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FORM 1099

During its debate on reauthorization of the Federal Aviation Administration (FAA), the Senate approved an amendment to repeal the Form 1099 tax information reporting expansion established by last year's health care reform law. The amendment, which was officially an amendment offered by Senator Debbie Stabenow (D-MI), was approved by an overwhelming margin. The amendment, which included a revenue offset consisting of a rescission of unspent funds, was virtually identical to the one introduced by Senator Mike Johanns (R-NE) who has been the leader of the repeal effort. A little parliamentary gamesmanship but the repeal was passed.

It does not look like the FAA bill will be the vehicle for repeal. The Senate may pass it this week but for practical and technical reasons, the House is not just going to take up the Senate FAA bill and pass it. In theory, the goal is for Congress to finish its work on the FAA reauthorization by the end of March when the FAA's current authorization expires. But the FAA's authorization expired in 2007 and Congress has been extending in short term bursts since.

Our strategy remains to urge the House to pass H.R. 4, Representative Dan Lungren's (R-CA) repeal bill. It does not have a revenue offset but under the House's new paygo (or probably more accurately, non paygo) rules (see 1-17-

11 Weekly) it does not need one (although, you never know, they just might add one to make the "no free health care reform" point). If the House passes it, the Senate can amend it with a revenue offset to meet its rules and then they can either go to conference or the House can pass the Senate version when it is returned. This fulfills a technical Constitutional requirement for revenue measures to begin in the House and let's everybody do their paygo/nonpaygo thing. But as the old saying goes, "one step at a time" and the next step, hopefully, is a House Ways and Means Committee mark up of H.R. 4.

PATENT REFORM

The Senate Judiciary Committee has cleared a patent reform bill, S. 23, for full Senate consideration. Congress has been debating patent reform for several Congresses now. So, in case someone asks you "what's this patent reform thing all about," here's the SBLC primer.

Article I, Section 8, of the United States Constitution gives Congress various powers. Among them is the power "To promote the Progress of Science and useful Arts, by securing for limited Times to Authors and Inventors the exclusive Right to their respective Writings and Discoveries"

From this provision springs the intellectual property rights we know as patents, copyrights and trademarks.

Copyright protects original works of authorship. A patent protects inventions or discoveries. A trademark protects words, phrases, symbols, or designs identifying the source of the goods or services of one party and distinguishing them from those of others.

Generally, the term of a new patent is 20 years from the date on which the application for the patent was filed in the United States. The right conferred by the patent grant is, in the language of the statute and of the grant itself, "the right to exclude others from making, using, offering for sale, or selling" the invention in the United States or "importing" the invention into the United States. What is granted is not the right to make, use, offer for sale, sell or import, but the right to exclude others from making, using, offering for sale, selling or importing the invention. Once a patent is issued, the patentee must enforce the patent without aid of the United States Patent and Trademark Office (USPTO.) (e.g. it's up to the patentees to sue, and they do, otherwise we might not be talking about reform.) There are three types of patents: 1) Utility patents may be granted to anyone who invents or discovers any new and useful process, machine, article of manufacture, or composition of matter, or any new and useful improvement thereof; 2) Design patents may be granted to anyone who invents a new, original, and ornamental design for an article of manufacture; and 3) Plant patents may be granted to

anyone who invents or discovers and asexually reproduces any distinct and new variety of plant.

The USPTO administers the patent granting process. Patent applications are received at the rate of over 350,000 per year. The USPTO has a backlog of over a million pending applications, over 700,000 of which have not received their first office action and, on average, it takes three years or more to process an application. Funding, fees and staffing for the USPTO as they relate to the processing and quality of patents are the subjects of controversy all of their own.

Since the late 1970's, the Office of Advocacy for Small Business has been documenting the small business sector's contributions to innovation, starting with the seminal report, "Small Business and Innovation" in 1979. Among the most recent findings in 2008, research funded by the Office of Advocacy has found that "small firms are a significant source of innovation and patent activity. Small businesses develop more patents per employee than larger businesses, with the smallest firms, those with fewer than 25 employees, producing the greatest number of patents per employee." The authors compiled a database of patenting firms consisting of any U.S. firm with 15 or more U.S. patents issued between 2002 and 2006. Of the firms, 40 percent of the firms with 15 or more patents in the period were small firms.

In recognition of the belief that small businesses are true innovators, federal law since the early 1980's has provided that small businesses are eligible for a 50 percent reduction in patent filing fees.

Patent litigation is a booming field; the costs of such litigation are astronomical.

Smaller businesses sometimes find themselves on the other side of patent disputes when they discover that they may have infringed on a patent that is extraordinarily broad in scope. These patents are sometimes referred to as "submarine" patents. When they were originally filed, they were general in nature and the full extent of potential uses was not known. When technology catches up later with the invention, the patent owner has a right that stretches across many industries. For many years, a patent applicant could delay the consideration of an application intentionally, to allow the world to catch up with the invention, thereby extending the length of the protection. Patent law was changed some time ago to prevent blatant delay manipulations. Another term heard in the small business community are "trolls" - individuals or companies that have acquired patents but have no real intent to commercialize or utilize the patent. Some refer to these as "patent speculators." However, some inventors who might be called "trolls" by others, are small businesses that do not have expertise or resources to develop the uses for their patent. They are true "innovators." There has been a spirited debate on how one distinguishes between a speculator and a true innovator. Most victims of speculators would say you would know a speculator when you see one. And for some big companies, speculators at the door are a daily occurrence.

That brings us to the current patent reform debate. It is a debate driven by intellectual property titans on both sides. To give you an idea, one steering committee of a coalition, the Coalition for Patent Fairness, consists of Adobe, Apple, Autodesk, Cisco, Dell, Google, Intel, Intuit, Micron, Oracle, RIM, SAP, Symantec, Verizon.

Another coalition is the Coalition for 21st Century Patent Reform, consisting of 3M, Abbott, Air Liquide, Air Products, American Intellectual Property Law Association (AIPLA), AstraZeneca, BP, Baxter Healthcare Corporation, Beckman Coulter, Boston

Scientific, Bridgestone Americas Holding, Inc., Bristