive license and that too many licenses dissipate the incentive of the patent grant as though there was no patent at all. Because in some instances, and in combination with certain other acts, opponents of the Scott Amendments can conceive of activities of a licensor that might offend certain provisions of antitrust, they would prefer to limit entirely the right of the patent owner to restrict his number of licensees beyond one and require that he license all comers. In the chemical field, this is simply not practical. Incentive to invest must operate in the hands of the licensee for carrying the basic invention into other fields just as it did for the inventors of the compounds themselves.

We submit that antitrust still would live and breathe where practices involving a field-of-use license in conjunction with other acts combine to offend and would be prosecuted, quite properly, as antitrust violations. But to forbid or unreasonably restrict the practice of licensing by field of use, either exclusively or nonexclusively, on the tenuous theory that the use of this practice could in some way, under some circumstances, or in some combination with other practices, lead to an antitrust violation is to lose the baby with the bathwater.

We hope you will not be swayed from support of these amendments, or the Scott Amendments in general, by the argument advanced from some quarters that the patent system does not have a legitimate role in encouraging investment, as distinguished in the minds of some from the act of inventing. Certainly, invention and investment in the people and tools for inventing cannot be separated in the patent context. Perhaps before research became such a highly organized endeavor it was realistic to speak of the incentive to invent as referring exclusively and literally to the act of inventing. But today this is not realistic. One need not refer to statistics to appreciate the substantial developments coming from industrial and university research laboratories. It is the encouragement of the mobilization of resources in an assault against a problem that is of foremost importance in that kind of research. The Constitution cares not in the least whether the ultimate progress in the useful arts stemed from encouragement of the individual to invent or encouragement of companies to invest in individuals and equipment to the same end. Both are part of the scene, and both are fostered by the unfettered freedom to license by field of use.

SECTION 261 (e) AND (f) : THE LEAR PROBLEM

You are, I am sure, well acquainted with the Supreme Court's decision in Lear v. Adkins. Of present concern is the holding in Lear that a licensee can challenge the validity of a patent under which he is licensed at any time even though he had agreed not to do so. The Supreme Court regarded the public policy considerations of identifying and dispatching invalid patents as outweighing the enforcement of private contracts. If this is to be the law, however, the patent owner needs protection against the licensee who would accept a license in order to be assured of the right to practice the invention and, then, without renouncing the license, challenge the patent, knowing that (1) if he loses and the patent is held valid he can continue to practice, and (2) if he wins and the patent is struck down he will be relieved of future royalties. (There are those who even argue that, despite the obvious benefits enjoyed by the licensee, the patent owner should refund the royalties previously paid.)

Senator Scott's Amendment No. 24, in the form of Section 261(f), would at least require the challenging licensee to renounce his license before commencing the challenge. There comes a point when fairness to the licensor should also be considered, and we believe this is it. The challenging licensee should not be permitted to have it both ways, that is, fight the patent but retain his rights under the license if the patent is held valid. The current climate in the federal courts, some of which almost never hold patents valid, places the licensing patent owner in constant jeopardy, particularly where the licensee can choose the federal court best calculated to strike the patent down in a declaratory judgment action.

Another undesirable situation would be arrested by this Amendment No. 24. With the high cost of litigation, the Lear decision gives the licensee a sort of hip-pocket trump toward the end of the period of the license. There is an increasing tendency for licensees to challenge the validity of the licensed patent when the period remaining in the life of the patent or the license is calculated to produce less income for the patent owner than the expense of a law suit defending the patent. This becomes simply a matter of mathematical projection, and the patent owner is trapped. Defense of a suit on a patent today frequently runs $150,000–$200,000, and higher, the costs being largely in the control of the plaintiff, who in this instance would be the licensee asserting the patent's invalidity. A provision as found in Amendment No. 24, by which the challenging licensee would be required to renounce his license, would provide some protection to the patent owner while still enabling a good faith challenge to go forward.

SECTION 301 : THE CHEMICAL INDUSTRY'S CONCERN WITH PREEMPTION

Finally, we are much concerned about the concurring view in Lear of Justice Black, in which he was joined by Justice Douglas, to the effect that no rights to trade secrets or confidential information should be enforceable by private contract. The very considerable income to American companies from licensing trade secrets and proprietary information in this country and abroad has been documented elsewhere, and I am sure you have ample data in this regard. Here at Dow, we pride ourslves in the development of chemical processes whose success depends on the many combinations of small improvements which together produce results not easily attainable by our competitors. Even when not patentable, we license such processes as trade secrets, and we sometimes thereby recover the considerable costs of development and even earn a profit.

The enforcement of private contracts respecting trade secrets was part of the common law brought to this country at its founding. There is no suggestion in the Constitution that any preemption was intended by the adoption of special protective legislation concerning inventions which can meet certain prescribed requirements. Inventors (and their assignees) should, in our considered view, continue to enjoy the privilege of selecting the path of disposition of trade secrets and proprietary information, necessarily accepting both the privileges and risks of each approach. While the trade secret route is unlimited as to time, it suffers every day the possibility that someone else may discover the same information and, indeed, obtain a patent on it, which would in most instances preclude the original inventor who chose the trade secret route from continuing to practice his own invention. The patent route, on the other hand, gives more assured protection in exchange for public disclosure of the information, but this approach, too, has its vagaries in the hands of the courts.

While many in the field were not greatly alarmed at the comments by Justice Black, we have now seen a decision out of a federal district court in New York, Painton v. Bourns, which actually adopts Justice Black's concept in most positive language. This decision has just been reversed on appeal, but we still cannot rest with any security in our licensing of process information not the subject of patents. In our view legislative intervention such as expressed in Senator Scott's Amendment No. 23, which would insert a new Section 301 in S. 643, is earnestly commended to your favorable consideration.

We do not express particular support for the amendments to Section 271, either in the form of the original Amendment No. 24 or the changes thereto suggested by the Tuesday-2 Group. We find much to be desired in proposed Sections 271(f) and (g), but we feel that Section 261 and Section 301 represent solutions to such serious problems that we hesitate to suggest an irrevocable unity between those two sections and the changes to Section 271. It is clear to us that portions of Section 271, notably subparagraph (f)(1), have drawn considerable fire from opponents of this legislation. Should the occasion arise for compromise, we would favor and urge the severability of these provisions and the retention of the amendments to Sections 261 and 301.

I would only add that the Patent Bar and industry generally are sincerely appreciative of the attention you have given patent-antitrust problems in the past. Since the now famous Recommendation 22 of the Report of the President's Commission on the Patent System, in 1966, you have repeatedly indicated concern for the treatment of this subject. I refer to your remarks accompanying the introduction of S. 3892 in 1968, S. 1246 in 1969 and S. 2756 in the same year. It is our sincere hope that your successful efforts to obtain jurisdiction of these amendments in connection with S. 643 will result in disposition of many of the problems in the patent-antitrust area. Like you, we look to solutions that will be in the public interest and advance the proper purpose of the patent system, but we note that much of the latter can be thwarted by inappropriate restrictions on the right of the patent owner to put his patent to work.

Very truly yours,

A. R. WHALE,
Manager, Organic Chemicals Section, Patent Department.

ESB, INC.
Philadelphia, Pa., April 29, 1971.

Senator JOHN MCCLELLAN,
Senate Office Building,
Washington, D.C.

DEAR SENATOR MCCLELLAN: Enclosed are three copies of a speech which I will deliver to the joint meeting of the Pacific Industrial Property Association and the National Association of Manufacturers Patents Committee on May 6, 1971. The topic of this speech is the U.S. patent system and the freedom of licensing patents, technology and other intellectual industrial property rights.

I understand that your Senate Judiciary Subcommittee will hold hearings on May 11 and 12 to receive testimony relating to the Patent Revision Bill which you re-introduced in the 92nd Congress as S. 643 and the Amendments 23 and 24 to S. 643 which have been re-introduced by Senator Hugh D. Scott. I would appreciate the introduction of this speech into the record of your Subcommittee Hearings. You will note that I fully support the amendments introduced by Senator Scott, and I urge passage of the Scott Amendments as part of your Patent Revision Bill.

Thank you for your consideration of this matter.

Sincerely,

E. J. DWYER.

Enclosures.

SPEECH BY EDWARD J. DWYER, CHAIRMAN OF THE BOARD OF THE NATIONAL ASSOCIATION OF MANUFACTURERS, TO THE PACIFIC INDUSTRIAL PROPERTY ASSOCIATION AND NAM PATENTS COMMITTEE IN WASHINGTON, D.C. ON MAY 6, 1971

I am very pleased to see once again so many of my friends on the NAM Patents Committee. It is also a pleasure to have this opportunity to meet many new friends who are associated with the Pacific Industrial Property Association. The continuing rapid growth of this international industrial association clearly demonstrates its important role in the advancement and development of industrial property in the international marketplace.

Though capital and labor are important elements of an industrial enterprise. The full utilization of science and technology is essential to the production of goods demanded by the people of all nations. The industrial revolution has been succeeded by the technological revolution. In this era of the computer, industrial organizations will have to be even more creative and versatile in employing the tools of technology for the betterment of mankind. I am sure that everyone present at this meeting is devoted to bringing prosperity and a better life to more people throughout the world.

I believe that the patent system in which inventions and improvements are disclosed to other persons skilled in the industrial arts to yield still more inventions will play an ever increasing role in the advancement of technology. As stated in the Constitution of the United States, the purpose of our patent system is to promote the progress of science and useful arts, and it has fulfilled this purpose. The importance of the patent system was reaffirmed by one of our great presidents, Abraham Lincoln, who said, "The patent system added the fuel of interest to the fire of genius." I am also convinced that the best method for providing the fruits of man's creativity to all nations is through international patent cooperation.

When the Patent Cooperation Treaty was recently approved on a diplomatic level, as a former patent attorney, I was pleased that the representatives of the many nations participating in the conference had the foresight and cooperative spirit to resolve the issues in a statesman-like manner.

Many of you here today played key roles in drafting the Patent Cooperation Treaty and will continue to provide sound advice and support in implementing the treaty.

It was evident in your discussions this morning that the freedom of licensing patents, technology and other intellectual industrial property rights has become a critical issue in the United States, particularly as a result of recent court decisions and governmental antitrust activities. The freedom to license patents and know-how vitually affects international trade and technological development and is not solely a domestic issue. Actually, the resolution of this matter is of vital interest to inventors and industrial organizations in Japan, Europe and throughout the world, including both developed and under-developed nations. As recently stated by Circuit Judge Kiley, the general rule favors the broadest freedom in the use or sale of rights under the patent law of the United States.

Unfortunately, some United States Government officials are opposed to freedom of licensing and have been attempting to establish restrictions and limitations in the guise of antitrust violations covering the licensing of patents and technology. Senator McClellan has re-introduced the Patent Revision Bill to the 92d Congress, and Senator Scott has re-introduced amendments to this bill seeking to clarify and preserve the freedom of licensing of patents rights and know-how. I urge your support for thes amendments.

The restrictions placed on the use and sale of patented inventions are technology developed by creative individuals and industrial innovators are impeding national and international economic progress. From a global viewpoint, American industry wants to satisfy the needs of other nations, and at the same time, partake of the benefits from the latest international technological developments. I submit that this can be accompanied best by preserving the patent system and the freedom to fully utilize patent rights and technology.

The Secretary of Commerce, Maurice Stans, has indicated that during the past few years our technological balance of payments has also been declining. This is directly related to the technological progress in the world today. There is certainly more research and scientific competition challenging our creativity, particularly in Japan. But another factor may be the decline of innovative activity throughout American industry because of restrictions placed on full utilization of patent rights and technological developments.

We should appreciate the fact that licensing enables the international transfer of highly useful knowledge which leads to an increasing flow of products for the betterment of everyone. As consumers, we must have protection as reflected in fair practices and pricing which are important objectives of antimonopoly laws. At the same time, as a society dependent on industrial viability, companies such as mine must be competitive. It is imperative to note that in order to go forward as originators and not become copiers, harrassment of our ability to fully utilize our technological developments must cease. Otherwise, we will not be able to enjoy the fruits of our ingenuity. In order for individuals and industrial organizations to establish fair and lasting license agreements domestically and on an international level, I believe that further assurance is required from our Congress, and again I urge passage of the Scott amendments to the Patent Revision Bill.

To the Japanese members of the Pacific Industrial Property Association, I want to extend my special hope that you are enjoying your visit to this country and my best wishes for a safe journey home. Sayonara.

UNIVERSITY OF OREGON,
DEPARTMENT OF ECONOMICS,
Eugene, Oreg., May 12, 1971.

SUBCOMMITTEE ON PATENTS, TRADEMARKS & COPYRIGHTS,
Old Senate Office Building,
Washington, D.C.

GENTLEMEN: Please include in the record of the hearings on S643 my opposition to the four-page Scott bill dated March 19, 1971, proposing certain amendments to S643. The purpose of these amendments appears to be to preclude by law various applications of the antitrust laws to restraints of trade that are cloaked as use of patent rights, and in the process to reverse parts of the law as it has been applied by the courts in cases by which the boundary between the patent laws and the antitrust laws has been carefully established.

The bill contains several amendments. The first of these, which would appear on page 37 of S643, would include a statutory guarantee of exclusive rights under patent applications, and would authorize the applicant to license these rights exclusively. Its practical affect would be to enable an applicant for a patent to control the technology covered by his application as though the application had been granted. The exclusive rights thus established would be broader than those that flow from patents themselves: Rights would attach not only to applications that eventually become patents but also to excessive claims in these applications, such are rejected by the Patent Office in determining the scope of an invention, and to applications that the Patent Office rejects in full. Were the amendment to become law, an applicant for a patent would be wise to keep his application pending for the maximum possible time, since decision by the Patent Office might destroy or materially curtail exclusive rights obtained by him by merely filing his application.

This amendment contains language, applicable both to patents and to applications for patents, that guarantees the right of the patentee or applicant to convey exclusive rights, by license or otherwise, for the whole or any part of the United States. In its bearing upon patent applications, it is objectionable for the reasons given above. In its bearing upon patents it unwisely stretches rights that, within proper limits, would be unobjectionable. There are doubtless instances in which exclusive license of a patent for a part of the United States results in use of an invention over a wider territory than that in which the patentee would use it, and in which the licensee would not be able or willing to use it if his rights were non-exclusive. In such instances territorially exclusive licensing is consistent with the Constitutional purpose of the patent law to foster the industrial arts. But there are also instances in which licensees are protected from competition with one another by exclusive territorial licenses that are not necessary to bring about use of the patent throughout the United States,—instances in which the restriction protects the licensees rather than the patentee and retards the industrial arts instead of promoting them. In the latter type of scheme, full territorial protection for licensees, giving each licensee the exclusive right to vend the subject matter of the patent in a given territory, can be, in its effects upon national trade, the equivalent of a system of prohibitive private protective tariffs applied to internal trade.

Statutory authorization of territorial exclusivity would validate not only the harmful or useful divisions of territory but also the harmful ones, and would protect the latter from attack under the antitrust laws. In a general revision of the Patent Laws the proper aim should be, not thus to authorize territorial exclusivity indiscriminately, but to distinguish restrictions that are consistent with the Constitutional purpose and with antitrust policy from those that are not.

The second amendment proposed in the bill, applicable to page 38 of S643, appears to be intended to change the law as declared unanimously by the Supreme Court in Lear v. Atkins. It would deprive licensees of the right to contest the validity of patents under which they are licensed unless they first unconditionally renounce all future benefit from their licenses. The effect of this provision would be to facilitate the continued enjoyment of patent monopolies under large numbers of invalid patents. According to such figures as I have been able to find, from half to two-thirds of all patents that are tested in infringement suits are declared invalid, and the proportion has been rising. This condition constitutes a problem for which the proper corrective is greater care in issuing patents and harmonization of the principles of validity applied by the Patent Office and the courts. Meanwhile, however, the United States is burdened by a substantially larger array of patent monopolies than are appropriate to the inventions actually made. To encourage action by business that is likely to reduce the number and scope of monopolies under invalid patents would be wise public policy. At present, an enterprise confronted by a patent that purports to give the holder monopoly rights must often choose among three options: to accept license under the patent with whatever costs and restrictions this involves, to abstain from use of patented technology that its competitors are using, or to risk the money penalties of an infringement suit. With the process by which patents are issued as slipshod as it now is, the fact that the patent exists is not adequate to guide the enterprise in this choice. If choice of the first option were to bar the enterprise from challenging the patent, challenges could come only from enterprises willing to risk technological backwardness or to incur, along with the costs of suit, the risk of damages for infringement. Challenges would be fewer and those who derive monopoly from invalid patents would be less vulnerable. Until the United States makes patents more reliable as evidence of patentable invention, it should not prevent enterprises that desire to use patented technology from taking licenses while they ascertain whether or not they are correct in suspecting that the licensed patents are not valid.

The third amendment proposed in the bill, an insertion on page 39, would bar use of the antitrust laws against various types of restrictions in licenses that are at present either unlawful or of doubtful legality. The new subsection (f) is couched in language so general that its full sweep, when tested by litigation, is difficult to forecast. Whatever may be its boundaries, however, it clearly would make an antitrust proceeding more difficult wherever the restrictions in a license could be plausibly described as beneficial to the patent owner. If, for example, an owner of a product patent who did not produce the patented product were to prescribe the prices at which his licensees should sell that product, the restriction would be for the benefit of the licensees; but a showing that the licensees were willing to pay larger royalties for protection of their prices than they would be willing to pay without price protection could be used to contend that sale of the patentee's services as price-fixer enhanced his benefits from his invention and hence was authorized by the statute.

Decision in this type of case would depend upon the meaning applied to the phrase "reasonable under the circumstances". The meaning of this phrase probably would be tested by litigation in numerous instances in which the law is now regarded as clearly prohibitory, so that the immediate effect would be to becloud various useful antitrust precedents. Possibly these precedents would be reversed; for one could plausibly argue that by enacting this part of the statute the Congress intended to change in some substantial way the judicial interpretations of statutory language that were currently in effect.

Indeed, since the proposed language applies explicitly to what might be, but for it, "illegal extension of patent rights", the provision could be interpreted to overrule numerous cases that hold that patent monopolies cannot be extended to cover unpatented subject matter. A patentee is now precluded from conditioning a license for a patented machine upon the licensee's use, in that machine, of unpatented materials bought exclusively from the patentee. Yet if such a restriction were applied it might often enhance the patentee's benefits. When this is so, the proposed amendment could be interpreted to mean that even such extensions of patent rights beyond the boundary of the patent must be reconsidered to determine whether or not they were "reasonable under the circumstances".

The new subsection (g) to be inserted on page 39 contains language that apparently validates certain restraints of trade that take the form of payments by licensees for the use of patent rights. The second numbered paragraph of this subsection makes lawful royalties and fees in any amount, however paid or measured, provided they pertain to the period before the patent expires. It would be possible for a wide variety of substantive restrictions to take the form of a schedule of fees. Production by a licensee could be limited by a prohibitive fee for production in excess of a stipulated quantity, or for production of specified kinds of goods; fees could be prohibitively high for sale in specified territories; fees could be so related to the prices charged by the licensee as to force him to charge the price preferred by the patent-owner; fees could be charged on the patentee's entire output, including parts of it in which the licensee did not use the patent; and fees could be set at prohibitive levels upon any part of the licensee's production in which he used patents licensed by a rival patentee. Discrimination in the fees paid by different licensees is explicity authorized. So are lump-sum fees that cover a whole group of the patentee's patents and thus have a tying effect that deprives the licensee of the right to hire and use only the patents he wants. The legality of such schemes is guaranteed without regard to the purpose of the patentee, the affect upon competition between patentees or between licensees, or the effect upon the industrial arts.

Sincerely,

CORWIN D. EDWARDS,
Professor of Economics.

WASHINGTON, D.C., *July 13, 1971.*

Hon. JOHN L. MCCLELLAN,
Chairman, Senate Subcommittee on Patents, Trademarks, and Copyrights,
Old Senate Office Building,
Washington, D.C.

DEAR SENATOR MCCLELLAN: As Chairman of Committee 404 of the American Bar Association Section on Patents, Trademarks, and Copyrights, I respectfully request that the enclosed Article entitled *The New Doctrinal Trend,* which first appeared in the February, 1948 issue of the Journal of the Patent Office Society, be reprinted as a portion of the appendix to the transcript of the recent hearings held by your Subcommittee on the Scott Amendments.

This paper is now regarded as a classic article on the important question of what makes a particular invention a great invention. Because of its age, copies of the article are now difficult to secure, and we feel that it would be both timely and appropriate to have it reprinted as a portion of the appendix to these very important hearings.

The authors, Laurence B. Dodds and Francis W. Crotty, have each personally given me permission for this reprinting of their article.

Sincerely yours,

MARCUS B. FINNEGAN.

"The New Doctrinal Trend" ‡

By
LAURENCE B. DODDS *
and
FRANCIS W. CROTTY †

A matter of utmost concern to all persons interested in a strong patent system is the general impression of the Federal Courts that all of the great and startling inventions belong in historical limbo and that current advances in the art, submitted as inventions in patent litigation, are minor, uneventful, evolutionary increments in the steady march of technical progress.

This fallacious impression is based on a preconceived notion that the truly great inventions of history have "burst full-blown from Athene's brow" during some incandescent flash of the inventor's genius and that all true inventions are born by a similar parthenogenetic process.

As a matter of fact, the record establishes that the majority of the great and classic inventions which have been tested in the Courts were hemmed about by the near inventions of many others and that, in each case, they represented that small advance which converted failure into commercial success. It will be developed below that if Bell's telephone, Tesla's induction motor, Westinghouse's air brake, Edison's electric lamp, to mention but a few, were to come before the Courts today, the prior art was so close that the strong probability is that each would be found to lack that flash of creative genius necessary to support invention and the respective patents would have been declared invalid! Yet each of these inventions, from a historical perspective is acclaimed as an outstanding achievement which established a whole new industry.

This article will make no attempt to restate the many factors which establish the direct relationship between

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the strength of this country's patent system and the amazing acceleration of its technological progress over the last century. That has been done ably and frequently by many individuals and committees. The starting point of this discussion is the assumption that the reader has fundamental faith in the value of our patent system and agrees with the basic tenets included in the First Report of the National Patent Planning Commission [1] to the late President Roosevelt. That report included the following:

> *The American patent system* established by the Constitution giving Congress the "power to promote the progress of science and useful arts," is over 150 years old. The system has accomplished all that the framers of the Constitution intended. It *is the only provision of the government for the promotion of invention and discovery and is the basis upon which our entire industrial civilization rests.*
>
> The American people and their government should recognize the fundamental rightness and fairness of protecting the creations of its inventors by the patent grant. The basic principles of the present system should be preserved. The system has contributed to the growth and greatness of our nation; it has:
>
> (1) encouraged and rewarded inventiveness and creativeness, producing new products and processes which have placed the United States far ahead of other countries in the field of scientific and technological endeavor;
>
> (2) stimulated American inventors to originate a major portion of the important industrial and basic inventions of the past 150 years;
>
> (3) facilitated the rapid development and general application of new discoveries in the United States to an extent exceeding that of any other country;

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[1] The National Patent Planning Commission was established by Executive Order No. 8977 of President Roosevelt dated December 12, 1941. The Commission comprised Dr. Charles F. Kettering, Chairman of the National Inventors' Council and Vice-President of General Motors Corporation in charge of its Research Laboratories; Chester C. Davis, Member of the Board of Governors of the Federal Reserve System; Francis P. Gaines, President of Washington and Lee University; Edward F. McGrady, formerly First Assistant Secretary of Labor, then in charge of Labor Relations for Radio Corporation of America; Owen D. Young, Honorary Chairman of the Board of the General Electric Company and Member of the Boards of Directors of Radio Corporation of America, the National Broadcasting Company, and the Federal Reserve Bank of New York City; Andrey A. Potter, Executive Director; and Conway P. Coe, then Commissioner of Patents, Executive Secretary.

(4) contributed to the achievement of the highest standard of living that any nation has ever enjoyed;
(5) stimulated creation and development of products and processes necessary to arm the nation and to wage successful war;
(6) contributed to the improvement of the public health and the public safety; and
(7) operated to protect the individual and small business concerns during the formative period of a new enterprise.

The strongest industrial nations have the most effective patent systems, and after a careful study, the Commission has reached the conclusion that the American system is the best in the world. (Italics added)

In passing discussion of the importance of the patent system in promoting "the progress of science and useful arts" (Constitution, Article I, Sec. 8), the writers cannot resist reference to an anecdote recently reported by former Commissioner of Patents Casper W. Ooms at a symposium on Patents and Industrial Research sponsored by the National Association of Manufacturers in New York on December 7, 1945. In that address he recalled:

I had an arresting demonstration of the value of the patent as a stimulus the day after I took office. An elderly gentleman, vigorous in his eighties, came to see me and announced himself as Noah Amstutz of Valparaiso, Indiana, patent attorney. "Valparaiso," I said to him, "brings two things to mind. When I was a boy my father drove a single-cylinder Cadillac. We frequently drove to Valparaiso for lunch. We could just make it from the South End of Chicago in half a day, what with changing two tires on the way, eat luncheon, and return in the afternoon." Then I added, "There is a set of telegraph instruments in the Smithsonian Institution by which a man in Valparaiso sent a picture thirty miles by telegraph in 1891. Do you happen to know anything about that?"

Amstutz beamed. "Those are my instruments," he said. "I gave them to Smithsonian. Did you ever hear of my two-way television in 1895?"

A few days later I went through the voluminous scrapbook of this inventor, working on facsimile transmission and television in the early 1890's. His instruments were marvels of workmanship. His television circuit, I am convinced, with more delicate photoelectric pickups than were available to him, and some means of synchronizing his sending with his receiving instruments, would have worked. Here were years of labor spent a generation before these concepts were recognized by commercial development. I asked Amstutz, who was a craftsman living by his own labors, what spurred him on in this almost endless work. His reply was simple, "I wanted to patent my inventions and earn money from their production."

It is generally recognized that the popular impression of the progressive deterioration of the quality of invention has pervaded a great many of the decisions of the Federal Courts, particularly the Circuit Court of Appeals for the Second Circuit and the Supreme Court, and this trend has built up in a steady crescendo during the last fifteen years. This impression is manifested by such statements as that of Mr. Justice Douglas in *Cuno Engineering Corporation* v. *Automatic Devices Corporation,* 314 U. S. 84; 51 USPQ 272.

> We may concede that the functions performed by Mead's combination were new and useful. But that does not necessarily make the device patentable. * * * That is to say the new device, however useful it may be, must reveal the flash of creative genius not merely the skill of the calling. If it fails, it has not established its right to a private grant on the public domain.

This extreme view was taken up and amplified by the Circuit Court of Appeals for the Second Circuit in the case of *Picard* v. *United Aircraft Corporation,* 128 F.(2d) 632; 53 USPQ 563, in which Mr. Justice L. Hand said:

> We cannot, moreover ignore the fact that the Supreme Court, whose word is final, has for a decade or more shown an increasing disposition to raise the standard of originality necessary for a patent. In this we recognize a pronounced new doctrinal trend which it is our duty, cautiously to be sure, to follow, not to resist.

The same misconception undoubtedly underlay the apocryphal story of the fear attributed to former Commissioner of Patents Ellsworth in his letter of resignation to the State Department in 1845 in which he offered as his reason for resigning the view that the limits of human ingenuity already had been reached, and that the prospects for further important work by the Patent Office appeared dim. Commissioner Ellsworth was finally cleared of this blot on his escutcheon by a research project of Dr. Eber Jeffrey reported in the Journal of the Patent Office Society, Vol. 22, page 479.

There is a ray of hope found in the indication that a few of the outstanding jurists of our time have not succumbed to this "new doctrinal trend." Perhaps the most forceful dissent is that of Mr. Justice Frankfurter in his dissenting opinion in *Marconi Wireless Telegraph Company* v. *United States,* 320 U. S. 1 (1943):

> To find in 1943 that what Marconi did really did not promote the progress of science because it had been anticipated is more than a mirage of hindsight. Wireless is so unconscious a part of us, like the automobile to the modern child, that it is almost impossible to imagine ourselves back into the time when Marconi gave to the world what for us is part of the order of our universe. * * * For all I know the basic assumption of our patent law may be false, and inventors and their financial backers do not need the incentive of a limited monopoly to stimulate invention. But whatever revamping our patent laws may need, it is the business of Congress to do the revamping. We have neither constitutional authority nor scientific competence for the task.
>
> * * *
>
> Until now law has united with almost universal repute in acknowledging Marconi as the first to establish wireless telegraphy on a commercial basis. Before his invention, now in issue, etherborne communication traveled some eighty miles. He lengthened the arc to 6000. Whether or not this was "inventive" legally, it was a great and beneficial achievement. Today, forty years after the event, the Court's decision reduces it to an electrical mechanic's application of mere skill in the art.

Judge Lenroot, in the case of *In re Shortell,* (CCPA 1944) 142 F.(2d) 292; 61 USPQ 362, also resisted the trend, saying:

> While recognizing, of course, that it is the duty of this court to follow the law as declared by the Supreme Court, we do not conceive it to be our duty to change our basis of decision merely because some courts assume that there is a "new doctrinal trend" with regard to the standards required for invention.

In our opinion it is not within the province of the courts to establish new standards by which invention is to be determined. It seems clear to us that the creation of new standards for the determination of what constitutes invention would be judicial legislation and not judicial interpretation.

It follows, from the foregoing, that until Congress shall otherwise legislate, or the Supreme Court shall otherwise specifically hold, this Court will continue to hold that if a process or thing constitutes patentable subject matter, is new and useful, and the process performed or thing produced would not be obvious to one skilled in the art, invention should be presumed and a patent may properly issue therefor.

Unfortunately, Mr. Justice Frankfurter and Judge Lenroot did not have any concrete evidence to demonstrate conclusively the fundamental error in this "new doctrinal trend." It is the purpose of this discussion to develop such evidence.

From reading all decisions in patent cases for many years and from watching the individual reactions of trial and appellate judges in many hard-fought litigations, there is found a perfectly natural basis for the growth of this spurious "new doctrinal trend." In so many cases the attorney for the plaintiff, a patent owner, in his opening statement to the Trial Court or his argument to the Appellate Court builds up invention of the patent in suit: the shortcomings of the prior devices; the long-felt need for a solution to these shortcomings; the struggle of the inventor to solve the problem; the startling advantages of the invented apparatus; and the ensuing commercial success. The Judge is nearly always considerably impressed. Then comes the disillusionment when the attorney for the defendant pricks the balloon. His attack also follows a rather stereotyped pattern and includes as defenses various technical defects in the patent instrument such as indefiniteness, inaccuracy or inoperativeness, functionality of claims, etc., and finally comes the bombshell: what the inventor has done is not at all an invention but a mere trivial departure from a host of examples of the prior art, each better known than the other and each, on paper, bearing a striking resemblance to the invention.

This disillusionment of the Court generally survives the rebuttal evidence of the plaintiff: that each of those examples of the prior art was in evidence for many years; that each was impractical and made no impression on commercial practices; that the apparent striking resemblances between the patented apparatus and the examples of the prior art are only superficial and that there are basic deficiencies in such prior art which account for their impracticality; that it is the very "trivia" added by the inventor that converted the impractical prior art device into a commercially successful one; and finally that many persons skilled in the art had attempted in the intervening years to convert those impractical examples into practical ones and had failed.

As a result, the Judge reluctantly reaches the conclusion that what the patentee has done was to take one of those almost imperceptible steps that lie clearly within the experience and skill of the routine worker in the art.

What the Court fails to realize is that the foregoing picture is typical of virtually *all* patent litigation and has been since the inception of our patent system. And this has been true even in the case of the majority of the great and classic inventions. It was true, for example, in the case of Edison's incandescent electric lamp, Glidden's barbed-wire fence, Bell's telephone, Tesla's induction motor, and Westinghouse's air brake for railroads.

Let us examine the records of these great inventions in the light of the prior art advanced in the litigation involving them to see how closely they were approached by other workers in their respective fields.

ELECTRIC LAMP (Incandescent)—Thomas A. Edison

Patent No. 223,898—1880

Invention Date—October 1879

It is generally conceded that the practical application of electric lighting to domestic, industrial, and other installations and the initiation and growth of the lighting industry are directly attributable to this invention of Mr. Edison. The invention as described in the patent

> * * * consists in a light-giving body of carbon wire or sheets coiled or arranged in such a manner as to offer great resistance to the passage of the electric current, and at the same time present but a slight surface from which radiation can take place.
>
> The invention further consists in placing such burner of great resistance in a nearly perfect vacuum, to prevent oxidation and injury to the conductor by the atmosphere.

The lamp (Fig. 1, page 93) comprises a filament *a*, a spiraled thread of carbon having a resistance of several hundred ohms as compared with the resistance of one to four ohms characteristic of earlier carbon lamps. Platinum wires *d,d* connect with the opposite ends of the filament and are attached to lead-in conductors *x,x* sealed in the glass bulb *m*. The bulb is exhausted and is hermetically sealed after a vacuum has been established.

Illustrative claim 2 of the patent reads as follows:

> 2. The combination of carbon filaments with a receiver made entirely of glass and conductors passing through the glass, and from which receiver the air is exhausted, for the purposes set forth.

This patent was involved in at least eight different infringement actions and each time claim 2 was held to be valid.[2] For convenience, reference is made to *Edison Electric Light Co.* v. *United States Electric Lighting Co.* (C. C. A. 2nd - 1892) 52 Fed. 300, in which the Court exhaustively considered the question of patentable novelty. The principal references relied upon in attacking the validity for want of patentable novelty were Edison's French patent 130,910 of May 28, 1879; British patent 10,919 of 1845 to King, and British patent 3,988 of 1878 to Fox.

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[2] In *Sawyer-Man Electric Co.* v. *Edison Electric Light Co.* (C. C. A. 2nd—1892) 53 F. 592, there was a holding of patent validity and infringement and a subsequent petition for a writ of certiorari was denied by the Supreme Court, 149 U. S. 785.

French Patent 130,910—1879—Edison

Edison's earlier French patent describes an electric lamp (Fig. 2, page 93) comprising an incandescent platinum or a platinum-alloy wire *a* rolled on a coil form and supported in a vacuum tube *b* up a rod *b'* of nonconductive material. The ends of the filament pass through and are sealed to the vacuum tube *b* and connect with terminal posts on a base *k*. A glass envelope *i* surrounds this structure.

The patent states that it is essential to construct lamps which have a resistance of several hundred ohms and describes a method of processing the filament *in situ* in which it is connected into an electrical circuit and heated. During the heating process, the air and gases occluded in the metal are expelled and drawn off by a vacuum pump. After several stages of heating and continuous exhausting, the glass is sealed off, so that *"the wire is in a perfect vacuum and in a state unknown until now."*

British Patent 10,919—1845—King

This patent states the need for a high-resistance lighting element and *proposes the use of carbon in a Tooricelieu Vacuum.* The lamp (Fig. 3, page 93) comprises a glass tube *a* enclosing a support rod *i* for clamps *f,g* which hold a carbon element *c*. Conductors *d* and *n* connect with the carbon element and extend to opposite ends of the tube. The tube is filled with mercury and has such a length that a vacuum to protect the carbon element is formed when the tube is inverted in a vessel of mercury. The carbon element *c* is in the form of thin pencils or thin plates.

British Patent 3,988—1879—Fox

This patent describes a lamp (Fig. 4, page 93) in which the incandescent element *a* is a fine wire of an alloy of platinum and iridium so that a high resistance is obtained without having a large extent of luminous surface. The incandescent element is suspended within a glass envelope *d* by lead-in conductors *b,b* passing through a top *c* sealed to the envelope. Nitrogen gas is included within the envelope to protect the incandescent element from deterioration during its operation.

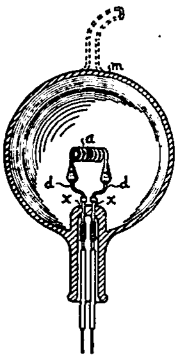
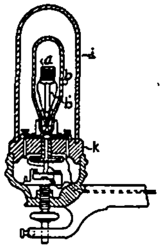
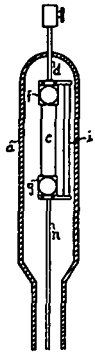
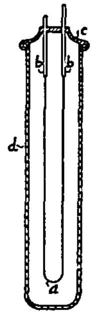
Decision as to Invention

The chart of page 93 shows that, prior to the invention of the Edison patent 223,898, the electric lamp art had already learned: (1) the need of a high-resistance incandescent element (Fr. 130,910 and Br. 3,988); (2) that this element may be made of carbon (Br. 10,919); (3) that it may be of spiraled filamentary form (Fr. 130,910); and (4) that, whether made of platinum or carbon, it may be operated in a vacuum for protection against deterioration (Fr. 130,910 and Br. 10,919). Notwithstanding the fact that *each* element of the claimed combination was old, the validity of claim 2 was upheld in the *Edison Electric Light Co.* case in which the Court stated:

> * * * we are satisfied that there was invention in the substitution of the carbon of the patent in suit for the platinum of the French patent, *even though all knowledge as to what should be the ratio of resistance to radiating surface were pointed out, either in the French patent or elsewhere in the art.* (Italics added)

This conclusion was undoubtedly influenced by the finding that, prior to Edison's invention, no one had attained any commercially successful embodiment of an electrical lamp for lighting purposes either of the arc or incandescent type, whereas subsequent to the Edison invention electric lighting by lamps of moderate intensity had indeed become a commercial success. The Court characterized the advance over the prior art in general as follows:

> Although all-glass globes, with leading wires passing through the glass and sealed into it, had been used before to preserve the conditions of the interior of a chamber from the effects of leakage at the joints, and although the prior art, including the French patent, indicated that subdivision of the electric light was to be obtained by the use of burners of high resistance and small radi-

223,898—1880 Edison	Fr.130,910—1879 Edison	Br.10,919—1845 King	Br.3,988—1879 Fox
 Fig. 1	 Fig. 2	 Fig. 3	 Fig. 4
Claim 2			
The combination of carbon filament *a*	The spiral filament *a* is platinum or a platinum alloy.	The high-resistance element *c* is a pencil or thin plate of carbon.	The filament *a* is an alloy of platinum and iridium.
with a receiver *m* made entirely of glass	Tube *b* is made of glass.	Tube *a* is made of glass.	Tube *d* is made of glass.
and conductors *x*, *x* passing through the glass,	The ends of the filament pass through the glass tube.	Conductors *d* and *n* extend to the ends of the tube.	Conductors *b*, *b* pass through the top *c* of the envelope *d*.
and from which receiver the air is exhausted, for the purposes set forth.	The tube *b* is evacuated.	The portion of the tube *a* in which the carbon element *c* is positioned is evacuated.	The tube is exhausted of air and filled with an inert gas.

ating surface, and although pencils of carbon had been tried in imperfect *vacua*, and found wanting, *it was invention*, in view of the teachings of the art as to the disintegration of carbon under the action of an electric current, *to still select that substance* as a suitable material from which to construct a burner *much more attenuated* than had ever been used before, *reduced in size to the filamentary form* in which economy of construction requires that it must be used in order to avail of the philosophy of high resistance and small radiating surface, *and so to combine old elements* that the disintegration due to 'air washing' should be practically eliminated, and the burner thus become commercially stable. * * *
* * * Finally and principally, by the substitution, there was presented the complete combination of elements, which for the first time in the art produced a practical electric light. We are of the opinion that on principle and under the authorities such a substitution of material is invention. * * * (Italics added)

BARBED-WIRE FENCE—J. S. GLIDDEN [3]

Patent No. 157,124—1874

This patent is the first link in the network of barbed-wire fences that stretches out across the country. It discloses a fence (Figs. 5 and 6, page 97) comprising two strands *a* and *z* suspended between supports. Spur wires D are individually formed of a short piece of wire bent at its middle portion E around the strand *a*. The spur wires are slipped over the strand *a* and are fixed in position by a key C for twisting the strands *a* and *z* together. The twisted strands prevent movement of the spurs in either direction along the fence and at the same time lock the spurs against rotation.

The single claim of the patent reads as follows:

A twisted fence-wire having the transverse spur-wire D bent at its middle portion about one of the wire strands *a* of said fence-wire, and clamped in position and place by the other wire strand *z*, twisted upon its fellow, substantially as specified.

[3] Included in a list of 16 basic inventions found in "Statement of Commissioner of Patents, Conway P. Coe before the Temporary National Economics Committee, January 16, 1939" 21 J. P. O. S. 87, p. 93.

The validity of this patent was upheld by several District Courts in five separate suits for patent infringement and the holding of patent validity was affirmed by the Supreme Court in the *Barbed Wire Patent case (Washburn & Moen Mfg. Co.* v. *The Beat 'em all Barbed Wire Co.)* 143 U. S. 275 (1891). The Court recognized that the use of wire fences, composed of either a single wire or two or more wires twisted together, antedated by many years the barbed feature of such fences and examined the issue of patentable novelty in the light of allegedly anticipating patents Nos. 67,117 to Hunt, 66,182 to Smith, and 74,379 to Kelly.

Patent 67,117—1867—Hunt

Hunt proposed a barbed fence (Fig. 7, page 97) in which fence wires B,B are supported by posts. A series of spur wheels C,C having sharpened spurs and centrally located openings fit loosely over the wire strands B to revolve thereon. Locking devices, not shown in the drawing, maintain the spur wheels in selected positions along the wire.

Patent 66,182—1867—Smith

The barbed-wire fence of the Smith patent (Fig. 8, page 97) includes wires *b,b* stretched between supporting posts A,A. Spools *c,c* provided with four short wire spurs are rotatably supported on the fence wires and are locked in place by deformed or offset portions of the wires.

Patent 74,379—1868—Kelly

The barbed-wire fence construction of the Kelly patent (Figs. 9 and 10, page 97) includes wire strands D and diamond-shaped thorn pieces or barbs E with a central hole *e*, slightly larger than the wire strands. After the barbs E have been positioned on the strand, they are locked in place by a hammer blow which compresses both the central aperture *e* of the barb and the enclosed section

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of the wire strand. As to a twisted-wire fence construction, the patentee states:

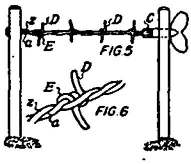
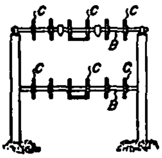
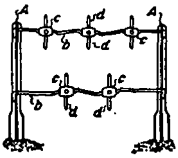
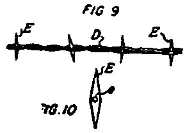
> I can, where it is desirable to increase the strength of the wire, lay another wire of the same or a different size alongside of a thorn-wire, and can twist the two together by any suitable mechanism.

The patent also described a fence in which cords of hemp or other analogous material are used as the strands. This modification contemplates stringing the thorns on the cords of hemp and "*holding them in place by twisting two or more cords together.*"

Decision as to Invention

As demonstrated by the chart on page 97, the barbed-wire fence construction of the Glidden patent represented a small step over the prior art. The Court very properly concluded that Glidden was not in a position to claim broadly the use of the plain or the twisted wire, nor the sharp thorns or barbs, *nor the combination of the two* as they appear in the Kelly patent. However, it was held that the use of the second twisted wire for the purpose of locking the thorn was not contemplated in the Kelly patent "though, of course, *it would prevent movement to any considerable extent in either direction.*" The vital difference in the two patents was said to be in the shape of the barb itself and, in upholding validity, the Court stated:

> * * * *The difference* between the Kelly fence and the Glidden fence *is not a radical one, but slight as it may seem to be,* it was apparently this which made the barbed-wire fence a practical and commercial success. (Italics added)

157,124—1874 Glidden	67,117—1867 Hunt	66,182—1867 Smith	74,379—1868 Kelly
			
Figs. 5 and 6	Fig. 7	Fig 8	Figs. 9 and 10
Claim			
A twisted fence-wire	Strands B,B form a wire fence.	Strands *b,b* form a wire fence.	Strands D provide a twisted fence wire.
having the transverse spur-wire D bent at its middle portion about one of the wire strands *a* of said fence wire,	Transverse spur wheels C have central holes through which they are supported about the strand B.	Transverse spur wires *d*, carried by spools C, are supported about the strand *b*.	Transverse spurs or thorns E thread over one strand and their mid portions are deformed or bent about that strand.
and clamped in position and place by the other wire strand *z*, twisted upon its fellow, substantially as specified.	The spur wheels C are clamped in position by locking devices.	The spools C are clamped in position by deformed sections of the wire strand.	The other twisted strand helps to clamp the thorns in place on the companion strand.

TELEPHONE—Alexander Graham Bell

Patent No. 174,465—1876

This invention of Alexander Graham Bell is the very foundation of the modern telephone industry and is the subject of an interesting story which the able Chauncey M. Depew tells on himself:[4]

> In 1876 Gardner Hubbard . . . said to me: "My son-in-law, Professor Bell, has made what I think a wonderful invention. It is a talking telegraph. We need ten thousand dollars, and I will give you one-sixth interest for that amount.
>
> I was very much impressed . . . however, I called upon my friend, Mr. William Orton, president of the Western Union Telegraph Co. Orton had the reputation of being the best informed and most accomplished electrical expert in the country. He said to me: "*There is nothing in this patent whatever, nor is there anything in the scheme itself, except as a toy.*" (Italics added)

The Bell patent[5] relates to a method of and apparatus for producing electrical undulations for the simultaneous transmission of musical notes and the telegraphic transmission of noises or sound of any kind. The invention utilizes electrical undulations resulting from gradual changes of intensity in an electrical current, as distinguished from electrical pulsations caused by sudden changes of current intensity. The current undulations exactly and continuously follow the changes in air pressure comprising the sound waves to be transmitted.

The transmitting apparatus (Fig. 11, page 103) comprises an electromagnet having a coil *b* upon one of its legs and having an armature *c* pivoted at one end to the magnet structure. The free end of the armature *c* projects over one pole of the magnet and is attached to the center of a membrane *a* stretched across one end of a cone A. A receiving apparatus including a coil *f* and an arma-

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[4] Pages 354-355, "My Memoirs of Eighty Years" by Chauncey M. Depew, published 1924 by Charles Scribner's Sons.

[5] Included in Commissioner Coe's list of important patents, supra.

ture *h*, is positioned at a remote point and the two are connected in a closed circuit. The armature *h* is affixed to a membrane *i* of a second cone L. When a sound is uttered into the cone A, its membrane *a* is set in vibration and the armature *c* partakes of the vibratory motion to induce in the closed electrical circuit E, *b*, *e*, *f*, *g*, undulations similar in form to the air vibrations caused by the sound. The undulatory currents passing through electromagnet *f* cause its armature *h* to vibrate and to actuate membrane *i* in a motion which is a replica of that initially established at the transmitting membrane *a*. Therefore, the sound uttered into cone A is heard at the cone L.

Claim 5 of the patent, adjudicated and held to be valid in over ten different actions for patent infringement and in the famous Telephone Cases 126 U. S. 1 (1887), reads as follows:

> 5. The method of, and apparatus for, transmitting vocal or other sounds telegraphically, as herein described, by causing electrical undulations, similar in form to the vibrations of the air accompanying the said vocal or other sound, substantially as set forth.

The defense of invalidity of that broad claim was vigorously urged in view of a publication by Charles Bourseul in "L'Illustration," Volume XXIX, Paris, August 26, 1854; an article "Concerning the Reproduction of Sounds by Means of Galvanic Electricity," by V. Legat, published in Zeitschrift Des Deutsch-Oesterreichischen Telegraphen Vereins (Journal of the German-Austrian Telegraph Association) Berlin, 1862, Vol. IX, p. 125; and British patent 1,044 of 1870 to Varley.

Bourseul's Publication—1854

Bourseul's paper starts with an appreciation of the operating principles of the electric telegraph in which an electric current circulates through a coil around a piece of soft iron which it converts into an electromagnet. The moment the current stops, the iron ceases to be a magnet and, therefore, the electromagnet may attract and then release a movable plate which, by its to and fro movement, produces the conventional signals employed in telegraphy. The author, in discussing the use of this tool as a means for transmitting the spoken word by electricity, states:

We know that sounds are made by vibrations, and are made sensible to the ear by the same vibrations, which are reproduced by the intervening medium. * * * Suppose that a man speaks near a movable disc, sufficiently flexible to lose none of the vibrations of the voice; that this disc alternately makes and breaks the connection with a battery; you may have at a distance another disc which will simultaneously execute the same vibrations.

It is true that the intensity of the sounds produced will be variable at the point of departure, at which the disc vibrates by means of the voice, and constant at the point of arrival, where it vibrates by means of electricity; but it has been shown that this does not change the sounds. It is, moreover, evident that the sounds will be reproduced at the same pitch.

* * * observe that syllables can only reproduce upon the sense of hearing the vibrations of the intervening medium. *Reproduce precisely these vibrations, and you will reproduce precisely these syllables.* (Italics added)

Legat's Publication—1862

This paper describes experiments conducted by one Philipp Reis. It discusses the vibratory nature of sound and the mechanism of the auditory system "to demonstrate that as soon as we are able to reproduce vibrations equivalent to the vibrations of any particular tone, or combination of tones, we shall have the same impressions as were produced upon us by this original tone or combination of tones." The apparatus (Fig. 12, page 103) comprises a transmitter including a conical tube *a,b* closed at one end by a flexible membrane *o*. One end *c* of a lever *c,d* rests upon the center of membrane *o*. The lever is supported upon a bracket *e* to be included in an electrical circuit between the transmitting and receiving points. The opposite end of lever *c,d* may close against a contact *g* to complete the circuit. The receiver comprises an electromagnet *m,m* mounted on a sounding board *u,w*. A reed *i* and an armature for the electromagnet are suspended from a standard *k* like a pendulum.

When one speaks into the transmitter tube *a,b*, its membrane *o* vibrates in accordance with the sound vibrations and the lever *c,d* following the motion of the membrane opens and closes the transmitting circuit. The electromagnet *m,m* is magnetized and demagnetized alternately and sets its armature and lever *i* into vibrations like those of the transmitting membrane *o* to reproduce at the receiver a tone corresponding to that transmitted.

Apparatus of this type was shown in practical experiments to be capable of transmitting tones and chords accurately, but spoken words were less distinctly reproduced.

British patent 1,044—1870—Varley

This patent increases the traffic capacity of telegraph circuits by superimposing "undulations" on the line circuit to enable more than one operator to signal independent messages at the same time. The apparatus (Fig. 13, page 103) located at one station of a telegraph system includes a line wire *a*, Morse receiving and transmitting instruments *b* and *c*, and a battery *d*. An auxiliary transmitter of "undulatory" currents comprises a tuning fork *k* and an electromagnet *m* which vibrate a movable contact between stationary contacts 1^1 and 1^2, alternately to energize two primary coils of an induction system including a secondary coil *n*. The secondary coil *n* may be connected through a switch *g* and condenser *f* to the line wire for transmission or the switch *g* may connect a receiver *h* to the line wire for reception. The receiver *h* is in the nature of a tuning fork subject to vibration at a particular frequency under the control of an electromagnet energized by received undulatory currents. The apparatus is duplicated at a second point with which communication is to be had.

One message may be transmitted over line wire *a* by means of the direct current Morse system in the usual way. At the same time, the auxiliary transmitter of any station may generate oscillations or undulatory currents in its coil *n* at a frequency determined by the vibratory frequency of its tuning fork *k* to transmit a second message. These undulations are applied to the line wire *a* and transmitted simultaneously to the receiving point. At that point, the switch *g* supplies the received undulations to the receiver *h* to operate that receiver if the frequency of such undulations corresponds with the resonant frequency of the receiver.

Decision as to Invention

The Supreme Court in the Telephone Cases found that *both Bourseul and Reis knew what had to be done in order to transmit speech by electricity* because each, in his publication, recognized the vibratory character of sound and stated that reproduction of similar vibrations through the aid of electric currents will permit reproduction of the sounds. While Reis could reproduce sounds and transmit singing through his apparatus, he employed the principle of intermittent current rather than the principle of varying the intensity of an unbroken current as in the Bell apparatus and method. Although Varley spoke in British patent 1,044 of "undulatory currents," it was concluded that his transmission was of the Morse signaling type and that the undulations did not result "from gradual changes of intensity exactly analogous to the changes in the density of air occasioned by simple pendulous vibrations" which was Bell's discovery. For these reasons, claim 5 of the Bell patent was held to be patentably novel and valid.

174,465—1876 Bell	Bourseul's Publication—1854	Legat's Publication 1862	Br. 1,044—1870 Varley
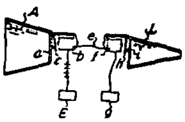		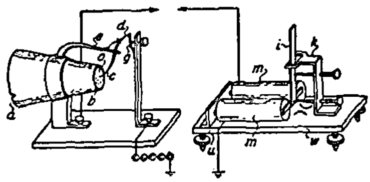	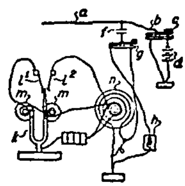
Fig. 11 Claim 5		Fig. 12	Fig. 13
The method of, and apparatus for, transmitting vocal or other sounds telegraphically, as herein described,	The publication describes a method of transmitting vocal sounds telegraphically.	This publication describes a method of, and apparatus for, transmitting sounds telegraphically.	This patent discloses a method of transmitting audible or super-audible tones.
by causing electrical undulations, similar in form to the vibrations of the air accompanying the said vocal or other sound, substantially as set forth (i.e. by gradual changes of intensity in a current exactly analogous to the changes in the air occasioned by simple pendulous vibrations).	The method is carried out by a telegraphic instrument having a flexible disc which makes and breaks an electric circuit in accordance with the vibrations of the air accompanying the sound. The intermittent current produced controls a receiving electromagnet which displaces a second disc to execute the same vibrations and reproduce the sound.	The membrane *o* of a speaking tube *a,b* vibrates a lever *c,d* to open and close a transmitting circuit in accordance with the vibrations of the air accompanying the sound. At the receiver an electromagnet *m,m* is alternately energized and de-energized by the intermittent current, causing its reed *i* to vibrate in the manner of the transmitting membrane *o* and reproduce the transmitted sound.	The tuning fork *k* and electromagnet *m,m* generate in coil *n* undulations (oscillations) of a particular frequency for transmission over a line wire *a* to operate a tuning fork receiver *h* at a remote point to reproduce the tone.

ELECTROMAGNETIC (Induction) MOTOR—
Nikola Tesla

Patent 381,968—1888

This patent is directed to a system for the transmission of electrical power, featuring the use of an alternating-current motor and an alternating-current generator. The method of power transmission utilized is claimed in patent No. 382,280,[6] issued on a divisional application.

Tesla's contribution extended the commercial utility of alternating currents from the narrow field of electric lighting to the broader and more general field of electric power transmission.

The transmission system (Fig. 14, page 110) comprises an alternating-current motor M and a generator G for driving the motor. The motor has a laminated annular or ring stator R on which are wound four coils C,C,C′,C′, diametrically opposed coils being connected in series-relation. The ends of the coils are connected with terminals T,T,T′,T′. A magnetic armature disc D is supported on a shaft *a* for rotation within the ring R. The alternating-current generator G is of conventional type, having field magnets N,S and an armature A wound with two independent coils B and B′. The free ends of each coil are carried through a shaft *a′* and individually connect to slip rings *b,b* and *b′,b′*. Brushes engaging the slip rings constitute terminals for the generator which are connected to the motor terminals by conductors L,L and L′,L′ to complete two circuits, one including the generator coil B and motor windings C′,C′ and the other including the generator coil B′ and motor windings C,C.

Rotation of the generator armature induces alternating currents in the coils B,B′ which are directly applied to the windings of the motor. The currents in the two circuits, extending between the generator and motor, are sinu-

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[6] Also included in Commissioner Coe's list of 16 of the most important patents, supra.

soidal alternating currents and have an electrical phase displacement of 90 degrees. The motor windings C,C and C′,C′, each of which is energized by one component or phase of the alternating current, produce in the ring R a magnetic field of uniform intensity the poles or axes of which shift or revolve in synchronism with the rotation of the generator armature A. The magnetic armature D of the motor M follows the rotation of the magnetic field, thereby producing motor action. This system obviated the need for the usual commutating devices required in direct-current power transmission.

A representative claim of the parent patent 381,968 is as follows:

> 1. The combination, with a motor containing separate or independent circuits on the armature or field-magnet, or both, of an alternating-current generator containing induced circuits connected independently to corresponding circuits in the motor, whereby a rotation of the generator produces a progressive shifting of the poles of the motor, as herein described.

The validity of that claim as well as the method claims of the divisional patent was vigorously challenged and upheld in each of four actions for patent infringement, for example, *Westinghouse Electric & Mfg. Co.* v. *New England Granite Co. et al,* (C. C. Conn.—1900); 103 F. 951, affirmed 110 F. 753. The defense charged that the claims were invalid for want of patentable novelty in view of Arago's classic experiment, British patent 3,134 of 1878 to Siemens, and publications of Marcel Deprez, 1880-1884, appearing in Centralblatt fur Electrotechnik and in Comptes Rendus of 1883.

Arago's Experiment

Arago suspended a copper disc at its center, horizontally above the poles of a horseshoe magnet. Rotation of the magnet about a vertical axis resulted in rotation of the disc due to the rotation of the field of the magnet.

British Patent 3,134—1878—Siemens

This patent defines dynamoelectric apparatus as apparatus employed for the conversion of mechanical power into electricity and states that "*the electricity produced can be applied in apparatus similar to that which produced it for the production of motive power, in which case the apparatus is said to act as electrodynamic apparatus.*"

In one form of the dynamoelectric or electrodynamic apparatus (Fig. 15, page 110), a ring-type stator structure B supports a circular series of radially extending electromagnets C,C having pole pieces F,F. A similar series of electromagnets C′,C′ having pole pieces F′,F′ are supported upon a stationary cylinder B′,B′. An annulus D, supported by a disc J rotatable with a shaft E, is positioned for rotation within the annular path defined by the pole pieces F,F and F′,F′. A plurality of spaced coils S,S are positioned around cylinder D to pass through the magnetic fields of the several electromagnets as shaft E is rotated. Coils S,S are connected with slip rings H,H in the usual manner and brushes K associated with the slip rings connect with the usual commutator G. The electromagnets C,C′ may be energized from connections with brushes K of the commutator G.

In operation, the electromagnets facing one another present like poles but the poles of successive pairs of electromagnets alternate in polarity. As shaft E is driven, coils S,S pass through magnet fields which alternate in polarity so that polyphase alternating currents are induced in these coils. While the alternating currents "may be transmitted separately from the machine," the slip rings H and commutator G are utilized to effect commutation, supplying a direct-current, as distinguished from an alternating-current, output from the generator. The patentee suggests a complete power-transmitting system as follows:

Although in what has preceded the apparatus has been mostly described as of the dynamoelectric kind, whereby mechanical power applied to drive them is converted into electricity, it is to be understood that *with suitable modifications these apparatus are generally applicable also as electrodynamic machines, their rotary parts being caused to revolve and give out mechanical power when electricity is applied to them, and thus one of these machines may be driven by any suitable motive power so as to generate electricity, and this electricity may be conducted to a similar machine at a distance, causing it to work and to give out a portion of the power applied in the first instance.* (Italics added)

Deprez Publications

Deprez set out to find a means of reproducing the displacement of two relatively rotatable objects at a distance and at any number of different points at once by obtaining "*an absolute synchronism.*" His apparatus (Fig. 16, page 110) comprises, at the left, a generator including a ring arranged between the poles of a magnet, as in the ordinary magnetoelectric machine except that the magnet instead of being stationary is arranged to revolve about the axis of the ring. Four brushes *e, f, g,* and *h* are connected in pairs at right angles on the collector and constitute terminals of this signal-generating device. To the right is a device called an "annular comparer of currents." It has a stationary iron ring which carries two windings, one having its poles at *j* and *l* and the other having poles *k* and *m*. The ends of the windings are connected with the brushes of the generator as indicated and a magnetized needle is rotatably mounted in the center of the current comparer. The arrow N,S represents the pole axis of the generator for a particular position of its rotatable magnet relative to the brush assembly.

When the magnet is revolved, a current flows through *g,l,j,e* with an intensity proportional to the magnetic component *a-b* of the generator and a second current flows through *h,m,k,f* with an intensity proportional to the magnetic component *a-c*. These current components determine the magnetization in the "comparer" and position the needle accordingly. The ratio of the current components varies between zero and one, the latter value being reached when the line of the poles of the magnet at the generator bisects the angle of the line of the brushes. For this condition, the two currents traversing the comparer are equal and the needle assumes an angle of 45 degrees. The arc described by the needle is synchronous with that of the magnet in the generator or, in other words, the needle of the comparer always shows the relative movement of the magnet and the brushes at the generator. The only application of this mechanism was to an electric compass.

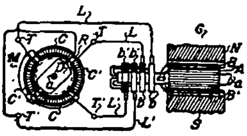
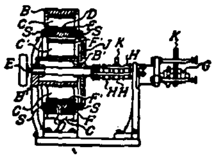
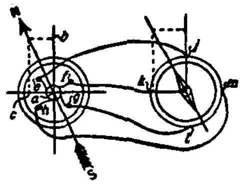
Decision as to Invention

The defendant contended that any generator, whether it be a direct-current or alternating-current one, may be reversed and used as a motor. "Supply it with currents such as it generates, and it will operate as a motor, * * * The art knew it could be done, and how to do it." Therefore, the Siemens patent was asserted to be a full disclosure of the alleged invention of Tesla. *It was conceded that, as of the date of the trial, it was easy to see that the Siemens machine could, by properly taking off the currents, have been used as a polyphase machine and also that, if any one had coupled two such properly arranged machines in a certain way and used them in a certain way the system so produced would have involved the use of the invention afterwards made by Tesla.* The Court nevertheless rejected the argument on the belief that at the date of the invention it was not known whether an alternating-current machine could be used as a motor. While the Siemens patent referred to the use of his apparatus as a motor or generator, the Court emphasized the fact that it did not describe any mode of using alternating current but did expressly refer to the use of commutators, indicating direct-current operation. The force of the patent was weakened because it failed to describe the "suitable modifications'' necessary to use the apparatus as an electrodynamic machine or motor.

The defendant further contended that the Deprez apparatus produced a progressively shifting magnetic field in a motor by means of independent alternating currents, differing in phase, and circuits which preserve the independent character and phase relations of such currents as Tesla had described as his broad invention. This position was strengthened by an admission of the *Complainant's expert that the Deprez articles ''demonstrated mathematically the fact, which is also stated in the Tesla patents, that the polar line of an annular magnet may be shifted about through the entire circumference of the ring by the action of two magnetizing forces properly related.''* The Court, in weighing the Deprez articles, was greatly influenced by a statement of Deprez in 1884, prior to Tesla's invention, to the effect that ''alternating currents are of no use in the transmission of power. They are suitable only for lighting purposes.'' The Court characterized Deprez's apparatus as a laboratory experiment, saying:

> * * * Therefore, although Deprez, * * * suggested that his system might be used for an impracticable and almost infinitesimal amount of power, the fact that these currents had never been practically used for any such purpose, and cannot, even now, be practically used for currents of high potential, shows that it required invention to select from an art that particular kind of current which was necessary for the production of the best results, and to adapt the mechanism of an art, analogous or non-analogous, to its practical application. * * *

Finally, it was concluded that Tesla did not discover the parallelogram forces (explained by Deprez) nor did he discover the rotary field (taught by Arago and Deprez) but he was the first to explain how to do practically what others said could be done, but without showing how to do it.

381,968—1888 Tesla	Br. 3,134—1878 Siemens	Deprez Publications 1880–1884
 Fig. 14	 Fig. 15	 Fig. 16
Claim 1		
The combination, with a motor (M) containing separate or independent circuits (C,C and C′,C′) on the armature or field magnet, or both,	One machine may be operated as a motor having separate circuits S on the armature and separate circuits C,C′ on the field structure.	The apparatus to the right is in the nature of a motor, having separate circuits *k*,m, and *j*, *l* on the field magnet.
of an alternating-current generator (G) containing induced circuits (B and B′) connected independently (by conductors L,L and L′,L′) to corresponding circuits (C,C and C′,C′) in the motor,	Suggests that a similar machine may be operated as an alternating-current generator having induced circuits S which may be independently connected to corresponding circuits in the motor.	The apparatus to the left is an alternating-current generator which has induced circuits *e*, *g*, and *f*, *h* connected independently by the horizontal conductors to the circuits *k*,*m* and *j*,*l* in the motor.
whereby a rotation of the generator produces a progressive shifting of the poles of the motor, as herein described.	If properly connected, rotation of the generator produces a progressive shifting of the poles of the motor, substantially as in Tesla's system.	Rotation of the magnet in the generator produces a progressive shifting of the poles of the motor, in the same manner as in Tesla's system.

AIR BRAKE—George Westinghouse, Jr.

Patent 88,929 [6]—1869
Reissue Patent 5,504—1873

The invention of this patent [7] resulted in the first practical application of air brakes to railroad equipment and led to the safe operation of modern railroad systems. The power brake system (Fig 17, page 118) includes an auxiliary steam engine *a′,a″* which receives steam from a line *b* connected with the locomotive boiler. This engine has a piston rod *e,e′* which actuates an air compressor *o* for charging a reservoir *d*. An air line *i* connects with the reservoir *d* through a three-way valve *h* and extends under the car. Coupling devices *k* interconnect similar feed lines of the remaining cars. A brake cylinder *m* is provided for each car and a branch line *i′* leads from the air line *i* to one end of the brake cylinder back of its piston *r*. A piston rod *m′* extends through the opposite end of the cylinder and connects with a brake lever *n′* for applying brake shoes *s* to the wheels *s′*. The valve systems of the auxiliary engine *a′* permit the air pump *o* to be operated irrespective of the movement or speed of the locomotive to maintain a constant air pressure in the reservoir *d*.

When the desired air pressure has been established in the reservoir *d*, the valve *h* may be operated to one position to open the air line *i* to the reservoir. The compressed air is then admitted through the branch pipes *i′* to each brake cylinder *m*. It displaces the piston *r* and operates the brake lever *n′*, whereby the brakes *s* are instantaneously applied. When the braking action has been completed, the valve *h* is operated to a second position in which it blocks the outlet from the reservoir *d* and connects the feed line *i* to exhaust ports so that compressed air in each brake cylinder *m* escapes into the atmosphere. The piston in each brake cylinder is returned to its initial position by a spring and the brakes are released. The braking

[6] See note 6, page 104.
[7] Also included in the list of important patents designated by Commissioner Coe, supra.

force may be controlled by the pressure maintained in the reservoir *d* and may be graduated in the brake cylinders by the valve system including the valve *h*.

The coupling devices *k* (Fig. 20, page 119) which extend the feed line *i* from car to car comprise valve sections *f* telescoping within one another and providing air-tight junctions. Each section *f* includes a puppet valve *p* having a stem *p′*,*p″* slidably supported by diaphragms *q*,*q′* Shoulders *y′* prevent the valve *p* from resting against the diaphragm *q′* and interrupting the air passage. Spring hooks *g* attached to one section engage a beveled shoulder *u* of the other to lock the sections in coupled relation.

The valve stems in the sections *f* are aligned so that when a coupling connection is made the ends of the stems abut against one another and position each valve *p* between its diaphragms *q and q′*. This extends an air passage from the supply line *i* through the coupled sections. When the hooks *g* are released to brake the coupling, compressed air within the feed line *i* advances the valve *p* of the last coupler *k* against its diaphragm *q*, closing the feed line at that point. All of the brake cylinders between the reservoir *d* and the closed end of the supply line *i* may then be operated at will.

Representative claims of the patent as reissued are as follows:

1. The combination of a brake, operating on the wheels of a railway locomotive, car, or truck, with an air-reservoir, an independent steam-pump, operated by steam from the locomotive-boiler, for charging the same, and a brake-cylinder, connected with the reservoir by suitable pipe or pipes, furnished with cocks for charging, discharging, and graduating the pressure in the brake-cylinder.

4. Valves arranged in the adjacent ends of the coupling *f*, and guided by stems and guides, so as to open each other when the couplings *f* are united, and to close automatically when uncoupled, substantially as above set forth.

The validity of those claims was most strenuously contested in *George Westinghouse, Jr.* v. *The Gardener and Ranson Air-Brake Co.* (Ohio—N. D.—1875); 29 F. C. 799;

76 C. D. 317. The defendant offered in evidence nearly 30 patents on the issue of novelty and priority of invention, the principal ones being: (1) as to the fluid pressure brake system, per se, British 1,737 of 1860 to Du Trembley, British 2,886 of 1853 to Hollinsworth, British 2,594 of 1860 to McInnes, and British 2,015 of 1863 to Siegrist; and (2) as to the coupler construction including automatically operated valves, British 2,015 of 1863 to Siegrist, patent 12,263, Wright, and patent 16,220, Carson.

British 1,737—1860—Du Trembley

The railroad brake system (Fig. 18, page 118) may be operated by compressed air but is described as a vacuum system. A vacuum pump A is actuated by an eccentric driven by a rotating part of the car truck. The intake of the pump is connected with a vacuum line *x* extending the length of the train with suitable couplings R between successive cars. A valve F is included in the line for regulating the admission of air to the pump A, and a smaller three-way valve F′ is provided for connecting the line *x* with the pump A or for admitting air to the line. The piston rod of a brake-actuating cylinder G connects through a link M with brake operating levers N,N.

The vacuum pump A operates continuously when the train is in motion but the brake system may be neutralized by opening valve F to admit air freely to the pump and by shutting valve F′ to close the line *x* against the action of the pump. To apply the brakes, the valve F is at least partially closed and the valve F′ is opened to permit the pump A to draw a vacuum in the line *x* and in the brake cylinders G. The braking force is proportional to the vacuum obtained and if the valve F is entirely shut, a maximum braking pressure results. *Therefore, manipulation of the valves F and F′ graduates the extent of the vacuum drawn and the braking pressure.* The brakes may be released by operating the valves F and F′ freely to admit air and destroy the vacuum of the system.

British 2,886—1853—Hollinsworth

The brake system of this patent (Fig. 19, page 118) includes an air pump *a* actuated by an eccentric *b* on the wheel axle to charge a reservoir *d*. A brake cylinder *p* connects through a three-way valve *o* and suitable pipes to the reservoir *d* and its piston rod is linked to the brake operating levers. In order to apply the brakes, the valve *o* is opened to admit compressed air from the reservoir *d* to the brake cylinder *p*. When the brakes are to be released, the valve *o* is returned to an initial position, closing the feed line from the reservoir *d* and connecting the cylinder *p* to an exhaust. *The text expressly states that the pump a may be worked by any mechanical arrangement independent of any motion obtained from the train.*

British 2,594—1860—McInnes

This patent describes an air-pressure braking system that is essentially the same as in Br. 2,886 (supra), having an air compressor actuated by an eccentric fixed to the axle of the engine tender. *It is stated in the text that a donkey engine may be used to drive the air compressor.* A donkey engine is an independent and auxiliary engine having a rating of a fraction of a horsepower.

Provisional British 2,015—1863—Siegrist

This provisional specification describes a braking system of the vacuum type wherein a vacuum is maintained in a vacuum vessel by a pump operated by an auxiliary *donkey engine on the locomotive engine.* Brake-actuating cylinders and suitable valve systems are provided for operating and releasing the brakes by selectively connecting the brake cylinders to the vacuum vessel and to an air supply.

The brake system includes a two-section coupler for extending the vacuum line from car to car. One section terminates in a cylindrical box enclosing a valve which is normally spring-pressed to closed position. The other section has a similar cylindrical box including a spring-pressed valve. The valve of each section has an operating lever to engage a projection within the opposite section and open the valve when the cylindrical boxes are nested to effect a coupling. In this way the vacuum line is extended through the coupler. When the sections are uncoupled, the valve springs automatically close their valves and close the vacuum line to preserve the braking system between the vacuum vessel and the broken coupler. This specification is not supported by illustrative drawings.

Patent 12,263—1855—Wright

Wright discloses a brake system having brake-operating cylinders operated by compressed air supplied from a reservoir charged by compression pumps actuated directly from the axle of the car. The pertinent portion of this patent is the coupling device (Figs. 21 and 22, page 119) for extending the air line from car to car. It comprises a section D of flexible tubing for receiving the ends *i* and *i'* of the air line of two adjacent cars. Each end of section D has a metallic bell-shaped insert *j*. The pipe section *i* includes a valve *k* and a valve seat. Between the valve *k* and the end of the section *i* there is a resilient tongue *l* deformed to project through a slot *m*. When the pipe *i* is uncoupled from the section D, the spring *l* is out of engagement with valve *k* and compressed air advances the valve against its seat to close the pipe section. However, when the end of the section *i* is inserted into the section D, the projecting portion of the spring *l* engages the insert *j* and is forced toward the center of the section *i*. In this position, the spring *l* abuts against and drives the valve *k* from its seat, thereby to complete an air passage from pipe section *i* into the coupler D.

A similar valve and coupling arrangement is provided for each car to extend the brake system throughout the train. Upon decoupling any car, the section D is removed and the valve *k* of the last car of the chain closes the fluid line and maintains the brake system in operating condition.

Patent 16,220—1856—Carson

This patent relates to a locomotive driven by compressed air. The locomotive *b* (Fig. 23, page 119) has a compressed air reservoir *b′* connected with a charging valve *g*. The valve *g* closes against a seat and has a forwardly projecting valve stem *h*. A local charging station has a bell mouth section *t* for receiving the charging valve *g* of the locomotive. A valve *v* and a valve seat are positioned within the bell mouth section normally to close the compressed air system of the charging station. The valve *v* has a forwardly projecting valve stem *w*.

As the locomotive *b* travels along the local track section, its charging valve *g* enters the bell mouth section *t* of the charging station to form a coupling therebetween. The stem *h* of the valve *g* abuts against the stem *w* of the valve *v* and the engagement of these stems displaces valves *g* and *v* from their seats to complete a fluid connection from the compressed air system of the charging station to the receiver *b′* of the locomotive. After the locomotive has received a sufficient charge of compressed air, its charging valve *g* is withdrawn from the bell mouth section *t*, and valves *g* and *v* automatically close under the pressure of the compressed air.

Decision as to Invention

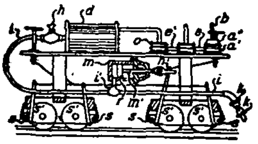
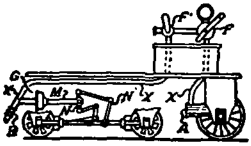
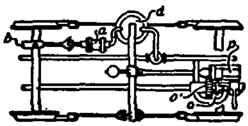
The charts (pages 118 and 119) show that fluid-pressure brake systems of the type contemplated by Westinghouse had already been known in the art. The use of a valve arrangement for charging, discharging, and regulating the pressure in brake cylinders had been proposed (Br. 1,737—Du Trembley); driving engines, independent of the movement of the locomotive, for charging a pressure reservoir were known (Br. 2,886—Hollinsworth and Br. 2,594—McInnes); and automatically operated valves in fluid couplers had been described (Br. 6,220—Carson and

Br. 2,015—Siegrist). And yet, in the *Westinghouse* case, supra, the Court rejected the patents as anticipations of the claims of Re. 5,504, stating that:

> * * * some are too general, indefinite, and ambiguous in their descriptive parts to constitute an anticipation of that which the complainant has patented and introduced into general public use almost the world over, with most marvelous results in point of increased safety to life and property; and those that are clear and intelligible in their terms fall short in one or more material respects of containing the subject-matter of the claims referred to.
>
> * * * *They go to show that Westinghouse was not the first to conceive the idea of operating railway brakes by air-pressure, that he was not the inventor of the larger part of the devices employed for such purposes.* But such fact does not detract at all from his merit or rights of a successful inventor. * * * (Italics added)
>
> Suggestive as these prior patents and provisional specifications may have been, they do not any of them embody that which Westinghouse has invented and claimed; and a prior description of a part cannot invalidate a patent for the whole.

The Court was strongly influenced by the fact of successful commercial use of the Westinghouse air-brake system as shown by the following comment:

> So far as appears from the testimony in this case, *none of the alleged prior inventions of air-brake apparatus have ever successfully been applied to practical use;* and when we consider the immense importance of the introduction of the air-brake on railroads, and the incalculable benefit which it has conferred on the public * * * in connection with the fact that *Westinghouse was the first,* so far as appears in the record and proofs, *to put an air-brake into successful actual use,* such considerations only strengthen and confirm the soundness of the conclusions to which a careful examination of these prior patents has led us, that there are substantial and essential differences between these prior patents and the Westinghouse apparatus, and that to these differences we may justly attribute the successful and extensive introduction of the Westinghouse air-brake. (Italics added)

Re. 5,504—1873 Westinghouse	Br. 1,737—1860 Du Trembley	Br. 2,886—1853 Hollinsworth
 Fig. 17	 Fig. 18	 Fig. 19
Claim 1		
The combination of a brake (*s*), operating on the wheels (*s'*) of a railway locomotive, car, or truck,	This combination includes brake shoes operating on the wheels of a railroad car.	A compressed air-braking system for railroad cars is shown.
with an air reservoir (*d*),	The brake system operates directly from a pump A without an intermediate reservoir.	It has an air reservoir *d*.
an independent steam pump (*a'*,*a''* and *o*), operated by steam from the locomotive boiler, for charging the same,	Pump A is driven by and is dependent upon the movement of the locomotive.	A pump *a*, driven from the car axle, charges the reservoir *d* but the text states that the driver for the pump may be independent of any motion of the train.
and a brake-cylinder (*m*), connected with the reservoir by suitable pipe or pipes (*t* and *t'*),	Brake cylinders G are connected directly with the pump A through the line *x*.	A brake cylinder *p* is connected with the reservoir *d* by pipes 1-2-3.
furnished with cocks (*h*) for charging, discharging, and graduating the pressure in the brake cylinder.	The line *x* is furnished with valves F and F' for charging, discharging, and graduating the vacuum pressure in the brake cylinders G.	The brake cylinder *p* is furnished with a three-way valve *o* for charging, discharging, and regulating air pressure in the brake cylinder.

Re. 5,504—1873 Westinghouse	Br. 2,015—1863 Siegrist	12,263—1855 Wright	6,220—1856 Carson

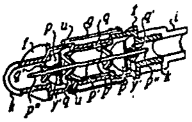
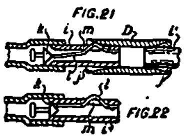
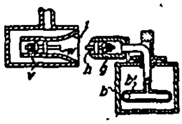

			

Fig. 20		Figs. 21 and 22	Fig. 23
Claim 4			
Valves arranged in the adjacent ends of the coupling *f*,	The patent describes a coupler to extend a brake system from car to car. Valves are arranged in the adjacent ends of the coupler.	In this brake system, valves *k* are arranged at the ends of a coupling sleeve D.	The charging system includes valves *g* and *v* arranged in the adjacent ends of a two-section coupler.
and guided by stems and guides,	The valves have stems and are guided for movement between open and closed positions.	Each valve has a stem and is guided for movement between open and closed positions.	Valves *g* and *v* have stems *h* and *w* and are guided for movement between open and closed positions.
so as to open each other (by engagement of the valve stems) when the couplings *f* are united, and to close automatically (in response to compressed air) when uncoupled, substantially as above set forth.	The valve stem in each coupler section engages a projection in the other for opening each valve when the sections are united. Bias springs automatically close each valve when the sections are uncoupled.	When the coupler is connected a valve lever *l* engages each valve *k* and opens the valve. When the coupler is disconnected, compressed air in the air line automatically advances the valve *k* against its seat and closes the valve.	The valves *g* and *v* open each other by engagement of the valve stems *h* and *w* when the coupling sections are united. The valves automatically close in response to compressed air when the sections are uncoupled.

Conclusion

In brief, what made the classical great inventions great was their subsequent tremendous commercial success rather than any incandescent "flash of creative genius" involved in their creation. The majority of the great inventions discussed above founded a whole new industry, but each represented a relatively minor structural deviation from its impractical or unsatisfactory forerunner represented in the "paper patents" adduced by the defendant in each case.

Let us hope that the courts will realize that not all the great inventions were made in the last century; they are before the courts every day. The principal difference is that the present tempo of our industrial progress produces such a constant stellar shower of great inventions that no individual one shines with the same apparent brilliance as in the days of Edison's lamp.

FORD MOTOR CO.,
Dearborn, Mich., April 27, 1971.

Senator JOHN L. MCCLELLAN,
Chairman, Committee on the Judiciary,
Washington, D.C.

DEAR SENATOR MCCLELLAN: Mr. Iacocca has asked me to respond to your letter of April 14, 1971, referring to the provisions concerning mandatory licensing of patents enacted in the Clean Air Amendments Act of 1970, P.L. 91-604.

We believe that mandatory licensing of patents is not appropriate in normal circumstances, but concern for clean air involves an extraordinary situation in which the public interest and the rights of patentees may be in conflict to some extent.

The mandatory provision in the Act may be regarded as being, in effect, a restatement of existing Federal patent case law under which a court may decline to enjoin the use of a patent when its use is required in the public interest (see *City of Milwaukee* v. *Activated Sludge*, 69 F2d 577 (7th Cir. 1934)). It does add however, a procedure that would authorize a District Court, in its discretion, to pass on the overriding question of public interest and establish a reasonable royalty at the outset rather than after a full trial on validity and infringement. To that extent it should be beneficial both to the patentee and the public.

It seems to us that the substitute proposal (i.e., that the Administrator of the Environmental Protection Agency should recommend Congressional modification of the patent laws if he determines that this becomes necessary in the future to achieve the purposes of the Clean Air Act) would introduce an element of delay in a situation where there is an unmistakable Congressional mandate that the problem of pollution must be solved in the shortest possible time. In view of this, we would be inclined to leave the matter as it now is.

We appreciate your continued support of the United States patent system and your efforts to perfect and strengthen it. We do not believe that the Clean Air Act patent provision, as it stands, detracts substantially from any present essential function of that system.

Sincerely yours,

WRIGHT TISDALE.

THE CHANGING CHARACTERISTICS OF PRIVATE PROPERTY OR THE SCOTT AMENDMENTS MAY THRUST CREEPING SOCIALISM*

(By Howard I. Forman, Philadelphia, Pa.)

It probably is reasonable to presume that in a non-socialist country, in a democracy such as the U.S.A., most people believe in the right of individuals to own and enjoy private property. The belief in such a right goes back to at least several hundred years B.C. Plato, in his *Republic*, had expressed the contrary view that the state should own and determine the uses of all property; but his disciple Aristotle, in *The Politics*, took issue with him and declared that the state is far better off without the disadvantages which attend a system of community of property.

Two thousand years later, in his *Two Treatises of Government*, John Locke formulated his theory of social contract in which he established the ultimate supremacy of the people over the government as per the terms of the contract. In doing so he emphasized the importance of private property to man in his discussion of the dissolution of governments, saying that such dissolution may occur "when the legislative, or the prince, or either of them acts contrary to their trust." Explaining this statement, Locke said "the legislative acts against the trust reposed in them when they endeavor to invade the property of the subject, and to make themselves, or any part of the communty, masters or arbitrary disposers of the lives, liberties, or fortunes of the people."

In the two centuries or more since Locke's time laws and customs have fairly well established what man may or may not do with his private prop-

* Presented at the 10th Conference of the National Industrial Conference Board 3/11/71.

erty in the United States. Broadly stated, man may expect to be able to use and dispose of his property, whether it be real, personal or mixed, in almost any way he pleases as long as such use or disposition does not unreasonably affect another man's right to enjoy his own property (and possibly other rights affecting his life, liberty and pursuit of happiness).

In the case of real property, for example, man normally has the rights to buy and sell land, and to use it for any lawful purpose for which it may be suited such as residential, farming, fishing, grazing, manufacturing, commerce, etc. By common consent of man and his neighbors, in a particular town, country or state, some limits or curbs may be established on any of those rights where they may otherwise affect the rights of others similarly to enjoy their property. Let us look at some of those rights more closely.

Man may lease all or a part of his land to one or a number of people. He may subdivide his land into two or more parcels, and lease each parcel to a different lessee at any mutually agreed upon figure. He could do this on the same day, and give each of his lessees a term of lease completely different and independent of the term of the adjoining lessee. If the man's land happened to extend over the boundaries of two or three different states, it is unlikely that any of the states would protest that the consideration given for the lease of land in their state was different than that demanded for the substantially identical parcel of land in the adjoining state.

If the landowner used one parcel of his land for granzing cattle, and leased another of his parcels with the proviso that it be used only for farming, it is doubtful that the state or county in which this arrangement were entered into would object. If the landowner farmed part of his land, raising corn, and leased another part of his land with the proviso that it not be used to raise corn so long as the lessor raised corn, it is doubtful whether any government agency would protest such a restriction in the lease. Possibly, too, no one would object if the landowner permitted his tenant farmer to raise corn on the condition that the latter did not undercut the price at which the former proposed to sell his corn, unless the size of the farm and the amounts of corn raised and sold were so large as to raise questions about restraints of trade caused by the price-fixing arrangement.

Suppose a man owned four farms, one in the eastern part of the United States, another in the west, a third in the north and a fourth in the south. He personally could only operate one. Rather than let the other three go fallow, he arranged to lease them to tenant farmers. This would seem normal and sensible. If the four farms were contiguous with one another, but each one was within a different state, would there be any difference? Would any of the states, or the federal government for that matter, find any fault with such an arrangement? I doubt it.

What about payment for the use of the leased properties? Ideally, from the point of view of the lessor, except for the possibility of having to pay increased income taxes, he would like and expect to be paid within the year the tenant occupied the leased land. But if the tenant couldn't pay it all in that time, possibly because he hoped to use some of his earnings from farming the leased land, would it not be logical to arrange some terms whereby the tenant could pay while the lease runs and pay the balance over a period of time thereafter in order to spread out reduced payments?

How about the situation where a man rents a building or leases some acreage from an owner, and then decides to contest the title of the owner to the building or the land? Would it not be proper, expecting such a possibility, to include a provision in the lease that the lessee waives any right to question the title?

In all of these hypothetical situations or questions reference has been made to real property. Would the situation or result be any different if the subjects had been personal property? Suppose, instead of farmlands, the property had been automobiles which were leased either individually or in fleets. Suppose there were impositions of restrictions such as geographical areas of use, the fields of use, the setting of a price floor below which the vehicles could not be hired out for use as taxicabs, or suppose the payments for use of the cars were permitted to extend past the term of actual use? Would some government agency complain over any such restrictions? I doubt it, unless it could be established that the restrictions actually caused restraint of trade or violation of some other provision of the Sherman or Clayton anti-trust laws.

These may seem like strange questions to raise, but questions much like them and others equally strange have been raised in numerous instances of litigation over patents and patent licenses in recent years. In almost all such instances I believe courts would have no difficulty finding that substantially none of the situations I've described constituted any wrongdoing on the part of the property owner. Yet, if the property in a number of the foregoing illustrations involved intellectual property, e.g. patents, rather than real or other forms of property, the courts might be expected to hold that the property owner had entered into an illegal agreement with his lessee (or licensee). Why the difference? Why does it appear to be a case of *lese majeste* in the case of patent property and not in the case of real property or of other forms of personal property? After all, the patent statute, Title 35 U.S. Code, has said for many decades that "subject to the provisions of this title, patents shall have all the attributes of personal property."[1]

The basis for the difference in the treatment of patent property, as we shall see, is in the application of our anti-trust laws. Those laws, without question, were established to protect the public against monopolistic trade and other unfair commercial practices according to which one person or group may cause serious adverse economic effects upon the private property of another. Remember, it was the people who gave their government both the requirement for and the obligation to enforce those anti-trust laws. But it was the same people who also gave their government not only the obligation to protect private property of the intellectual variety, but also the mandate that special privileges be accorded those who publicly disclose the essence of their intellectual property to the end that all the people ultimately may benefit therefrom. Thus, it would appear that the government, in its zeal to protect against improper acts that might adversely affect the rights of the public to certain private property, must be just as zealous in protecting the public's interest in the development and utilization of other private property.

In other words, following Locke's admonition, the government must not so invade the property of the people as to become the arbitrary disposers of that property. When it comes to patents and patent licensing it would appear that the Justice Department may be guilty of just such an invasion even though its avowed purpose is to protect the people's property rights. If so, it is time for the people to speak up or else the anti-trust enforcers will become the arbitrary disposers of all patent property, and the way that property is disposed of may not be for the public good or what the people want. That time, I submit, has come! The voice of the people is being heard in the Scott Amendments[2] to the licensing provisions of the McClellan bill[3] to revise all of the patent laws. Those amendments are the voice of the people saying to those who would destroy some of the most important attributes of patent property—of private property—that in their zeal to protect the public against possible misuse thereof, which actually may be against the public interest, they may be fanning the flames of a form of creeping socialism, something the people do not want.

Before discussing the pros and cons of the Scott Amendments it might be in order to consider the problems that led to their promulgation. Ever since patents came into being with passage of the first Patent Act in 1790 patent owners have, just like real property owner-lessors, found it beneficial to license others to use, i.e. practice their patented inventions. Until only very recently patent licenses were considered to be simply agreements between a patent owner and a licensee, and the arrangements were subject to conventional, non-statutory laws of contracts.

Licensors do not in reality guarantee licensees the right to make, use or sell a licensed invention or patent. Patent rights of others may be involved, over which the licensor has no jurisdiction, and therefore the licensor cannot assure the licensee permission lawfully to practice the entire licened invention. What the licensor actually can and does do is to guarantee that he himself will not sue the licensee for infringement of his patent. In other words, he grants the licensee an immunity from suit under the licensor's patent.

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[1] Title 35, U.S.C., Sec. 261.

[2] Originally introduced on April 8, 1970 as Amendment No. 578 to Senator John L. McClellan's bill S. 2756 (91st Cong., 2nd Sess.), Senator Hugh Scott re-introduced it as Amendment No. 24 to the new McClellan bill S. 643 on March 19, 1971.

[3] S. 643 (92nd Cong., 1st Sess.) introduced February 8, 1971 as an up-dated version of S. 2756.

A patent license may be granted for practically any royalty and subject to practically any condition agreed upon by the parties, except where prohibited by anti-trust laws and the like.[4] The fact that the conditions may be heavily weighted on one side, usually the licensor's, traditionally will not of itself make the license invalid. However, some recent cases have shaken this tradition, for the amount of royalties, the period of their payment, and the basis of their computation have been challenged successfully.[5]

A patent owner, like a real or other personal property owner, might find himself in the position of being unable to utilize or to practice all aspects of his patented invention. Suppose, for example, the patent concerned ion exchange resins, and the patent owner's only interest in or industrial capacity for manufacturing and selling such resins was in connection with their use in the treatment of water. However, another important use of the invention, possibly with some minor manufacturing refinement or new marketing technique, was in the production of certain pharmaceuticals. Rather than deny himself the fruits of this additional use of the invention, and also not to deny the public the benefits thereof, the patent owner might agree to license a pharmaceutical manufacturer to use his invention. He might not want to grant the manufacturer a general license to use the patented invention as this might create a competitor in the water treatment field having the advantage which the patent owner had obtained by virtue of his patented invention. But it could make an important contribution to another industry—the pharmaceutical field. Such an arrangement is known as a field of use license, and the law has long considered such a license proper.[6] But the Justice Department now threatens to challenge certain types of those licenses.[7]

Traditionally, a patent owner has had the right to select his licensees when he elects to license his patent. Now a White House Task Force on Antitrust Policy has recommended "legislation to establish the principal that a patent which has been licensed to one person shall be made available to all other qualified applicants on equivalent terms."[8] If that should come to pass we may be shifting from creeping socialism to something more akin to a galloping variety.

A patent license usually conveys the right to make, use *and* sell the licensed invention, insofar as the patent grant permits. However, all three of these rights are separable and can be separately licensed independently of one another.[9]

Suppose a patent owner finds himself unable to make, use or sell his invention all over the United States. Rather than deny himself the full economic benefits of his patent grant, and likewise so as not to deny people all over the country the opportunity to benefit from his invention, it is logical for him to arrange to license others to make, and/or use, and/or sell the invention in geographical areas where the patent owner cannot operate conveniently or successfully. Thus, just like the land owner who sub-let parcels of his land to tenant farmers, or the person who decides to lease cars in certain sections of the country, the patent owner is able to license parties to make a patented product in any specific geographical area, such as by states, regions, or sections of the country.[10]

Having decided to grant a license, to whom, and possibly with regard to what part or all of the rights incumbent upon the patent owner, the next question to be considered is the basis for the license, i.e. the financial and

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4 United States v. American Linen Supply Co., 141 F. Supp. 105 (N.D. Ill. 1956), 109 U.S.P.Q. 273.

5 Meurer Steel Barrel Co., Inc. v. Martin, 1 F. 2d 687 (3rd Cir. 1924). But see American Photocopy Equipment Company v. Rovico, Inc., 359 F. 2d 745 (7th Cir. 1966), cert. den. 390 U.S. 945 (1968); Ansul Company v. Uniroyal, Inc., 306 F. Supp. 541 (S.D.N.Y. 1969); Brulotte v. Thys, 379 U.S. 29 (1964); and Zenith Radio Corp. v. Hazeltine Research, Inc., 395 U.S. 100 (1969).

6 General Talking Pictures v. Western Electric Co., 305 U.S. 124 (1938).

7 Address by Assistant Attorney General Richard W. McLaren, "Patent Licenses and Antitrust Considerations", before the Patent, Trademark and Copyright Research Institute, June 5, 1969.

8 Antitrust and Trade Regulation Report, No. 411, Special Supplement, Part II, May 27, 1969, page 3.

9 Cf. Ethyl Corp. v. Hercules Powder Co., Stauffer Chemical Co., and Texas Aklyls, 139 U.S.P.Q. 471 (1963) and 143 U.S.P.Q. 57 (D. Del. 1964).

10 Buffalo Specialty Co. v. Indiana Rubber & I. Wire Co., 234 Fed. 334 (7th Cir. 1916); Cold Metal Processing Co. v. United Engineering & Foundry Co., 235 F. 2d 224 (3rd Cir. 1956), 110 U.S.P.Q. 332.

related conditions under which the license is granted. There is no such thing as a "usual" royalty, although long experience with licensing in certain fields of business activity has led to so-called "customary" rates for licenses of certain categories of patented inventions. The amount of royalty is a negotiable item, and it will depend on how much the licensor feels he is giving and how much the licensee feels he is getting. Other factors may be: whether the license is to be exclusive or non-exclusive; for an entire machine or a small part; whether it includes know-how and trademarks (although some recent judicial decisions have shrouded such licensing activity in clouds of doubt); the size of the market and the share of which the licensee is likely to get. If the invention concerns an article or a composition of matter, royalties can be based upon the quantity, weight, volume, or some other physical measurement. If a process is involved it may be satisfactory to base the royalty on the measure of articles or of the compositions employed in the process, or the objects treated, or even the products made by the process. Whatever the yardstick, it may be applied to the price at which a product is sold, or the profit, or the sales made by the manufacturer.

If the royalty is based upon price, payments could be made proportional to:

(a) The product of the quantity made and the current price (wholesale or retail).

(b) Gross sales (i.e., money that manufacturers would receive if paid in full for all articles sold, even if sold but never paid for).

(c) Net sales (i.e. gross sales less returns and allowances—in this way royalties are based only on the money actually paid for articles involving the invention).

Basing royalties on profits probably is the fairest method of all, but it involves difficult problems in agreeing on the overhead rate to be figured in the cost, amounts to be spent for advertising, and other such items of expense which if allowed to be set off against gross income could cause little to be left for the licensor.

Royalties may be based upon the total sales of a product, even though such sales include non-patented items. This is not a case of tieing in the licensing of a patented product with an unpatented product; the sales volume of both categories of products is just a convenient way to measure royalty due on the use of the patented item.

Instead of basing royalty on dollar volume one may base it on such items as corporate stock value, net profits, an entire proruction (which may include patented and non-patented items; unpatented input or output, e.g. crude oil input or refined oil output, both unpatented).

Royalties frequently are based on a lump sum rather than any running arrangement. A major company in an industry may find it preferable to pay a flat sum based upon its production capacity of an item covered by a licensed patent, with additional flat sums payable if that capacity is increased to specified levels. A smaller licensee may favor the pay-as-you-go or running royalty arrangement so that if conditions dictate discontinuance of the licensed patent it will not lose any investment made in an unused license.

Traditionally, the length of time that royalties may be payable could be just about any period agreed upon by the parties. It may begin when an application is filed,[11] or after it has issued as a patent. (Here, it may be noted, is a doubtful area in the future of patent licensing. People in the Justice Department's Anti-Trust Division are already making noises about pre-patent issuance royalty agreements being illegal because they may support a competitively significant restraint on the licensee[12]). It may continue for a fixed number of years less than or equal to the life of the patent. It used to be O.K. to provide for the payment of royalties after the patent has expired. Now, however, even if the parties have so agreed for the convenience of the licensee, such extensions are illegal.[13]

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[11] Immunity from suit which thus is guaranteed when the patent issues is the consideration for the payment of royalties before issuance. Cf. Cook Pottery Co. v. J. H. Parker & Son, 89 W. Va. 7, 109 S.E. 744 (St. Ct. W. Va. 1921).

[12] Cf. statement by Prof. S. Chesterfield Oppenheim, in *Idea,* vol. 14, No. 3, Fall 1970, pp. 426–427, citing Richard H. Stern of Department of Justice.

[13] Brulotte v. Thys, 143 U.S.P.Q. 264 (Sup. Ct. 1964), in effect overruling E. R. Squibb & Sons v. Chemical Foundation, Inc., 93 F. 2d 475 (2nd Cir. 1937), 36 U.S.P.Q. 282; Rocform Corp. v. Acitelli-Standard Concrete Wall, Inc., 143 U.S.P.Q. 405 (D.E.D. Mich. 1964), et al.

Many of these and other patent licensing practices have in recent years come under scrutiny and either actual or threatened attack in the courts by aggressive anti-trust units of the Department of Justice. The result, particularly in the light of some recent decisions of the U.S. Supreme and lower federal courts, has been to create a climate of utter uncertainty in the law of patent licensing. The most skilled patent licensing or anti-trust lawyer is at his wit's end in trying to advise his clients regarding almost anything but a relatively routine patent licensing situation. As Marcus Hollabaugh has suggested:

". . . since the trend of the decisions have clearly been pro antitrust, one can assume that they will continue to be and advise against inclusion of any restriction or practice which might remotely be held to be an antitrust violation or a misuse. If he does that, he may end up with a legally immaculate document but the client may be financially defunct.

"The alternative course of permitting the client to engage in field of use licensing or in any of the other practices which the Justice Department is now testing or proposes to test, is fraught with danger to the client. He may find himself a defendant in a lawsuit or a counterclaim, the possessor of a patent which he cannot enforce and worst of all, paying treble damages." [14]

The Scott Amendments dealing with patent licensing are aimed at eliminating this confusion and restoring to patent owners, would-be licensees, and to their attorneys some reasonably clear-cut guidelines as to what licensing practices are illegal. They are not designed to make lawful by statute those misuses of patents which both patent and anti-trust lawyers have long ago agreed were against the public interest. They are designed to restore some viability to the patent system by explicitly legalizing some patent licensing practices which at one time were approved by the courts but which, under the incessant attacks by the Justice Department, have more recently been judicially disapproved or are in danger of being held illegal by judicial decree if the threats of future suits by the Justice Department should materialize. Let us review what the Scott Amendments propose to do and not to do.

Upon enactment of the Scott Amendments, it will still be illegal to tie in a patent license with an unpatented product or a restriction against buying unpatentable items from someone else.[15] It probably will be illegal (although this is a point to be thrashed out at the Hearings on the Amendments) to so fix the prices at which a licensee may sell the item he is licensed to make, use or sell as indirectly to fix the prices on unpatented elements and unpatented materials embodied in the patented items. It will still be illegal to so fix prices of patented processes or machines as indirectly to fix prices and other conditions of unpatented products made by the patented process or machine.[16]

Any patent license contract or combinations that have the effect of improperly restraining trade will continue to be illegal.[17] Any patent license agreement having provisions which are not reasonable to secure the patent owner the full benefit of the invention and patent grant will be illegal, an example being a requirement that the licensees abstain from making or selling products that compete with a patented product.[18]

On the other side of the coin the right of a patent owner to license all or less than all of his patent grant would be clearly established. He could license for less than the full term of his patent; license to make, use and sell, or just to make, just to use, or just to sell; license the practice of his patent only for specified sizes of items, or for specified purposes or fields.[19]

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[14] Hollabaugh, "The Scott Amendments v. The Second Crusade", address before Annual Meeting of Section of Antitrust Law of American Bar Association, St. Louis ,Mo., August 10, 1970.

[15] "Antitrust Problems in the Exploitation of Patents", a staff report to Subcommittee No. 5 of the Committee on the Judiciary, House of Representatives, October 15, 1956, pp. 9–12.

[16] Farley, "Price-Fixing and Royalty Provisions in Patent Licenses", 34 J. Pat. Off. Soc'y (1952). Cf. Sherman Act. 26 Stat. 209 (1980). 15 U.S.C.S. (1937); Section 3 of Clayton Act. 38 Stat. 731 (1914); 15 U.S.C. 14 (1937): U.S. v. Socony-Vacuum Oil Co., 310 U.S. 150 (1940); F.T.C. v. Cement Institute. 333 U.S. 683 (1948); U.S. v. General Electric Co., 272 U.S. 476 (1926): U.S. v. Line Material Co., 333 U.S. 287 (1948); U.S. v. Gypsum, 333 U.S. 364 (1948); and U.S. v. Huck Manufacturing Co. et al. (D.E.D. Mich. 1964), 140 U.S.P.Q. 544. aff'd. U.S. Sup. Ct., 147 U.S.P.Q. 404 (1965).

[17] Hartford-Empire Co. v. U.S., 323 U.S. 386 (1945).

[18] National Lockwasher Co. v. George K. Garrett Co., 137 F. (2d) 255 (3rd Cir. 1943).

[19] Section 271 (f) (1), reaffirming the rule of General Talking Pictures v. Western Electric Co., Inc., 305 U.S. 124 (1938); Atlas Imperial Diesel Co. v. Lanova Corporation, 79 Fed. Supp. 1002 (D. Del. (1948).

The so-called "reasonableness" of all or of a particular portion of the total patent right to exclude, that is offered for license or is licensed, would not be subject to question. Nor would the refusal of a patent owner to grant a license be subject to review (except possibly only where the public health and welfare were at stake).

Any terms in a license that are reasonable to secure to the licensor the full benefit of his invention and patent grant would be lawful and free from challenge under the antitrust or other laws, an example being a requirement that the licensee furnish data as to what is sold by the licensee so as to determine that royalties based on a percentage of the sales price are correctly paid.[20]

Cross-licenses and non-exclusive grant backs of rights to improvements on licensed patents will be stamped as lawful.[21] The amount of royalties will clearly be left to the parties concerned as a matter of private bargaining, and not as a matter of concern to the public at large.[22] Moreover, the licensee will be able to pay royalties after expiration of a licensed patent, provided that the payment is based upon activities which clearly took place prior to such expiration.[23]

The law will be reaffirmed to the effect that one need not measure consideration for a patent license by the extent of use of the patented invention. Minimum royalties, for example, once an accepted feature of patent licenses but recently questioned as being improper, will be firmly established as a lawful practice.[24] Package licensing will likewise be approved, as is now the case but even though the royalty charge is not segregated as to any particular patent or patent claim such licensing practices will not be considered unlawful.[25]

The law will be settled that a patent owner may, without laying himself open to a charge of patent misuse, charge different licensees dissimilar royalty rates.[26] This is not to say that if in so doing the patentee actually violates the Sherman or Clayton Acts or the Federal Trade Commission Act.[27] and the licensing practice truly causes restraint of trade or adversely affects a segment of industry, the arrangement with the licensee will be considered legal.

The doctrine of licensee estoppel will be partially restored to the status it had before a recent decision of the U.S. Supreme Court.[28] Before the 1969 decision threw out such provisions, by virtue of a stipulation to that effect in a patent license agreement a licensee could be estopped to contest the validity of a licensed patent. The Scott Amendments[29] will make it possible for a licensee, regardless of a contractual stipulation to the contrary, to contest patent validity but only after he gives written notice to the licensor that he unconditionally renounces all future benefits from the license. Furthermore, notwithstanding such renunciation the renouncing party is still liable for his obligations due the licensor prior to the renunciation.

Keeping on balance the equities between patent owners and the purchasers of patent rights, an assignor of a patent shall be forbidden from contesting the validity of an assigned patent asserted against him unless he (1) returns to the assignee the consideration given for the patent, and (2) asserts a new ground for patent invalidity not known to him when he assigned the patent.[30]

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[20] Section 271 (f) (2).

[21] Section 271 (g) (1). See U.S. v. National Lead, 332 U.S. 319, 359 (1947); Transwrap Machine Corp. v. Stokes & Smith Co., 329 U.S. 637 (1947) held assignment of improvement patents to licensor was not per se illegal. This may not be the law today. Non-exclusive grant-backs clearly should be, as they foster rather than restrict competition, and are proper so long as they are not accompanied by sublicensing rights. Cf. Binks Mfg. Co. v. Ransburg Electro Coating Corp., 281 F, (2d) 252 7th Cir. (1960).

[22] Section 471 (g) (2) (A). Cf. American Photocopy v. Rovico Co., Inc., 359 F. (2d) 745 (7th Cir. 1966), cert. den. 390 U.S. 945 (1968); 384 F(2d) 812 (7th Cir. 1967).

[23] Section 271 (g) (2) (A). in effect reversing or at least limiting the effect of Brulotte v. Thys. 43 U.S.P.O. 264 (Sup. Ct. 1964).

[24] Section 271 (g) (2) (B). Cf. Automatic Radio Mfg. Co. v. Hazeltine Research, Inc., 339 U.S. 827 (1950).

[25] Section 271 (g) (2) (C). Cf. Rocform Corp. v. Acitelli-Standard Concrete Wall, Inc., 367 F. (2d) 678 (6th Cir. 1966); American Securit Co. v. Shatterproof Glass Corp., 268 F (2d) 769 (3rd Cir. 1959); Allied Research Products, Inc. v. Heatbath Corp., 300 F. Supp. 656 (N.D. Ill., 1969).

[26] Section 271 (g) (2) (D).

[27] For example, if as in La Peyre v. F.T.C., 366 F (2d) 117 (5th Cir. 1966), the facts are such as to warrant a charge that the licensor's demands offended Section 5 of the FTC Act or the Sherman Act, the demands might be held unlawful. The right to grant licenses at dissimilar royalty rates to different licensees would not be permissible if the result would be to substantially and unjustifiably impair competition in an industry.

[28] Lear v. Adkins, 395 U.S. 653 (1969).

[29] Section 261 (f).

[30] Section 261 (e).

If there is any doubt over an inventor's right to license or assign an application for patent, or a patent, or any interest in either and to do so for the whole or any part of the United States, the Scott Amendments will remove them with some categorical provisions authorizing such practices.[31]

In concluding, I must observe that there have indeed been some startling changes in the characteristics of private property taking place in the United States. They are not so apparent in the case of real property. Although I haven't discussed in any detail the characteristics of personal property of the tangible variety, I might dare generalize by saying that the law in that field has not changed radically, either. People always could lease automobiles or motor boats to almost anyone they chose, at almost any rates or most any basis they pleased, in almost any area of the country they desired, and lease them as a package for a package price regardless of the variances of need or use for members of the package. With rare exception, would any government official find legal fault with such arrangements per se, providing they weren't used in some manner so as to break some law? How different has been the situation with leases or licenses of patents and other forms of intellectual property.

The early objections against patent licensing practices came from Justice Department officials charged with enforcement of the Sherman and Clayton anti-trust acts, and were directed at any misuse of patents resulting in unreasonable restraints of trade. These were and are proper acts of government, seeking to protect the economic rights of people who were being unlawfully set upon by people who used patents and patent licensing restrictions for the creation of such unlawful trade restraints. But the anti-trust enforcers have gone too far in the other direction when they have attacked patent licensing provisions to the point where patents are becoming more and more of questionable value to their owners, and the value of even seeking patents or of investing in research, the fruits of which can probably only be protected against industrial piracy by patents, is becoming a seriously doubtful one.

The people of this country saw in the patent incentive system the means of contributing to the progress of the arts and sciences of the nation, and therefore provided for such a system in the Constitution.[32] The people gave to their government the duty of establishing laws to make that system work effectively to accomplish that objective. The same people gave to their government the duty to establish laws to prevent unlawful restraints of trade by any means, including the unlawful use of devices which otherwise are lawful, and "devices" include patents. It is doubtful, however, that the people, heeding John Locke's advice, gave their government the authority arbitrarily to decide that one system of laws—the anti-trust laws—shall be employed to make another system of laws—the patent laws—impotent to achieve their stated objectives. If there is any question regarding that doubt at this time, enactment into law of the substance of the Scott Amendments will help materially to resolve the question with relatively complete clarity, hopeful for all time to come.

General Motors Corp.,
Detroit, May 3, 1971.

Hon. John L. McClellan,
U.S. Senate,
Washington, D.C.

Dear Senator McClellan: In response to your letter of April 14, 1971, concerning S. 643, we are not aware of a current need to modify the traditional functioning of the patent system in order to achieve the objectives of the Clean Air Act, as amended.

As a matter of policy, we have granted licenses on reasonable terms under our patents which relate to safety and health items. We did not oppose or sup-

[31] Section 261 (b).
[32] Article 1, Section 8.

port the mandatory patent licensing provisions of the Clean Air Act, as amended.

If you wish, R. F. Magill, Vice President, GM Industry-Government Relations, will be pleased to meet with your staff for further discussions.

Sincerely,

E. N. COLE.

NEW YORK, N.Y., *June 4, 1971.*

THOMAS C. BRENNAN, Esq.,
Chief Counsel, Subcommittee on Patents, Trademarks, and Copyrights, U.S. Senate, Washington, D.C.

DEAR MR. BRENNAN: In connection with the hearings on the Scott Amendments, the attached paper may be of some interest. It is my understanding that, although the hearings are closed, the record may still be open for additional submissions of material.

The enclosed document was written by me and the "we" to which it refers is the editorial "we".

Very truly yours,

ELIOT S. GERBER.

THE LICENSABLE NATURE OF PATENT RIGHTS AND ITS RELATIONSHIP TO THE ANTI-TRUST LAWS

With the increasing specialization and sophistication of research activity it often happens that the university, person or company which makes an invention is in no position to exploit it in the marketplace, or at least is in a less good position than others. Under present law he can assign his rights, assignments being expressly permitted in the Patent Act, 35 U.S.C. § 261.[1]

But it has long been recognized that a more varied choice of contract relationships relating to patents would be likely to provide for a greater return to the patentee, encouraging him to invest in research and to invent, and would also better enable the patent to come into use sooner and on a wider scale, benefiting industry and the consuming public.[2] Such a varied bundle of contract rights is consistent with real estate law, with its leaseholds, easements, licenses, etc. Similarly, licensing is a way of life in other areas of the law in which the originator of the material allows others to exploit it, for example, in trade mark law (including franchising), copyright law, and entertainment law. A parallel development has not occurred in some areas of governmental franchise in which the franchise is granted to those personally able to exploit it, for example, in the grant of air line routes, broadcasting channels and the right to dam navigable rivers.

The passage of the anti-trust laws initiated years of litigation in which, on a case-by-case basis, patent license clauses were attacked on the grounds that they violated the ant-trust laws. Agreements entered into in good faith, and with the advice of competent counsel, were held to be illegal, resulting in monetary loss and the effective destruction of patents. Similarly, due to the patchwork nature of case development, patent license practices have been sanctioned by court cases which are perhaps inconsistent with the general development of this area.

The need for some type of sanction and certainty has engendered a number of legislative proposals which may be introduced into Congress. Regardless of one's views as to whether Congress is a better forum than the courts for establishing some borderline between patent license rights and the anti-trust laws, it is entirely possible that Congress will take some sort of action. It is our understanding that the "Scott Amendment" No. 24 to amend S. 643 (92d Congress) has been introduced for this purpose.

Rather than attempt to criticize the exact language of such proposals, as such language is bound to be revised in the course of hearings, this report is based upon a broad view of the basic principles involved in the licensing of patents, with some occasional suggestions for statutory language.

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[1] But assignments obtained as part of an illegal purpose or plan are improper—United States v. United States Gypsum Co., 333 U.S. 364 (1948) and patents are "assets" under the Anti-Merger Act, PL 899.

[2] Motion Pictures Patents Co. v. Universal Film Mfg. Co., 243 U.S. 502 (1917).

I. SOME GAPS IN THE PRESENT PATENT ACT

It seems relatively uncontroversial that some statutory sanction be given to the licensing of patents. At the present time 35 U.S.C. § 261 provides that patents may be assigned and that patents are personal property. A parallel provision stating that a patentee may license or waive his rights by an exclusive or non-exclusive arrangement would provide broad, and itself innocuous, sanction for current and accepted practice. A suitable clause would be:

> "Applications for patent, patents or any interest therein shall be assignable in law by an instrument in writing. The applicant, patentee, or his legal representative in like manner may license or otherwise grant or waive any of his rights under his patent or patent application for the whole or any specified part of the United States by exclusive or non-exclusive arrangement with a party or parties of his selection."

The Patent Act presently provides that patents shall have the attributes of personal property. To be consistent and avoid unnecessary questions, for example, in bankruptcy law or decedent's estates, the Patent Act should also provide that patent applications are personal property.

The Patent Act now provides that patents may be assigned in a division by territory. An exclusive license, for most purposes, is but an assignment with the retention of a security interest to insure payment. There has not come to wide attention any abuses of the territorial assignment grant, so that the right to license on an exclusive basis should also be expressed in the Patent Act. All territorial restrictions are subject to the overriding doctrine of freedom of alienation, in which the first sale of the goods terminates any territorial restriction and the purchaser is free to use anywhere.[3] In the case of industrial process a territorial restriction may be a sensible way of exploiting the invention and would not lead to monopoly, as those who buy the goods produced would be free to use or resell them anywhere.

In addition, the franchise system of distribution, although subject to financial abuse, has proved an incentive for independent businessmen. In certain cases exclusive and non-exclusive territorially restricted license is a basis, or a useful adjunct, in a franchising system. The cure for any abuses of franchising which may exist would seem to be in enforcement by the Securities and Exchange Commission and possible legislation specifically directed to such abuses. The cure does not lie in restrictions on patent licensing, because in many cases patents are not even part of the franchising system.

Non-exclusive licensing, on a territorial basis, may, at least conceptually, be subject to abuse and consequently should be the subject to the standard of reasonableness which should be applicable by statute, to other license provisions.

II. REASONABLENESS AS A STANDARD FOR LICENSE CLAUSES SANCTIONED BY STATUTE

We believe that the patent license terms which are sanctioned by statute, except for territorial assignments and exclusive licenses, should be subject to a standard of reasonableness. This middle ground has the benefits of: (i) assuring the patentee that such provisions, when utilized by him, would not be a "per se" violation of the anti-trust laws or constitute patent misuse, and (ii) preventing patentees from erecting or maintaining shocking or oppressive license schemes because the license provisions necessary to effectuate such a scheme happened to fall literally within the wording of a provision sanctioned by the Patent Act.

Some legislative proposals in this area, such as the "Scott Amendment", use language which sounds at first hearing like a standard of reasonableness under the anti-trust laws, but which could be otherwise interpreted. The "Scott Amendment" states that a patentee's conduct is permissible, if it "excludes or restricts conduct in a manner that is reasonable under the circumstances to secure to the patent owner the full benefits of his invention and patent grant".[4] Such language ties "reasonableness" to benefiting the patentee, and does not make clear that other interests and factors must be weighed as well.

What, then, should be the standard of reasonableness in a license agreement?

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[3] Adams v. Burke, 17 Wall. 453 (1873) ; Boston Store of Chicago v. American Graphophone Co., 246 U.S. 8 (1918).

[4] This approach to the definition of "reasonableness" is consistent with the Report of the Atty. Gen. Nat ; 1 Comm. to Study the Anti-Trust Laws 231 (1955) ; and United States v. General Electric Co., 272 U.S. 476, 490 (1926).

We believe that a license is "reasonable", in this context, if it (i) assures the payment to the patentee of royalties agreed to be paid him by reason of the use or sale of the patented invention with his consent, *or* (ii) secures to him in his own manufacture, use or sale of the patented invention such price or cost advantage as would have accrued to him in the absence of infringement by others without his consent. However, a license restriction would not be "reasonable" if the effect of the restriction is to lessen competition or create a monopoly in the manufacture, use or sale of any product or process not covered by the patent rights licensed.

We omit from our definition of "reasonabless" the effect of substantially lessening of competition of the goods covered by the patent, since the effect of any successful patent is to lessen such competition or eliminate it. Particularly with the tendency of the courts to more narrowly define a line of commerce, it may come about that a line of commerce is defined to be exactly the patented goods or process. However, it is the very rare patent which gives monopoly power in the anti-trust sense, to fix prices or exclude competitors from a commercially significant market, as distinct from the legal monopoly of the patent grant.

If the terms of a waiver, license or grant of the patentee or patent applicant are "reasonable", as defined by the Patent Act, and those terms fall within the list of sanctioned license terms, then he should not be denied relief, either in court or by administrative action, or be deemed guilty of misuse or illegal extension of patent rights.

In this connection, legislative proposals have used the phrase, "otherwise entitled to relief under this title", i.e., under the Patent Act. However, that phrase, similar to the language in 35 U.S.C. § 271(d), is objectionable because, if taken literally, it may cause a patentee who sued and lost on the issues of infringement or validity, to be guilty of misuse or illegal extension of patent rights even though his license provisions were sanctioned by the Patent Act.

III. A LISTING OF SANCTIONED LICENSE PROVISIONS

The "Scott Amendment" has a general statement that "reasonable" license provisions are sanctioned and then various provisions are listed as being proper without reference to any test of reasonableness. We do not approve this statutory scheme. Nor do we accept the alternative scheme of sanctioning all "reasonable" provisions and then listing provisions which are not legal.

We prefer a positive list of acceptable license provisions, with each such provision being subject to a general "reasonableness" clause. Since the minds of lawyers, and the facts of commercial life, are endlessly complex, we recognize that we cannot list all the license provisions which might be needed. For that reason we suggest a general saving type clause remitting license provisions outside the list to the mercy of the general anti-trust and patent misuse doctrines. A suitable general saving type clause would be:

> "A license, assignment or waiver of rights not within the foregoing provisions of this section shall not be deemed to be a misuse or illegal extension of patent rights merely by reason of the fact that it is not within such foregoing provisions."

A. *Patent Term*

It is clear that a patent or patent application cannot be licensed beyond its term. Sometimes a patentee or patent applicant may wish to license for less than the full term of years, for example, to test the effectiveness of the licensee, to test the market, or to accumulate capital. We approve of a provision which would permit a license, assignment or waiver of rights to some part less than all of the patent term.

B. *Field of Use and Embodiments*

It sometimes happens that an invention is useful in two separate markets which are best served by different licensees. For example, a sonic inspection device may be used in hospitals and in steel mills, and normally manufactured and sold to those different markets by different companies and at different royalty rates. No reason is seen not to permit license provisions which would license only some of the uses or embodiments covered by a patent or patent application provided the markets are non-competitive.[5]

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[5] General Talking Pictures Corp. v. Western Electric Co., 305 U.S. 124 (1938) but see Vulcan Mfg. Co. v. Maytag Co., 73 F. 2d 136 (8th Cir. 1934).

Where, however, the markets are competitive, as for example, where only one form or use of the patented device is licensed and other forms or uses, if licensed, would compete in the very same market, or where sales are licensed to a limited class of customers and not to other potential customers, we would not per se approve express statutory sanction of such "field of use" or "embodiments" license because of their potential anti-competitive effects, but would leave those questions to the ordinary operation of the anti-trust laws.

A license agreement limited to a class of customers has the effect of limiting customers' free choice of purchase and is close, in effect, to price fixing, since the customer will not be free to purchase the licensed goods from another. A limitation to a class of customers, for example, hospitals, may often be expressed as a use, i.e., hospital use. In those instances when a class of customers cannot be expressed as a field of use or embodiment restriction, it may constitute a division of the market without a general economic justification. In these instances, as elsewhere, licenses may be found to contain provisions, for example, divisions into classes of customers, not sanctioned by the Patent Act. Such licenses would be subject to the ordinary operation of the anti-trust laws.

C. Restrictions on Quantity

The term "quantity" means, in the case of a product patent, the number of such products and, in the case of a process patent, the number of times the process is performed. A limitation on quantity is similar to a limitation on term of the agreement, except expressed numerically instead of by the passage of time. It may be reasonable for a patentee or patent applicant to have one, or more, of his licensees produce enough only to satisfy part of the demand, so that he, or other licensees, may satisfy the rest. For example, a small company may wish to limit the quantity produced by a licensed larger competitor, lest his own production be swamped by that of the competitor. As in the case of the patent term the strong commercial interest of licensees in retaining for themselves the market they develop, rather than handing it back to the licensor, would help prevent abuse. Quantity restrictions, by themselves, are not a mask for price fixing or divisions of the market, since each licensor is free to sell his allotted quantity to whomever he wants at whatever price he desires.

Likewise we see no harm in permitting patent applicants or patentees to license different claims of their applications or patents to different licensees, provided such licenses are subject to the overall standard of reasonableness we have proposed.

D. The Licensing of Making, Using or Selling as Separate Rights

The Patent Act 35 U.S.C. § 154 states that a patent shall grant the "right to exclude others from making, using or selling the invention throughout the United States . . ." These rights have traditionally been considered as separate rights which may be individually licensed, for example, a company in a selling business may have an employee who has made an invention and may wish to have others licensed to manufacture the invention and yet retain for itself the exclusive right to sell it. There is an economic justification for permitting such division of rights, in that the individuals in an industry are better able to appraise how a particular product or process may be most profitably and widely brought to the market. Their judgment on such matters, unless it runs afoul of public policy, including the anti-trust laws, should not be fettered. While it is conceivable that the separate rights to manufacture, sell and use may be subjected to abuse as in the case of other license rights, they should be subject, under our view, to the "reasonableness" requirement. The distinct licensing of making, using and selling have been widely utilized in license agreements for many years. As far as we are aware, these provisions are not controversial.

E. The Non-Sanctioned Provisions

We have also considered other license provisions some of which have received the approval of the courts and others which have not. We have omitted these from our list of sanctioned provisions for various reasons, generally because they were, except in unusual situations, illegal, of little commercial importance, or so dependent upon the commercial facts of a particular industry that a general statutory provision was inappropriate.

We mention the excluded provisions merely for completeness and, in some instances, for comment. These excluded provisions are:

1. Price fixing clauses. The only area of possible legality left here is the fixing of the prices of a sole licensee.[6] However, that type of licensing is of no practical importance of which we are aware and is highly controversial. We do not imply that all other price fixing provisions are "per se" violations, because there may yet be a set of circumstances where a court would find it reasonable.

2. Tying provisions. The tying cases are among the earliest in which license provisions, namely, the forced purchase by a licensee of non-infringing goods, were considered.[7] As in price fixing, the burden rests on licensors to prove that their tying clause situation is legal.

3. Resale restrictions. It has long been law that the first sale exhausts the patent monopoly, that is, the purchaser's freedom of alienation cannot be restricted by the license of his seller. To some extent such freedom is restricted by a field of use license in which a purchaser who uses the goods for an unlicensed use would infringe. We do not sanction restrictions on resale as such, but the economic justification for field of use licenses outweighs the resulting effective limitation on purchasers.

4. Licenses involving joint power to issue sublicenses. This type of provision has been subject to careful judicial scrutiny.[8] It is, however, difficult to see why, if the licensor or the licensee could each sub-license, for what good purpose they should agree before doing so. However, we think the subject is too arcane and too trivial for inclusion in the statute.

5. Interchange of patent rights (pooling). In an interchange agreement one or more of the patent owners may license the patents of all. This subject does not require legislation at this time as the case law seems to delineate satisfactorily what is proper from what is improper conduct.[9]

6. Recording of all license agreements. It has been suggested that all patent license agreements should be recorded, in order to be eligible to be enforceable, in order to expose illegal license clauses.[10] However, patent agreements are no more subject to abuse than are other contracts. The preservation of commercial privacy would seem to outweight any benefit in forcing businessmen to expose such agreements. In addition, the bare terms of an agreement do not reveal its factual context upon which its legality may rest.

IV. PERMITTED FORMS OF COMPENSATION

The simplest form of compensation to a patentee or patent applicant would be a lump sum payment for his waiver of rights or license. However, lump sum payments are seldom used because they involve a speculative guess as to future use or sale of the patented invention. Compensation, consequently, more often takes the form of a running royalty in which the royalty is proportional to the number or value of the goods made, used or sold.

The problem of the permitted forms of compensation involves two aspects. First, it is clear that a statute ought not to authorize a compensation so structured as to provide a monetary benefit in performing an otherwise illegal act; for example, the royalty rate usually ought not to be dependent upon the licensee's purchase of non-infringing goods from the licensor. On the other hand, the types of compensation should not be so limited by statute that commercial situations which may involve a more complex compensation scheme would become impossible.

We recommend that sanctioned considerations be listed under a statutory provision which would state that the patentee or applicant shall not be denied relief or deemed guilty of a misuse or illegal extension of patent rights solely because he has entered into, or only will enter into, an assignment, license or waiver of some of his own rights under the Patent Act for the considerations listed in the statute. In addition, a general saving clause which would permit

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[6] United States v. General Electric Co., 272 U.S. 476 (1926) and Atty. Gen. Nat. Comm. to Study the Anti-Trust Laws 233 (1955), but see United States v. Line Material Co., 333 U.S. 287 (1948).

[7] Heaton-Peninsular Button-Fastener Co. v. Eureka Specialty Co. (6th Cir. 1896) 77 F. 288.

[8] United States v. Besser Mfg. Co., 96 F.S. 304 (D.C. Mich. 1951) aff'd 343 U.S. 444 (1952).

[9] See United States v. General Electric. 80 F.S. 989 (DC NY 1948) ; Cutter Laboratories v. Lyophile-Cryochem Corp.. 179 F. 2d 80 (9th Cir. 1949) ; Hartford Empire Co. v. United States. 323 U.S. 386 (1945).

[10] National Patent Planning Commission IIIA (1941).

other types of compensation than those which are listed should be utilized, with the understanding that such other compensation schemes would not be specifically sanctioned by the statute and consequently the parties entering such other compensation schemes face the same problems that they now face in showing legality or lack of patent misuse. A suitable saving clause would be as follows:

> "A license, assignment or waiver of rights for a consideration not within the foregoing provisions of this section shall not be deemed to be a misuse or illegal extension of patent rights merely by reason of the fact that it is not within such foregoing provisions."

Our suggested list for sanctioned compensation devices is as follows:

A. The licensor may receive back from the licensee a non-exclusive license or waiver of patent rights. This type of provision would sanction cross-licensing and grant-back provisions.[11] In our belief, a non-exclusive license back to the licensor would broaden rather than hinder competition because it would permit another party, namely, the licensor, to compete in the same market.

The scope, if any, of permissible *exclusive* grant-back provisions is highly controversial. On the one hand, there is little incentive to a manufacturing licensor to license a larger competitor when the greater inventing-facilities of the licensee are likely to overwhelm and ultimately exclude the licensor from the business. On the other hand, the owner of a dominant patent may use grant-back provisions to strengthen his own patent position and to weaken that of his competitors. The "Scott Amendment" does not meet this issue. We think it covered by ordinary application of the anti-trust laws.

B. The disclosure of confidential information to the licensor. We recommend a provision providing that the licensor shall be permitted to receive a disclosure of trade secrets, know-how or the contents of pending patent applications from the licensee or assignee. It will be understood that, as used in this context, the term "licensee" or "licensor" includes reference to other arrangements which are not true licenses, namely, assignments and waivers of patent rights. The disclosure of confidential information by licensee to his licensor may be necessary for them both to fully exploit the invention.

In many ways a licensor-licensee arrangement is a joint venture and the parties, as in other joint ventures, should be able, as between themselves, to exchange confidential information. Such exchanges of confidential information should be limited to trade secrets, know-how or contents of pending patent applications which are related to the subject matter of the license, to avoid any question being raised that the disclosure could be used as a guise for the exchange of other secret, price or customer information between competitors.

C. The royalty fee or purchase price should be broadly permissive as to its form. The money consideration, which may be in the form of royalty fee or purchase price, should, generally speaking, be broadly sanctioned as long as it is not a guise for activities which go beyond the patent grant. The permitted money consideration should be acceptable if it is in any amount, and however and whenever paid, provided that any amount paid after the expiration of a patent is not based upon activities subsequent to such expiration. This type of provision would allow financial arrangements which extend the period of payment beyond the term of a patent, but would avoid the effect of a licensee paying for patent rights which extend beyond the term of the patent.[12] In effect, this sanctions financing schemes which would have the same effect as issuing a note or bond to be paid over a 30-year period in return for an assignment or license of a patent for a 17-year term. We see no harm in such financing schemes and, insofar as it permits smaller companies to bear the financial burdens, such schemes may be beneficial.

There has been considerable dispute as to whether or not the money consideration must be measured by the subject matter of the application for patent or patents, or by the extent of the use of the rights licensed, assigned or waived. There has been similar controversy as to whether such consideration is legal if it fails to segregate the royalty fee or purchase price for any right licensed, assigned or waived from any other right licensed, assigned or waived. We take the view that such package licensing should be entirely permissible where it is for the mutual convenience of the parties and is not a device by which a licensor extracts payments from an unwilling licensee based upon patents which the

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[11] Stokes & Smith Co. v. Transparent-Wrap Co., 161 F. 2d 565 (2d Cir. 1947), cert. den. 332 U.S. 787 (1947).

[12] Brulotte v. Thys, 379 U.S. 29 (1964).

licensee does not want or intend to use or based upon goods not related to under the licensed patents.[13] We would suggest statutory language using an appropriate term such as "for the mutual convenience of the parties", which would sanction licensing only on those conditions.

We would also sanction a royalty fee or purchase price differing from that provided in other arrangements. This is price discrimination in regard to the royalty payments.[14] However, such discrimination may be economically justified, for example, a patent may cover a method of plating both gold and brass and we do not see any objection to having those who plate gold pay more than those who plate brass. This is consistent with other factors of industrial production. One does not expect that an office building landlord will give all of his tenants, regardless of the prestige they may bring to the building, their credit standing or their bargaining power, the same rental, so similarly we see no compelling reason why licensees should all receive the same royalty rate.

PAUL LOUIS GOMORY,
Washington, D.C., May 14, 1971.

Hon. JOHN L. MCCLELLAN,
U.S. Senate,
Washington, D.C.

DEAR SENATOR MCCLELLAN: Having attended the recently held hearings before your subcommittee and having worked for years in various committees dealing with patent law and currently serving on the D.C. Bar Association Patent Section, Antitrust Law Committee, and also as Chairman of the Section's Patent Law Committee, I believe that I am qualified fully to state the following views which are my own but in which I know I have the support of a great many persons, some of whom are patent lawyers, some of whom are professors of law and a good many of whom are in business and who are not necessarily even lawyers.

During the hearings, I could not help but reflect upon the problems relating to "misuse" of patents which I first encountered when drafting licensing agreements at the tender age of 25 years. In those days "misuse" was fraught with many questions. After a host of cases decided in the field, the same state of affairs exists. True, we now know that some courts have held some practices to constitute misuse. We also know that there are practices which have not yet been held to be per se illegal. There exists need for clarification.

In passing, I cannot refrain from noting that, depending upon the particular atmosphere prevailing at the time, courts do change their minds. Witness our own Supereme Court in the last fifteen or twenty years!

That there is need for Congress to exercise its plenary legislative powers has been emphasized to anyone who has attended the hearings. A reading of the record of the hearings, including the papers presented, questions asked and answers received, must even to the casual onlooker explain the need for legislation. As one of the witnesses for industry who is president of a small company, Mr. Cole of Philadelphia, stated it is time for the other shoe to be permanently suspended or to be allowed to drop!

I wholeheartedly subscribe to the evidence given by spokesman from industry, particularly to the *specific examples* given by them, which I need not here repeat. They are emblazoned on the record for all time. I also heartily subscribe to the views put by the Department of Commerce, former Commissioner of Patents Edward J. Brenner and Profesor Glenn Weston of George Washington University School of Law.

My letter would be incomplete if I did not disagree, in substance as well as in principle, with the testimony of Professor Stedman in particular and others in general.

The practical matter of fact is that business, upon which America depends for its economic posture here and abroad, should be given at least guidelines based upon which they can act. I do not for a moment believe that any

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[13] Zenith Radio Corp. v. Hazeltine Research, 395 U.S. 100 (1952) ; Ethyl Gasoline Corp. v. U.S., 309 U.S. 436, 459 (1940) ; Automatic Radio Mfg. Co., Inc. v. Hazeltine Research, Inc., 339 U.S. 827 (1950).

[14] LaSalle St. Press Inc. v. McCormick & Henderson, Inc., 293 F.S. 1004 (DC Ill. 1968) and Laithram Corp. v. King Crab, Inc., 244 F.S. 9 (DC Alaska 1965).

guideline given will be perfect. No legislation can ever be such. However, it is time we got started. With time, additional legislation and, unavoidably, court interpretation thereof will ensue. This will be to the general good.

I particularly subscribe to the fact that Department of Justice spokesmen, as in my presence, have repeatedly made assertions which would cause me to shun certain practices which I know today have not been held to be per se illegal. I do not for a moment condone practices which some few have followed. However, there appears to be no need compelling upon Congress or the Department of Justice to cause business in general to bear the brunt.

One final point. I believe it is crystal clear from the *intent* of the Scott Amendments that no final court decision is sought to be overruled. When asked the question, the Department of Justice spokesman could not point to any decision which would be overruled. I would urge that any legislation drafted include a statement of intent that no final court decision is intended to be overruled in the enactment of the legislation. Whether such a decision may be overruled at a later time, as by a court or further legislation, would be a different question to answer at a time other than this.

Concluding, it seemed to me that some of the witnesses who did not believe legislation is now needed were misreading the intent and the wording of the Scott Amendments. I do not by this subscribe to the precise wording. In fact, as you know no doubt, there are several redrafts now current and no doubt more will be coming. Accordingly, any decision reached by the Congress should be reached in the light of the best language which all parties concerned can draft.

There should be legislation to clarify the confusion which the hearings amply demonstrated exist, even among the most knowledgeable of us.

Thank you for your kind attention to this letter.

Sincerely yours,

PAUL L. GOMORY.

P.S. I would like to have this letter printed in the record.

MAY 6, 1971.

SENATE SUBCOMMITTEE ON PATENTS, TRADEMARKS, AND COPYRIGHTS,
Old Senate Office Building,
Washington, D.C.

GENTLEMEN: Senator Hart, by letter dated April 29, 1971, has asked me to give you my comments on the "Scott Amendments" to the proposed revision of the Patent Code.

In order to form opinions as to the wisdom of any proposed legislation, presumably it is necessary first to have an understanding of the purposes of the proposals. So far as I can judge from the materials I have examined, three purposes are put forth by the proponents as follows:

1. To clarify the law.
2. To protect the rights of patent owners.
3. To promote research and development and investment therein and the commercialization of inventions.

In *Appalachian Coals, Inc.* v. *United States*, 288 U.S. 344, 359–60 (1933), Chief Justice Hughes said: "As a charter of freedom, the [Sherman] Act has a generality and adaptability comparable to that found to be desirable in constitutional provisions." Like the phrase "due process of law" in the Fifth and Fourteenth Amendments to the Constitution, the phrase in the Sherman Act prohibiting conspiracies "in restraint of trade" expresses an ideal thought desirable in the conduct of American business. The phrase "restraint of trade" takes on content and meaning only in terms of the decisions of the courts—particularly the Supreme Court—in interpreting it. Consequently, the meaning of the Sherman Act has continuously been changing to reflect the views of the courts as to the desirability of various forms of restrictive business conduct on society as a whole. The Sherman Act itself expresses no more—and no less—than an ideal. For 80 years, Americans have left to the courts the task of deciding how that ideal shall be translated into enforceable prohibitions.

While there has been continuing debate for almost 80 years over the question whether the courts' antitrust decisions have gone too far in one direction or another, there has been general recognition that it is the courts and not the Congress that make the law of antitrust.

The proposed amendments to the Patent Code would change all this.

The primary purpose of the amendments, it is said, is to clarify the law. If the amendments were adopted, I fear that, to the extent they clarify the law, the amendments will freeze the relationship of antitrust and patent law into a mold which would soon be out of date. There have been other occasions when Congress has sought to be specific in phrasing antitrust prohibitions rather than following the generalities it adopted in the Sherman Act. The results, almost all agree, have been unsatisfactory.

Two examples may serve to illustrate the point. The Robinson-Patman amendments to Section 2 of the Clayton Act were an effort by Congress to close previous loopholes existing in Section 2 of the Act as originally enacted in 1914. Most commentators now agree that the amendments have placed much of the law of price discrimination in a straight jacket from which both the Federal Trade Commission and the courts are still having trouble extricating themselves.

Another example is Section 8 of the Clayton Act, prohibiting certain interlocking directorships. President Wilson regarded Section 8 as one of the cornerstones of his "New Freedom." But the section was drawn so specifically and, as it turned out, so narrowly that, while its meaning has been reasonably clear from the start, its impact on the problems posed by interlocking directorships has been virtually nil.

These, I believe, are examples of the disadvantages in enacting detailed legislation for the purpose of clarifying the relationship between patent and antitrust law. Clarity is achieved only at the expense of judicial adaptability to changing business conditions. Americans have opted for adaptability in their basic antitrust law and I see no reason to change that choice now.

Two further reasons advanced in favor of the proposed legislation are that it is needed to protect the rights of patent owners and to promote research and development. My own experience has been that patent owners require no more protection than the law now affords them. I have observed no diminution in the proliferation of inventions or in the issuance of patents on those inventions. I am conscious of no decline in investment in research and development by American industry. On the contrary, it would seem to me that one of America's principal contributions to the history of civilization has been in the invention and exploitation at relatively low cost of processes and products thought to be useful by the overwhelming majority of human beings.

Some of the proposed amendments would amend existing antitrust law by overruling some of the decisions of the Supreme Court. Surely, before such radical changes are made in our law, the evidence for the change must be both clear and compelling. I am aware of no such evidence.

The proposed amendments submitted with the letter from Senator Hart would appear either to overrule or modify many decisions of the Supreme Court, including the following: *Brulotte* v. *Thys Co.*, 379 U.S. 29 (1964); *Zenith Corp.* v. *Hazeltine*, 395 U.S. 100 (1969); and, *Lear* v. *Adkins*, 395 U.S. 653 (1969). I believe the consequences, however well-intended, of legislation designed to have such a broad impact on the Supreme Court's opinions is certain to be mischievous. In the first place, if enacted, the amendments would set into concrete for all time the relationship between the Sherman Act and the Patent Code with respect to the particular subjects that are covered by the amendments.

A single example should suffice to illustrate the point. It is proposed that a patentee may lawfully license "the whole or any part of his rights under a patent." I assume that at least one of the purposes of this provision is to validate for all time patent licenses limiting the field of use of the patented invention and the customers to whom the patented products may be sold. Field of use restrictions were upheld by the Supreme Court in *General Talking Pictures* v. *Western Electric Co., Inc.*, 305 U.S. 124 (1938). I am aware of no decision of the Supreme Court that overrules the *General Talking Pictures* case. Moreover, I know of no reason today to overrule the basic holding in the opinion in that case. But, I believe it is unwise to legislate the *General Talking Pictures* decision into statutory law. For one thing, I am not certain that that opinion is of sufficient importance to warrant its statutory codification. Nor am I reasonably sure that in the course of the next 30 or 50 years it will prove as wise a decision as it appears to be today.

In sum, I conclude that the proposed revisions of the Patent Code are not necessary to clarify the law, to protect the rights of patent owners or to promote commercialization of inventions. If these amendments were to be enacted, they would overrule or seriously modify many decisions of the Supreme Court. Under the guise of clarifying the law, the proposed amendments would freeze the relationship between the patent laws and the antitrust laws into a mold from which succeeding generations, facing new and different circumstances, would find it difficult, if not impossible, to extricate themselves.

Sincerely,

VICTOR H. KRAMER.

LICENSING EXECUTIVES SOCIETY, INC.,
May 7, 1971.

Subject: S.643—Patent Codification and Revision Bill; Amendments Proposed by Senator Scott.

Hon. SENATOR MCCLELLAN,
Chairman of the Judiciary Subcommittee on Patents, Trademarks and Copyrights,
New Senate Office Building,
Washington, D.C.

DEAR SENATOR MCCELLAN: I am writing you as President of the Licensing Executives Society on behalf of the polled membership of that society to express our support in principle of the Scott Amendments to the Patent Law Revision Bill.

The Licensing Executives Society is a non-profit organization of more than 1,000 members comprised of businessmen, research directors, attorneys, and other individuals having responsibility for the transfer and utilization of technology. Our aims and programs are broadly involved in facilitating the transfer and business use of technology.

Although there are a number of provisions in these Amendments, we will discuss what to us are the two basic technology rights involved. The first is the right of an individual to his inventions clearly established by the patent provisions of the Constitution and to freely deal with this right in the flow of commerce. The second right, no less important, is the Common Law property right in know-how and trade secrets which accrue to one from the ingenuity and risk-taking involved in technological development. Each of these rights has been a keystone in building our nation into the strong technology nation that it is today.

Unfortunately in the past two or three years, and particularly in recent months, we have witnessed a serious erosion of the basic constitutional patent right as well as the property right in Trade Secrets.

Senator Scott's action would serve to stem this erosion. His proposed Amendments to Section 261 of the Patent Laws deals with the first right and would preserve "reasonable" flexibility to the owners of patent rights in licensing. "Reasonable" latitude in exploiting rights is necessary to maintain the incentives for risking time and money on research and development.

The proposed Amendments to Section 261 would provide for the reasonable division of the patent grant for commercialization into various fields of use whether they be defined in terms of product, market, time or geography. This division is critical to the successful exploitation of technology. An inventor of a basic invention rarely is able to promote his invention in all fields to which it is applicable. Unless he can present to a number of different licensees sufficient exclusive protection to encourage them to risk development of their respective fields of the invention, both the public and the inventor will lose much of the benefit of his invention.

Turning to the thrust of the Scott Amendments, Section 301, this deals with what we consider to be the second fundamental right which must be protected. This Section is intended to preserve Common Law rights in Trade Secret and Unfair Competition fields. We believe that these rights are completely compatible with the constitutionally founded patent right. The two rights have lived side by side through our history and should continue to coexist for our nation's technological health.

In clarifying the doctrine of Federal preemption in the patent area, the words of Chief Justice Marshall in the famous steamboat case are on point: "The extraordinary boldness of this position (preemption) must surprise and astonish" (Gibbons v. Ogden, 6 L.Ed. 23, at p. 140). Here the state statute guaranteeing technical property rights was not held unconstitutional as conflicting with Federal Patent Laws as requested by the Defendant. (However, the court held for the Defendant on other grounds.) We consider that Section 301 is essentially a Codification of this classic Supreme Court declaration of Chief Justice Marshall.

Senator McClellan, we believe that unless the current trend towards erosion of these two proprietary rights is stopped, many corporate managers and inventors will decide to spend less effort and resources in research, development and inventive work. In fact, we already have noted some signs that a significant slow down in United States research and development is taking place, particularly in relation to certain foreign countries such as Japan, Russia, and West Germany. As the inducement to the individual and corporate inventor is limited more and more, the high risk of developing technology and innovated products will not be acceptable.

We also should be seriously concerned about the adverse effect of this technology decline on the United States' Balance of Payments, and from a longer range standpoint, the adverse effect on the technological capability of the United States to compete on an international basis.

In conclusion, the Licensing Executives Society strongly supports the principles set forth in the Scott Amendments for inclusion in the new patent legislation.

Respectfully,

ROBERT P. WHIPPLE,
President.

MANUFACTURING CHEMISTS ASSOCIATION,
Washington, D.C., May 28, 1971.

Hon. JOHN L. MCCLELLAN, *Chairman,*
Subcommittee on Patents, Trademarks, and Copyrights, Committee on the Judiciary, U.S. Senate,
Washington, D.C.

DEAR MR. CHAIRMAN: On March 24, 1971, you announced that the Subcommittee on Patents, Trademarks, and Copyrights of the Committee on the Judiciary would conduct hearings on May 11 and 12 on legislation for the general revision of the patent laws. At that time you indicated that individuals could request to testify at the hearings or submit written statements concerning the subject of the hearings. On behalf of the Manufacturing Chemists Association, I wish to express our support for amendments 23 and 24 to S. 643, introduced by Senator Hugh Scott.

The Manufacturing Chemists Association is a nonprofit trade association of 171 United States company members representing more than 90 percent of the production capacity of basic industrial chemicals within this country.

Amendment 24 would amend sections 261 and 271 of S. 643 dealing with patent licensing provisions and is intended primarily to implement recommendation XXII of the Report of the President's Commission on the Patent System.

The President's Commission on the Patent System suggested that uncertainty existed as to the licensable nature of the patent right, and indicated that this has "produced confusion in the public mind and a reluctance by patent owners and others to enter into contracts or other arrangements pertaining to patents or related licenses". The Commission suggested that specific statutory language defining, for the purpose of assignments and licenses, the nature of the right which may be lawfully conveyed by such assignments and licenses would eliminate this confusion.

We concur with the views expressed by the President's Commission on this issue and believe that amendment 24 will accomplish this purpose. It is our opinion that the proposed amendment is in the public interest and, by eliminating uncertainty in this area, will encourage technicial and economic progress.

Amendment 23 would amend section 301 of S. 643 to make it clear that the patent laws shall not be construed to preempt the rights of individuals and companies to enter into contracts involving technical know-how, trade secrets and other such forms of non-patented or non-patentable intellectual property.

As indicated in a supporting statement submitted by Senator Scott when he proposed this amendment, recent judicial decisions cast doubt on the propriety of entering into contracts for the protection of such property, and suggest that such contracts are preempted by the patent laws. We wholeheartedly support this amendment which would clarify existing laws and more fully protect the owner of intellectual property by insuring that he could enforce contracts of this sort under general contract or tort law.

We have noted with interest the difference in views expressed by witnesses from the Departments of Justice and Commerce on the amendments proposed by Senator Scott. In our opinion, this disagreement between Government agencies emphasizes the need for legislative clarification of the issue involved.

I appreciate the opportunity to submit the views of the Manufacturing Chemists Association regarding these matters and respectfully request that this letter be included in the record of your Subcommittee's hearings on patent revision legislation.

Sincerely,

W. J. DRIVER.

MONSANTO COMPANY,
St. Louis, Mo., April 30, 1971.

Re: McClellan S–643 and the so-called Scott Amendments 23 and 24.

Hon. JOHN L. MCCLELLAN, *Chairman,*
Subcommittee on Patents, Trademarks, and Copyrights, Committee on the Judiciary, U.S. Senate,
Washington, D.C.

DEAR SENATOR MCCLELLAN: My company has previously written you and expressed approval of McClellan S-2756, General Revision of the Patent Laws, and we take this occasion to express our approval of the so-called Scott Amendments 23 and 24.

These amendments address themselves to sound and frequently used business practices in the field of patent licensing and they do not, in our opinion, interfere with the intended purpose of the antitrust laws. In particular, we support and wish to comment on the need for the addition of these two amendments and Section 301. Some language changes may be required for the purpose of making these amendments more specific, but the thrust and intent should remain unchanged.

Amendment 23 would codify the well established case law of the courts concerning field-of-use licensing. A patent owner is entitled to all uses of his claimed invention. Limited licenses have, at least until quite recently, been considered legal in the same respect as are unlimited licenses. From a business viewpoint, limited licenses are a necessary tool. They are used to fit the scope of the license to the needs or capabilities of each licensee and adjust the royalty or license fee to the value of the license. The unlicensed part of the claimed invention is, in many cases, retained for use in the licensor's own business. None of this constitutes an undue restraint. The *Patent, Trademark & Copyright Journal* for April 1, 1971 (copy attached) reported a typical field-of-use license situation adopted by NASA. This agency owns a patent on an energy-absorbing device. It now proposes to grant an exclusive license to the Denver Research Institute to use the invention in three fields of use as an energy absorber for (1) a trailer support wheel, (2) passenger automobile bumpers, and (3) elevators. NASA is reserving for the Department of Transportation a license to study the use of the invention in highway and bridge guard rails. It is further pointed out that NASA has granted two nonexclusive licenses under this patent in fields not allocated to the Denver Research Institute. Surely, the antitrust laws were not designed to challenge a common business practice of this type.

Without the receipt of an exclusive license in the defined fields, it is unlikely the Denver Research Institute would undertake to invest the money necessary to develop the invention for commercial use since they would have inadequate protection of their investment. One might also speculate whether NASA would have licensed the invention at all if it were not possible to reserve specified fields of use for the Department of Transportation.

There are many situations where, for practical and legitimate business reasons, licenses would not be granted were it not possible to provide for limited licenes, and certainly the granting of a limited license is more competitive than not granting a license at all.

The President's Commission on the Patent System concluded that the field-of-use license, like a license for a particular territory (which is specifically sanctioned by the Patent Statute), should receive statutory approval.

The Amendments codify several common provisions used in license arrangements that have not been questioned until recently. Many factors affect the royalty rate or purchase price of a license and these matters should be left to private bargaining. Attempts to write patent law in the courts are expensive and businessmen as well as lawyers need a stable statutory base from which to operate.

New Section 301 is extremely important to any organization or company that finances research and development, or buys or sells know-how. This Section would make it clear that the Patent laws do not pre-empt the right of the courts under State or Federal law to decide issues with respect to the enforcement of contracts involving rights to, or the sale and purchase of, trade secrets and technical know-how. The process industries pertaining to chemical manufacture, oil refining, metallurgy, plastics, and the like have acquired from their research, development, and engineering expenditures a valuable background of non-patentable technical know-how. In many cases, this know-how is in knowing what not to do in order to make a process or operation perform at top efficiency. Detailed engineering specifications and operating procedures for a manufacturing unit are usually non-patentable but represent a very valuable property right. The purchase of know-how is frequently looked upon as a means of buying time and thereby enables the purchaser to speed up his own development and marketing efforts. The buying and selling of technical know-how is big business. It is reported that in 1968, the U.S. technological balance of payments from foreign countries for agreements to exchange such technical information credited the U.S. with 1.5 billion dollars.

The dictum in the recent (1969) Supreme Court case of Lear v. Adkins, 395 U.S. 653, and the holding of Judge Motley in Painton v. Bourns, Southern District of New York, 309 F.Supp. 271 (1970), have created much concern that a Federal pre-emption doctrine, based upon the Patent Code, might close the door to opportunities for one company to purchase technical know-how from another. Now is certainly the time to clarify this important question and adopt, in substance, Section 301.

Your efforts to bring forward the general revision of the Patent laws are certainly appreciated and we hope you will lend full support to the so-called Scott Amendments.

Respectfully submitted,

JOHN B. CLARK,
Director, Patent Department.

NATIONAL ASSOCIATION OF PLANT PATENT OWNERS,
Washington, D.C., May 13, 1971.

Hon. JOHN L. MCCLELLAN, *Chairman,*
Subcommittee on Patents, Trademarks, and Copyrights, Committee on Judiciary, U.S. Senate,
Washington, D.C.

DEAR SENATOR MCCLELLAN: The National Association of Plant Patent Owners is a trade association representing member firms holding one or more existing plant patents. We wish to comment on S. 1255 "to fix the fees payable to the Patent Office."

Our position remains unchanged from the testimony of Richard J. Hutton before your Committee in March of 1964 and a letter to you on March 3, 1965 from the American Association of Nurserymen. We support a reasonable increase in existing patent fees. We feel it is perfectly in order for the Patent Office to charge higher fees. Their fees have not been raised in many years and it is obvious they need more income. It is our understanding that S. 1255 would increase filing fees from $65 to $90. Currently the fee schedule provides a basic issue fee of $100 plus additional fees averaging nearly $50 per application based on the number of printed pages of specifications and sheets of drawings.

Our greatest hope in supporting this legislation is that patent application processing can be expedited. Presently it takes two years or more for a plant patent application to negotiate its way through the Patent Office and be issued.

In summary, Mr. Chairman, while in favor of realistic increases in patent fees, we urge that every effort be made by the Patent Office to shorten the length of time between application for and issuance of a plant patent. We respectfully request this letter be made part of the record of hearings before your Subcommittee.

Sincerely,

RICHARD F. TURNEY,
Administrator.

STATEMENT OF THE NATIONAL ASSOCIATION OF MANUFACTURERS

This statement is submitted by the National Association of Manufacturers, a voluntary association of business concerns of all sizes and types and located in every state. Its membership represents a substantial portion of the technical capacity in American industry. The purpose of this submittal is to emphasize what are considered to be among the most critical aspects of S. 643 and Senate Amendments 23 and 24 and it supplements the oral testimony offered in behalf of the NAM by Mr. John A. McKinney on May 11, 1971.

Today, the freedom of licensing of patents, industrial know-how, and other intellectual industrial property rights has become a critical issue, particularly as a result of recent court decisions and governmental antitrust activities. This area of concern is not only having repercussions on the domestic front but the posture of U.S. international trade is crucially affected. For one thing, licensing has been providing the nation with well over $1.5 billion surplus on our important annual balance of payments.

It is a fact publicly proclaimed by certain key government attorneys that antitrust caveats covering licensing of patents and know-how are something they would want to develop on a case-by-case basis. This poses a broad threat against creative individuals and company innovators which is bound to have an effect on our economic well-being as a nation. From a global viewpoint, American manufacturers want to satisfy the needs of companies abroad, and at the same time, partake of the latest developments made overseas. But in a sense, the United States is in the process of being the only country that is erecting a high Chinese wall around its industrial technology.

That is exactly the direction in which licensing is being steered. Unless companies are able to have more assurance as contained in S. 643 and Amendments 23 and 24, there will be a further eroding of the technological involvement of American industry.

Secretary of Commerce Stans has indicated that during the past couple of years our technological balance of payments has been declining. That fact has a direct relationship to what is going on in the world today.

To be sure, there is more research and development competition and breakthroughs from Japanese and European forces that are serving to challenge our Yankee ingenuity. But in addition, one notes an apprehension and loss of innovative spirit evident throughout American industry because of the erosion of licensing prerogatives.

Today's situation has company executives, lawyers and negotiators sometimes vacillating between fright, annoyance, and an attitude of let's-skip-the-whole-thing when contemplating specific licensing arrangements.

We should appreciate fully one fact: licensing enables the domestic and international transfer of highly useful knowledge and crucial funding, all of which leads to an increase of growth everywhere.

As consumers, we must have protection as reflected in fair practices and pricing which are important objectives of anti-monopoly laws. At the same time, as a society dependent on industrial vigor, innovative companies must be kept in the competitive stream of things.

But it is imperative to note that in order for us to go forward as originators and not become stagnant copiers, harassment of industry's capacity to conduct technological licensing—transfers at home and abroad must stop. Otherwise it will simply eat away the fruits of our native ingenuity.

If companies are to be able to work out necessarily fair and lasting license agreements domestically and in the international fields of competition, some further assurance now appears to be absolutely required on a legislative level.

Non-Pre-Emption

S. 643 presently contains Section 301 which provides that the Federal patent law shall not pre-empt obligations or right other than patent rights. This section restates the traditional interpretation that the Federal patent statute does not pre-empt contractual or other rights or obligations not in the nature of patent rights, imposed by State or Federal law on particular parties with regard to inventions or discoveries, whether or not subject to the Federal patent statutes. A provision of this kind in S. 643 is especially timely in view of the suggestions in the minority opinion of the recent Supreme Court case of *Lear v. Adkins* which some see as indicating that there can be no contractual protection for trade secrets, know-how, technical information and so forth. The NAM strongly favors the incorporation of a provision such as Section 301 but prefers that the provision be reworded along the lines of Amendment No. 23 proposed by Senator Scott.

The property rights potentially involved in the above proposal are of tremendous importance in the development and use of American technology. It is quite common to enter into agreements between companies in the United States and in foreign countries for the exchange of technical information, know-how and the like so that in effect the recipient company is placed in a position to produce some product or practice some process at the same level of quality and efficiency that the first company spent many years, much effort and large sums of money reaching. This serves a very beneficial purpose in both spreading technical capabilities between companies and geographically diffusing new technology throughout the United States and the world much more efficiently than would otherwise be the case, with the resultant early benefit of the best of new technology to all mankind.

In the usual case, the bulk of this transfer of technological information is not of a true "trade secret" variety but is of a much more mundane nature such as which machines to use, the source of raw materials, tolerance limitations between moving parts, testing procedures, proper alloy and heat treatment of components, and so forth. However, this information results in a product or process having the properties and characteristics which are desired and for which the recipient is willing to pay substantial sums of money. For example, based on figures from 1968, the United States' technological balance of payments for the technical information type of agreements credited the United States with one and one-half billion dollars. As is well known, the balance of payments problem for the United States is a constant one, and the figure involved plays a highly significant and valuable direct role in such balance.

If the law ever did develop that contracts of this nature were not enforceable, then devastating economic results could ensue. While these technical information agreements oftentimes include trade secrets, trademarks and patent rights in addition to technical know-how, the latter is the principal ingredient desired by the recipient in practically all of the contracts. Therefore, the suggestion that such contracts be limited to "truly trade secrets" and patent rights fails to appreciate the true nature of these agreements.

Licensable Nature of Patent Rights

The President's Commission on the Patent System, after making a thorough and exhaustive study, formulated Recommendation XXII which pertains to the licensable nature of patent rights and reads as follows:

The licensable nature of the rights granted by a patent should be clarified by specifically stating in the patent statute that: (1) applications for patents, patents, or any interests therein may be licensed in the whole, or in any specified part, of the field of use to which the subject matter of the claims of the patent are directly applicable, and (2) a patent owner shall not be deemed guilty of patent misuse merely because he agreed to contractual provision or imposed a condition on a licensee, which has (a) a direct relation to the disclosure and claims of the patent, and (b) the performance of which is reasonable under the circumstances to secure to the patent owner the full benefit of his invention and patent grant. This recommendation is intended to make clear that the "rule of reason" shall constitute the guideline for determining patent misuse.

Recommendation XXII has not been incorporated into S. 643 apparently for the sole reason that the Antitrust Division of the Justice Department has opposed the provision, not because it reverses existing law but because the Antitrust Division prefers to develop the law on a case-by-case basis.

This approach is believed to be unrealistic and not in the public interest since agreements are being negotiated daily which may extend for the next ten years or longer. For example, in negotiating patent licenses between companies in the United States and in foreign countries, there is a tremendous amount of give and take by the business decision makers and this is the principal reason that simple license agreements frequently are complex documents. During these negotiations, the antitrust laws are always considered and prohibitions are avoided. However, there exists much uncertainty as to what the antitrust laws are today and what they will be tomorrow. The Antitrust Division, in its view, seems to consider the law as it will be after it has managed to have overruled some of the present Supreme Court cases, which so far it has failed to do. Whether or not it will be successful in overruling these cases in the future is where most of the uncertainty lies. Generally, Recommendation XXII does not ask for any overruling of current laws but merely the stabilizing and clarification of the law so that businessmen can, with more assurance than they have at the moment, enter into agreements that will be valid for the lifetime of the agreement and not have to resort to an impossible guessing game. It is believed that legislation is the only way that this matter can or should be satisfactorily handled and that waiting for the law to develop on a case-by-case basis would be harmful and against the public interest. NAM strongly feels that Recommendation XXII should be incorporated into S. 643 and suggests that it be done by amending S. 643 along the lines of Amendment Number 24 proposed by Senator Scott.

It is not believed any of the provisions of Amendment 24 overrule what is clearly the law of the land today, although the opinions in some conflicting lower court cases would probably be clarified and made more uniform with the establishment of a greater degree of certainty to the law in this area.

Reasonable licensing privileges for those who produce technology and obtain patents is a fundamental need. In order to encourage the flow of technology, and its expanded use, logical licensing practices should be encouraged, not discouraged by unnecessary legal sanctions. There is a major public interest to be served by encouraging American inventors and American companies to increase their expenditures of money and effort in first generating new technology and then sharing it with others on the basis of mutually acceptable license terms. Restrictions on the freedom to license technology tend toward lessening competition in the development of new technology. This technology development not only strengthens the United States at home, but greatly improves its balance of payments position internationally.

It is extremely important that provisions of a nature similar to those proposed be incorporated in any patent revision bill in order to help bring some stability and clarification to the law in this field so that agreements relating to patent rights can be entered into with some assurance that they are legal not only today but will continue to be legal ten years or some longer period from now.

Mandatory Licensing

A mandatory licensing provision was included, without the benefit of hearings, in the recently enacted Clean Air Amendments of 1970. It is believed that such a provision is unnecessary and would reduce the incentive for innovation in a manner that would be counter to the intents and purposes of the Clean Air Act. Certainly, no need has as yet been shown that such a provision is needed. If a need for mandatory licensing is demonstrated, which is believed to be extremely unlikely, for such a radical and unprecedented departure from our existing law, then that is the time such a provision should be considered for enactment into law. Therefore, the NAM endorses the provision of S. 643 which deletes the mandatory licensing provision from the Clean Air Amendments.

Statement of Eric P. Schellin on Behalf of National Small Business Association and National Patent Council

Mr. Chairman and Members of the Committee, my name is Eric P. Schellin. I am a small businessman and an attorney with offices in this area. This statement is presented on behalf of National Small Business Association representing some forty thousand business concerns, a substantial number of which are manufacturing firms doing business in over five hundred different industry categories. It is also given on behalf of the National Patent Council representing those interested in the patent system and those relying on that system. The majority of the National Patent Council's membership is also small business. We appreciate the Committee's giving us an opportunity to comment on certain matters pertaining to patent legislation.

As you well know, the patent system finds its roots in the Constitution. However, it has been the many members of Congress who have labored in subcommittees such as yours that have given flesh to the patent system based upon the sparse language of the Constitution.

Not for narrow self-interest, but for the public good, the framers of the Constitution, without dissent, set the patent system into being. It has been well established and documented that the public interest is served by nurturing innovation, which is the principal objective of the patent system.

Patents do this, first by either encouraging invention, or the investment in inventive effort. Patents give a degree of exclusivity thus making it worthwhile for the small business inventor to bring to profitable fruition the investment of time and money in an invention. The small business man requires this degree of exclusivity afforded by the patent system as he does not possess the market place clout of big business. Let us not forget that many a big business of today was little yesterday and became big through encouraged innovation.

Patents encourage innovation, secondly, by being a species of property which may be disposed. The present statute declares that "patents shall have the attributes of personal property". Yet, curiously, the disposition of a patent as property is encumbered. Some of these restrictions are a result of: judicial decisions because the present patent laws do not say enough positively as to the nature of the patent property; by the saber rattling of the Justice Department which disseminates press releases, threatens court actions and addresses meetings of patent attorneys to tell us what the patent is not. In the wake of all this, patent attorneys and those charged with licensing of patents have held meetings, formed new societies and conducted workshops. In spite of the fact that the patent attorney works in the forefront of what is new he is a pretty cautious fellow. And rightly so, because if he charts a patent licensing course that gives the appearance of straying onto the antitrust shoals, which spring up anew, the entire patent may flounder and sink. By preying on the patent attorney's reticence, the patent as a licensable property has been severely curtailed. Confusion reigns. Clarification is needed and a reversal of the trend is in order.

As was stated, patents are species of personal property. An important attribute of patent property should therefore be the patent owner's right to the benefits of ownership use and disposition. A normal incident of patent ownership should be the right of the patent owner to either retain the entire patent property for his own use, or to dispose of all or part of it whenever, wherever and to whomever he chooses.

It has been stated that patents and matters involving patents have no constant advocate as does antitrust. The organization which I represent have worked diligently to offset this thought. However, in order to conserve time and to stress that which is of the utmost importance, my comments are directed to the need for the inclusion of Amendment No. 24 into the patent reform legislation now before this Subcommittee. We of NSB and NPC take strength in the knowledge that we can petition our Government to accept salutary legislative language breathing life anew into the patent system, whose life seems to be ebbing away. Even beyond the confusion as to what a patent affords, it must be noted that the patent system is under severe attack. More often than not when a patent is litigated in an infringement action, it is found to be invalid. If the invalidity hurdle is overcome, the patent may be unenforceable as a result of misuse bringing with it an antitrust violation.

In almost any context, except if one has none, having only a half a loaf is arduous in any event; and in the context of the patent grant half a loaf is particularly arduous on small business. For example, under today's climate, one of our members who is making a patented machine tool in Philadelphia could not validly license other small manufacturers in a way to give him the best royalty return and at the same time retain a segment of the market for himself based on a geographic and field of use limitation. As a result, our Philadelphia member will not share his patent with anyone and will fill the market in his area to the best of his ability. The rest of the U.S. will have to be satisfied with prior art alternatives, satisfactory, yet, but not as good. As a result, the public has not been served. Furthermore, our Philadelphia member has given up on the patent system. For he too was making a profit manufacturing marketable prior art machine tools. A half a loaf patent is not sufficient encouragement for him to expend time, effort and money to make a better machine tool as the reward for the risks taken are not sufficient.

Now big business is usually not faced with the same problem. By having countrywide coverage, the large manufacturer can cover the market due to a combination of nationwide distribution facilities and a multiplicity of strategically located plants. Field of use is accomplished for the large manufacturer by possessing divisions geared to supply certain segments of the market. Prices for the patented item are set by headquarters for uniformity. For the large manufacturer, the half a loaf should be much more palatable as, you see, the large manufacturer can do by virtue of its size what our member from Philadelphia cannot do. We believe Amendment 24 will put the large and the small on at least a more even footing by being encouraged to innovate.

Spokesmen for the Justice Department have said that they will look at the degree of restraint resulting from licensing steps before taking action; and that small business may in fact infrequently meet the test requiring action. The spate of recent decisions, as are all decisions, are the law of the land, regardless of the size of the licensor and apply equally to both big and small. How can the practicing attorney, for instance, tell his small business client, that it is perfectly legal to accept cogent variable royalty rates by telling him that he is immune as he is small; therefore the Justice Department won't come gunning for him. Since the large multidivisioned manufacturer is not faced with the same problems and therefore does not incur the same liabilities, just who is the Justice Department going to go after?

In conclusion, if the patent owner can deny access of all others to his invention, it would seem appropriate that he be entitled to control the degree to which he relinquishes his exclusive right. Without Amendment 24, the public interest is not served and the fostering of innovation as the primary principal of the patent system is withdrawn as far as small business is concerned.

Address by S. Chesterfield Oppenheim Before Licensing Executive Society, April 21, 1970, Washington, D.C.

The Patent-Antitrust Spectrum of Patent and Know-How License Limitations: Accommodation? Conflict? or Antitrust Supremacy?

About the Speaker: Formerly Professor of Law, The George Washington University and the University of Michigan; Co-Chairman, Attorney General's National Committee to Study the Antitrust Laws 1953–1954; Chairman, Section of Antitrust Law, American Bar Association 1961–1962; Adviser on Research, The Patent, Trademark & Copyright Research Institute, The George Washington University; Author of Cases on Federal Antitrust Laws (3d ed. 1968) (with Profesor Glen E. Weston) (1970 Supp.); Author of Cases on Unfair Trade Practices (2d ed. 1965) and Supps.; Editor-in-Chief, Trade Regulation Series (Little, Brown & Co.).

In 1955 I published a law review article[1] in which my thesis was that so long as the Patent Code and the antitrust laws are judicially interpreted to protect the "hard core" lawful exclusivity of patent rights, and to condemn "hard core" patent misuse and antitrust violations, the two bodies of law can peacefully coexist.

With respect to license limitations in domestic commerce, which is the sole subject of this address, it may fairly be concluded that placed in perpective, the corpus of judicial decisions dealing case-by-case with the interactions of patent and antitrust public policies does not reveal substantial

[1] Oppenheim, Patents and Antitrust: Peaceful Coexistence?, 54 Mich. L. Rev. 199 (1954). See also Oppenheim, A New Approach to Evaluation of the American Patent System, 33 J.Pat.Off.Soc. 551 (1951).

evidence of a trend toward undermining judicial protection of the "hard core" of license limitations ancillary to the lawful scope of the patent grant.

This conclusion may come as a surprise to patent counselors who complain about the uncertainty of the state of the law because of a few conflicting decisions of the District Courts or the Courts of Appeals on license limitations or because of ambiguities or a dictum in certain Supreme Court opinions in that area. But this yearning for certainty must be balanced against the need for flexibility, two opposing forces which are as old as the process of law itself.[2] We must be on our guard against extension of the certainty of "*per se*" rules beyond their proper bounds but we must also be reconciled to the imprecision of an antitrust policy Rule of Reason applied to restraints beyond the rights of exclusion inherent in the patent grant.[3]

Apart from the dark cloud the dictum of Justice Black in *Lear* v. *Adkins*[4] has cast over federal and state protection of valid trade secret or know-how rights, a topic I shall later discuss, the first part of this paper on patent license restrictions will show that my prime concern is that the pronouncements of top officials of the Department of Justice Antitrust Division from 1965 to date reflect enforcement attitudes which tend to subordinate the Congressionally sanctioned exclusive rights of the patentee to antitrust policy considerations. If the courts should respond favorably to this reoriented thinking of the Antitrust Division, the end result would be to drift from progress toward accommodation of patent and antitrust policies to increase conflict between them, if not to antitrust erosion of lawful patent rights. The Congress would then be faced with the need for corrective legislation.

The second part of this paper will explain why I believe the Antitrust Division's approach to trade secret or secret know-how license limitations, as announced by the head of the Division, Mr. McLaren, is basically sound in advocating protection of such rights under state as well as federal law. Here the current controversial issue is whether this should be accomplished by a case-by-case adjudication or whether Congress should negate the dictum of Justice Black in *Lear* v. *Adkins* by a Congressional amendment. In fairness the Patent Bar should recognize that the Black dictum, not the Antitrust Division's thinking, has generated the alarm regarding the continued vitality of genuine trade secret protection.

PART I

PATENT LICENSE LIMITATIONS

As a backdrop to patent license limitations, first let me remind you that the premise that patent and antitrust policy are not intrinsically in conflict, and that both policies stem from the paramount objective of maintaining private competitive enterprise, appears to be generally accepted.[5] This is the position taken in the 1955 Report of the Attorney General's National

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[2] See Cardozo, The Nature of the Judicial Process (1921). The interaction of the judicial and legislative process in a cognate area is depicted in my paper on The Judicial Process in Unfair Competition Law, 2 Idea 116 (1958) (Conference Number).

[3] Elman, "Petrified Opinions" and Competitive Realities, 66 Col. L. Rev. 625 (1966).

[4] *Lear, Inc.* v. *Adkins*, 395 U.S. 653 (1969).

[5] For collection of cases and commentaries on the American Patent System and patent-antitrust issues, see Oppenheim and Weston, Federal Antitrust Laws Ch. 13, Third Edition (1968) (1970 *Supplement*); *Nordhaus & Jurow, Patent-Antitrust Law* (1961).

Recent surveys are Wood, Patents, Antitrust and Prima Facie Attitudes, 50 Va. L. Rev. 571 (1964); Symposium on Patents, Know-how and Antitrust, 28 U. Pitt. L. Rev. 147 (1966); Patents and Antitrust (Analyses), BNA Antitrust and Trade Regulation Today, 131–165 (1967); Kadish, Patents and Antitrust Guides and Caveats, 13 Idea 83 (1969).

For other earlier surveys of the case law, see Report of the Attorney General's National Committee to Study the Antitrust Laws, Ch. 5 (1955); Antitrust Problems in the Exploitation of Patents, Staff Report to Subcommittee No. 5, Committee on the Judiciary, House of Representatives (1956). For a challenging conceptual approach, see Harris & Siegel, Positive Competition and the Patent System, 3 Idea 21 (1959).

The PTC Research Institute has conducted empirical studies on industrial property licensing: Behrman, U.S. Companies As Licensees Under Foreign-Owned Patents, Trademarks and Know-how, 5 Idea 16 (1961); Banks, Use of Industrial Property in Foreign Countries, 13 Idea 553 (1970); Lightman, Company Patterns in U.S. Foreign Licensing, 14 Idea 1 (1970); Oppenheim and Scott, Empirical Study of Limitations in Domestic Patent and Know-how Licensing (First Report), 14 Idea 193 (1970); Second Report, 14 Idea 123 (Conference Issue) (1970). See also *infra* notes 65, 66.

Committee to Study the Antitrust Laws[6] and in the recent Report of the President's Commission on the Patent System.[7] The Commission declared that the Patent System and the antitrust laws are fully compatible and not mutually exclusive in the sense that the limited time exclusiveness of the patent grant threatens effective antitrust enforcement.[8]

The goal of this approach is to achieve accommodation of patent and antitrust so that each public policy may operate on a parity within its own Congressionally appointed and judicially defined orbit.

The speeches of the present head of the Antitrust Division and his chief officials contain assurances that the Patent System is not inherently at odds with the antitrust laws, although the two at times do conflict.[9] We are told that the Antitrust Division seeks to reconcile the patentee's rightful claim to reward for his invention and the antitrust objective of promoting competitive innovation through application of a Rule of Reason to license restrictions which do not presently fall within the well established illegal *per se* category. Regrettably, these words of promise may not be fulfilled when placed in the full context of recent pronouncements of the Antitrust Division.[10] From them emerges a fundamental question of whether there is failure to distinguish between criteria for determining whether patent license limitations are inherent in, and ancillary to, the patentee's rights of exclusion and the criteria for determining whether the license restrictions are purely contractual provisions of an antitrust nature beyond the scope of the lawful monopoly of the patent grant.

The policy guides of the Antitrust Division reveal coalescence of patent policy and an antitrust Rule of Reason. Mr. McLaren[11] and his staff associates have stated their approach as follows:

"In considering whether to attack a particular licensing provision or practice, we ask two fundamental questions. First, is the particular provision justifiable as necessary to the patentee's exploitation of his lawful monopoly. Second, are there less restrictive alternatives which are more likely to foster competition available to the patentee? Where the answer to the first question is No, and to the second Yes, we will consider bringing a case challenging the restriction involved."

I believe those criteria are not compatible with the patent policy standard for determining the metes and bounds of the patentee's reward as formulated

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[6] Report at 224-225. After stating that "Reconciliation of the Inventor's private rewards with the public interest in promotion of technological progress has often been stressed by the Supreme Court," the Report continues:

"The private reward of the patent grant aims to achieve its public purpose in a number of ways. Prominent among these is the encouragement of the early disclosure of patentable inventions—and their ultimate availability to the public upon expiration of the patent. The offer of patent protection thus serves to head off the secrecy that might otherwise blanket the use of the invention. Second, the patent system seeks to achieve its public purpose by encouraging investment of risk capital. This is accomplished by affording a market within which the patent owner can invest and induce others to invest without fear of competition. New products and processes have always entailed substantial investment at considerable risk. In recent years the expenditures required to this end have increased. By protecting such investment—and thereby encouraging new technologies—the patent seeks to increase competition by what is superficially an inconsistent grant of monopoly, but is in fact a mechanism intended to assure competition in invention."

[7] The Report was transmitted to the President on November 17, 1966. The Commission was established on April 8, 1965.

[8] The Staff Report to the House Subcommittee No. 5, op. cit. supra note 5, as of 1957 concluded that "The present statutory scheme and judicial climate afford ample means for preserving the rights of patent owners in the legitimate exploitation of their property, while at the same time correcting patent abuse and safeguarding competitive opportunity."

[9] See addresses cited *infra* note 10.

[10] McLaren, Patent Licenses and Antitrust Considerations, 13 Idea 6 (Conference Number, 1969); McLaren, Recent Cases, Current Enforcement Views, and Possible New Antitrust Legislation, 38 ABA Antitrust L.J. 211 at 212 (1969). Wilson, Patents and Antitrust, the Legitimate Bounds of the Lawful Monopoly, address before the Patent Law Association of Pittsburgh, November 19, 1969 (mimeographed); Donnem, The Antitrust Attack Upon Restrictive Patent Licenses, 49 Mich. State Bar Journal 36 (1970); Stern, The Antitrust Laws and Restrictive Patent License Provisions, address before Patent Office Academy, United States Patent Office, April 20, 1970 (mimeographed); Stern, The Antitrust Laws and Restrictive Field Provisions in Patent Licenses, address before the Licensing Executives Society Workshop, October 15, 1970 (mimeographed). For similar official views of a former head of the Antitrust Division, Donald F. Turner, see Antitrust Enforcement Policy, 29 ABA Antitrust L.J. 187 at 188 (1965); Patents, Antitrust and Innovation, 26 U.Pitt.L.Rev. 151 (1966); 10 Idea 32 (1966) (Conference Number).

[11] McLaren, Patent Licenses and Antitrust Considerations, *supra*, note 10 at 63.

in the unanimous Supreme Court opinion in the 1926 *General Electric* case[12] as follows:

"Conveying less than title to the patent or part of it, the patentee may grant a license to make, use, and vend articles under the specifications of his patent for any royalty, or upon any condition the performance of which is reasonably within the reward which the patentee by the grant of the patent is entitled to secure."

Postponing for later comment the sanction of a first sale price license restriction, the "reasonably within the reward" standard announced in *General Electric* is properly interpreted only if it makes permissible licensing restrictions which are an integral part of the patent grant's right to exclude. Construed with the 1912 *Motion Picture Patents* opinion of the Supreme Court,[13] the patent law places outside the normal and pecuniary reward of the patentee only license restrictions which extend the monopoly grant to control any product, service or other subject matter not within the scope of the patent.

The tying clause license condition is the prime example of this extra-patent control condemned in *Motion Picture Patents* and later reaffirmed as *per se* patent misuse in violation of the public policy of the patent laws in a series of Supreme Court decisions in private patent infringement suits.[14] The basic distinction between intra-patent and extra-patent license restrictions should be observed to preserve the patentee's right to exact all the pecuniary reward his rights of exclusion will lawfully allow. However, when the patentee tries to charge all the traffic will bear from licensing royalties or in profits from his own operations by imposing restraints outside the patent grant, he is subject to the prohibitions of the patent laws and, on additional proof, he may also be found in violation of the antitrust laws.[15]

The starting point for accommodation of patent and antitrust is Section 154 of the Patent Code which, pursuant to the intent of the Constitutional provision, declares that every patent shall contain a grant to the patentee, his heirs or assigns, for the term of seventeen years "of the right to exclude others from making, using, or selling the invention throughout the United States."

This limited time exclusiveness is the only way Congress has power to legislate because Article I, Clause 8, of the Constitution, in unequivocal terms, states that "Congress shall have Power * * * to Promote the Progress of Science and Useful Arts by securing for limited Times to * * * Inventors the exclusive Right to their * * * Discoveries."[16] Congress can fix the limited term to less than the present seventeen years but it has no power to make the patent grant less than exclusive, *i.e.*, the right to exclude others. So long as he stays within the claims of his patented invention, the patentee, acting individually, may refuse to license anyone. This is integral to his

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[12] *United States* v. *General Electric Co.*, 272 U.S. 476 at 490 (1926).

[13] *Motion Picture Patents Co.* v. *Universal Film Mfg. Co.*, 243 U.S. 502 (1917).

[14] *Carbice Corp. of America* v. *American Patents Development Corp.*, 283 U.S. 27 (1931); *Leitch Mfg. Co.* v. *Barker*, 302 U.S. 458 (1938): *Morton Salt Co.* v. *G. S. Suppiger Co.*, 314 U.S. 488 (1942); *B. B. Chemical Co.* v. *Ellis*, 314 U.S. 495 (1942).

[15] Illustrative of patent misuse are the cases, cited *supra*, notes 13 and 14, where the patentee-licensor uses his patent to control unpatented subject matter outside the scope of the invention described in the claims of the patent. Also outside the metes and bounds of the patent grant are attempts by the patentee to control the resale price of a patented article after a first sale *authorized* by the patent license and from which the patentee already received the reward the patent law secured to him. Such extra-patent control may constitute both patent misuse and antitrust violation. *Ethyl Gasoline Corp.* v. *United States*, 309 U.S. 436 (1940); *United States* v. *Univis Lens Co.*, 316 U.S. 241 (1942).

[16] The Genesis of American Patent and Copyright Law (1967), by Professor Bruce W. Bugbee, is the leading scholarly account of the colonial background leading to the Constitutional provision on patents and copyrights. That provision was unanimously adopted by the Constitutional Convention with no recorded debate.

Professor Bugbee states: "Clearly the legal safeguarding of an originator's rights in his inventions, writings, or other discoveries was a fundamental principle upon which the delegates were in complete agreement." (p. 2) Professor Bugbee further observes: "Like many other Constitutional provisions, the unanimously approved 'intellectual property' clause was neither accidental nor unprecedented; along with the legislation of 1790 which it authorized, it was in large part the product of colonial and early state experience." (p. 3).

It is interesting to note that Professor Bugbee prefers the term "inventive property" to denote the creative aspect of inventing. He points out that the term "industrial property" stresses the commercial rights in an invention.

right to exclude. It includes his right to select his licensees. In that connection, Mr.McLaren properly stated that "it is desirable to perserve intact the patentee's power to grant licenses unilaterally, when and to whom he pleases".[17] Furthermore, the Patent Code affirms the divisibility of patent rights.[18] Hence, the patentee may license less than all of his rights and for less than the entire term of the patent.[19] In sum, the patent laws do not obligate the patentee to promote the kind and extent of competition demanded by the antitrust laws.[20]

The Antitrust Division's tests for determining whether to challenge a particular licensing provision unwarrantedly uses antitrust Rule of Reason criteria which become relevant only if the patentee's conduct involves the plus elements of antitrust violation. The standard applicable to the patentee as formulated in the *General Electric* opinion requires only a showing that the particular patent license restriction is ancillary to the pecuniary reward for the patentee's lawful rights of exclusion. Nowhere in the Patent Code or in the body of court decisions is there any support for the Antitrust Division's position that the patentee must justify a license provision as necessary to utilization of his patent. If the limitation is within the monopoly of the patent grant, it is *per se* lawful. Moreover, the patent grant does not place upon the patentee the burden of showing that he did not have available to him less restrictive alternatives more likely to foster competition than the license restriction embodies in the license agreement.

The patent laws have different measures of permissible and wrongful conduct than the standards of the antitrust laws. For example, patent misuse is not invariably also an antitrust violation unless there is additional proof of anticompetitive conduct violating the Sherman and Clayton Acts or Section 5 of the Federal Trade Commission Act.[21] Lower federal courts have clarified and sharpened these distinctions in a series of private patent-antitrust suits decided in the 1960's.[22] There are, of course, instances where the conduct of the patentee may transgress both the patent and antitrust laws. Factual

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[17] Mr. McLaren has also said: "A patentee may decline to issue any licenses at all." *Supra* note 10, 13 Idea at 64. The courts have recognized this refusal to license. In *Sylvania Industrial Corp.* v. *Visking Corp.*, 132 F.2d 947 at 958 (4th Cir. 1943), the Court said:

"It is the right of a patentee to withhold licenses if he sees fit to do so and to confine his patented methods to the manufacture of his own goods . . . . Any advantage accruing from this practice is not unlawful, but is attributable to the monopoly conferred by the patent statute."

[18] For a depth analysis, see Powell, The Nature of a Patent Right, 17 Col. Rev. 663 (1917).

[19] The Attorney General's Antitrust Committee's Report, *supra,* at p. 225 summed up the public interest objectives in the transferability of the property rights of the patentee:

"It is now well settled, in the words of the Patent Code, that a patent has 'the attributes of personal property.' Like other property it achieves its social and economic purpose by its transferability as well as by its existence. The statutes have accordingly long provided that the whole of the patent right may be transferred by assignment, and the right transferred as to a specified part of the United States by a grant Similarly, less than the whole of the patent right may be transferred by license, which may be express or by implication. These rights of transfer may serve directly to adapt private interest to the public purpose of elevating our national standard of living through technological progress and increased productivity."

Justice Holmes has said: "A patent is property carried to the highest degree of abstraction—a right in rem to exclude, without a physical object or content". Holmes-Pollock Letters at 53 (1941).

[20] A patent grant "carries, of course, the right to be free from competition in the practice of the invention." Justice Douglas' opinion for the Court in *Mercoid Corp.* v. *Mid-Continent Investment Co.*, 320 U.S. 661 at 665 (1944).

Justice Douglas also recognized that the patent laws limit the scope of antitrust enforcement:

The patent laws which give a 17-year monopoly on 'making, using, or selling the invention' are *in pari materia* with the antitrust laws and modify them *pro tanto.* This was the *ratio decidendi* of the *General Electric* case. See 272 U.S. at 485. We decline the invitation to extend it. *Simpson* v. *Union Oil Co.*, 377 U.S. 13 (1964).

Since the 1890 Sherman Act was enacted one hundred years after the first United States Patent Act, Justice Douglas' observations, *supra,* coming from a justice who is noted as an antitrust stalwart, would remind the Antitrust Division officials that the patent laws cut down the scope of the antitrust laws rather than viewing the patent laws as merely an exception to antitrust policy.

[21] See Attorney General's Antitrust Committee Report at 254 (1955).

[22] *Columbus Automotive Corp.* v. *Oldberg Mfg. Co.*, 264 F.Supp. 779, 793 (D.Col. 1967); *Laitram Corp.* v. *King Crab, Inc.*, 245 F.Supp. 1019, 1020 (D.Alaska, 1965); *Berlanbach* v. *Anderson & Thompson Ski Co.*, 329 F.2d 782 (9th Cir. 1964); *Baldwin-Lima-Hamilton Co.* v. *Tatnall.* 288 F.2d 395 (3d Cir. 1959); *Waco-Porter Corp.* v. *Tubular Structures Corp.*, 222 F.Supp. 332, 336 (S.D.Cal. 1963).

situations involving the horizontal element of combination or conspiracy among patent owners or among their licensees are identifiable as "hard core" antitrust violations.[23] Likewise, patent license tying clause conditions are categorized as "hard core" patent misuse.[24]

The Antitrust Division criteria for testing the legality of a particular licensing provision equates rather than differentiates patent policy and antitrust Rule of Reason considerations. This tends to defeat rather than to achieve an accommodation of patent and antitrust policies applied to licensing practices. It tends to generate conflicts inconsistent with the inherent nature of the patent grant as well as to make antitrust considerations paramount. That kind of an approach sets the course for unwarrantedly cutting down the statutory scope of the patentee's lawful rights of exclusion.

My criticisms of the Antitrust Division's approach stem from fundamental beliefs I have held over the years regarding the premises and rationale for accommodating patent and antitrust policies. In my 1955 article, I expressed the belief that the Patent System benefited from the success of the Antitrust Division in purging "hard core" antitrust violations coupled with abuse of patent rights in a series of cases decided by the Supreme Court and lower federal courts in the 1940's.[25] Several of these cases involved illegal international cartels. Those government victories were clearly not in derogation of lawful patent rights. Today patent and antitrust counselors generally regard them as a catharsis which was long overdue.

My criticisms do not question the obligation of the Antitrust Division to test borderland issues on which judicial clarification on patent license limitations is needed.[26] But the guideline tests announced by the Antitrust Division for challenging particular patent license restrictions go far beyond that objective. The Antitrust Division, among other pronouncements, has declared its determination to seek drastic modification of the Supreme Court precedents favorable to the patentee in the 1938 *General Talking Pictures* case,[27] involving field of use restrictions, and the 1947 *Transparent-Wrap* case[28] involving an assignment grant-back. Regardless of differences of view on the merits of those rulings, patent counselors have relied upon those explicit precedents on permissible licensing restrictions as the law of the land.

The bar and patent licensing executives are now faced with speculative evaluations regarding the impact these newly announced challenges of the Antitrust Division may have on the courts or on the Congress. Under our system of checks and balances, either the judiciary or the Congress may have the final say. In the interim, however, legal counselors may be in a quandary on how to advise company managements. Shall they advise on the basis of what the law *is* or on what the Antitrust Division believes the law *ought to be?* It is understandable that some attorneys may be heeding the advice of Bruce B. Wilson, Mr. McLaren's Special Assistant, who said in a recent address:[29]

"One of the jobs of the lawyer in private practice is to keep his client out of antitrust trouble. One of the ways to accomplish this objective is to be cautious as to the types of restrictions which you put into license agreements. I found in private practice that it is much easier to answer the question of whether I should put a particular restriction in a license agreement, than it is in my present position to answer the question of whether the Division should challenge the same restriction. I believe this is one area in which it is wise for the private practitioner to err on the side of caution."

When one considers the fear of private treble damage suits if the government should succeed in its attack upon a particular license provision, it should not be surprising that the inhibitory effects of the warnings of the Antitrust Division officials may cause some counselors to hesitate to exercise a judgment based solely on existing judicial precedents.

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[23] See cases cited *infra* note 25.

[24] See *Ethyl Gasoline* and *Univis Lens* cases, cited *supra* note 15.

[25] *United States* v. *Masonite Corp.*, 316 U.S. 265 (1942); *Hartford-Empire Co.* v. *United States*, 323 U.S. 386 (1945); *United States* v. *National Lead Co.*, 332 U.S. 319 (1947); *United States* v. *United States Gypsum Co.*, 333 U.S. 364 (1948); *United States* v. *General Electric Co.*, 80 F.Supp. 989 (S.D.N.Y. 1948) (*Carboloy* case).

[26] As of 1955 my article, cited *supra*, note 1, indicated the borderline issues which existed at that time and some of which still need clarification.

[27] See *infra* notes 31–34.

[28] *See infra* notes 39–42.

[29] *Wilson*, supra note 10.

I now turn to specific examples of why and how the Antitrust Division's tests for challenging particular judicially approved licensing practices are relevant to antitrust considerations rather than patent policy considerations.

ANTITRUST DIVISION VIEWS ON FIELD OF USE LICENSE RESTRICTIONS

Field of use patent license limitations are widespread.[30] The Division does not question all such restrictions but its warnings reveal that it regards many of them as purely contractual provisions subject to antitrust attack rather than restrictions integral to the patentee's rightful reward.[31]

Mr. Stern, Chief of the Division's Patent Unit, speaking for himself has articulated the Division's reasoning in some detail.[32] He begins by questioning the assumption that limiting the field of uses for which the license may sell the patented product is valid under the authority of the 1938 *General Talking Pictures* case.[33] There, the Supreme Court, in an opinion by Justice Brandeis, sustained a provision in a license to make and sell a patented sound recording system only in the commercial field. Applying the 1926 *General Electric* standard of reward normally within the patent grant, Justice Brandeis said that the legality of a use restriction had never been questioned. The Court held there was patent infringement when a licensee, authorized to make and sell only for private home use, violated that restriction by selling the equipment in the commercial field in which it was not licensed.

Mr. Stern is hopeful that if and when the 1926 *GE* first sale price license restriction is overruled, any residual precedent value of that case will be reduced, thus requiring *General Talking Pictures* to stand, if at all, on some other basis.

I find that reasoning puzzling. Even if the first sale price restriction sanction, which has already been reduced by lower federal court decisions to the vanishing point, should be outlawed by the Supreme Court, the *GE* case general standard of permissible licensing restrictions within the reward and the scope of the patent grant would not necessarily be affected as applied to restrictions other than price.

Mr. Stern's statements also apply antitrust principles to field of use licensing in a manner which fails to distinguish patent law and antitrust

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[30] The PTC Research Institute Empirical Study, by Oppenheim and Scott, *supra*, note 5, revealed that only 28 percent (74 of 108 respondents) stated they never engage in field of use licensing. The reasons for use of this type of license restriction yielded a variety of explanations. See 14 Idea, note 5 *supra* at 145.

[31] Mr. McLaren has stated the Antitrust Division's position on field of use licensing as follows:

* * * there may be some justification for a patentee reserving for himself a well-defined field out of the various potential applications for his invention. On the other hand, it is difficult to see how justification can be shown for the type of restriction which divides fields of use among licensees who otherwise would compete. Such restrictions in effect grant a submonopoly to each of the licensees, and all competition among those who would be likely competitors is eliminated. In due course, I expect that we will bring a case directly challenging restrictions of this type.

Some of those who seek to justify all field-of-use restrictions may point out that that such restraints are likely to arise where there is a substantial disparity in the value of the invention as applied in various non-competing end uses. A patentee, if he is to gain a maximum royalty, will try to charge different royalties depending on the market served. Royalty discrimination, it is argued, is inherent in the lawful patent monopoly and depends for its success on field-of-use restrictions. However, it is not necessary to eliminate, by contractual restriction, all competition between licensees, in order to achieve maximum royalties from various end-use applications. In some circumstances, the patentee may be able to maximize his return by, for example, establishing different royalty rates for the various uses and then offering to license freely throughout the range of application. (McLaren, Patent Licenses and Antitrust Considerations, *supra* note 10 at 63–64.)

Mr. Wilson, Special Assistant to Mr. McLaren, has observed:

With respect to field-of-use restrictions, I initially should make one thing clear. We see no difference between a license which contains a positive prohibition against sales in particular fields and one which merely grants a license limited to a particular field. Our investigations have shown that the *effect* of these two types of provisions is precisely the same. The licensee in fact sells only in the fields of which he is licensed. We are not willing to permit the form of the agreement to take precedence over its substance. (Wilson, Patents and Antitrust, *supra* note 10. See also Donnem, *supra* note 10 at 37–39.)

[32] The two addresses of Mr. Stern, to which my discussion refers, are cited *supra*, note 10.

[33] *General Talking Pictures Corp. v. Western Electric Co.*, 305 U.S. 124 (1938).

considerations. Mr. Stern states that, under some circumstances, it would be reasonable for a patentee to reserve to himself a field of use in which he operates in order to induce him to license another use not in competition with him. That is not a patent law test. The patentee is under no duty to justify excluding all others from a field of use. I also differ with the position questioning the right of the patentee to carve out separate exclusive licenses for separate fields of use. So long as the patentee acts unilaterally, negotiates vertically with each exclusive licensee, does not restrict the licensee's activity outside the granted field of use, and does not attempt to exercise control over the product after a valid first sale within the authorized field of use, such a practice does not transgress patent law policy.[34] Any challenge of such conduct should be made under the antitrust laws by proving horizontal or vertical restraints on competition outside the scope of the patent grant.

It is apparent to me that from the various addresses of Antitrust Division officials there emerges a pattern of testing field of use limitations by substituting antitrust considerations for patent law principles. The entire line of reasoning is geared to the Division's tests of whether there are less restrictive alternatives available to the patentee which are more likely to foster competition and whether the more restrictive provision is justifiable as necessary to the utilization of the patent grant. If the restriction is within the patent grant's scope, it is strange indeed to argue that the patentee's rights of exclusion must be exercised only if this promotes optimum competition in his patented invention.

Another contradiction comes to the surface in connection with the judicially approved right of the patentee to grant an exclusive license, exclusive even of the patentee himself.[35] Whether the exclusive license applies to a field of use or other divisible rights of the patent grant, the patent law public policy does not require the patentee to justify an exclusive license or to defend it against the charge that it does not foster competition as would be the case with non-exclusive licenses. Yet the Antitrust Division strays from such patent policy criteria of legality by emphasizing that non-exclusive licensing would usually be more profitable to the patentee and would relieve the patentee of the burden of proving absolute economic necessity for the exclusive license either for his own benefit, or to induce acceptance of a license by a company which will not otherwise risk investment in a new market relevant to the patent. Again these are antitrust considerations, which would not even be evidence of illegal conduct since the patentee, acting alone, has the option of granting an exclusive license or non-exclusive license as he sees fit.

The argument that multiple exclusive field of use licenses are for the benefit of the licensees and not for the benefit of the patentee is questionable. When the patentee engages in such field of use licensing because his licensees will not otherwise risk investment, is he not being motivated by economic necessity and is he not in reality licensing for his own benefit? The courts have not condemned mere multiple licenses unilaterally granted by

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[34] Subsequent to the *General Talking Pictures* case, the courts have continued to uphold field of use restrictions in patent licenses, except in particular circumstances where they have been used as the cover for industry-wide cartel arrangements, or have adversely affected competition in unpatented goods, or have involved attempts to restrict the use of products that have been sold in ordinary channels of trade. For decisions holding field of use restrictions in patent licenses valid, see *Automatic Radio Mfg. Co. v. Hazeltine Research*, 176 F.2d 799 (1st Cir. 1949), *aff'd on other grounds* 339 U.S. 827 (1950); *Hazeltine Research v. Admiral Corp.*, 183 F.2d 953 (7th Cir. 1950), *cert. denied* 340 U.S. 896 1950); *Sperry Products v. Aluminum Co. of America*, 171 F.Supp. 901 (N.D.Ohio 1959); *Eversharp, Inc. v. Fisher Pen Co.*, 204 F.Supp. 649 (N.D.Ill. 1961); *Chemagro Corp. v. Universal Chemical Co.*, 244 F.Supp. 486 (E.D.Texas 1964); *Benger Laboratories, Ltd. v. R. K. Laros Co.*, 209 F.Supp. 639 (E.D.Pa. 1963), *aff'd per curiam* 317 F.2d 455 (3d Cir. 1963), *cert. denied* 375 U.S. 833 (1963); *Barr Rubber Products Co. v. Sun Rubber Co.*, 277 F.Supp. 484 (S.D.N.Y. 1967); *Good Humor Corp. v. Popsicle Corp.*, 59 F.2d 344 (1932), *aff'd* 66 F.2d 659 (3d Cir. 1933); *Westinghouse Electric Corp. v. Bulldog Electric Products Co.*, 106 F.Supp. 819 (D.W.Va. 1952), *aff'd on other grounds* 206 F.2d 574 (4th Cir. 1953), *cert. denied* 346 U.S. 909 (1953).

[35] *Rail-Trailer Co. v. ACF Industries, Inc.*, 358 F.2d 15 (7th Cir. 1966), where the court said that "without more" an exclusive license "does not constitute an illegal restraint of trade."

the patentee.[36] Such restrictions still relate to the patentee's pecuniary reward for his patented invention. The type of restriction designed solely for the benefit of the licensee is illustrated by a license agreement such as that in the *Ethyl Gasoline* and *Univis Lens* cases[37] where the patentee receives his full price reward for the sale of a patented product but fixes the resale price or other terms from which only the licensees derive profit. This is as clearly patent misuse as in the case where the patentee includes tying clause in his patent license to derive profits from unpatented parts or supplies.[38]

The root error in the Antitrust Division's thinking, as I previously stressed, is its challenge of judicially approved license restrictions inherent in the patentee's legitimate reward as though they were purely contractual provisions with the purpose and effect of extending the patent monopoly beyond its lawful boundaries.

DIVISION QUESTIONS TRANSPARENT-WRAP SUPREME COURT SANCTION OF ASSIGNMENT GRANT-BACK

Another Division target is the *Transparent-Wrap* Supreme Court decision[39] upholding a patent license provision requiring the licensee to assign back to the patentee improvement patents of the licensee. This was held not in itself illegal *per se* and justified by the assignment provision of the Patent Code. On remand on antitrust aspects, Judge Hand held there were no illegal antitrust restraints.[40]

The Division seeks to circumscribe the *Transparent-Wrap* ruling. Applying its less restrictive alternatives criterion, the Division indulges the assumption that all assignment grants-back tend to stifle research and development. It advocates non-exclusive grants-back as the desired alternative.

Our PTC Research Institute empirical study revealed that while grant-back provisions are quite common, an assignment and an exclusive grant-back is relatively uncommon.[41] It is ironic that the Division begrudges reliance on a Supreme Court decision in the *Transparent-Wrap* case where Justice Douglas, a stalwart antitruster, and often charged with being hostile to patent rights, wrote the Court's opinion. Even though that decision is still the law,[42] the

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[36] As the Attorney General's Antitrust Committee Report stated at 241:

In general, a patent license, valid when standing alone, does not become invalid because other licenses are granted. Illegality would attach only through a finding equivalent to a conspiracy among the licensees. However, the presence of a multiplicity of patent licenses with restrictions may indicate something more than the repeated individual grant of proper licenses. Thus a showing of joint efforts of the licensees to find patents under which all can be licensed subject, for example, to identical price fixing provisions—or a showing that the licensees gathered at meetings to discuss price fixing licenses—goes far to show illicit horizontal agreement between licensees. Such agreement has been properly held to be outside the range of proper license activity and to be contrary to the antitrust laws.

In short, to the extent that such licenses are entered into as individual licenses, and are legal as such, they may stand. To the extent that they involve horizontal agreement between the licensees, antitrust violation follows.

For examples of horizontal agreements beyond the scope of individual patent rights and involving the plus elements of antitrust violation, see cases cited *supra* note 25.

[37] *Supra* note 15.

[38] *Supra* notes 13, 14.

[39] *Transparent-Wrap Machine Corp.* v. *Stokes & Smith Co.*, 329 U.S. 637 (1947). The Attorney General's Committee's Antitrust Report at 227 (1955) defines a grant-back in these terms:

Grant back covenants, sometimes included in patent licenses, provide for license or assignment to the licensor of any improvement patented by the licensee in the products or processes of the licensed patent.

[40] *Stokes & Smith Co.* v. *Transparent-Wrap Machine Corp.*, 161 F.2d 565 (2d Cir. 1947), *cert. denied* 331 U.S. 837 (1947).

[41] 14 Idea at 139–142, study cited *supra* note 5. Improvement patents are the most common type of patents covered by grant-back provisions (about 60 percent reported by respondents to the questionnaire). The reasons for requiring grant-back commitments are summarized at 141–142.

[42] The lower federal courts have generally sustained grants-back, including assignment grants-back, absent proof of a conspiracy to restrain or monopolize interstate trade: *Modern Art Printing Co.* v. *Skeels*, 123 F.Supp. 426 (D.N.J. 1954); *rev'd on other grounds* 223 F.2d 719 (3d Cir. 1955) (assignment): *United States* v. *Birdsboro Steel Foundry & Machine Co.*, 139 F.Supp. 244 (W.D.Pa. 1956) (assignment); *International Nickel Co.* v. *Ford Motor Co.*, 166 F.Supp. 551 (S.D.N.Y. 1958); *Sperry Products, Inc.* v. *Aluminum Co. of America*, 171 F.Supp. 901 (N.D.Ohio 1959), *aff'd* 285 F.2d 911 (6th Cir. 1960) (assignment); *Zajicek* v. *Koolvent Metal Awning Corp. of America*, 283 F.2d 127 (9th Cir. 1960) (assignment); *Binks Mfg. Co.* v. *Ransburg Electro-Coating Corp.*, 281 F.2d 252 (7th Cir. 1960), *cert. dismissed*, 366 U.S. 211 (1961) (nonexclusive with right to sublicense); *B & M Corp.* v. *Miller*, 150 F.Supp. 942 (W.D.Ky. 1967) (not clear whether assignment or license back); *Old Dominion Box Co.* v. *Continental Can Co.*, 273 F.Supp. 550 (S.D.N.Y. 1967) (license back).

Division places it under an antitrust cloud by threatening to attack it when it finds the occasion to do so. As a counseling approach, I think an assignment grant-back should not be required unless the licensor's position as a small company is so disparate compared to the large-scale size and resources of the licensee that the licensor needs protection against the licensee's massive research and development resources. A *per se* illegality rule would block this lawful option of the licensor.

FIRST SALE PRICE LICENSE LIMITATION

There is little usefulness in dwelling on the Antitrust Division's repeated efforts to get the Supreme Court to overrule the 1926 *General Electric* decision[43] sustaining a first sale price restriction in a patent license. Our empirical study revealed that such a limitation was used by only two companies out of 108 companies responding to our questionnaire.[44] Furthermore, court decisions subsequent to 1926 have so hemmed in the scope of permissible use of a first sale price license limitation that, as a practical matter, patent counselors are fully aware of its narrow vitality.[45] The Division has also questioned quantity limitations in a patent license as akin to a price limitation[46] but the few court decisions on that point approve that limitation.[47]

TERRITORIAL LIMITATIONS WITHIN THE UNITED STATES

It is not clear precisely what the Division's position is on territorial patent license restrictions within the United States. Mr. Donnem has expressed doubt regarding the assumption that Section 261 of the Patent Code legalizes such limitations.[48] Yet that provision explicitly states that an applicant, patentee or his assigns may grant an exclusive right under his application or patent to the whole or any part of the United States. The Attorney General's National Antitrust Committee 1955 Report, relying on Section 261, declares there is "no doubt of the right of the patentee to place territorial restrictions upon his assigns or licensee within the United States."[49] As Committee Co-Chairman

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[43] *United States* v. *General Electric Co.*, 272 U.S. 426 (1926).

[44] 14 Idea at 137–139, study cited *supra* note 5.

[45] *The following holdings have narrowed the permissive use of a first sale price re*striction ancillary to the patent license: a patentee cannot fix the price charged by his licensee if only part of the product involved is covered by the patent, *United States* v. *General Electric Co.*, 80 F.Supp. 789 at 1004–1005 (S.D.N.Y. 1948); if his patent covers the process and machine used in producing the product but not the product itself, *Barber-Colman Co.* v. *National Tube Co.*, 136 F.2d 339 (6th Cir. 1943); *the patent owner may not fix the price when he issues more than one license, Newburgh Moire Co.* v. *Superior Moire Co.*, 237 F.2d 283 (3d Cir. 1956); a licensee price cannot be fixed by patent owners participating in a cross-licensing arrangement, *United States* v. *Line Material Co.*, 333 U.S. 287 (1948).

It is well known that the Antitrust Division came close to achieving an overruling of the first sale price restriction in *Line Material, supra,* and *United States* v. *Huck Mfg. Co.*, 382 U.S. 197 (1965), where a divided Court affirmed without opinion the District Court's dismissal of the government's charges of a conspiracy in violation of Sections 1 and 2 of the Sherman Act. Huck had granted Townsend, the sole licensee, a license to make and sell patented devices covered by the Huck patents. The agreement provided that Townsend was to maintain at least Huck's prices on the licensed products. The District Court held that the evidence in all material respects made controlling the 1926 General Electric decision.

The General Electric sanction apparently would not apply to a sole licensee who does not manufacture in competition with the patentee-licensor. See *Royal Industries* v. *St. Regis Paper Co.*, 420 F.2d 449 (9th Cir. 1969).

The Antitrust Division has declared its intention to continue to seek an overruling of the first sale price restriction sanctioned in the 1926 General Electric decision. McLaren, *supra* note 10; Donnem, *supra* note 10.

[46] Donnem, *supra* note 10 at 40. The same view was expressed by a former head of the Antitrust Division. Turner, Patents, Antitrust and Innovation, 28 U.Pitt.L.Rev. 151 (1966).

[47] *Rubber Tire Wheel Co.* v. *Milwaukee Rubber Wheel Co.*, 154 F. 358 (7th Cir. 1907); *Q-Tips, Inc.* v. *Johnson & Johnson*, 109 F.Supp. 657 (D.N.J. 1951), *aff'd* 207 F.2d 509 (3d Cir. 1953), *cert. denied* 347 U.S. 935 (1954); *Williams* v. *Hughes Tool Co.*, 186 F.2d 278 (10th Cir. 1950); *United States* v. *E. I. DuPont de Nemours & Co.*, 118 F. Supp. 41 at 224–226 (D.Del. 1953), *aff'd on other grounds* 351 U.S. 377 (1956), where the Court said: "The cases are to the effect [that] owner of a valid product patent may by license restrict production of the licensee to a specified quantity, at a specified place."

The PTC Research Institute empirical study, *supra* note 5 at 150 revealed that 76 percent of the respondents said they never limit the licensee's production.

[48] Donnem, *supra*, note 10 at 39.

[49] At 237. The PTC Research Institute empirical study, *supra* note 5, at 148 showed that nearly 70 percent of the questionnaire respondents said they never use territorial restrictions.

I concurred in that view. Two District Courts have upheld such domestic patent license limitations.[50] Territorial restrictions in international patent licensing is a subject presenting different problems.

It is also not clear how the Division would regard a situation where the patentee, acting unilaterally, negotiates independently with each of several parties licenses containing vertical territorial restrictions in different parts of the United States. My view is that these multiple vertical territorial restrictions are lawful within Section 261. If, however, there is proof of a horizontal agreement to divide markets of the type that is prohibited under the Sherman Act, then the illegality stems solely from antitrust considerations.

RESTRICTIONS ON PURCHASER

General Talking Pictures did not involve a purchaser who bought for value in good faith and without notice of the use restriction in the license. Therefore, there was no inception of a valid sale since both the seller and the buyer of the sound equipment had knowledge that the use restriction was being violated.[51]

It is beyond dispute that restrictions upon purchasers after an *authorized first sale* of a patented article by the licensee clearly exhausts the patentee's monopoly. If the sale is made within the licensed field of use or territory, the patentee cannot restrict the resale price or territory in which the resale is made.

ONLY THE PATENTEE CAN SELECT HIS LICENSEES

The Antitrust Division is on sound ground in attacking any agreement where the patentee delegates to another a veto power over the selection of licensees under the patent. The patentee or his assignee to whom he conveys all right and title is the only one legally entitled to grant licenses under the patent. Hence the *Besser*, *Krasnov* and *McCullough* cases[52] are clearly correct in condemning a purely contractual provision whereby the patentee grants another, or others jointly, a veto power over the selection of licensees. The patentee's right to exclude must always be exercised unilaterally. The patentee may, however, grant a licensee authority to sub-license. The Antitrust Division is, therefore, correct in its position that only the patentee, acting unilaterally, may select his licensees.

PART II

TRADE SECRET OR KNOW-HOW LICENSE LIMITATIONS

As previously stated, on this topic my concern is not the rationale of the Antitrust Division as stated by Mr. McLaren. Rather it is the startling dictum of Justice Black in *Lear* v. *Adkins*.[53]

Before discussing that dictum, a summation of Mr. McLaren's view and a resume of the legal principles underlying trade secret protection may avoid misunderstanding of the nature of the controversy. In my discussion I use the terms "trade secret" and "secret know-how" as virtually interchangeable.

Mr. McLaren is to be commended for declaring that he favors protection of valid trade secret rights in both federal and state courts. He specified the ele-

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[50] *United States* v. *Crown Zellerbach Corp.* 141 F.Supp. 118, 127 (N.D.Ill. 1956); *Deering Milliken & Co.* v. *Temp-Resisto Corp.*, 160 F.Supp. 463 (S.D.N.Y. 1958).

[51] There is need for carefully distinguishing the situations where there is a *first authorized sale* of a patented article which "exhausts" the patent monopoly and situations where a patent license restriction, such as in the *General Talking Pictures* case, is violated by a sale of a patented article unauthorized by the license. In that event it is erroneous to contend that antitrust principles override the license restriction and therefore calls for the application of the rule that the purchaser may resell or use the article as he pleases and also determine the resale price of the patented article. This confusion still persists by reason of the failure to confine the rule against restrictions on purchasers to cases where there is inception of a lawful first sale. There is an area of uncertainty where the purchaser acts in good faith and pays value without notice of the license restriction. No court has been called upon to decide that narrow question.

[52] *United States* v. *Besser Mfg. Co.*, 96 F.Supp. 304 (E.D. Mich. 1951), *aff'd* 343 U.S. 444 (1952); *United States* v. *Krasnov*, 143 F.Supp. 484 (E.D.Pa. 1956), *aff'd per curiam* 355 U.S. 5 (1957); *McCullough Tool Co.* v. *Wells Surveys, Inc.*, 343 F.2d 381 (10th Cir. 1965), *cert. denied* 383 U.S. 933 (1966).

[53] *Lear, Inc.* v. *Adkins*, 395 U.S. 653 (1969).

ments of his advocated Rule of Reason approach to restrictions in know-how licensing as follows:[54]

"First, the restriction must be ancillary to carrying out the lawful primary purpose of the agreement. Second, the scope and duration of the restraint must be no broader than is necessary to support that primary purpose. And third, the restrictions must be otherwise reasonable under the circumstances. In effect, the rule on know-how licensing is pretty much the same as the rule on patent licensing. Except as to certain well-known restraints which are *per se* unlawful, the standard is the rule of reason."

Bear in mind that unpatented trade secret subject matter does not give the owner the statutory rights of exclusion set forth in Section 154 of the Patent Code. A trade secret is not a monopoly. Mr. McLaren's Rule of Reason properly formulates an ancillary restraints doctrine which would permit the courts to distinguish between restrictions in royalty-bearing know-how license agreements reasonably ancillary to the main lawful purpose of the agreement and restrictions which involve plus antitrust restraints beyond the proprietary information rights disclosed in confidence under the license. If any other official of the Division should express a view to the contrary, I presume he is speaking for himself and not for Mr. McLaren.

It should be kept in mind that each trade secret case is decided on the specific factual situation. The courts have used various theories of protection, such as property rights, contract, unfair competition, quasi-contract, and breach of trust or confidence.[55] The Restatement, Torts, Sections 757[56] and 758, sets forth the basic principles governing liability.

The Restatement defines a trade secret as "Any information of peculiar value to its owner, not protected by patent and not generally known or accessible to everyone." This is far more extensive than patentable subject matter and supplements, rather than conflicts with, patents. The Restatement does not purport to present an exclusive enumeration of specific kinds of trade secrets. Examples given are "a formula for a chemical compound, a process of manufacturing, treating or preserving materials, a pattern for a machine or device, or a list of customers."

Trade secrets last only as long as substantial secrecy is preserved. Ideas in general circulation are obviously in the public domain. Any person who independently learns the secret may lawfully use the secret or disclose it to others. The main elements of a plaintiff's trade secret or secret know-how case are (1) proof of existence of a specific trade secret not discovered by fair means; (2) a confidential disclosure to defendant in trust or confidence; and (3) the confidence was violated by disclosure to others to the injury of the plaintiff. I presume that Mr. McLaren had these requirements in mind when referring to valid trade secret rights which have value.

Turning to Mr. Justice Black's dictum in *Lear* v. *Adkins*, I believe it asserts an unwarranted broad federal preemption of unpatented trade secret rights. The premise of the dictum is that if an owner of a trade secret discloses it in confidence in return for contractual royalty payments, this runs counter to

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[54] McLaren, Competition in the Foreign Commerce of the United States, address before a symposium at the Marshall-Wythe School of Law, College of William and Mary, Williamsburg, Virginia, October 16, 1970. My article on Foreign Commerce Under the Sherman Act—Points and Implications of the Timken Case, 42 Trade-Mark Rep. 3 at 20 (1942) stated a like Rule of Reason approach:

In respects similar to, but not necessarily identical with, patent rights, restrictions accompanying transactions in secret information should be regarded as lawful when they are reasonably ancillary to a main lawful purpose within the ambit of the confidential disclosure.

[55] For cases and comments on trade secrets, see Oppenheim, Unfair Trade Practices, 229–279 (2d ed. 1965) (1969 Supp.). Comprehensive texts are Turner, The Law of Trade Secrets (1962), and Callmann, Unfair Competition, Trademarks and Monopolies, Ch. 14 (3d ed. 1968). See also Trade Secrets: Report of An Institute Clinic, 14 Idea 212 (1970); Harris & Siegel, Trade Secrets in the Context of Positive Competition, 10 Idea 297 (1966).

[56] Restatement, Torts, Section 757, states the general principles:

Liability for disclosure or use of another's trade secret—general principle.

"One who discloses or uses another's trade secret, without a privilege to do so, is liable to the other if (a) he discovered the secret by improper means, or; (b) his disclosure or use constitutes a breach of confidence reposed in him by the other in disclosing the secret to him, or; (c) he learned the secret from a third person with notice of the facts that it was a secret and that the third person discovered it by improper means or that the third person's disclosure of it was otherwise a breach of his duty to the other; or (d) he learned the secret with notice of the facts that it was a secret that its disclosure was made to him by mistake."

federal patent policy and to the Supremacy Clause of the federal Constitution.

With the concurrence of Chief Justice Warren and Justice Douglas, Justice Black said:

"The national policy expressed in the patent laws, favoring free competition and narrowly limiting monopoly, cannot be frustrated by private agreements among individuals with or without approval of the State."

In essence, Mr. Justice Black construes the Constitutional provision on patents and the Patent Code as preempting contractual arrangements for licensing trade secrets for royalty payments. The Justice cited in support the *Sears* and *Compco* decisions of the Court.[57]

The demise of the licensee estoppel doctrine in *Lear* v. *Adkins*, on which all Justices concurred, occasioned no surprise to members of the patent and antitrust bars who knew that previous decisions of the Court had eroded the license estoppel doctrine by exceptions. The suit in *Lear* was by the inventor against the licensee of the patent for breach of a patent licensing agreement. To understand the thrust of Justice Black's dictum, note that the license was executed in 1955 while a patent application disclosing trade secrets was pending in the United States Patent Office. Lear thus obtained access to Adkins' ideas for which Lear promised to pay royalties five years before the patent issued to Adkins in 1960. This raised the heart of the question whether federal patent policy bars a state from enforcing an agreement governing access to unpatented trade secrets.

The Supreme Court held that with respect to royalty payments due after the patent issued, the licensee was not obligated to pay unless the patent was valid. But regarding royalties accrued and unpaid prior to the issuance of the patent, the Court declined to resolve the question whether a state may protect the owner of unpatented trade secrets. Hence, the majority of the Court did not accept Justice Black's dissenting view that trade secret licenses run contrary to national patent policy.

In my opinion Justice Black's dictum misconceives the public policy considerations supporting federal and state enforcement of trade secret licensing for agreed upon royalty payments. Patent and trade secret rights have coexisted in the United States for more than a century. Prior to the Black dictum the Supreme Court has not questioned trade secret licensing.[58] Congressional enactment of patent laws, including the Patent Code of 1952, has not even intimated that the patent laws preempt enforcement of contractual provisions in trade secret licenses.

Federal statutes protect against disclosure of trade secrets by various federal agencies.[59] A federal statute makes it a crime for a federal government employee to disclose trade secrets. Nineteen states make it a crime to misappropriate trade secrets.[60] The Internal Revenue Code recognizes trade secrets as property subject to capital gains treatment.[61] Despite the alarm that the *Sears* and *Compco* decisions of the Supreme Court would be applied expan-

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[57] *Sears, Roebuck & Co.* v. *Stiffel*, 376 U.S. 225 (1964); *Compco Corp.* v. *Day-Brite Lighting, Inc.*, 376 U.S. 234 (1964). See Doerfer, The Limits on Trade Secret Law Imposed by Federal Patent and Antitrust Supremacy, 80 Harv.L.Rev. 432 (1967).

On March 19, 1971 Senator Scott reintroduced in the 92nd Congress, 1st Session, a proposed Amendment No. 23, to S.643, which is intended to counteract the preemptive effect of The Black dictum in *Lear* v. *Adkins* and in *Sears* and *Compco, supra.* The Amendment reads as follows:

"§ 301. *Preservation of other rights.*

"This title shall not be construed to preempt, or otherwise affect in any manner, rights or obligations not expressly arising by operation of this title whether arising by operation of State or Federal law of contracts, of confidential or proprietary information, of trade secrets, of unfair competition, or of other nature."

[58] As early as 1889 the Supreme Court recognized the enforceability of a trade secret license. *Dr. Miles Medical Co.* v. *Park & Sons Co.*, 220 U.S. 373 (1911). Since then Circuit Court of Appeals have not questioned trade secret licenses. See *Foundry Services, Inc.* v. *Beneflux Corp.*, 206 F.2d 214 (2nd Cir. 1953); *Formulabs, Inc.* v. *Hartley Pen Co.*, 275 F.2d 52 (9th Cir. 1950) *cert. denied* 363 U.S. 830 (1960); *Imperial Chemical Industries Ltd.* v. *National Distillers & Chemical Corp.*, 342 F.2d 737 (2nd Cir. 1965), modified 354 F.2d 459 (2nd Cir. 1965).

[59] Congress has enacted various laws which prohibit disclosure or publication of trade secrets. Illustrative are the Freedom of Information Act, 5 U.S.C. § 552(b)(4), Supp. IV. (1969); the Federal Trade Commission Act, 15 U.S.C. § 46(f) (1964); the Securities and Exchange Act of 1934, 15 U.S.C. §78x (a) (1964).

[60] 18 U.S.C. § 1905 (1964).

[61] 26 U.S.C. § 2314–2315 (1964). Congress has more specifically recognized that trade secrets may be licensed by providing tax treatment for rentals and royalties secured from licenses of "secret processes and formulas," 26 U.S.C. § 861(a)(4); 862(a)(4) (1964).

sively, the federal and state courts have generally not applied that phase of federal preemption to deny protection to trade secrets.[62]

I have long been against giving a competitor a "free ride" by misappropriation of what equitably belongs to another, such as innovation resulting from the labor, efforts and expenditures of one who innovates trade secrets.[63] The Black dictum would sanction unjust enrichment by allowing one to "reap where he has not sown."

It is elementary that a patent may issue only on a process, machine, manufacture or composition of matter. Trade secret subject matter covers a much greater scope than patentable subject matter.

Justice Black's dictum would obstruct rather than promote competition in unpatented trade secrets. This competition is as important as the competition of patented and patentable art. Trade secret licensing opens up, rather than suppresses that art. To say that the owner of a trade secret can only lawfully keep the secret to himself, use it in his own business, or sell it outright, unless he obtains a patent covering the secret subject matter, is inherently at odds with antitrust policy. Moreover, our patent policy does not obligate an inventor to disclose either patentable or trade secret subject matter. The option to seek a patent for commercial exploitation or to license trade secrets for royalty payments rests with the inventor. Even when the inventor files a patent application, which is preserved in secrecy while the application is pending, the inventor still retains the option of whether to pay the final fee and accept a patent which the Patent Office decides has allowable claims, or to rely upon trade secret protection.

The Black dictum also overlooks the risks the owner of trade secrets assumes in licensing their use for royalties on a confidential disclosure basis. One is the risk that a third party may discover the secret by fair means. Another risk is that the licensee may be able to innovate through fair means his own improved trade secret by what he has learned from the licensed trade secrets. Perhaps the most significant risk is that of rapid obsolescence of one's trade secrets by technological advancements. It is naive to suppose that trade secrets have perpetual existence. No empirical study of the life of trade secrets has been made but it would not be surprising if it were found that a substantial percentage of trade secrets have a shorter life than the 17 year patent monopoly—and even so, many patents become outmoded before the patent expires.

When one considers how widespread trade secrets are in our competitive economy, it is a matter of great concern to contemplate to what extent the Black dictum would open the door to sanctioned misappropriation of trade secrets and breaches of confidential disclosures. This would put a premium on rewarding fradulent conduct rather than promoting the public interest in protecting valid trade secrets.

In *Painton & Co. v. Bourns*,[64] the District Court applied hte Justice Black dictum in *Lear* v. *Adkins* by holding that the enforcement of a trade secret license for royalty payments would be contrary to "our national patent law and policy." The case is now on appeal in the Second Circuit.

Painton v. *Bourns* has stirred up a tempest of alarm which I hope the appellate court will dissipate. The Second Circuit may dispose of the issue as a question of interpretation of the contract pursuant to California law, the forum prescribed by the agreement. My reading of the terms of the contract persuades me that Bourns is right in contending that Painton had a mere license to use the Bourns trade secrets on payment of royalties and that the termination of the license ended the licensee's right to use the sceret information. The District Court held to the contrary on a rationale which misinterprets the majority Supreme Court holding in *Lear* v. *Adkins* and gives the dissenting dictum of Justice Black the weight that is only warranted by a Supreme Court decision precedent. This injection of a misreading of the public policy of our patent laws led the District Court to rule that Painton could use Bourns' trade secrets as long as it desired and that the termination of the contract only terminated the royalty payments. For reasons I have already

[62] See Handler, Some Comments on Selected Current Rulings and the Burning Issues of the Day, 38 ABA Antitrust L.J., No. 4,574 at 578, footnote 23 (1969).

[63] See my comments in Unfair Trade Practices Relating to Industrial-Intellectual Property, 14 Idea 384 at 459–461 (1970), PTC Research Institute Clinic. See also, Harold F. Baker, Monopoly Concept of Trade Marks and Trade Names and "Free Ride" Theory of Unfair Competition, 17 Geo.Wash.L.Rev. 112 (1948).

[64] *Painton & Co., Ltd.* v. *Bourns, Inc.*, 309 F. Supp. 271 (S.D. N.Y. 1970).

discussed with respect to the Justice Black dictum, I consider the District Court's reasoning completely untenable.

The PTC Research Institute conducted empirical studies relating to trade secrets. Several surveys showed that there has been increased reliance by American companies on trade secrets.[65] Other surveys revealed that trade secrets or secret know-how from American companies was sought more often by prospective foreign licensees than patents or trademarks.[66] Often the principal asset the licensees want is know-how.

The Rule of Reason ancillary restraints doctrine gives promise of continued federal and state court sanctioning of limitations ancillary to valid trade secrets without impairment of antitrust enforcement against restraints of an illegal *per se* nature or those which, taking into consideration all of the relevant circumstances, are non-ancillary and unreasonable. That approach also maps out the road to a proper accommodation of trade secret and unfair competition doctrines to patent policy.

In conclusion I recapitulate three fundamentals for accommodation of patent public policy and antitrust policy related to license limitations:

First, preserve to the patentee the full reward to which the exclusive rights of the patent grant entitle him within the scope of the claims of his patented invention.

Second, apply the antitrust laws *only* when there is proof of plus antitrust elements arising from restraints beyond the exclusivity bounds of the patent grant.

Third, reject the fallacy that federal patent policy preempts licensing for royalties of trade secret or secret know-how and continue to protect valid secret proprietary information pursuant to long-established federal and state judicial precedents.

OWENS-ILLINOIS,
Toledo, Ohio May 24, 1971.

Re S. 643, S. 1255 and Other Bills Proposing Amendments to the Patent Laws.

Hon. JOHN L. MCCLELLAN,
Chairman of the Subcommittee on Patents, Trademarks, and Copyrights, of the Senate Committee on the Judiciary,
Senate Office Building
Washington, D.C.

DEAR SIR: Enclosed are three copies of an amended statement setting forth our Company's position on these very important Bills pending before your Subcommittee. This amended statement is intended to be substituted for the Statement forwarded with our letter dated May 21, 1971 to correct several minor errors.

We hope that this Statement will be of assistance to you in your deliberations and would appreciate your making it a part of the record.

Very truly yours,

E. J. HOLLER,
Director of Patents.

STATEMENT OF OWENS-ILLINOIS, INC. CONCERNING S. 643, S. 1255 AND OTHER BILLS PROPOSING AMENDMENTS TO THE PATENT LAWS BEING CONSIDERED BY THE SENATE SUBCOMMITTEE ON PATENTS, TRADEMARKS AND COPYRIGHTS

Owens-Illinois, Inc., as a manufacturer of articles covering a broad segment of our economy, from old line products such as glass and plastic containers, corrugated boxes, cups and laboratory ware to newer and more exotic products such as glass rods and discs for use in lasers, plasma display panels, and glazed package parts for use in microelectronics, has a substantial interest in a sound patent system. We are convinced that without the protection afforded by our patent system, we and other manufacturers would have little incentive for making substantial investments in research and development.

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[65] Harris & Siegel, Protection of Trade Secrets: Initial Report, 8 Idea 360 (1964); Harris & Siegel, Trade Secrets in the Context of Positive Competition, 10 Idea 297 (1966); Harris & Siegel, Patents and Trade Secrets: Instruments of Positive Competition, 12 Idea 631 (1968).

[66] Behrman, Licensing Abroad Under Patents, Trademarks and Know-How by United States Companies, 2 Idea 181 (1958); Behrman & Schmidt, Royalty Provisions in Foreign Licensing Contracts, 3 Idea 272 (1959); Behrman & Schmidt, New Data on Foreign Licensing, 3 Idea 357 (1959); Behrman, Foreign Licensing Investment and Economic Policy, 4 Idea 150 (1960).

Inasmuch as the proposed revisions to the patent laws are rather complicated and have been extensively critiqued in various publications, we will attempt to set forth our views briefly in only three key areas, namely:

1. Patent Office Fees.
2. Mandatory Patent Licensing.
3. The Scott Amendments.

We endorse a Patent Office issue fee which is established at a prescribed dollar amount. Under the law presently in effect, the issue fee is based in part upon the number of printed pages of the published patent, as well as the number and kind of claims which stand allowed. Inasmuch as the number of printed pages can only be approximated at the time the issue fee is paid, the resulting procedures have required, in many instances, the payment of excessive fees by the applicant or a refund by the Patent Office. This has caused needless paper work and much confusion resulting in considerable inefficiency in both the U.S. Patent Office and applicants' offices without any tangible benefits.

With regard to the subject of mandatory patent licensing, the Clean Air Act was passed by the 91st Congress as Public Law 91–604. It included Section 308 which provided for mandatory licensing of patents in the field of anti-pollution devices and methods. We are opposed to this provision because of its potential for stifling and retarding research and development in this very important area of environmental control. In the case of many inventions, it will be extremely difficult to determine whether the present law applies to the claimed subject matter. Moreover, it may result in some cases of inventors treating their inventions as trade secrets rather than seeking to obtain the benefits of the patent laws, and thus preclude their publication as issued patents. Senator McClellan's Patent Reform Bill S. 643 proposes, at Section 6, to delete the mandatory licensing Section 308 from the Clean Air Act. We favor Senator McClellan's proposal because we believe that such mandatory licensing provisions are not in the best public interest, and may well hinder instead of promote efforts to improve our environment.

Finally, we endorse the proposed amendments of the Patent Laws set forth in the so-called Scott Amendments, Amendment Nos. 23 and 24. At present, there is great confusion and uncertainty as to the legality of certain patent licensing practices under the Antitrust Laws as presently construed. Recently, this uncertainty has been compounded because of statements made by government officials indicating plans to attack certain licensing practices heretofore generally regarded as entirely lawful. The Scott Amendments will not, in our view, have any anti-competitive consequences; rather, they will provide a much needed statutory framework designed only to eliminate much of the uncertainty and anti-patent bias which presently abounds in this important area of the law.

Please make this statement a part of the record on this legislation.

THE NEW YORK PATENT LAW ASSOCIATION,
New York, N.Y., May 27, 1971.

HON. JOHN L. MCCLELLAN, *Chairman,*
Subcommittee on Patents, Trademarks, and Copyrights,
U.S. Senate,
Washington, D.C.

MY DEAR SENATOR MCCLELLAN: The Board of Governors of The New York Patent Law Association has carefully considered the Scott Amendments to S. 643 (Amendments 23 and 24), including the so-called "Tuesday Two" suggestions for modifications thereof, with the hope that it could be of some assistance to your committee in its consideration of the amendments. The Board has had the benefit of detailed reports from its committees on Antitrust and on Patent Law Revision, and of expressions of views from the membership at a formal meeting of the Association devoted to the proposed Scott amendments.

The Board continues its strong endorsement in principle of Scott Amendment 24, but recognizes the need for still further consideration of the specific language and provisions thereof. In general, the Board favored the Tuesday

Two version of Amendment 24, with one exception. The Board felt that the language proposed by the Tuesday Two group for insertion in § 261(b)(2) (line 6) of Amendment 24 was confusing and unnecessary, and should be deleted.

Regarding Scott Amendment 23, the Board is of the opinion that the original form of Section 301 of the bill is preferable to the version proposed by Senator Scott or the Tuesday Two modification. In reaching this conclusion, which is at some variance with its position communicated to you last year, the Board was moved by the recent decision of the Court of Appeals for the Second Circuit in *Painton* v. *Bourns* affirming the propriety of licensing trade secrets. To a considerable extent, the Board felt this decision rendered Amendment 23 unnecessary. Further, the Board views the very recently reported decision of the Court of Appeals of the Seventh Circuit in *Bailey* v. *Logan Square*, —— F2d——, 169 USPQ 322, as also tending to allay concern in this area. At the same time, concern was voiced that Amendment 23 might be considered by some to set aside clearly desirable aspects of the Supreme Court's decisions in *Sears* v. *Stiffle*, 376 US 225 (1964) and *Comco* v. *Day Brite*, 376 US 234 (1964). To the extent that this effect would encourage a multitude of state unfair competition laws, the Board felt such would be undesirable. On balance, the original language of § 301 seems preferable.

We hope these thoughts will assist the committee in its deliberations. We remain ready to be of further assistance in any way that we can.

Yours very truly,

ALFRED L. HAFFNER, JR.,
President.

PATENT OFFICE SOCIETY,
DEVOTED TO IMPROVEMENT OF THE PATENT SYSTEM,
Arlington, Va., April 30, 1971.

HON. JOHN L. MCCLELLAN, *Chairman,*
Subcommittee on Patents, Trademarks, and Copyrights,
Committee on the Judiciary,
U.S. Senate,
Washington, D.C.

DEAR CHAIRMAN MCCLELLAN: The Patent Office Society, an organization devoted to the improvement of the patent system and professional development of patent examiners, wishes to apprise you of the Society's consideration of the proposed general revision of the Patent Laws.

The Society supported adoption of S 2756, 91st Congress, but suggested constructive changes to improve the form thereof and a few constructive changes affecting the substance thereof. See attachment of Statement of Society Position on S 2756. The statement of the Society's position has appeared at pages 813–822 of Vol. 52, No. 12, December 1970 issue of Journal of the Patent Office Society.

The Society basically supports adoption of S 643, 92nd Congress, and has found that the statement of position taken on S 2756, 91st Congress, is also applicable to S 643, 92nd Congress.

We trust that this statement will be helpful to you in your deliberations and thank you for the opportunity to make this presentation.

Sincerely,

LOUIS J. PERLSTEIN, *President.*

Patent Office Society's position on S 2756, A Bill for the general Revision of the Patent Laws, title 35 of the United States Code, and for other purposes. The following are our proposed changes:

Section 3. Officers and employees

(a) There shall be in the Patent Office a Commissioner of Patents, one [first assistant] *Deputy* Commissioner [two other], four Assistant Commissioners, [and] not more than twenty-four Examiners-in-Chief, *and such supervisory personnel and Primary Examiners as may be necessary for the efficient operation of the Patent Office.* The Assistant Commissioners shall perform the duties pertaining to the Office of Commissioner assigned to them by the Commissioner. The [first assistant] Deputy Commissioner, or, in the event of a vacancy in that office, the Assistant Commissioner senior in date of appointment, shall fill the Office of Commissioner during a vacancy in that office until a Commissioner is appointed and takes office. The Commissioner of Patents, *the Deputy Commissioner*, and the Assistant Commissioners shall be appointed by the President, by and with the advice and consent of the Senate. The Secretary of Commerce, upon the nomination of the Commissioner in accordance with law, shall appoint all other officers and employees.

Section 7. Board of Appeals

(a) The Commissioner, *the Deputy Commissioner*, the Assistant Commissioners, and the Examiners-in-Chief shall constitute a Board of Appeals in the Patent Office . . .

Section 8. Library

The Commissioner shall maintain a *current* library of scientific and other works and periodicals, both foreign and domestic, in the Patent Office *and if desirable in other locations* to aid the officers [in the discharge of their duties] *of the Patent Office in establishing the state of arts and sciences and the general public in promoting the progress of science and the useful arts.*

Section 41. Patent fees

(c) The Commissioner may establish charges for copies of records, publications, or services furnished by the Patent Office, not specified above. *Fees received for new publications or services can be applied by the Commissioner to pay for the cost of said new publications or services, within a period not to exceed two years from the time of institution.*

Section 100. Definitions

When used in this title unless the context otherwise indicates—

(a) The term "invention" means invention or discovery.

(b) *The term "claimed invention" means the subject matter sought to be patented as defined by a claim.*

Subsections (b) through (g) relettered (c) through (h).

(e) The term "applicant means any person who owns an *interest in an* application for a patent, as provided in this title.

[(f)] (g) The term "actual filing date in the United States" includes the filing date to which an application or patent, or the subject matter of any claim thereof, may be entitled under the provisions of sections *119 and 120* of this title [and excludes any date under section 119 of this title]. An application or the resulting patent may contain separate claims for subject matter having different actual filing dates in the United States by virtue of the provisions of section 120 of this title or may contain claims entitled to the benefit of a prior date under the provisions of section 119 of this title, in addition to claims not so entitled.

[(g)] (h) The term "useful" shall include, but shall not be limited to, utility in agriculture, commerce, industry, or research.

(i) *The term "inventor" means the originator of the claimed invention.*

Section 101

Whoever invents or discovers any new and useful process, machine, manufacture, or compsition of matter, or any new and useful improvement thereof, or his successor in title, may obtain a patent therefor, subject to the conditions and requirements of this title. *For each invention there shall issue only one patent.*

Section 102. Conditions for patentability; novelty and loss of right to patent

An applicant shall be entitled to a patent on the *claimed* invention [defined in each claim of his application] upon establishing by a preponderance of proof that the *claimed* invention meets the conditions for patentability. A patent may not be obtained if:

(a) The applicant or any of his predecessors in title has abandoned the *claimed* invention; or

(b) The *claimed* invention was first patented or caused to be patented by the inventor or his legal representative or assign, or his predecessors in title, in a foreign country before the actual filing date in the United States of his application, on an application in such foreign country filed more than twelve months before such actual filing date in the United States, or described prior to such actual filing date in the official publication of such foreign application in the country where filed; or

(c) The inventor did not himself invent the [subject matter sought to be patented] *claimed invention*, but derived it from another; or

(d) The *claimed* invention is identically disclosed or described in any of the following prior art:

(1) A patent or publication in this or a foreign country reasonably available to the public of the United States in printed or other tangible form before the *claimed* invention was made by the inventor, or more than one year before the actual filing date in the United States of the application; or

(2) A published United States patent application or United States patent of another which has an actual filing date in the United States before the *claimed* invention was made by the inventor named in the application; or

(3) Subject matter made known to persons in the art to which it pertains, or used by others, in this country before the *claimed* invention was made by the inventor named in the application; or

(5) An invention made in this country by another before the *claimed* invention was made by the inventor, provided the other had not abandoned his invention. In determining priority, there shall be considered not only the respective dates of conception and reduction to practice of the *claimed* invention, but also the reasonable diligence of one who was first to conceive and last to reduce to practice, from a time before conception by the other until his own reduction to practice. One year of inactivity, *prior to filing an application*, with respect to the *claimed* invention shall prima facie constitute abandonment. *Between two or more applications, that application which has an actual filing date greater than one year with respect to the others shall be awarded priority.*

Section 103

A patent may not be obtained though the *claimed* invention is not identically disclosed or described in the prior art as set forth in section 102 of this title, if the differences between the *claimed invention* [subject matter sought to be patented] and such prior art are such that the *claimed invention* [subject matter] as a whole *would have been* [was] obvious from such prior art to a person having ordinary skill in the art to which said *claimed invention* [subject matter] pertains. Patentability shall not be negatived by the manner in which the invention was made, nor because the invention has simplicity or is the last step in an evolutionary development, nor because it is not revolutionary, basic, scientific or technical in character. Claims for a new combination or assemblage of known mechanical or other elements shall be subjected to the same standard of patentability as is applied to claims for other types of subject matter.

Section 104

In proceedings in the Patent Office and in the Courts, an applicant for a patent, or a patentee, may not establish [a date of invention] *when the invention was made* by reference to knowledge or use thereof, or other activity with respect thereto, in a foreign country, except as provided in Section 119 of this title. Where an invention was made by a person, civil or military, while domiciled in the United States and serving in a foreign country in connection with operations by or on behalf of the United States, he shall be entitled to the same rights of priority with respect to such invention as if the same had been made in the United States.

Section 111

(c) For purposes of filing a patent application and securing a filing date, an application may be signed by an agent of the applicant provided that the agent is authorized *to do so* or provided that the application is ratified by the signature of the applicant within [six months after filing] *such period of time as set by the Commissioner*. Failure of the applicant to ratify such application within [six months] *such period of time as set by the Commissioner* after the filing of the application shall result in abandonment of the application.

Section 112

(b) The specification shall conclude with one or more claims particularly pointing out and distinctly claiming the subject matter *sought to be patented* [regarded as the invention]. A claim may be written independent or dependent form, and if in dependent form, it shall be construed to include all the limitations of the claim incorporated by reference into the dependent claim *and shall limit and not enlarge or broaden the scope of the parent claim. The number of claims presented must not be unduly multiplied so as to confuse the claimed invention(s) or to unduly burden the examination process.*

(e) For the dissemination of information and other purposes, the Commissioner, in accordance with such regulations as he establishes, may require a brief abstract of all or part of the application. The abstract shall not be used for interpreting the scope of any claims of a patent, nor shall it affect in any way the validity of the patent.

(f) *Allegations of obviousness to overcome an incomplete disclosure may be required to be supported by evidence as defined under Section 102d(1) of this title.*

(g) *If a combination of elements is claimed, wherein one or more elements thereof may be new or improved, but where the coaction betwen elements is substantially the same as in the prior art, the applicant may be required to limit the claimed invention to the new or improved element(s).*

Section 119

(a) An application for patent for [an] *a claimed* invention filed in this country by any person who has, or whose predecessor or successor in title has previously regularly filed an application for a patent for the same *claimed* invention in a foreign country which affords similar privileges in the case of applications filed in the United States or to citizens of the United States, shall have the same effect as the same application would have if filed in the United States on the date on which the application for patent for the same *claimed* invention was first filed in any such foreign country, if the application in this country is filed within twelve months from the earliest date on which such foreign application was filed.

Section 120(a)(3)

The applicant specifically claims the benefit of the date of filing of the prior application for the *claimed invention* [subject matter claimed] in the second application.

(c) An applicant must claim the benefit of the filing date of the earliest application on which he intends to rely in a later filed application within three months of the time of filing such later application, or during examination or reexamination of such application as provided in chapter 12 of this title upon an adequate showing why the claim was not made earlier. In a series, each application must claim the benefit of the immediately preceding application in accordance with the provisions herein. *Where applicant avails himself of the benefits of this section he must clearly and particularly point out wherein the earlier filed application(s) provide(s) support for the common subject matter upon which he relies in his new specification and claims.*

Section 124

Neither inadvertent failure nor mistake in judgment of a non-criminal nature in trying to comply with the provisions of any section of this title shall constitute grounds for holding a patent invalid or unenforceable. or subject the patentee to a charge of misuse or fraud.

Section 131

(c) The Commissioner may require applicants, within such time *and in such* format as he may prescribe by regulation, to submit copies of or cite [any] *a reasonable number of* relevant patents, publications and other prior art which the applicant has specifically considered *most pertinent* in preparing his application for patent. [, together with an explanation as to why the claims in such application are patentable over such prior art, or, if no specific relevant prior art was considered, a statement to that effect and an explanation as to why the claims in such application are believed to be patentable. An inadvertent failure to comply with the provisions of this section shall not constitute a grounds for holding a patent invalid or unenforceable, or subject the patentee to a charge of misuse.]

(d) [The granting of a patent shall not be refused solely on the ground that if it occurred there would then exist more than one patent for the same invention where the patents will expire on the same date as a result of filing on the same date or as the result of a terminal disclaimer pursuant to section 253 of this title so long as the right to sue for infringement of said patents is in the same legal entity.]

Another application for an invention other than a divisional application under section 121 of this title must satisfy the provisions of sections 102 and 103 of this title and such provisions may not be mitigated by the filing of a terminal disclaimer under section 253 of this title.

Section 132

Whenever, on examination, any claim of an application is rejected, *and/*or any objection *made, and/*or requirement made, the Commissioner shall notify the applicant thereof, stating the reasons therefor, together with such information and references as may be useful in judging the propriety *of any rejection, and/or any objection, and/or requirement made* [of continuing the prosecution of the application]; and if after receiving such notice, the applicant requests reexamination, with or without amendment, the *Commissioner shall cause a reexamination of such rejection, and/or objection, and/or requirement made* [application shall be reexamined]. No amendment shall introduce new matter into the disclosure of the invention.

Section 134

An applicant for a patent [, any of whose claims has been finally or twice rejected,] may appeal from the *final* decision of the Primary Examiner to the Board of Appeals, having once paid the fee for such appeal. *The Board of Appeals shall act as an appellate review on the merits of the final determination set forth by the Primary Examiner.*

Section 155

An applicant for patent may, after seeking review under section 141 or 145 of this title, request the issuance of a patent for claims standing allowed in the application *if such request is made within the time limit set by the Commissioner.* Upon payment of the prescribed fee, issuance of such patent shall occur in accordance with this chapter. As to claims which stand allowed, the patent shall have the force and effect specified in section 154 of this chapter. Each claim in the application not standing allowed shall be identified as such, and shall not have any force and effect, except as provided in section 257 of this title.

Section 161

(a) Whoever invents or discovers and asexually reproduces any distinct and new variety of plant including cultivated sports, mutants, hybrids, and newly found seedlings, [other than a tuber propagated plant or a plant found in an uncultivated state,] may obtain a patent therefor, subject to the conditions and requirements of this title.

Section 172

The right of priority provided for by section 119 of this title and the time specified in section 102[(d)](*b*) of this title shall be six months in the case of designs. Applications for design registrations and such registrations in foreign countries shall have the same effect as applications for design patents and design patents for the purpose of section 102 [(d)](*b*) and 119 of this title.

Section 193

(a) Whenever there are two *or more* applications naming different inventors claiming the same or substantially the same subject matter, *or an obvious variant thereof* a patent shall be issued on the application having the earliest actual filing date in the United States, if otherwise allowable. The application having the later filing date in the United States with respect to such subject matter shall be rejected on the basis of such patent. Whenever the applicant for such application, found otherwise allowable, makes a prima facie showing of priority of invention with respect to the actual filing date in the United States of such patent in accordance with section 102(d)(5) of this title, and offers to present evidence in support of such showing, within one year after the issuance of the patent or within three months after a rejection of claims in his application on the basis of the invention claimed in the patent, the matter of priority of invention shall be determined by the Board of Appeals in such proceedings as the Commissioner shall establish. The Commissioner upon the institution of procedings under this section, shall issue a patent at the request of such applicant if his application is otherwise allowable. Failure of that applicant to proceed hereunder within the time specified shall preclude such applicant from asserting priority of his invention with respect to the invention claimed in the patent for the purpose of obtaining a patent.

(c) If two applications for the same or substantially the same subject matter *or an obvious variant thereof* have the same actual filing date in the United States, the Commissioner may initiate a priority contest under this section on his own motion whether or not one of the applications may have been issued as a patent. The Commissioner shall, upon the institution of proceedings under this subsection and at the request of either applicant, issue a patent on his otherwise allowable application.

(d) A claim for the same or substantially the same subject matter *or an obvious variant thereof* as a claim of an issued patent may not be made in any application unless such claim is made prior to one year after the date on which the patent was granted.

Section 282(b)

(2) Invalidity of the patent or any claim in suit on any ground specified in part II of this title as a condition for patentability [:], [Provided, however, That the validity of a patent may not be questioned solely because of the existence of two or more patents where said patents will expire on the same date as a result of filing on the same date or as a result of a terminal disclaimer pursuant to section 253 of this title so long as the right to sue for infringement of said patents is maintained in the same legal entity,]

Section 302

Nothing in this title shall preempt, annul or limit the right at common law or in equity of experimental use in research.

Final draft as adopted by the P.O.S. Executive Committee on May 14, 1970.

ROHM AND HAAS CO.,
Philadelphia, Pa., May 24, 1971.

Hon. JOHN L. MCCLELLAN, *Chairman,*
Subcommittee on Patents, Trademarks, and Copyrights,
Committee on the Judiciary,
U.S. Senate,
Washington, D.C.

DEAR MR. CHAIRMAN: I am informed that June 1 is the deadline for submitting comments on amendments 23 and 24 to S.643, introduced by Senator Hugh Scott. I would imagine that the views of those favoring the so-called "Scott Amendments" must follow a similar pattern. This is logical since we share a common concern and sense of urgency on a specific problem confronting American business—the future of technological innovation as a component of American business.

I understand that there are those who deny that patents are designed to stimulate investments or even that there is any real relationship between patents and the development of technology. I do not know the amount of experience such people have had in the development of technology, but I would expect it to be minimal at best. Based on my own 28 years of personal experience in an industry highly concerned with the development of technology, I can attest that there is indeed a direct relationship between patents and the development of technology.

Corporate research costs large sums of money. Research must compete with other opportunities for investment in obtaining its allotment of corporate funds. If capital earns more profits if deposited in a bank or invested in a building or machine than in research, a corporation cannot justify employing a research staff and continuing to invest in research. The inflationary pressures seemingly irrevocably built into our present American society require corporations to watch, and justify, all expenditures as seldom before.

Patents afford a means of recovering research and development costs and of earning a profit on the investment represented by such costs. If there were no patents, competitors would be free to copy any successful development commercialized by an innovating company with no investment of its own in research facilities or research personnel, with no costs for unsuccessful research projects that must be charged off, with no investment in development projects which failed. As duPont's experience with Corfam shows, these costs can be significant. Competitors without these cost factors to take into account would be able to either undersell the innovator in the market place or to earn a substantially higher profit if the price level stayed at the same point.

Under these circumstances no corporation limited to the United States market could efford to invest in innovative research. International companies having significant sales in countries with patent systems could continue with innovative research, justifying such investment on profits in these patent-conscious countries. Moreover, there would, over the long term, be a tendency for new investments in research facilities to be made primarily in such countries rather than in the United States.

This does not mean that research, even corporate research, would stop in the United States. Customer service work and process improvement work would continue at the corporate level, but innovative research would have to be sponsored by organizations not responsive to the profit motive such as the government or the university—and even universities now have much of their research tied to the existence of a viable American patent system (for example, the invention of vitamin D, Warfarin and stannons fluoride toothpaste).

Experience has shown that compared to corporate research government research is highly unproductive in terms of products and processes actually used in commerce to produce better and/or cheaper products for people to use. Another drawback of looking to the government as the sole source for funding research is the tremendous concentration of power given to the government to direct research and consequently the future of the American economy. Further, since the general policy of the U.S. government (unlike that of foreign governments) is to make the results of unclassified research available to all without charge, foreign competitors would benefit from such research equally with the American firms. Under a patent system only those using the patented product or process and thus benefitting from the discovery pay for the research. Under a system of government-sponsored research, the cost is shafted to the general taxpayer. With the growth of industrialization throughout the world and the lowering of tariff barriers, American industry must compete in every area with countries having substantially lower labor costs. The only way by which American industry can continue to pay such higher wages is through improved technology which, in turn, requires a continuing investment in research.

The patent statutes are founded on a constitutional provision. Under the American system of Government the Constitution is the basic law of the land. The anti-trust laws trace their origin to an act of Congress in the latter part of the 19th century. Yet many present day theorists, and I emphasize "theorists" because these men for the most part are that, have raised their personal interpretations of the anti-trust laws to be superior to the Constitution as the supreme law of the land. The grant of a patent monopoly takes nothing away from the public, for the monopoly granted by the patent is in a product or process which, by definition, was not pre-existing but rather was itself created by the patentee. Not only is the monopoly limited to what was created by the patentee, but it is limited in time and after that time it may be freely enjoyed by the entire public. Further, even during this limited time the subject matter of the monopoly is disclosed to the public and may be used by the public as a spring-board for further innovations and improvements. Indeed, this is often the case.

This remarkably simple device has played an important part in the increasing rate of technological progress in this country. The problems now facing our society such as increasing population, pollution, competition from low cost foreign industry, require the best efforts of our society to surmount these problems. A strong and viable patent system will encourage industry to make the investment needed to come up with the innovations which are desperately needed by our country and the world.

The Scott amendments will not change the law, but rather would merely codify earlier judicial decisions interpreting the patent laws in the present context of the anti-trust laws. The main effect of such codification would be to stop the process of judicial erosion of the patent law caused by new internpretations of the anti-trust laws. Such erosion in effect constitutes judicial legislation. The power of literally hundreds of federal judges to take such action and today hold illegal what the courts in the past had held to be legal introduces a vast area of uncertainty into the entire field of patent rights. So anti-patent have some courts become that on the one hand, a Justice of the Supreme Court was moved to say that the only valid patents are those which the Supreme Court could not get its hands on and, on the other, a litigant in the 8th Circuit recently was prompted to petition for a trial in another circuit on the ground that he could not get a fair trial in that circuit as shown by their actions in holding invalid every patent litigated in that circuit over a number of years. Failure to enact the Scott amendments would amount to Congress forfeiting to the courts the power to modify and thus recodify the patent laws in a piecemeal fashion. It is submitted that the due deliberations of the Congress are a far better means to write the law than a process which substitutes decisions of individual judges based upon relatively limited factual situations that cannot take into consideration the overall problems of the nation's economy and technology that may be affected by such decisions.

The uncertainty regarding the rights of patentees is undoubtedly one factor leading to the present lack of growth in corporate investment in research. The McGraw-Hill economics department survey shows that in 1971 the chemical industry will spend only 2% more than in 1970 on research and development, an increase not even sufficient to offset the effects of inflation; and in 1970, the chemical industry spent less on research and development than in 1969.

I urge this committee to act favorably on the Scott amendments to help create the degree of certainty in the licensing of patent rights which is needed to spur increased investment in innovative research.

Sincerely,

D. W. Kenny,
Vice-President.

Quarles, Herriott, Clemons, Teschner & Noelke,
Milwaukee, Wis., May 27, 1971.

Re Scott Amendments, Nos. 23 and 24, for Patent Revision Bill, S. 643.

Senator John L. McClellan, *Chairman,*
Senate Subcommitee on Patents, Trademarks, and Copyrights,
Senate Office Building,
Washington, D.C.

Dear Senator McClellan: This letter responds to certain testimony given in the May 1971 hearings on the "Scott Amendments" that was critical of these proposals. The testimony questioned the need for the amendments, and implied that provisions of the proposed amendments may raise objectionable uncertainties. The writer believes that there has been a demonstrated need, and that the proposed amendments would serve a very useful purpose for the general good. It is respectfully asked that this letter be made of record. Copies of the letter, and of the accompanying reprint are being sent to Senators Burdick, Fong, Hart and Scott.

I. A NEED EXISTS

Our law has struck a fair balance between a patent owner's legitimate rights under his patent grant and abuses condemned by the rule of patent misuse and the antitrust laws. There is a general harmony in which the antitrust laws prohibit extension of a patent grant over control of things *outside* the claims of a patent, while the patent owner retains control over things *within* the scope of his patent claims. There are strong movements afoot, however, to upset this balance, and there is a resulting clear and present need for statutory enactment which will retain the harmony we have achieved. The harmony is compatible with the Constitutional plan of the inventor having exclusive domain and control over his invention, but not receiving rights that enable him to use his patent as leverage to obtain control of things outside his patent grant. At present, the antitrust law does not invade the nucleus of the patent grant, i.e. control over the patented invention. The large majority of those persons who are knowledgeable in patent matters, by virtue of working with inventors and patent owners on a day to day basis, believe that we have a harmony which is both inducing innovation through the patent system, thus enhancing competition by virtue of developing different but competing goods, and encouraging the sharing of inventions through the granting of licenses. Such opinion of experts constitutes compelling data for implementing the Scott proposals, which will stabilize the law.

The movements afoot to unduly restrict the patent owner, to less than his exclusive dominion over his invention, can be summarized as follows:

1. The Assistant Attorney General has, in a public address, stated that the Department of Justice will consider attacking a license provision if it believes the provision is not necessary, and if there might have been a less restrictive alternative covenant betwen a licensor and his licensee. This is a handsight test which can make any license agreement, no matter how carefully written to adhere to antitrust and patent misuse rules, vulnerable to very expensive and time consuming litigation. In no other area of law, is there a rule that one must only bargain for the least restrictive covenants. This is absurd on its face, but the contention is an actual reality in the area of patent licensing.

It is a test that would drive many patent owners away from sharing their inventions through the route of licenses, and in the last analysis this would be detrimental to the public good. Furthermore, this test is a complete disregard of the fundamental nature of patent rights, in which the inventor has exclusive dominion over his invention. The statement of the Assistant Attorney General has been reiterated, and consequently there is a present danger to make inroads which are unnecessary and undesirable. Officials of government are threatening unwarranted litigation, the expense of which will be injurious to individuals forced to defend against such assertions.

A threat by the administrative arm of government, such as we have here, produces an *in terrorem* body of quasi-law, wherein patent owners refrain from exercising their full rights because of fear of stated government positions which are not actual law.

2. Members of the Department of Justice have made statements that attack field of use licenses. For example, the Assistant Attorney General stated in a June 5, 1969 speech that in due course they expect to bring a case directly challenging such type of restriction. This statement has been reiterated by the Director of Policy and Planning for the Antitrust Division, who said that it is unlikely that field of use licenses could be justified, and that there should be a burden upon the patent owner of proving absolute economic necessity. He also predicted that the leading case on field of use licenses, *General Talking Pictures* v. *Western Electric*, 304 U.S. 175 (1938) may fall. These men fail to consider the alternative that will occur from eliminating this type of license, which would be a refusal of patentees to grant licenses, wherefore introduction of new inventions would be lessened.

A problem here, is that there is not a fully developed body of law on the subject of field of use licenses, very probably for the reason that all persons have heretofore deemed them to be viable licensing tools well within the nucleus of the patent grant, without any question of antitrust or patent misuse consequences. Many persons have found in actual experience that field of use licenses are one of the best methods available for patentees sharing the practice of their invention with others, for it is a method of licensing in which the patentee can protect himself from competition in his *own* invention, for which he holds exclusive rights for a limited period of time. A field of use license is nothing more than a patentee's exercise of dominion over a lesser part of the larger right to exclude altogether, and therefore antitrust concepts, as applied by present members of the Department of Justice, are an improper invasion *into* the subject matter of the patent.

With respect to field of use licenses the government has already instituted attacks on this type of licensing practice in some of its drug cases. These cases do not involve a broad frontal attack upon field of use licenses, but if successful they would be the first step towards a broader attack at a later date. Thus the law is not stable, but it should be made so.

3. It has become increasingly difficult in the last few years to negotiate licenses where several patents exist as a group relating to a specific item of technology. Some courts have held that when there are several patents involved the royalty rate must decrease as patents expire, regardless of whether the parties even considered such a matter. *American Securit* v. *Shatterproof Glass*, 268 F.2d 769 (3rd Cir. 1959); *Rocform* v. *Acitelli Standard*, 367 F.2d 678 (6th Cir. 1966). Some other cases hold that a licensor must have coerced the licensee into adopting a set royalty rate for a plurality of patents. *McCullough Tool* v. *Well Surveys*, 343 F.2d 381 (10th Cir. 1965); *Well Surveys* v. *Perfo-Log*, 396 F.2d 15 (10th Cir. 1958).

A complementary problem is where a licensee tries to split up a licensor's group of patents relating to an item of technology, and demands unrealistically low royalty rates for only one or two of a group of patents, on the theory that licensing less than all the patents must necessarily require a lower royalty rate. Cases that support such an approach include *Hazeltine Research* v. *Zenith Radio Corp.*, 156 USPQ 229 (7th Cir. 1967). However, in the actual market place a product can only stand a royalty rate within a very narrow range regardless of how many patents cover it. Thus a possibility developing rule that royalty rates must always vary with the number of patents is unrealistic, and quite unworkable.

4. It is now illegal to make payments for a patent license after the patent expires, even if such payments were based on activities under the patent during its life. *Brulotte* v. *Thys*, 379 U.S. 29 (1964). Such rule overlooks the fact that the parties may wish to spread out a period of payment for activities under the patent, similarly as in the common cases of loans and security transactions such as mortgages. The time period for payment should be extendable if the parties desire, so long as the payments are for activities under the patent during the life of the patent.

We have a corollary problem here that some persons have hinted that a rule may develop denying the right to receive royalties during the time period before the patent issues. This could greatly jeopardize the exchange of technical information in this country, upon which we are becoming dependent for our general economic good, and a clarification should be made at this time.

5. The law with regard to grant backs of improvements is becoming unsettled. Some statements of administrative officials indicate that all types of grant backs, even simple licenses of a non-exclusive nature, may be subject to attack. Since the matter of grant backs is very important in many licensing negotiations, there should be some stabilization of the law at this time.

6. The right of an individual inventor to grant exclusive licenses without the right to sub-license has been under attack from the government. Inventors, for their own necessary security interests, carefully select the parties to whom they grant exclusive licenses. Inventors have little control over the efforts an exclusive licensee may put forth in commercializing an invention. If the right to grant sub-licenses is included, then the inventor loses one of his paramount rights he has today. We need stabilization in this area.

7. We now have some judicial decisions on the books in which the amount of a royalty has become the subject of inquiry. The effects of *American Photocopy Equipment Co.* v. *Rovico*, 359 F.2d 745 (7th Cir. 1966) although tempered at 257 F. Supp. 192 (D.C. Ill. 1966), which was affirmed at 384 F.2d 819 (7th Cir. 1967), still lingers with us, and we can be sure that there will be attempts to relitigate this issue. Again, stabilization is required.

8. We also have a White House Task Force Report which states that all licensees should be licensed at equal royalty rates. This is unrealistic, for patent owners cannot set prices in the same manner as manufacturers set prices for their goods. The economic leverage of licensees, and the greatly different situations in which different licensees reside make this totally impractical. Again, stabilization is required.

9. We have also had statements in the White House Task Force Report that once a patent owner grants one license he should be required to license all other parties that apply for a license. This thought has been echoed in *Allied Research* v. *Heatbath*, 300 F.Supp. 656 (N. D. Ill. 1969). Such a rule

would be sheer catastrophe for licensing programs, and we should have a statute prohibiting the development of such a *per se* rule.

10. The rule of *Lear* v. *Adkins*, 395 U.S. 653 (1968) if not tempered, leaves licensees in an overly strong position. They can challenge patents under which they are licensed without giving up their license rights. They can bargain for a right, then challenge the situation, and if they lose they are not jeopardized. Imagine leasees of real estate or of chattels being able to have such an advantageous position! A patent owner can be put to expensive litigation only to receive royalties for which he had already bargained in good faith. Such unfairness should not continue. At the very least, a licensee should be required to renounce his license before attacking patent validity.

11. We have in the concurring opinion in *Lear* v. *Adkins*, and in some language in *Sears* v. *Compco*, strong judicial statements that if an item cannot be patented state laws cannot protect it. In a case of technical information, such information could not be disclosed for a fee, and in the matter of the dress of goods the *public* is denied protection from confusion which may exist from unfair copying of mere ornamental appearance. Some tempering of these judicial statements is required at this time by statutory enactment.

The foregoing points establish that there is an impending, but unnecessary flux in the law, so that without question a need for the Scott amendments exists at this time.

Invention is an economic asset that can be increased in quantity in a quite different fashion than our other economic assets of land, natural resources, labor productivity, and management skills, all of which are quite limited in quantity. Congress should act to define and stabilize a core of rights for patent owners, in the exercise of sharing their Constitutional dominion over their inventions, so that we will encourage innovation. We need to bring innovation to bear upon our many social problems. Stabilizing the law, without making any substantial change, will be in our interest.

Stabilization, or the maintenance of a harmony between patent and antitrust laws, cannot be accomplished on a case by case basis. Courts necessarily fail to consider the patent system as a whole, for they only see limited facts which are of record before them. Courts do not have access to general facts, or experience, or expertise in the matter of judging the patent system as a whole. This is in the province of Congress, and Congress should act.

Another need for the enactment of the Scott amendments, is to fix some basic ground rules for that large majority of persons dealing with patents who cannot, for practical reasons of limitations upon one's time, follow intricate, erudite distinctions the law may develop in the field of patent licensing. Most licenses are negotiated and drafted by inventors, businessmen, and counsel who are quite unaware of fine line distinctions of recent decisions, because they are not in a position to continually maintain vigilance over an ever shifting body of law. It may be an intellectual stimulation to professors and students of this field of law to have a case by case approach which maintains their continued interest in the field. But, the law of licensing is not some form of mental stimulation for those who invest in and license inventions. We have here an important part of the market place which should have some fixed, basic rules. Stabilization is what our business community needs, and because of an apparent accelerating state of flux in the law, this is an opportune time to adopt the Scott amendments.

Our society is dependent upon innovation for jobs. for both the professional and working man, business growth, combating problems of ecology and overpopulation, and very importantly survival from domination by foreign competition. Some statutory definitions of the basic rights on licensing will serve our goals, better than an undefined drifting of case by case litigation, which does not consider or serve the system as a whole.

II. THE PROPOSED AMENDMENTS WILL STABILIZE THE LAW AND NOT INTRODUCE UNCERTAINTY

Some of the testimony at the hearings attempted to discredit the language of the Scott amendments. The writer wishes, at this point, to review the proposed language to indicate how unfounded are these objections.

1. The Scott amendment No. 24 inserts §261(b)(2) to define some basic rights of a licensor. This new section states that an applicant, patentee, or

his legal representative may license. This makes it clear that one owning a patent application can negotiate licenses, and this is certainly socially necessary. There has been some thought that the right of an applicant should not extend to the negotiation of a license and the receipt of royalties until his patent issues. This would be a social monstrosity, and it is desirable to have the issue clarified by statute.

Next, this new sub-section states that the whole or any part of the patent rights may be licensed, and this is intended to authorize field of use licenses. A field of use license is nothing more than a patentee granting part of his rights, similarly as a landlord grants a lease to a part of a premises. In other fields of law it is an entirely acceptable practice to grant less than the whole, and it should be just as acceptable with patents.

Next, this new sub-section states that a patent may be licensed for the whole or any part of the United States. This falls in line with the provision from time memorial that assignments can be for a whole or any part of the United States.

Next, the new sub-section provides that exclusive or non-exclusive arrangements may be made, and this of course is inserted because of the White House Report and statements of government officials that they will seek to require patentees to license everyone once they have grantd a first license. Again, it would be an economic disaster to patent owners attempting to share their invention if anyone could practice the invention. We should have a statutory enactment to clarify the situation.

One should recognize that in judging patent licensing, that the matter of competition is to be judged between the invention, which previously did not exist, with other items, and competition in the invention itself is really within the province of the patent owner, for it is a part of his exclusive right of control. Therefore, it should be stated clearly that a patent owner can enter exclusive or non-exclusive arrangements with parties of his selection.

2. The next section of Scott amendment No. 24 treats the rule of *Lear* v. *Adkins*. A reading of this § 261(e) and 261(f) makes it clear that all that is being done is to introduce a fairness, under which a licensee or assignor attacking the validity of a patent for which he has negotiated a contract should renounce the contract or restore consideration he received for the patent which he now denies. An attack on a patent, and the simultaneous holding of rights under the patent are totally incompatible. The basic rule of *Lear* v. *Adkins* remains under the Scott amendments, but we temper the results to achieve fundamental fairness.

3. The next portion of the Scott amendment No. 24 is § 271(f). It deals with the rule of reason. Our law over the years, as developed by the courts, has been based upon a rule of reason with respect to restrictions a patentee may impose on matters ancillary to the patent grant. Under this rule of reason tie-in arrangements and price fixing have been deemed illegal, and this is well settled. There is no change at all in such rules of law under the rule or reason provision of the Scott amendments. The Scott amendments are retaining the underlying doctrine, and what they do is to prohibit the development of rules of *per se* illegality which may otherwise develop.

The critics of the Scott amendments are totally unfounded in their assertions that this provision may create uncertainty. Quite to the contrary, it preserves the law and allows a continued case by case development in those areas where case by case development will be of advantage. The law can continue to grow and to remain viable to meet changing conditions. This is what the critics want, and this is what they have under this section.

4. The next provision of the Scott amendment No. 25 is § 271(g). It itemizes some rights of the patent owner in the form of consideration he may receive in return for a license grant. None of the items stated herein become *per se* legal under all circumstances. The total conduct of agreements of which a patent is a part may produce an antitrust violation, just as under existing law. What the Scott amendment does is to point out that the enumerated considerations are not *per se* illegal, and that their mere existence does not create illegality. This is quite different from the saying that they are *per se* legal at all times. The criticism that has been levelled at this language is clearly unjustified.

Scott amendment No. 23 introduces a § 301. This deals with the preservation of unfair competition law which has served us so well for a countless number of years. It also allows for the continued licensing of technical information. There can be no objection to such a provision.

Enclosed with this letter is a reprint of an article on the general subject covered by the Scott amendments. Parts of the article are marked for rapid, and easy reading. A scanning of the article will be appreciated, for it illustrates the need, and desirableness, of enactments such as the Scott amendments.

Yours very truly,

ARTHUR H. SEIDEL.

LAW SCHOOL OF HARVARD UNIVERSITY,
Cambridge, Mass., May 13, 1971.

THOMAS C. BRENNAN, *Esq., Chief Counsel,*
Senate Subcommittee on Patents, Trademarks, and Copyrights,
Washington, D.C.

DEAR MR. BRENNAN: Pursuant to Chairman McClellan's request to select excerpts from my article and Profesor Baxter's article for inclusion in the record, I have eliminated all except the discussions dealing with patent licensing restrictions. What is left is not brief, but any truncation would eliminate important parts of the analysis.

I am enclosing herewith the parts for inclusion in the record.

Sincerely yours,

DONALD F. TURNER.

THE PATENT SYSTEM AND COMPETITIVE POLICY*

(By Donald F. Turner)**

Since patents are legal monopolies, they have often been considered in conflict with antitrust principles. Analyzing the basic rationales of patent and antitrust law, Professor Turner argues that competition could be furthered by a broader application of antitrust law to cases involving patents, without significantly lessening the incentive for invention which patent law provides. While not challenging the patent system itself, Professor Turner discusses areas in which a patentee's rights might be subjected to antitrust limitations without impinging upon the patentee's legitimate interests.

My ultimate purpose will be to discuss the antitrust limitations that should be imposed on the sale and licensing of patents. The solution of these issues has typically been viewed as a problem of resolving conflicts between antitrust principles and the basic purposes of the patent system. For reasons that I shall later set forth, I believe this to be a largely inaccurate characterization, and one that has contributed heavily to the confusion and questionable legal precedents that have studded this field.

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As mentioned at the outset, I believe it to be largely inaccurate and misleading to view the application of antitrust law to patentees as a problem of resolving conflicts between antitrust principles and the main purpose of the patent system. The main purpose of the patent system is to enlarge the flow of inventive and innovative activity by enlarging the potential rewards. Thus, antitrust law would conflict with this purpose only if the limitations which it imposed on the exploitation of patents so reduced the potential rewards as to have adverse effects on decisions to carry on inventive activity. But it does not necessarily follow that minor or even substantial reductions in the value of the rewards flowing from existing patents in some circumstances would have any significant effect on the investment decisions of those contemplating further inventive activity. To the contrary, a close relationship seems highly unlikely.

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* Adapted from the Crews Lecture delivered at New York University School of Law on December 4, 1968. Professor Turner has agreed to include this article in the Symposium in honor of Professor Derenberg.

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Briefly put, the reasons are these. A corporation or individual contemplating whether or not to put money and effort into a particular research project can make only the grossest calculation of whether the prospective rewards are likely to exced ethe costs. At the outset, when the decision whether or not to invest in inventive activity is made, there is usually great uncertainty as to what the nature of the inventive output will be. Consequently, one can rarely, if ever, calculate with any degree of precision the ultimate commercial value that will be gained. To the extent that the patent system enhances the ultimate potential reward for any invention, its major contribution is simply that the patent confers a monopoly—the right to exclude all others from making, using, or selling the subject matter of the invention. Given the fact that the patentee can exclude all others, can extract returns by licensing for royalties, or can sell the patent to someone else, it seems virtually certain that some limits on the buyers to whom a patentee may sell, or prohibitions on price fixing or other restrictions on licensees, would be of far too marginal importance to have any significant effect on decisions whether or not to invest in research.

Even if the opportunities foreclosed by antitrust law were of more than marginal value, there is still reason to doubt that a substantial reduction in potential rewards would have a comparable adverse effect on inventive activity. Inventive activity resembles a lottery in that among the possibilities are some extremely high payoffs. It is doubtful that anyone who would be induced to invest in research in hopes of a thousand-to-one payoff would be deterred if the potential payoff were reduced to eight hundred-to-one. Again, more generally, the uncertainties are too great to believe that people will even try to make the kind of close calculation that would be materially affected by relatively moderate, though substantial, changes in the value of the patent reward.

I do not suggest that the effect on the patent reward should be totally disregarded in formulating antitrust rules. One can conceive of extreme antitrust interpretations that might materially cut across the main purpose of the patent system. However, none of the antitrust rules that I shall suggest would appear to me to raise any real problem on this score.

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B. *Restriction in Patent Licenses* [11]

I turn now to the application of antitrust law to such patent licensing practices as price fixing, territorial restrictions, and field-of-use limitations. For reasons set forth earlier, it seems clear to me that the right to impose anticompetitive restrictions in the licensing of patents makes far too marginal a contribution to the value of the patent reward to have any practical effect on the flow of inventive and innovative activity. That being so, application of straight antitrust principles raises questions only because prohibition on the the use of a particular restriction may lead patentees in some cases not to license at all or to license less widely. If patentees would make the same licensing decisions whether or not they were entitled to impose a minimum price limitation on licensees, then prohibition of the restriction would be a no-loss, clear-gain solution.[12]

But if the application of ordinary antitrust rules to restrictions in patent licenses would tend to reduce licensing, such a possibility must be taken into account, because reduction of licensing may have the following adverse effects: (1) lower utilization of a patent, either in quantity of goods produced or in variety of applications; (2) less present competition for the patentee; (3) less future competition after the patent runs out.

Given the possibility of one or more of these adverse effects, we must ask and endeavor to answer as best we can a series of questions in trying to determine the appropriate antitrust rules with regard to various licensing restrictions. The questions are as follows:

(1) Is prohibition of a particular restriction likely to cause patentees not to license, or to license much less widely, in a significant number of cases?

(2) In what situations is prohibition most likely to have such an effect?

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[11] The following discussion, in most of the important particulars, substantially parallels Professor Baxter's analysis. See Baxter, Legal Restrictions on Exploitation of the Patent Monopoly: An Economic Analysis, 76 Yale L.J. 267, 329–52 (1966).

[12] Note that for this reason a statutory amendment of the patent statute providing for compulsory licensing would substantialy remove any grounds for permitting license restrictions that would violate customary antitrust rules.

(3) In those circumstances would the failure to license lead to less desirable results? To more desirable results? What is the relative frequency of the two classes of cases, and are they more or less readily identifiable?

Thus, if prohibiting the use of a particular restriction would only rarely cause patentees not to license, if licensing were economically preferable to no licensing in only a fraction of those cases, and if those situations where licensing would be better or worse are not readily identifiable within the resources available to us, then a rule of per se illegality is indicated.

That is my conclusion with regard to minimum price-fixing provisions in patent licenses. I shall analyse the reasons along the lines I have just suggested and then turn to other kinds of restrictions.

1. Minimum Price Restrictions

First, would a flat prohibition on minimum price-fixing clauses in patent licenses cause patentees not to license, or to license much less widely, in a significant number of cases?

Where the patentee is not himself producing the patented product or utilizing a patented process, he must issue at least one license to get any returns at all, and withdrawal of the price-fixing would leave that situation unaltered. The question is whether the nonexistence of the opportunity to impose a minimum price-fixing clause would have any effect on the number of licenses the non-manufacturing patentee decides to issue.

It seems fairly clear that if a minimum price clause has any utility to the patentee, it would have it only in a multiple licensing situation. A minimum price clause would not appear to serve any substantial purpose in an exclusive license, no matter what reason the patentee might have for granting an exclusive license. Thus, it is conceivable that a patentee might be able in some circumstances to maximize his returns by granting an exclusive license for a royalty calculated as a percentage of the net profits of the licensee. This appears to be relatively rare, because for such a scheme to yield greater returns than multiple licensing with royalties set as a percentage of gross sales or on a per unit basis, the patentee would probably have to take so high a percentage of the exclusive licensee's profits that the license would be unattractive to the licensee. But even if such a license could be successfully negotiated, a minimum price clause is unnecessary because the patentee could count on the licensee striving to maximize his net returns. Similarly, in those situations where the patentee must grant an exclusive license in order to get any exploitation at all—where there are high uncertainties and/or high innovational costs—and where the royalty is based on gross sales or units of output, the patentee might well wish to insert a maximum price clause. This would enable him to prevent the exclusive licensee from unduly restricting output and thus reducing the patentee's total royalties.[13] But here again the patentee should have no interest in setting a minimum price.

Consequently, a minimum price clause could be useful to the patentee—and might have an effect on the number of licenses he would issue—only where unrestricted price competition would reduce royalty revenues below the maximum attainable. This could not be so where royalty rates are set on the basis of physical units of output. In such cases the patentee will always benefit from unrestricted competition among licensees—the lower the price charged by licensees, the greater the total unit sales and therefore the greater the patentee's royalty revenue.

Where royalty rates are based on gross revenues of the licensees, restrictions on price competition could produce higher royalty returns, at least in the short run, in the relatively uncommon case where the demand for the patented product is inelastic within the relevant range of profitable prices, that is, where total revenues decline with a fall in price. Where this is so, and where maximum royalties could be obtained by a combination of minimum price restrictions and royalties based on gross revenues (rather than by royalties based on physical units of sale), the inability of the patentee to impose a minimum price restriction might conceivably lead him to restrict licenses to a small enough number of licensees that oligopoly price behavior

[13] Since in this case the patentee's interest and the public interest more or less coincide, there is much to say for permitting patentees to employ maximum price clauses in exclusive licenses. This is but another example of the proposition that maximum price fixing is different from minimum price fixing, a proposition rejected in Albrecht v. Herald Co., 390 U.S. 145 (1968), and in my opinion wrongly so.

could be more or less counted on, that is, mutual avoidance of price reduction that would lower the gross revenues of the industry. But it is by no means certain that the noncompetitive price will in fact produce higher royalties than a fully competitive price.

Gross revenues—and royalties based on gross revenues—are maximized at the point where marginal revenue from a price reduction reaches zero; that is, where any further price reduction would actually lower total dollar sales. But a monopolist or perfectly cooperating oligopolists would never push price reductions to this point; they would stop at the point where marginal revenue equals marginal cost, because any further reductions, while increasing total revenues up to a point, would reduce net revenues. Thus, both a monopoly price and a fully competitive price would be less than ideal to the patentee in the relatively uncommon situation we are discussing, and unless the patentee knows the demand and cost conditions fairly precisely—which he rarely if ever does—it is not possible to predict which would be better. In short, even if one assumes that the patentee's decision on the number of licenses to be granted is governed solely by short-run royalty maximization, there would ordinarily be no clear reason for him to prefer oligopoly over competition among licensees. And long-run considerations would seem to dictate a preference for competition. Limitation on the number of licensees—and on competition—may be expected to produce less intensive or less varied efforts to develop the market—to create new demands—than would be forthcoming with a larger number of licensees. For this reason, one would expect nonmanufacturing patentees to prefer wider rather than narrower licensing much more often than not, even where noncompetitive pricing might produce higher royalties in the short run.

Finally, one cannot assume that the patentee will always be able to determine the minimum price unilaterally, solely in terms of his own interests. Indeed, participation of some sort by licensees in the price-setting process seems inevitable. And once licensees play a role, it is highly likely that the minimum price would tend to be set higher than the price that would merely reflect the value of the patent; in short, the scheme would acquire the characteristics of a price-fixing cartel.

To sum up, one can imagine circumstances in which a prohibition on minimum price clauses might lead nonmanufacturing patentees to license less widely than they otherwise would. But there is good reason to conclude that those instances would be relatively rare and that in at least some of them, minimum price fixing would worsen matters by becoming a vehicle for cartels.

This brings us to the use of a minimum price clause by manufacturing patentees. How likely is it that a prohibition would have a significant deleterious effect on licensing? There is no doubt that in many cases, perhaps most cases, there are one or more of several reasons why a manufacturing patentee may wish to license even though he cannot control the licensee's prices. First, his productive capacity may be inadequate to meet expected market demands, and he may be either unable or unwilling to risk the additional capital investment that would enable him to meet the demands himself. In addition to the ordinary market risks that any capital investment entails, there is the additional risk that his patent may be rendered obsolete by superior inventions developed by others. He of course avoids these capital risks by licensing others to provide the additional supply. Second, a patentee's potential customers may insist upon additional sources in order to minimize the risk of interruptions of supply caused by strikes, acts of God, or other vicissitudes. Third, the patentee may be able to exploit the existing demand much more rapidly by licensing those with existing capacity, and the existence of several sellers may lead to wider promotion of new demands. Fourth, he may be impelled to license his competitors because of doubt concerning the validity, coverage, or competitive strength of his patent. He may fear that without licensing, competitors will seek to invalidate the patent, establish lack of infringement, or circumvent it by developing superior or less expensive substitutes.

The additional contribution made by the minimum price-fixing clause is to protect the patentee's monopoly price on his own output. But ordinarily a mere royalty would accomplish the same purpose. A royalty, which is a cost to the licensees, creates a protective margin of that amount, and, if there are several interested licensees, the patent is likly to get a royalty that approximates the value of the patent. Thus, a minimum price clause makes a net contribution only when it enables the patentee to get more protection than a royalty would afford. This will be true if the patentee is substantially less efficient than one or more of his licensees; but in that case, he could make greater returns by setting the highest royalty he could get and letting the licensees carry on all of the production.

There may be cases in which a firm might rationally make more long-run calculations. The patent holder may be a new firm or a small firm which hopes eventually to establish a much larger market position, but which will operate at a cost disadvantage until a larger scale of operations is reached. The firm may in those circumstances seek to cash in on the immediate demand by enlisting the productive capacity of others, without prejudicing its opportunities for growth. In such a case, the patent holder may well need an output restriction as well as a price restriction in order to achieve its purposes. But I believe we may reasonably doubt that such instances will be very common, particularly when it is recognized that where the patents are strong and the future relatively assured, the patentee may not license in any event.

This suggests that the right to impose minimum prices will usually be a decisive consideration only in those situations where it enables the patent holder and his licensees to share monopoly profits well in excess of the value of the patent; in short, where the chief value of a minimum price clause, over and above the mere charging of royalties, is to facilitate the establishment of a price cartel.[14] Price fixing has this effect for several reasons. Licensees have minimal incentive to challenge the validity of the patent because successful challenge will end price fixing and destroy their monopoly profits. Similarly, licensees are led to suppress any unpatented product that competes closely with the patented product. And finally, licensees have much less incentive to develop new substitutes, again because present monopoly profits would be reduced by the reintroduction of competition.

To sum up, the chief utility of a minimum price-fixing restriction to a manufacturing patentee is to enable him and his licensees to obtain monopolistic exploitation well beyond the value of what the patentee has contributed. In all such cases, prohibition of the restriction may lead to no licensing, but the result would be better rather than worse.

In theory, one should permit minimum price fixing in licenses in those cases in which the opportunity to do so is a decisive consideration and where no licensing, or less licensing, would be more undesirable from the economic standpoint than if licenses, or more licenses, were issued. But for this course to be practical, one has to be able to make the necessary determinations with reasonable facility, and I doubt very much that at least some can be made. The first question—whether the right to fix prices is of decisive importance—is particularly intractable because one or more of the other reasons which impel a patentee to license, or to license widely rather than narrowly, will almost always be present, and it will be extremely difficult if not impossible to determine how vital the price-fixing clause was. The patentee will invariably assert that it was vital; but needless to say such self-serving testimony would be entitled to little or no weight. Moreover, whether licensing or no licensing is the preferable result in a particular case is a question that is not easy to answer. In the hypothetical that I described of the new firm wishing to cash in on present demands by licensing others, but not wishing to compromise its long-term growth, the long-run competitive structure may be better off if new firms do not license existing dominant companies.

Similarly, one might stop short of a per se rule if the bad cases—where patent licensing with price fixing is simply a vehicle for a price cartel—could be quickly detected and always brought to heel. Cartels are probably more readily detectable and provable than those few cases in which price fixing may arguably serve a useful purpose. But as a practical matter, enforcement could never be close to perfect and many cartels would exist either undetected or undissolved for a considerable period of time. Thus, it seems that the cost of not having a per se rule would in all probability greatly exceed any gains from permitting exceptions. A flat prohibition of minimum price fixing in patent licenses would be wise antitrust law and wise public policy.

2. *Other Restrictions*

I turn now to three other kinds of restrictions on licenses: (1) output limitations, (2) field-of-use limitations, and (3) territorial restrictions.

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[14] See, e.g., United States v. United States Gypsum Co., 333 U.S. 364 (1948).

Output limitations may be disposed of rather summarily: they pose much the same dangers as minimum price provisions and appear to offer no more in the way of a possible economic contribution. Here, as in the case of price restricttions, licensees will typically share monopoly profits beyond those intrinsic to the patents involved, and hence will have sharply reduced incentives to market substitutes, to challenge the patents, or to develop new non-infringing products. Moreover, output limitations are even more harmful than price restrictions because, in addition to virtually eliminating price competition, they also eliminate quality and all other forms of competition among the patentee and his licensees. Accordingly, output limitations, like minimum price restrictions, should be flatly prohibited.

However, when we turn to field-of-use restrictions, the case for outright prohibition would appear to be considerably weaker. For one thing, compared with price fixing and output limitations, there appears to be a wider range of situations in which the opportunity to impose a field-of-use restriction may be critical to a patentee's decision to grant licenses. A patentee often may strongly prefer to preserve a monopoly on his own manufacturing use. Patentees, whether manufacturers or not, generally wish to extract the maximum value of the patent in each of its various applications, and this requires the setting of differential royalties. Finally, all of the possible applications of the patent, and the value of those applications, may not be known at the time a license is granted; accordingly, patentees have strong reasons for issuing limited licenses, leaving the issuance of licenses for other uses, and the calculation of royalties on those uses, to the future when more information becomes known.

Without field-of-use restrictions, a patentee cannot fully achieve these aims. A scheme of differential royalties would enable a patentee to extract maximum returns from those applications which are known and can be presently evaluated. But differential royalties cannot protect the patentee's monopoly on his own chosen use unless the royalty on that use is set prohibitively high, which would of course be indistinguishable from an explicit field-of-use restriction. And, of course, one cannot establish royalties on applications not yet apparent or of undeterminable value. A patentee could conceivably issue an unrestricted license designating royalties on known uses, leaving the negotiation of royalties on new uses to a later time. But this would again raise bargaining problems unless the patentee reserved the option to withdraw from the licensee the right to practice new applications in the event that no agreement could be reached on royalties—which of course means the imposition of field-of-use restrictions.

To repeat, there appears to be a rather wide range of situations in which the right to impose field-of-use restrictions may be critical to licensing. Moreover, unlike the case of minimum price fixing, where possibly legitimate employment would seem to be rare, none of the suggested reasons for employing field-of-use restrictions are particularly objectionable. Each is consistent with the patentee's desire simply to extract the full economic value of the patent itself, as contrasted with seeking to obtain, and share with licensees, monopoly profits in excess of the patent's worth. Simply protecting a monopoly on the patentee's own use raises none of the cartel problems that infect minimum price fixing. Nor, on balance, is it objectionable for a patentee to endeavor to maximize his returns by charging different royalties for different fields of use.[15] Differential royalties will permit the use of the patent over a wider range of applications than would a single royalty rate, except in the unusual case where the single royalty rate that would maximize returns happens to be the same as the lowest rate that any particular class of users can afford to pay. Of course, royalty distcrimination—which almost inevitably means a higher royalty rate for high-valued uses that would be charged in the absence of discrimination—will lead to somewhat lower output in the high-valued uses: but overall exploitation of the patent may well be greater with discrimination than without it.

Generally, therefore, there would appear to be a rather significant number of situations in which a prohibition of field-of-use restrictions would dis-

[15] Price discrimination among licensees in the same field of use raises quite different questions. See Grand Caillou Packing Co., Trade Reg. Rep. ¶ 16927, at 7887 (FTC 1964), aff'd in part sub nom. La Peyre v. FTC, 336 F.2d 117 (5th Cir. 1966).

courage licensing, and where such reduction of licensing would either serve no useful purpose or would produce less desirable results than licensing with field-of-use restrictions. Field-of-use restrictions, however, like minimum price-fixing clauses, can be, and no doubt have been, used to effect a cartel-like division of markets, patentees parcelling out product monopolies by giving a series of exclusive licenses or by giving a highly limited number of licenses in each particular field. Moreover, as I suggested earlier, it would seem that the patentee's legitimate interests in obtaining maximum rewards would most often be met by nonexclusive licensing in fields other than his own, the principal exception being where exclusivity is necesary to get any takers at all.

In light of these considerations I would conclude, drawing on Professor Baxter's proposal,[16] that the legitimate interests of patentees can be adequately accommodated, and the misuse of field-of-use restrictions avoided, by making the granting of exclusive or a limited number of licenses for particular fields of use presumptively unlawful. More precisely, whenever a patentee issues a license with a field-of-use restriction, he should be obligated to issue a comparable license to any qualified applicant, unless it can be established that exclusivity for a reasonable period of time is necessary to obtain any commercial development and exploitation of the patent in the field of use concerned.

Can such a rule appropriately be imposed under existing antitrust law? A requirement of multiple licensing once any license is issued comes close to compulsory dealing. Compulsory dealing on a nondiscriminatory basis is not unknown to antitrust law, but it has been more or less confined to cases where access to the goods or services involved is a competitive necessity or close to it.[17] I am fairly sure that the scope of such a doctrine is considerably greater than that covered by what few precedents we have. For example, while I am not aware of any such cases, I have little doubt that a monopoly newspaper, or even any one of two or three papers, would be forbidden to discriminate among competing local enterprises by accepting ads from one or two and refusing to take ads from others.[18]

It would, therefore, involve little or no strain to impose the kind of conditional compulsory dealing rule I have described on patentees whose patents have such substantial economic worth that a license to one or a limited number of competitors would confer a significant competitive advantage over those who were excluded. And, of course, antitrust law is readily applicable to a series of field-of-use licenses that have cartel-like effects.

The novelty of the proposed rule would lie in applying it to patentees generally, even where their patents had only minor economic significance.

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[16] Baxter, supra note 11, at 345–46.

[17] See, e.g., United States v. Terminal R.R. Ass'n, 224 U.S. 383 (1912). While the issue was not reached in Associated Press v. United States 326 U.S. 1 (1945), I have always supposed that a flat refusal of defendant to provide its services to any new entrants would have been subject to successful antitrust attack.

[18] Of course the cases just cited involved a combination of competitors discriminating against other competitors, not a single "monopolist" playing favorites among those with whom he deals or refuses to deal. But the vice of exclusion is the same in either event, and an agreement between the seller and the favored buyer or buyers might readily be inferred. If not, the behavior is probably within the reach of § 2 of the Sherman Act. Even in the old *Colgate case*, the Supreme Court stated that a manufacturer could "freely exercise his own independent discretion as to parties with whom he will deal" only "in the absence of any purpose to create or maintain a monopoly." United States v. Colgate & Co., 250 U.S. 300, 307 (1919). And, of course, § 5 of the F.T.C. Act can be applied. See Grand Caillou Packing Co., Trade Reg. Rep. ¶ 16927, at 7887 (FTC 1964), aff'd in part sub nom. La Peyre v. FTC, 366 F.2d 117 (5th Cir. 1966) (involving discriminatory royalties among competing shrimp canners), where Commissioner Elman commented as follows:

"Firms possessing monopoly power may not be ipso facto unlawful monopolists under the antitrust laws, but the permissible limits of lawful business conduct for such firms are more narrowly circumscribed than in the case of firms not possessing such economic power. . . . They are accordingly subject . . . to some of the obligations of fair and equal treatment borne by publicly regulated utilities. See, e.g., Associated Press v. United States. 326 U.S. 1; United States v. Terminal R.R. Ass'n, 224 U.S. 383. A course of conduct that would be lawful if engaged in by a non-monopolist may, therefore, be an unfair method of competition when engaged in by a monopolist. . . . The right of a monopolist to exploit his monopoly (whether such monopoly is conferred by patentes or otherwise) by charging a monopolist's discriminatory price does not, in my opinion, include the right to destroy or cripple a major segment of an industry, but must yield in such a case to the policy of competition embodied in the antitrust laws. . . . In the circumstances, respondent's refusal to treat the Northwest and Gulf Coast shrimp canners on equal terms is an abuse of monopoly power. It has substantially and unjustifiably injured competition in the shrimp canning industry. It is therefore an unfair method of competition forbidden by § 5.

There is precedent for assuming that a patent confers substantial monopoly power in the economic as well as in the legal sense. In tying clause cases, it is presumed that a patent confers the requisite degree of "substantial power in the market for the tying product" to make a tying clause unlawful if a not insignificant amount of commerce in the tied product is affected.[19] But the reasonableness of that assumption probably rests in large part on a judgment that tying clauses are ordinarily so lacking in merit that a fairly stiff rule is appropriate.

Nevertheless, while such reasoning may not be directly applicable to the matter we are talking about, it is not the only avenue for reaching an affirmative result. The essence of good antitrust law is the formulation of reasonable rules. Classically, unreasonable restraints of trade have been defined to include behavior more restrictive than is necessary to achieve the legitimate purposes of the parties involved. Rules of general applicability have been deemed appropriate—even though they may cover some instances in which negligible restraints are involved, and even where their application may in some instances abort arrangements of some benefit—where it seems highly probable that the general rule will in practice yield greater net benefits than a more refined approach. These characteristics apply to the proposed rule. With exclusive licensing protected when it seems reasonably necessary to licensee exploitation, the patentee's legitimate interests would be only marginally affected, and in too few instances to warrant undertaking the task of separating the good cases from the bad.

I would conclude, therefore, that the Sherman Act can fairly be interpreted to impose upon patentees generally the obligation to grant additional comparable licenses to all qualified applicants once any license containing a field-of-use restriction has been granted, except where exclusivity is demonstrably necessary to there being any exploitation at all in the field of use concerned.[20]

Much the same analysis is applicable to territorial restrictions, and I again reach the same result, namely that when a patentee grants a license with a territorial limitation, he must grant comparable licenses to all qualified applicants unless an exclusive license is necessary to anyone's undertaking exploitation of the patent in that territory.[21]

3. *A Final Issue*

I come now to a more far-reaching question: whether the rule applicable to licenses containing field-of-use or territorial restrictions should be extended to licensing generally, including those licenses containing none of the restrictions that I have discussed. In other words, would it be appropriate to impose a general rule that once a patentee has issued a license, he must give a comparable license to any qualified applicant?

There is much to be said for such a rule. Licensing only a limited number of competitors often involves the same invidious purposes and effects as attend the use of minimum price fixing and output restrictions. It leads to cartel-like behavior resting on tacit collusion or the mutual eschewal of competition characteristic of oligopoly. In such cases, as with price fixing and quota limitations, limited licensing enables the patentee and his licensees to share monopoly profits in excess of the value of the patent, which typically will be of questionable validity or have only modest worth. In such cases, licenses generally will be extended only to those companies which, if not taken care of, are most likely to disregard the patent, attack it directly, or compete with noninfringing substitutes. In addition ,limited licensing may be part of a pattern of mutual accommodation among leading companies in an industry, a pattern coming very close to what is achieved by a continuing closed patent pool.

Patentees, however, may limit the number of licensees for reasons less subject to criticism. For example, a patentee may wish to license solely

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[19] United States v. Loew's Inc., 371 U.S. 38, 45 n.4 (1962).

[20] Alternatively, as suggested by Professor Baxter, supra note 11, at 356–57, refusal of a patentee to grant additional licenses might be classified under patent law as a misuse of the patent. Perhaps that would be a more suitable way of going about it. But the argument is virtually the same under either approach, and I see no strong reason for preferring one to the other.

[21] For the proposition that 35 U.S.C. § 261 (1964) of the patent statute does not validate exclusive territorial licenses, see Baxter, supra note 11, at 349–52.

because his customers demand an additional source or sources, or solely because he does not care to expand his capacity to cover all existing demands, and yet not want to license so widely as substantially to reduce his own sales. In such situations, limited licensing is better than no licensing at all. But a rule requiring general licensing once a single license had been issued would hardly cause patentees to abandon licensing in all of these situations. The nonmanufacturing patentee would have no real option, because he would have to license in order to obtain any returns. And a manufacturing licensee would not likely be in a position to resist customer demands that he license additional sources. A general licensing rule, therefore, would appear to have undesirable economic consequences only in those situations where a manufacturing patentee elected not to license at all, and let some existing demands go unsatisfied, rather than run the risk of serious impairment of his market share, and it is by no means certain that patentees would always or even usually make that election.[22]

This would lead me to conclude that the suggested rule, while possibly involving somewhat greater costs than would similar rules governing licensing with field-of-use or territorial restrictions, would still confer substantial net benefits.

The more difficult question is whether such a general rule is a fair interpretation of existing antitrust law. Here again there are doubtless particular situations where antitrust law can readily be applied. Compulsory issuance of additional licenses may be necessary to preserve the effectiveness of section 7 limitations on the sale or exclusive licensing of patents. There is clear room to attack the license that is nonexclusive in name but exclusive in fact, where exclusivity can be shown to have the requisite anticompetitive effects. And it is not too large a step beyond this to compel additional licensing where the patentee has licensed only two or three favored members of an industry, and the patent is significant enough to threaten the extinction of nonlicensed competitors. I also see no serious difficulty in applying the Sherman Act to limited licensing patterns that resemble a closed patent pool. The terms "combination" and "conspiracy" are sufficiently comprehensive to cover tacit cooperation of that kind. And there are probably other situations in which an antitrust remedy of compulsory licensing to additional qualified applicants would be supportable.

The argument in support of interpreting the Sherman Act to require general licensing once a single license has been issued is essentially the same as that for similar rules governing licensing where field-of-use or territorial limitations are employed. The case is weaker here: the broader rule is clearly more sweeping in its impact on patentee options; there is somewhat more justification for a patentee wishing to maintain a large share of he market for his own application of the patent by licensing only one or two other producers than there is for his transferring partial monopolies to others; and the rule might eliminate licensing in more situations where, if we could get all the facts, we would prefer limited licensing to no licensing at all. However, the case is at least tenable, and, as applied to nonmanufacturing patentees, it appears fairly strong.

IV

My conclusions are as follows:

(a) Acquisition of patents or patent licenses should be governed by the same antitrust principles applied to the acquisition of other assets.

(b) Minimum price and quota restrictions in patent licenses should be flatly prohibited.

(c) Under antitrust law or, if necessary, by legislation, a patentee who has granted a license should be required to grant comparable licenses to all qualified applicants, unless he can show that the granting of an exclusive license for a reasonable period of time is necessary to induce exploitation of the patent.

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[22] The patentee would be balancing a sure loss of income from unsatisfied demands, not against loss of profit on his own sales but against the aggregate difference, if any, between the profits on sales taken from him by others and royalties they would have to pay him on such sales. Moreover, the risk of reduced sales may not be too great—he may be more efficient than any likely licensees, and the royalty cost to licensees creates a cost margin in his favor.

(d) In any event, rule (c) should be applied whenever a patentee issues a license with a field-of-use or territorial restrictions.

Such rules would not seriously interfere with the legitimate interests of patentees; they would have little or no adverse effect on the incentive to inventive and innovative activity provided by the patent system; and they would measurably reduce the dimensions of the monopoly and oligopoly problem in the American économy.

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LEGAL RESTRICTIONS ON EXPLOITATION OF THE PATENT MONOPOLY: AN ECONOMIC ANALYSIS

(By William F. Baxter)*

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C. *Restrictions on Price or Output*

The most notorious of patent license restraints is limitation of the price at which the licensee can see his endproduct. The validiy of such restraints has been litigated repeatedly over most of the life of the antitrust laws.[94] Several variations of this type of restriction must be considered: the endproduct for which the selling price is fixed may itself be patented or it may be an unpatented product to which the invention is an input of greater or lesser essentiality. Each of these two variations may involve a limit either on price or on quantity. Four prototype restrictive clauses are thus identified. Each of the four may occur in a factual setting which does or does not involve two or more competing licensees. The possible variations will be examined in light of the general criterion I have invoked throughout this article: is the restriction of a type that impairs assurance of comparability between the social utility of the invention and the disutility of monopolistic restraint? Here as elsewhere assurance of comparability may be impaired either because the restraint is significantly less detrimental to the licensee than advantageous to the patentee, or because the restrictive impact of the license falls upon unpatented goods and services to a greater extent than is justified by technological and administrative considerations.[95]

A license which restricts the price at which the licensee can sell an unpatented endproduct to which the invention is merely one of various inputs should be prohibited even if only one licensee is involved. Such a clause generates a monopoly return to the patentee only by sheltering his own sales from licensee competition. This is plainly so if no royalty is being paid by the licensee: patentee sales are then the only source of patentee income. Less obviously but no less inevitably, this is the only effect of a price restriction even if the license calls for royalties too. A royalty obligation increases licensee costs and therefore the price at which he must sell if his total costs, including return to his capital and personal labor ("profits"), are to be covered. The amount if royalty obligation either is or is not of sufficient magnitude to force the licensee to sell at the fixed price. If it is of sufficient magnitude, the price clause serves no independent purpose; if it is not, the economic effect of the price clause on patentee income is to shelter his own sales at the fixed price.

But sales at the fixed price generate a monopoly profit that depends on the elasticity of demand for the endproduct; and as I have shown, the percentage change in the quantity of endproduct demanded will generally be less than the percentage changes in the quantity of patented input demanded in response to a change in input price. Hence monopoly profits will be greater and output of the endproduct lower than if the monopolistic restraint were confiend to the invention itself. Use of other inputs in the production process is unduly restricted both because of excessive endproduct restraint and because, in the case of licensee production, input substitution occurs less extensively than if the same selling price were compelled by royalty obligations. Thus in any case in which the price restriction serves any function, the clause fails to meet the requirement that the patentee confine as narrowly as practicable the

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[94] See, *e.g.*, Bement v. National Harrow Co., 186 U.S. 70 (1902); United States v. Huck Mfg. Co., 382 U.S. 197 (1966).

[95] See pp. 312–14 *supra*.

restrictive impact on unpatented goods and services.[96] Such price restrictions are also objectionable on grounds which will be discussed in conjunction with patented endproducts.

A limit on licensee output of an unpatented endproduct has all the adverse consequences of a price restriction. The restriction is inoperative if royalty obligations would force a price as high and an output as low as that imposed by the output quota. Whenever the quota is operative, the licensee will charge the highest price at which he can dispose of his quota; and the effects on patentee income and input substitution are those which would result from a price limit. In one important respect an output limit is even more harmful than a price restriction: the latter eliminates price competition; output quotas render futile all forms of non-price competition as well. The two types of clauses should be subject to the same legal prohibition.

The foregoing analysis of price or output limits on unpatented endproducts applies equally to cases involving only one licensee and to those involving two or more selling the endproduct in competition with one another. Additional adverse effects of such clauses in multiple licensee cases will be discussed hereafter.

Where the price or output restriction applies to sales of a patented endproduct, the restriction is not open to the foregoing objections. Although consumption of unpatented goods and services which are inputs to the endproduct will be restricted, that restriction is inherent in the lawful restriction on use of the invention and essential to the generation of monopoly profits correlative to the utility of the invention. Hence if one could assume that the same degree of restriction would occur in the generality of cases from increased licensee costs attributable to royalty obligations and from direct license restraints on price or output, there would be little reason to prohibit direct restraints. There are, however, persuasive reasons for rejecting that assumption and for accepting the contrary proposition that far more drastic restrictions are likely to follow from price or output restraints than from the cost pressure of royalty obligations.

Although I think patentee purpose should be dismissed as irrelevant for legal purposes because of difficulty of ascertainment, a consideration of patentee purpose is suggestive of economic consequences in the present context. The patentee would seem to have a strong incentive to achieve monopolistic restriction on output of his invention by means of royalties rather than by direct restraints on price or output. Assume that the maximizing price for patented widgets is $1.00 each, that industry sales will be ten million units at that price, that marginal and average total costs for all producers at that output are $.85, and that the patentee's direct sales constitute 25% of the market. Potential monopoly profit is $1,500,000,[97] and the patentee can garner all that profit if the industry, apart from the patent, is competitive and the royalty is 15% of gross sales. If, instead, the patentee sets price at $1.00 and imposes a 5% royalty he will receive only $750,000 in monopoly profits, half from his own sales and half from royalties.[98] The other three-quarter million in monopoly profit will be realized by the industry, but it will stay in the pockets of the licensees. In addition to giving up half the potential monopoly profits the patentee will incur significant costs in assuring compliance with the $1.00 price by his licensees, who will be in an economic position to shave prices and further eat into his profits by taking away his market share. This example can be generalized as follows: a price restriction is inoperative except to the extent it dictates a price in excess of that which would be dictated by royalties; and imposition of an effective price restriction forsakes monopoly profit to the extent sales are made by licensees. In the present example the effective price restriction is $.10 per unit,[99] licensee sales are 7.5 million units and $750,000 of profits are forsaken. In view of this inevitability one would suppose that there was no need for prohibiting price restrictions: patentees would not use them.

Two objections to the foregoing analysis are likely to be made, but neither will withstand examination. First, it may be objected that the patentee is

[96] Cases involving price restrictions on unpatented end products have held them invalid. See, *e.g.*, Standard Sanitary Mfg. Co. v. United States, 226 U.S. 20 (1912); United States v. General Electric Co., 82 F. Supp. 753 (D.N.J. 1949).

[97] ($1.00–.85) 10 million.

[98] $.15 (¼) (10,000,000) from his own sales plus $.05 (¾) (10,000,000 from royalties.

[99] $1.00 sale price less (.85 average cost + .05 royalty) = $.10.

entitled to protect himself against licensee price competition and that a royalty does not guarantee that objective.[100] But if the patentee is as efficient as his licensees, a royalty does protect him by giving him a cost advantage to the extent of the royalty. Only if his costs, which include no royalty, exceed the sum of licensee costs plus royalty will the licensees be able to compete with him effectively. Since the patentee can demand royalties of a magnitude correlative to the utility of the invention,[101] royalties afford a cost advantage proportionate to patentee contribution. Unless the patentee is substantially less efficient than his licensees, royalties will afford a wholly adequate competitive shelter. And if the patentee is substantially less efficient than his licensees, it is contrary to his economic interest to substitute his inefficient production for that of his licensees.[102] Therefore an economically rational patentee can derive through royalties as much protection from licensee competition as is justified by the value of his contribution.

Second, it may be objected that a price restriction gives the patentee continuing flexibility of control where as a royalty provision is fixed once the license is executed. It is true that the typical price clause, which requires the licensee to charge at any point in time the same price the patentee is then charging, gives more flexibility than the typical royalty clause which sets a percentage of some base for the entire life of the license. But clauses of these types need not be used; a rigid price clause could be used although the parties are unlikely to find it desirable; and a royalty clause could reserve to the patentee power to alter the royalty rate, perhaps within limits, from time to time. It is no doubt true that licensees would resist variable royalty clauses more strenuously than they resist variable price clauses: but the difference in resistance to be expected is closely related to the vice of price clauses—namely, that licensees are beneficiaries of such clauses and have little incentive to resist them. There is no reason to believe that a patentee could not bargain successfully for a royalty rate subject to his unilateral power of alteration from time to time up to some fixed maximum rate; and for the reasons stated above, such a clause would serve the patentee's economic interests much more effectively than would a variable price clause. Hence the objective based on flexibility, at least in the naive form stated in this paragraph, assumes the point it attempts to prove by starting with a rigid royalty and a flexible price clause.

A more sophisticated form of the inflexibility argument can be made. It tate price gives him a flexible tool with which to assure that the industry

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[100] See *Hearings on H.R. 4523 Before the House Committee on Patents,* 74th Cong., 1st Sess., at 1032 (1935) (testimony of Charles Neave).

[101] A patentee will not necessarily be able to bargain for royalties fully commensurate with the economic value of his invention; for the market for the invention may be highly imperfect. Because substantially all the patentee's costs are sunk costs, he will license the invention for almost nothing if he has no other alternatives. The full economic value of the invention to a prospective licensee sets a ceiling on what the licensee will pay. The precise point within that range at which agreement will be reached will depend on the bargaining skills and on the alternatives of the parties.

A patentee with capacity to exploit the invention directly in the licensee's field has a substantialy stronger bargaining position than does a patentee who lacks that capacity. Similarly, if the potential licensee industry is competitively structured, the patentee will have alternatives; and he will be able to negotiate a royalty approximating the value of his invention.

On the other hand, a patentee who lacks capacity for direct exploitation and whose invention is applicable in an industry which is monopolistically or oligopolistically structured will have very little bargaining strength. The situation of such a patentee is not materially improved by his ability to use a price restriction. By hypothesis he has no substantial direct sales to shelter with the restriction. A potential licensee who already has a monopoly will pay nothing for the service of being subjected to a price restriction. Potential licensees in an oligopolistic industry often would be benefited by a price restriction and this fact will increase the value to them of the *license* as opposed to the invention. This increase in value raises the ceiling but not the floor of the bargaining range. But patentee continues to lack any significant alternative, and he is unlikely to receive a substantially higher royalty.

Any incremental royalty such a patentee does receive is a payment for the service of eliminating inter-licensee competition rather than for use of the invention.

Attempts to justify the use of price restrictions by reference to the plight of such a patentee should be rejected. His unfortunate situation is similar to that of all other suppliers and customers who must deal with an industry so structured. The appropriate legal response is an assault upon the industry structure. It is wholly inappropriate to allow such a patentee to improve his position marginally by selling, not his invention but a restrictive clause that will further suppress competition in the industry and thus worsen the position of all others who must deal with the industry. It is even more inappropriate to make price restrictions available to patentees generally because of the asserted marginal value of the clauses to patentees in the situation described.

[102] See pp. 316–17 *supra.*

operates at the price and output that maximum industry profits.[103] Next it starts with the roughly accurate observation that a patentee's ability to dic- is correctly asserted that even a flexible royalty clause would not assure to the patentee ability to bring about this maximizing of industry price and output, particularly in an oligopolistic industry. In such an industry there may be no such close relationship between firm costs and prices as under either competitive or monopolistic conditions. Therefore a small increase in the flexible royalty rate might not produce the desired price increase; and a small reduction in royalties would be even more likely to fail to bring about the desired price decrease.

All this may be conceded; the deficiency of the argument lies in its irrelevance. What interest has the patentee in whether the industry is operating an optimum price and output? None, except insofar as he is either a direct seller or a royalty recipient or both. In his capacity as a direct seller, he benefits from control over industry price only in accordance with his percentage of total sales; he shares his potential monopoly profit with licensees to the extent they make direct sales. He would be better off with the less precise control device of a flexible royalty rate unless he has a very large fraction of the market.

With respect to the patentee's capacity as a collector of royalties, generalization is more difficult. If, as is usually the case, his royalty is a percentage of sales, he has no interest in optimum industry price. Royalty income would be maximized by a lower price where demand elasticity was unitary. Similarly, a lower price would benefit him more than the maximizing price if his royalty was based on a production input. Only if the royalty base was net profit, a base I believe is seldom used, would royalties be increased by industry price maximization.

This second argument regarding the flexibility of price restrictions, then, is plainly invalid unless the patentee's direct sales constitute a large share of the market; and even in that situation he is failing to capture all his profit. Such a patentee should insist on both a price restriction and a flexible royalty rate. The former would allow precise control over industry price and output, and the latter would enable him to extract all the resulting benefits. Arguably a price clause should be permitted if the patentee enjoys a large share of the market and also has power to vary royalties and uses that power to garner all monopoly profit.

But even that argument should be rejected. Such a patentee can achieve his legitimate objectives without the price clause. By setting his own price at the industry optimum he can prevent any licensee from charging significantly higher prices. And by raising royalty rates he can prevent any licensee from charging less. Such a patentee does not need a price restriction: and since restrictions pose grave threats of abuse in other contexts they should be flatly prohibited.

In view of the fact that royalty obligations serve the interest of patentees much better than do price clauses, how does one account for the fact that price clauses are so extensively used? The answer is that price clauses are used precisely because their favorable economic impact inures to licensees as well as patentees, because their adverse economic impact falls not on the parties but upon the customers of the parties, and because the monopoly income they generate may exceed substantitlly the value of the licensed invention.[104]

In the one situation of the patentee who makes a large percentage of direct sales and also has the power to vary royalties, there would be little difference in industry performance whether or not there was a price clause. A form of low-cost-firm-price-leadership would result, the patentee being the low-cost firm by reason of his control over royalties. A patentee could bargin successfully for such a powerful position only if his patent was both economically valuable and legally invulnerable.

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[103] Even this statement is not wholly accurate since it ignores the possibility that firms may be operating at outputs at which their individual marginal costs may be unequal and therefore the industry is not operating at minimal cost. See LEFTWICH, THE PRICE SYSTEM AND RESOURCE ALLOCATION 216 (3d ed. 1966).

[104] The argument in this and immediately following paragraphs is made by Helmut F. Furthr in one of the few useful prices of scholarship dealing with patent licensing problems. Furth, *Price Restrictive Licenses Under the Sherman Act*, 71 HARV. L. REV. 815 (1958).

It is in situations of patents which are not both valuable and invulnerable that price restrictions significantly affect industry performance. Control over price is used to achieve monopolistic pricing in the industry, but a large part of the profits remain in the pockets of licensees. The patentee does not extract it because he does not have the bargaining power to extract it. The price restriction is the backbone of a loose-knit cartel.

More specifically, a price restriction clause that is operative always has the primary consequence of dividing with the licensees, in proportion to their share of market sales, the monopoly profit potential of the endproduct. Because it does so it has several secondary consequences. First, licensees have no incentive to challenge validity of the patent. If the patent were held invalid, competition among the licensees, the patentee and perhaps new entrants would deprive licensees of their present share of monopoly profits. It is true that some outsider might challenge, or threaten to challenge the patent, but this fact does little to compensate for the elimination of licensee incenive to challenge: the licensees constitute the group most likely to possess knowledge revealing invalidity; and, moreover, an outside challanger can often be bought off by issuing him a license containing price restrictions and thus bringing him aboard the gravy train.

Second, the licensees have an incentive to suppress any unpatented product that competes with the patented product. An agreement to suppress such products is, of course, a prohibited conspiracy. But conspiracies are difficult to prove even if something sufficiently formal to be called an agreement does exist. And in any event the parties have no need of agreement: each will realize that the interests of all call for suppression. Again, introduction of such a competing product by an outsider is possible, but licensees constitute the group most likely to possess knowledge of the existence and market potential of such a product. Again, the outsider may be bought off by letting him into the club, and the outsider's incentive to break up the game is minimized by the facts that he would possess no shelter from competition and would suffer the hostility of the club members in the ensuing competition.

Third, licensee incentive to invent around the licensed patent is far less than if all monopoly profits were being absorbed by royalty obligations. Investment in experimentation that would be warranted by the prospect of avoiding royalty obligations and acquiring a monopoly position for himself is less attractive to a licensee who already has a shared monopoly and is paying low or nominal royalties.

Because of these effects on licensees, the price restrictive license destroys all assurance of comparability between the degree monopoly restriction being imposed on customers and the value of the patentee's contribution. The suppression of potentially competitive products may afford a substantial degree of monopoly power to a patent which is invalid or which constitutes little or no contribution to knowledge. If the suppressed products are old products on which the patented product is an "improvement," the conspiratorial overtones of the arrangement may be quite obvious.[105] Licenses will probably have to be issued to all existing producers of the old product before any licensee will commit himself to even a nominal royalty; and the awareness of customers and other outsiders of the existence of the "unimproved" product will generate resistance to substantial price increases for the new product, may lead to cheating by licensees, and may require elaborate policing steps by the patentee. These circumstances may generate sufficient evidence of "conspiracy" to support a § 1 charge. But where the patented product is new and the alternatives are suppresed by the failure to introduce them rather than by their withdrawal, proof of conspiracy will be difficult or impossible. Since the anticompetitive conduct is inherent in the price restriction, use of such clauses should be flatly prohibited. Not only do they threaten monopolistic exploitation far beyond that commensurate with the value of the patentee's contribution, but they also undermine the objectives of patent policy by weakening incentives of licensees to invent around the licensed patent since it is a source of benefits rather than of royalty obligations.

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[105] *Cf.* United States v. United States Gypsum Co., 333 U.S. 364 (1948).

The position regarding price restrictions suggested by the Third Circuit, that such a clause is permissible if it appears in only one license, is unsound.[106] All the harmful effects described above can occur where there is only one licensee if he and the patentee hold a substantial portion of the relevant product market. A far more sensible distinction would permit price restrictions if the patentee and his licensees, whatever their number, enjoyed less than half the relevant market; for the existence of substantial competition from companies not being force-fed monopoly profits would minimize the potential damage of the price restriction. But in the absence of some demonstration that the clause yields patentees some advantage not obtainable by devices less destructive of competition, I see no reason ever to uphold such a clause.

In discussing royalty structures that increased more than proportionately with increases in licensee output, I suggested that such clauses were tolerable if they occurred in a single license. Such clauses are different from price restrictions because, unless there are multiple licensees, they benefit only the patentee. A price restriction would be more analogous to such clauses if the patentee had power to sell for any price he wished but the licensee could not sell below a set price; but the analogy would still be defective. Under the increasing royalty percentage the licensee's output is restricted only by the pinch of increasing royalty obligations and those obligations represent gains to the patentee. The licensee's willingness to incur those royalty obligations gives some assurance of comparability, for he has received no assurance of monopoly profit from the face of the license. A price restriction not tied to the patente's own prices also suggests that the patentee had a patent of some inherent value; for on its face it affords the licensee only the small comfort of high prices on whatever fraction of industry sales the patentee chooses to allow him. But a critical difference remains: under the price clause, to the extent the fixed licensee price exceeds that to which a greater royalty obligation could have forced it, the patentee is sharing the monopoly profits; and this fact suggests restraint unwarranted by the value of the invention.

A license restriction on licensee output—restriction to a set percentage of industry sales, or to a specific quantity quota or to a quota set from time

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[106] Newburgh Moire Co. v. Superior Moire Co., 237 F.2d 283 (3d Cir. 1956) (dictum). The court was led to this position not by any economic consideration but by attempting to parse language in earlier and inconsistent Supreme Court opinions. An intelligent commet on the case can be found in Note, *Patent Price Restrictions and the Antitrust Laws: A Balance Upset*, 67 YALE L.J. 700 (1958).

The conclusion reached in the Note is that the "narrow revision" of the law by judicial action is unsatisfactory and that "broad revision, requiring delicate adjustments" must be left to Congress. Narrow revision, including flat prohibition of price clauses, is found unsatisfactory because: (1) it would not prohibit other anticompetitive license practices that have similar effects, and (2) because it would affect some patentees more drastically than others.

The first objection to flat prohibition by judicial action ignores the ability of the courts to control the use of other restrictive clauses and thus reestablish the logical symmetry of which the author is enamored.

The second objection, based on equity as between various types of patentees, is unpersuasive for more complex reasons. Patentees of consumer products would be more drastically affected than patentees of intermediate products, the Note argues, because demand for the former is more elastic than for the latter. The existence of this asserted difference in demand characteristics is neither documented empiricaly nor supported by persuasive theoretical argument. Demand elasticity for intermediate products attributable to input substitutability is ignored; and elasticity attributable to elasticity of demand for the end product to which the patented product is intermediate is acknowledged in the last sentence of a long footnote but is ignored in the text. 67 YALE L.J. at 709–10 n.31.

Patentees capable of producing the entire optimum volume of the patented product would be less drastically affected by flat prohibition than those not capable of doing so, the Note argues. The basis for this assertion is inadequate for two reasons. First, the Note relies upon advantages which would be held by patentees capable of large scale production whether or not price clauses are prohibited. See text at n.26. Second, the ability of the patentee to control industry output by using a price clause is assumed to be equivalent to is ability to maximize his own revenue. It probably is true that a patentee with power to vary selling price unilaterally can control industry price and output more delicately than one who can vary royalties; but except to the extent of his profits on direct sales, controlling industry output and price does him no good. See note 103 *supra*. He maximizes royalty income only to the extent he varies royalties. This fact is acknowledged cryptically in the last sentence of another long footnote, see 67 YALE L.J. at 707–08 n.25, but it is ignored in the text. The argument in the text is gravely impaired by the footnote acknowledgement.

Finally, I do not think that minor differences in impact upon different types of patentees—if any differences in impact exist—justify preservation of a licensing device that has the primary function of destroying comparability between the patentee's contribution and the degree to which monopoly restraint is imposed on the endproduct market.

to time by the patentee—should be treated just as a price restriction for the consequences are identical. Licensees share the benefit of restriction on industry output through resultant high prices; they have no incentive to market competitive products or to challenge validity of or to invent around the patent; therefore assurance of comparability is destroyed.

D. *Restrictions on the Field of Utilization*

The term "field restrictions" causes difficult problems of analysis primarily because it is used to refer to license clauses that have very different functions and that should be recognized as raising very different problems. For several reasons a patentee whose invention is susceptible to application in two or more independent areas of economic activity may wish to impose different terms on applications in the different areas. He may wish to charge different royalty rates or base royalty rates on different royalty bases in the different fields; or he may wish to vary as between filds the license terms in other respects—for example, to bargain for a grant-back clause from licensees in field #1 but to forego grant-backs and concentrate on bargaining for the highest possible royalty in field #2.

This general function of the field restriction is entirely appropriate. Use of differential royalties raises the pervasive problem of economic discrimination and requires further discussion; but assuming that in each type of license the royalty structure and any restrictions imposed are lawful, it is my conclusion that field restrictions used to perform this function should not be prohibited.

Assume a patentee whose invention is useful in fields #1 through #5 issues identical licenses to one hundred licensees, twenty of whom are in each of the five fields at the time of agreement. Each license expressly contemplates that the licensee may enter any one or all of the other four fields and provides in substance the following arrangement: Royalties in field #1 shall be 5¢ per unit of input *a* consumed; in field #2 they shall be 10% of your expenditures for input *b*, and you shall issue to me a royalty free, nonexclusive license under any improvement patent you may acquire that is useful in field #2; royalties in field #3 shall be 7¢ per unit of input *c* consumed, etc.

No objection can be taken to this license pattern except on the ground that the patentee is maximizing his royalty income by setting rates on the basis of elasticity of demand for use of the invention in the different areas. For reasons previously given that objection is unpersuasive. To require a uniform royalty structure in different areas of economic activity would substantially diminish rewards to patentees to no useful purpose and often with harmful consequences. Uniform royalties would require not only the same rate but the same base, and a common base would not be available in the different areas in many cases unless an endproduct sales base were permitted. Such a base is unacceptable because of its effect on input substitution.

Even if a common base were available in a given case in the sense that there was a common input in the several production processes, it would not necessarily be an appropriate base in each area—appropriate in the sense of constituting an input closely related to the invention. And if the common input was an appropriate base in all areas it would nevertheless be likely that producers in one area would use the base more intensively than those in other areas so that discrimination would not really be eliminated but merely disguised. Phonic but not economic equality would have been achieved. The very factor that makes an input base appropriate is its capacity to measure the utility which the licensee is deriving from the invention.

All of the foregoing difficulties inhere in the fact that the classical concept of economic discrimination furnishes no adequate basis for normative rules when applied to a product which has no marginal cost.

Finally, if one managed, in some way I cannot conceive, to eliminate charges based on licensee utility, one would not have accomplished anything worthwhile. Forced to abandon charges based on utility in each field of application, a patentee would maximize against an aggregate demand for use of his invention and select a point on that demand curve approximating unitary elasticity. All potential applications of the invention having lesser utilities would be abandoned: they could not afford the uniform price which would exceed their old price. All applications with a higher utility would use the invention, many with greater intensity than before. One cannot generalize that the resulting shift of resources from low utility uses to high utility uses would reflect an advance for the economy. One cannot even predict that more extensive use would be made of the invention; for although prohibiting the sepation of markets diminishes income to the seller, it does not necessarily increase the quantity of the product that will be purchased.[107]

Field restrictions may be misused, however, to achieve an allocation of markets among actual or potential competitors. Like price restriction clauses, the greatest potential for causing economic harm exists when field restrictions are used in conjunction with patents of little commercial value. The economic loss caused by a price restriction is indicated by the difference between the fixed price and the price that would have been compelled by royalty obligations; the loss caused by a field restriction is the difference between the endproduct price that occurs as a result of the field restriction and the highest price that might have been compelled by royalty obligations. Since in both cases a practical limit on endproduct price is set by the relationship between demand for the endproduct and costs other than royalties, the potential of the restrictions for harm varies inversely with the value of the patentee's contribution and his resultant ability to bargain for royalties. Any monopoly income that prevailing endproduct price yields that does not flow to the patentee either through royalties or his own direct sales remains in the pocket of the licensee. Such income does not serve the purpose of the patent system and hence corresponds to unjustified restriction on output.

The foregoing conclusion can be illustrated by examining the cases, first, of a very valuable patent and, subsequently, of a trivial patent. Assume a patentee makes a startling breakthrough in laser technology which makes possible inexpensive and reliable motion picture photography and the reproduction of sharp images in three dimensions, a significant advance on present holography techniques; and assume, further, that viewers of all types find three dimensional reproductions so much more satisfactory than plane images that the technique has the potential to supplant totally present motion picture technology. The device would obviously have potential application in motion picture entertainment, industrial training, films, military training films, advertising films, educational films and perhaps home movies. The elasticity of demand for use of the technique would differ in each of these fields, and the patentee might license its use at maximizing royalty R_1 in field #1, R_2 in field #2, etc., issuing licenses at those royalties to all applicants in each of the several fields. In each field there would be a number of licensed competitors. Each licensee would pay royalties according to the rate for his field and his individual rate of utilizing the royalty base for his field. From the several licensees in field #1 the patentee would receive a total sum of royalties, TR_1, from those in field #2, TR_2, etc., and his aggregate royalty income would be the sum of these totals. This pattern of licenses is wholly appropriate.

Assume, alternatively, that the patentee licensed only one user in each field at the highest royalty for which he can bargain, and the single licensee then, because of the commercial significance of the patent, displaced all unlicensed competition in his field. Several inquiries concerning this alternative are appropriate: (1) Is output in any given field likely to be more severely restricted under this alternative than under the first license pattern described, with the consequence that this license pattern may be labeled "undesirable"? (2) Is the total royalty income obtainable from any given field likely to be greater under this than the first described license pattern with the consequence that patentees will have an incentive to adopt this license pattern if allowed to do so?

During the life of the patent, output of the field is likely to be lower but probably not significantly lower, under the one-per-field license pattern than under a multiple-license pattern, and this is true whether the patent covers the endproduct itself or only a vital input.[108] If the patent covers only a

[107] See Appendix, *infra*, at note 5.

[108] In my discussion at this point I assume that the patentee is confined to an appropriate royalty base, but the assumption is not essential to the analysis. If the patentee is free to use an endproduct royalty structure although the endproduct itself is not subject to the patent, then the degree of restriction under both patterns will be greater; but the comparative restriction attributable to the license pattern will not be affected.

vital input, then to some extent other inputs will be substituted against it; but this will occur whether there are one or many licensees. If the single licensee selected in the one-per-field pattern is not as efficient as other potential licensees, output in the field will be further restricted by the licensee's higher costs; but since selection of an inefficient licensee is contrary to the patentee's interest, reasonable assurance against this possibility is afforded; and this possibility alone would not seem to warrant legal prohibition. To the extent that the patentee misjudges field demand or licensee costs and fails to bargain successfully for a royalty which extracts full monopoly potential, output is likely to be more restricted under the one-per-field pattern; for the single licensee presumably will capture the remaining monopoly potential himself, whereas competition between multiple licensees may cause the differential to be passed on. Multiple licensees may also be preferable because they will offer greater product differentiation and will have greater incentive to achieve technological advance.

Consideration of the performance of the field after expiration of the patent affords a further basis for preferring multiple licensees. Competitive conditions are likely to be restored more quickly if the field has not been confined for the patent's life to a single licensee who, by the expiration of the patent, may have achieved a position which heightens entry barriers.

Finally, the strong ideological preference of our society for multiple participationas opposed to monopoly should not be disregarded if economic considerations are roughly in balance.

The second inquiry is whether one-per-field license patterns yield incremental returns to patentees. If the answer to this question were negative, then prohibition of such license patterns could easily be justified since the objectives of the patent system would not be thwarted in any way. However it is probable that such patterns yield incremental returns to the patentee even in the case of a valuable patent. If the patentee has correctly estimated and successfully bargained for the full monopoly potential of the patent in the field, the sole licensee is little benefited by his exclusive position during the life of the patent. While he enjoys his exclusive position, he has the quiet life of the monopolist but none of its economic fruits. It seems probable that the licensee will pay a premium royalty rate if, but only if, he has some assurance of the continuity of his exclusive position and in addition, one of the following factors is present: he values the prospect of establishing a dominant position in the field during patent life because of the possibility of exploiting that position subsequent to patent expiration; or he estimates demand and cost functions in the field differently than has the patentee, expects to be able to garner monopoly profits beyond those which would be absorbed by the royalty demanded for a nonexclusive position, and offers the premium royalty for the exclusive position as a mode of sharing with the patentee the additional monopoly profits the licensee expects.

To the extent that payment of the premium is induced by the licensee's long-run expectation of a dominant position sheltered by entry barriers of some sort, the premium does not constitute income of the kind contemplated by the patent system. Such income does not correspond to the value of the patentee's measured during the permissible time period but is comparable to an extension of patent life. To the extent the premium is attributable to what has been described as different estimates of cost and demand functions in the field, it is income that corresponds to patent value: the position of exclusivity is a factor strengthening the bargaining power of the patentee in his attempt to extract the full monopoly power of the patent as estimated in advance of agreement.

If one considered only cases involving very valuable patents, the arguments for and against toleration of one-per-field licensing patterns would thus be fairly closely balanced. While such patterns probably generate incremental income for patentees, the magnitude of the incremental income is likely to be small: and only some indeterminate portion of it will be attributable to invention value. In any case where there is incremental income there will be incremental restraint on output; and some indeterminate part of the restraint will be unjustifiable in terms of patent policy because it is attributable to monopoly profit shared with the licensee and licensee anticipation of post-patent market position.

Cases involving comparatively trivial patents must also be considered, however; and in such cases resultant restraint on output may substantially exceed than justifiable by invention value. An industry characterized by loose and fairly competitive oligopolistic structure can be restructured into a series of monopolistic satraps by parceling out exclusive fields within the industry to the existing participants. Here too the one-per-field license pattern, if permitted, will generate patentee income; for in addition to whatever value the invention may have, licensees will pay something for the service of carving up the market into monopolized fields. But patentee interest in such income plainly is not protected by patent policy, and the resultant restraint transgresses antitrust objectives.

To this analysis it may be objected that if the patent is not of great commercial significance, there is no real barrier to entry by outsiders into any one or all of the fields. While technically valid, the objection is not persuasive: it proves too much. On similar reasoning there is no reason to forbid price conspiracies or monopolization or horizontal mergers; for in theory the existence of monopoly profits will signal entrants who will erode the established market positions. But in practice the unjustified market positions endure long enough to make the game worth the candle for conspirators and monopolists. With one-per-field license patterns as with price restrictions, those in the best position to assess correctly the true value of the invention and the practicality of operating without using it or of having the patent declared invalid are, by the licensing device, converted from potential attackers to committed defenders. The fact that some were willing to take licenses, pay royalties of some amount, and abandon alternative production routes to the endproduct creates a facade of legal invulnerability and economic importance for the patent which may be enough to deter more thorough examination by individuals whose primary efforts are directed elsewhere. Unless a device which has such adverse economic potential is also essential to achievement of desirable goals, the argument against blocking its use must fail.

In my opinion the limited utility of one-per-field licensing patterns to patentees as a bargaining device to extract the last drop of potential royalty revenue from valuable patents does not justify acceptance of misuse of the device; nor do I believe that proper and improper use can be identified by factual inquiry on a case-by-case basis.

In formulating rules governing this problem, however, care must be taken lest more be thrown out than bathwater. Any prohibition so sweeping in its scope as to block differential royalty rates applicable to different fields would be unwise. Nor is it realistic to require a patentee, in negotiating with a potential licensee presently interested in field #1, to anticipate all other possible fields of use and prescribe in the license what royalties would be if the licensee chose to expand his operations into other fields. The parties should be free under those circumstances to execute a license that applies only to field #1. Negotiations between them on a mutually acceptable royalty applicable to field #2 can be left for a future date when the licensee's interest in that field becomes less theoretical. Whether the license is merely silent as to other fields, leaving application by the licensee in other fields subject to infringement remedies, or contains promises that the licensee will not practice the invention in other fields, should be immaterial; neither a misuse defense nor an antitrust claim should be available to the licensee or to any third person on this state of facts alone.

The appropriate weapon with which to strike at the restricted field license is to require the patentee to issue to any qualified applicant a license to practice the invention in any field previously licensed on terms equal to those in existing licenses. A licensee under a currently effective license in any field, by reason of that fact alone, should be regarded as a qualified applicant with respect to any other field and as entitled, upon application, to be licensed to practice in such other field if that other field has been licensed to any third person. Only a breach of his original license of sufficient importance to warrant its cancellation which the licensor has invoked as a basis for cancellation should exclude from eligibility a person to whom the patentee has voluntarily issued a license. An applicant who is not licensed under the patent in any field should be presumed qualified, subject to the patentee's ability to prove the existence of facts justifying a refusal to deal with him. Such facts would include prior acts of commercial dishonesty by the applicant or lack of financial solvency or other facts which raise substantial doubt about the applicant's willingness or ability to comply fully with the license terms. Not withstanding proof of such facts, issuance of the license should be required if, in light of the facts shown, the court can issue an order which fully protects the interests of the patentee in faithful performance. If, for example, the refusal is based on undercapitalization of the applicant, the court should order the license issued on the condition that the applicant posts a bond or establishes a trust fund to insure royalty payments. Reasons for refusal other than financial would be more difficult to deal with by protective order; and if the facts asserted are found true and the refusal reasonable in light of the facts, issuance of a license would not be required.

Although this proposal may be said to involve "compulsory licensing" and has an objective embraced by earlier compulsory licensing proposals, it differs from them in two important respects. First, it avoids the nearly insuperable problem of deciding what constitutes a reasonable royalty. Issuance of a license would never be compelled until the patentee's resort to the market place on a voluntary basis had provided an answer to that question. Second, the patentee is not precluded from reserving for exploitation through his own direct production and sales the whole or any subpart of his invention's possible applications. He merely is precluded from auctioning off monopolistic positions to others, the restrictive impact of which may far exceed the real value of his invention because a division of markets rather than rights to practice the invention is the objective of the licensees.

For much the same reason, it cannot be objected that the definition of a "field" is difficult and that the proposal is unworkable for that reason. The patentee adequately defines the field in which the applicant has an option to practice when he issues the first license. Whether the field as defined in the first license constitutes a separable market in economic terms is an issue with which the court need not concern itself: it is enough that a first licensee wanted a license thus circumscribed and that the applicant now also wants such a license.

E. *Territorial Restrictions*

Most of what has been said regarding field limitations is equally applicable to territorial limitations. A pattern of licenses or assignments which carves the United States up into geographic subdivisions and thereby confers on licensees a monopoly position in their respective subdivisions has obvious potential for economic harm. Obviously, too, it makes possible imposition by the patentee of different royalty rates in different areas scaled to the demand elasticity in each area. The latter should not be a source of concern; the former should.

Again in the present context it is true that the potential for harm from market subdivision is inversely related to the economic value of the invention. The more valuable the invention, the more likely it is that royalty obligations would force an endproduct price approximating a monopoly price in the area; and the less valuable the invention, the more likely it is that licensees will be seeking not the right to use the invention so much as a legal umbrella for market division.

As with respect to field restrictions the optimum solution, in my opinion, is to compel the issuance of identical licenses to all qualified applicants with respect to any geographical area for which an assignment or a license has previously ben issued. The patentee's power to auction off exclusive positions will thus be destroyed without impairing significantly his ability to capture through royalties the economic value of his innovative contribution.

Also left unimpaired is the patentee's ability to preserve for himself a territorial monopoly. Until he has issued at least once license or assignment with respect to a territory, there would be no obligation to issue any license for that territory. Hence it cannot be asserted persuasively that the proposed solution would bear more harshly on small than on large patentees; each would be able to reserve for himself an area suitable to his potential for direct exploitation and to gather royalty income from the balance of the United States. The patentee would also be able to provide for subsequent expansion of his exclusive area in anticipation of the growth of his own productive and distributive facilities. Licenses to adjoining territories could be made terminable on a given future date or at the patentee's option on or after a given date. Licenses then issued involuntarily to qualified applicants would similarly be terminable and the patentee's interest would be preserved.

Two points peculiar to territorial restrictions should be noted. The potential of territorial restrictions for economic harm has been limited by the longstanding doctrine that the patentee's monopoly is "exhausted" by the first sale of a patented product.[109] Although the basis for this doctrine is probably to be found in the historic hostility to restraints on alienation[110] rather than judicial devotion to competitive processes, a major impact of the doctrine is to allow patented products to flow across the territorial boundaries of restrictive licenses. This erotion of insularity mitigates the restrictive effect of geographic monopolies. It also reduces the patentee's ability to impose differential royalty rates; to the extent there is inter-area competition through resales, disparities in demand elasticity in different areas cannot be exploited by local licensees and hence cannot be exploited through royalty differentials by the patentee.

But the check imposed by the resale doctrine is only partial. To the extent that the cost of transportation and of additional handling by the redistributor is a significant fraction of final price, a tariff wall remains to shelter the local licensee. The redistributor's costs, apart from transportation, may be substantial, among other reasons because some degree of surreptitiousness may be required to avoid impact of infringement and contributory infringement doctrines: the law is not entirely clear as to the significance of knowledge on the part of either the seller or redistributor of the fact that the latter intends to redistribute in an area foreclosed to the seller.[111] And since the courts have treated the "first sale" rule as one of metaphysics rather than of the purposeful implementation of social objectives,[112] it is difficult to predict results in any given case. Hence the existence of this conceptual doctrine, whatever its reach, should not be thought to make unnecessary or inappropriate purposeful doctrinal modifications which strike specifically at potential abuses of territorial restrictions.

A second peculiarity of the territorial restriction is the presence in the patent code of language asserted to be a statutory basis for such restrictions.[113] Indeed, it has ben suggested that since territorial restrictions are no less harmful than price, output and field restrictions, all such restrictions must be tolerated so as not to create inconsistencies.[114]

Only by amateurish literalism or cynical distortion can it be argued that § 261 places a general imprimatur of legality on territorial restrictions. As the total content of the present section and its history shows, the purpose of the provision is totally irrelevant to the issues discussed in this paper; and the language of § 261 can be given its full intended effect quite consistently with the suggestions I have made.

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[109] See, *e.g.*, Bloomer v. McQuewan, 55 U.S. (14 How.) 539 (1852); Adams v. Burke, 84 U.S. (17 Wall.) 453 (1873); Keeler v. Standard Folding Bed Co., 157 U.S. 659 (1895); Bauer & Cie. v. O'Donnell, 229 U.S. 1 (1913). But see Skee Ball Co. v. Cohen, 286 Fed. 275 (1922).

[110] Chafee, *Equitable Servitudes on Chattels*. 41 HARV. L. REV. 945, 999 (1928).

[111] *Compare* Hobbie v. Jennison, 149 U.S. 355 (1893) (territorial assignee who knew that buyer intended to use product in another territory not liable for infringement by reason of sale) *with* Keeler v. Standard Folding Bed. Co., 157 U.S. 659, 666 (1895) ("Whether a patentee may protect himself and his assignees by special contracts brought home to the purchasers is not a question before us . . . . [H]owever . . . such a question would arise as a question of contract and not as one under the inherent meaning . . . of the patent laws.") See also General Talking Pictures Corp. v. Western Electric Co., 305 U.S. 124 (1938) where the Court declined to answer, because not posed by the record, the analogous question in the context of field restrictions.

[112] "In the essential nature of things, when the patentee sells a machine . . . whose sole value is in its use . . . he parts with the right to restrict that use. The article passes without the limit of the monopoly," Adams v. Burke, 84 U.S. (17 Wall.) 453, 456 (1873).

[113] 35 U.S.C. § 261 (1964). "[P]latents, or any interest therein, shall be assignable in law by an instrument in writing. The patentee . . . may in like manner . . . convey an exclusive right under his . . . patents, to the whole or any specified part of the

"A certificate of acknowledgement under the hand and official seal of a person authorized to administer oaths in the United States . . . shall be prima facie evidence of the execution of an assignment. . . .
United States.

"An assignment . . . shall be void as against any subsequent purchaser . . . for valuable consideration, without notice . . . unless it is recorded in the Patent Office . . . ."

[114] Note, *Patent Price Restrictions and the Antitrust Laws: A Balance Upset*, 67 YALE L.J. 700, 706 (1958).

Section 261 has its genesis in § 4 of the Patent Act of 1793[115] which merely authorized *assignment* by the patentee of his title and interest in his invention.[116] Statutory authorization was necessary "because since patent rights are creatures of statute and not of common law, the transfer of legal title thereto cannot be regulated by the rules of the latter system."[117]

The procedural and formal rigidities of the 19th century between law and equity, between legal and equitable title, and between contracts and conveyances lead to distinctions of substantial practical import between patent *assignments* and patent *licenses*. Made in compliance with the statute, an assignment vested in the assignee a legal title which was an adequate basis for the commencement by the assignee of infringement actions, the execution of licenses or further assignments, and application for extensions of the patent term.[118] A warranty of title was implied unless negated by the instrument.[119] Legal title prevailed over prior equitable incumbrances if obtained for value and without notice,[120] could be held by several persons as tenants in common and perhaps by joint-tenancy,[121] and was subject to voluntary, but not involuntary, partition.[122]

But any transfer of interest that did not convey a sufficiently broad range of interest to the transferee was regarded not as an assignment but as a mere license.[123] Unlike an assignee, a licensee was merely a contracting party, not a property owner with title.[124] He received nothing more than the privilege of practicing the invention to the extent described in the license without being subject to liability for infringement.[125] Licenses could be written or oral and did not have to be recorded.[126] Unless the document expresly authorized transfer, a license was not transferable; and if made transferable, it was such only in its entirety unless expressly made transferable in parts and to a plurality of persons.[127]

Because of the important differences between assignment and license, it was important that there be a sharp definition of that range of interest which was sufficiently broad to be the subject of assignment as opposed to license. No such definition was written into the 1793 provision.[128] This deficiency was corrected in the 1836 act which assimilated to the assignment category "every grant . . . of the exclusive right . . . to make and use, and to grant to others to make and use the thing patented within and throughout any specified part . . . of the United States."[129] Transfers of that breadth were required to be recorded[130] and were regarded as the minimum quantum of interest to which the qualities of "property" and "title" attached; and with those qualities went a complex body of interpretive rules.[131] Finally in 1870 an express statement of the sanction for failure to record, nullify as

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[115] 1 Stat. 318, § 4 (1793).

[116] *Ibid.* "[I]t shall be lawful for any inventor . . . to assign the title and interest in the said invention . . . and the assignee, having recorded the . . . assignment . . . shall thereafter stand in the place of the . . . inventor. . . ."

[117] WALKER, PATENTS § 274 (1st ed. 1883).

[118] *Id.* at §§ 272–95.

[119] *Id.* at § 282.

[120] *Id.* at § 286.

[121] *Id.* at § 292.

[122] *Id.* at § 295.

[123] *Id.* at § 296.

[124] *Id.* at §§ 305, 306.

[125] *Id.* at §§ 296–300.

[126] *Id.* at §§ 303, 304.

[127] *Id.* at § 310.

[128] See note 116 *supra*.

[129] Act of July 4, 1836, ch. 357, § 11, 5 Stat. 117 (1836): "[E]very patent shall be assignable in law, either as to the whole interest, or any undivided part thereof, by any instrument in writing; which assignment, and also every grant . . . of the exclusive right . . . to make and use, and to grant to others to make and use, the thing patented within and throughout any specified part . . . of the United States, shall be recorded in the Patent Office. . . ."

[130] See note 129 *supra*.

[131] See, *e.g.*, Waterman v. Mackenzie, 138 U.S. 252 (1891). See WALKER, PATENTS § 296 (1st ed. 1883).

Even today it is not unusual for courts to allow characterizations of legal relationships to control the answer to questions bearing little apparent relationship to those characterizations. See, *e.g.*, Ohio Valley Advertising Corp. v. Linzell, 107 Ohio App. 351, 152 N.E.2d 380 (1957), *aff'd*, 168 Ohio St. 259, 153 N.E.2d 773 (1958) (plaintiff had received "mere licenses" rather than leases to maintain signs on property subsequently taken by eminent domain and therefore was not entitled to compensation.)

against a bona fide purchaser, was added.[132] When reprinted in the Revised Statutes of 1875, the section was broken into two sentences;[133] in 1897, the sentence making certificates of notaries prima facie evidence of execution of an assignment was added;[134] in 1941 the section was expanded to include applications as well as patents;[135] and in 1952 the several sentences were rearranged into their present order, placing the paragraph relating to certificates between the authorization to assign and the requirement of recordation.[136]

As a consequence of these technical modifications the basic authorization to transfer by assignment rather than by license interests of a minimal quantum now stands alone in the first principal paragraph of § 261 and is susceptible to being misread as a legalization for all purposes of assignments of executive right to a specified part of the United States. But that reading is wholly erroneous. The section remains today what it has been for over a century: a demarcation of the dividing line between interests sufficiently extensive to be transferred by assignment and those which are to be transferred by license. The modern reader, less sensitive than his predecessors to refined distinctions between contract and conveyance, legal and equitable title, and persons who are and are not proper parties in interest, is liable to err; but internal corroboration of the original purpose is present in the section: It deals with assignments, not licenses; and the sentence that is critical for present purposes still reads, "The . . . patentee . . . may, *in like manner* (*i.e.*, by assignment), grant an exclusive right . . . to . . . any specified part . . . ."

The section should be given the full import intended for it. The assignee of an exclusive territorial right has "property" and may sue for infringement within his territory. His document should be interpreted by the suppletive rules appropriate to assignments, and so forth. But to allow this section to preclude intelligent harmonization of divergent objectives of the patent and antitrust laws would be to parody the process of statutory interpretation. The statutory phrase antedates the Sherman Act by more than fifty years, and neither at the time of its passage nor at any time during the interim hundred forty years has Congress given any evidence that the language represented a considered judgment on the substantive propriety of territorial restrictions and their economic consequences.[137] On its face the section leaves untouched the validity of territorial restrictions in licenses; it should be construed as irrelevant to the substantive validity of similar restrictions in assignments.

VIII. In Anticipation of Rebuttal

In retrospect it can be seen that a major theme of the proposals made in this paper is that patentees should be blocked from conferring upon licensees the ability to monopolize generic endproducts and thus to capture the monopoly profit potential in the demand for the endproducts rather than the profit potential in the demand for the invention. I use the term "generic endproduct" to emphasize that the theme has embraced situations where the endproduct itself was patented. A patented endproduct may have more or less close functional substitutes, and if licensees are deprived of incentive to substitute functionally equivalent endproducts against the patented endproduct, the situation is analogous to those in which incentive to substitute unpatented inputs for the patented input is blocked.

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[132] Act of July 8, 1870, ch. 230, § 36, 16 Stat. 198: ". . . part of the United States; and said assignment . . . shall be void as against any subsequent purchaser . . . unless it is recorded in the Patent Office. . . ."

[133] REV. STAT. § 4898 (1875): ". . . part of the United States. An assignment . . . shall be void . . . ."

[134] Act of March 3, 1897, ch. 391, § 5, 29 Stat. 692.

[135] Act of Aug. 18, 1941, ch. 370, 55 Stat. 634: "Every application for patent or patent . . . shall be assignable . . . ."

[136] 35 U.S.C. § 261 (1964).

[137] I have been unable to find any discussion of the territorial assignment language in § 261 either in Congressional reports or in floor debate. The general references that have been made to the section as a whole confirm the view that it has been carried forward without any purpose to alter the meaning it had in 1836.

See, *e.g.*, CONG. GLOBE, 41st Cong., 2d Sess. 2683 (1870) ("[t]here are not new nor additional provisions. . . ."); 29 CONG RECORD 901 (1897) (the only change is "a matter of detail."); H.R. REP. No. 790, 77th Cong., 1st Sess 1–2 (1941) (the only change intended was to make § 261 . . . "applicable to assignments of application as well as of patents."); H.R. REP. No. 1923, 82d Cong., 2d Sess. 3, 5, 9 (1952) (purpose of the bill was the codification and enactment of title 35 with only minor procedural changes).

To this theme it might be objected that the patentee who licenses would be put in a less advantageous position than one who exploits directly through his own manufacture and sales. In the case of direct exploitation, a patentee will not substitute against his patented input or against his patented endproduct. Surely the economy is no worse off, the argument would run, if licensees are enabled to behave in essentially the same way. Indeed, it could be said, the economic value of the invention is best measured by the extent of restriction and profits that would attend direct patentee exploitation; and to prevent the patentee from capturing a part of these incremental profits by splitting them with licensees on whom he has conferred sheltered positions is to deprive the patentee of part of that value. The argument concludes by asserting that an important consequence of depriving patentees of the ability to auction off positions of market power over generic endproducts is that fewer licenses will be issued and exploitation by direct patentee sales will be more frequent with the ultimate consequence of greater concentration and diminished opportunties for small potential licensees.

Although this line of objection cannot be dismissed as patently frivolous, I find it wholly unpersuasive for several reasons. First, it is inconsistent with the basic structure of the patent system. The only possible justification for adopting the private monopoly device as a mode of subsidizing innovative activity is to take advantage of free market assessment of the value of a patentee's contribution. A direct system of government subsidy would avoid all the economic damage of monopolistic restraint and would certainly be preferable but for the enormous political and administrative difficulties of determining an appropriate reward.

But free market assessment is thwarted if the patentee is permitted to sell not the bare right to use the invention but the right to monopolize generic endproducts in which it is useful. The two things are not the same, the latter always being as great or greater in value as the former; and moreover they do not bear any constant proportion to one another. To permit patentees to sell endproduct monopoly positions both impairs the degree of precision with which comparative invention values are assessed and generally increases the values assigned.

I do not imply that the market for innovation is perfect and would make highly refined assessments but for license restrictions. It is not. As Professor Kaysen and Turner have argued with admirable style, the market is highly imperfect: "innovation is a lottery, and it is the high prizes that count.[138] But that unavoidable fact does not justify the further avoidable impairment of market operation that results from requiring that it assess invention value by assesing generic endproducts.[139]

Even when the invention is "essential" to the generic endproduct in the sense sense that without use of the invention no functionally equivalent product can be produced at a cost anyone is willing to pay, the value of the invention is what the market places on use of the invention, not on the endproduct. For the susceptibility of the invention to input substitution in the production process is an unavoidable element of value. *Hamlet* cannot be played without Hamlet; but the merit of the performance will depend heavily on the rest of the cast, the scenery, and even the padding on the seats.

In the more frequent situation where the invention is not essential to the generic endproduct because of the availability of either old or easily discovered new substitutes for it, it is of vital importance for market assessment to focus on invention use. If the patentee is permitted to share a monopoly over the endproduct, incentive, among licensees to bring those substitutes into play is diminished or destroyed; and since the licensees will usually be those in the best technological position to learn of the substitutes and assess them comparatively with the invention, alternative routes to the generic endproduct will often be obliterated.

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[138] KAYSEN & TURNER, *ANTITRUST POLICY* 163 (1959).

[139] A footnote is the appropriate place to anticipate the observation that the ultimate logical conclusion to which my position leads is that patentees should be required to license in all cases so that they will be denied the possibility of endproduct monopolization through self-production. The observation recalls a parable which ends, "I know how to spell 'banana' but I don't know when to stop."

This last, logical, step would require, for reasons of administration, denial of self-utilization until one or more licenses were issued.

When the alternative route to the endproduct is already known, restrictive license patterns blend indistinguishably with the classic patent-umbrella cartel. And distinction is difficult between what is already known, what is already perceptible and what, itself, ranks as invention. To require that invention utilizaiton rather than endproducts be the focus of market assessment would restore incentive to resort to alternatives and would constitute a major step toward eliminating this type of horizontal parallelism. That step is important because of its direct economic consequences in product markets. It is important because of the potential savings of scarce human resources now invested in antitrust enforcement. And it is important because decisions in such cases, turning as they must on highly speculative assessments of the comparability of patent value with obversed restraint, are a source of considerable business community disaffection for the antitrust laws generally.

Finally, the prediction that substantially fewer patentees will issue any licenses does not trouble me at all. Its accuracy is doubtful. Holders of strong and valuable patents—patents than will serve as the cornerstone for an industry—who have or can acquire the capacity to exploit the invention fully by self-production probably do so now. That course yields monopoly profits for patent life, affords a strong market position thereafter, and avoids the administrative costs of establishing and policing a license system. Those who neither have nor can acquire adequate capacity will license because they must. There may be a shift at the margin, but there is little reason to think the shift will be substantial. Any negative value that reasonably may be assigned to that shift will be far outweighed, I believe, by the impact of the proposals on markets affected by patents which are not both legally invulnerable and economically valuable.

It is wholly unimportant whether willingness to license is diminished on the part of holders of patents which are either legally vulnerable or of minor economic value; and the vast preponderance of patents falls in these categories. No shift even at the margin is predictable, for to insist upon exclusive utilization will provoke assaults on validity of patents in the first category and investigation of alternative methods so as to circumvent those in the second category. If the patentees choose to license, they will do so for royalties commensurate with invention value and the probability of validity. With rare exceptions readiness of patentees to license is a mixed blessing for which no substantial price should be paid.

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M. P. VENEMA, CHAIRMAN OF THE BOARD AND CHIEF EXECUTIVE OFFICER, UNIVERSAL OIL PRODUCTS COMPANY

It seems to me we need to do everything possible to encourage invention and the development of new ideas; especially at this time when the United States is falling behind in many areas of technology.

Because of the increased uncertainty in the law governing patent and technology licensing wrought by recent judicial pronouncements which currently frustrate the daily conduct of businesses both big and small, the time is ripe for Congress to declare in terms certain the scope of the applicability of antitrust doctrines to licensing arrangements, and the extent, if any, to which federal patent law restricts or precludes the licensing of technological know-how.

On the one hand are judicial statements to the effect that contractual arrangements whereby one agrees to disclose technical information for a fee runs counter to the plan of our patent laws and policies favoring free competition unless the arrangement is restricted to the claims of an issued patent. On the other, are statements of scientists, engineers and businessmen that the extremely expensive and speculative nature of developing new technology requires the incentive of financial gain. To prohibit licensing of know-how, most of which is inherently incapable of patenting, would inhibit competition by forcing its owner to maintain it secret and exploit it to the exclusion of others in order to pay for its development. Only by permitting each businessman the right to decide to either purchase a technological advance, or develop it himself, will free competition be promoted. For without this choice, industry may well decide innovation is not worth the risk. Small business may be totally unable to afford the cost of developing its own new ventures. Existing enterprises might then be the only prudent investment.

Amendments Numbers 23 and 24 will (i) continue the right of States to protect know-how and trade secrets which have been put in question by recent court decisions and provide remedies against unfair competition, (ii) re-establish the rules governing licensee and assignor estoppel, and (iii) clarify the rights of a licensor in granting licenses under patents owned by him.

Our patent system was established to encourage the disclosure and publication of new technology and the development of new inventions. It also affords protection to the patent owners for a fixed period of time during which they would have the exclusive right to make, use and sell their inventions. The investment of substantial sums is needed to bring inventions and developments to the commercial arena for the good of the public. These incentives are needed in order to promote competition in the development and utilization of new technology.

The patent and antitrust laws are both critically important to the American economic system. The temporary monopoly granted under our patent system is critical to our economic system in order to encourage the development and commercialization of inventions through the use of risk capital. This will not be available unless we have a system in which inventors as well as investors are protected with clear and unambiguous guidelines.

Clarity and certainly in licensing or otherwise granting rights under a patent is important both to the inventor and to the proper functioning of the patent system. The greater the clarity and certainty, the greater the likelihood of invention and investment in inventions for the commercialization thereof.

The real issue is whether this entire matter should be clarified for the benefit of all through appropriate legislation or whether it should remain in its present uncertain state with the probability of becoming more uncertain through more attacks on what were once considered established licensing practices.

Universal Oil Products Company believes that clarification of the above matter is urgently needed to afford to patent and know-how owners some degree of clarity and certainty of action without at the same time destroying the effectiveness of either the patent or antitrust laws.

Accordingly, I strongly urge the adoption of Amendments Numbers 23 and 24 to S. 643, introduced by Senator Scott.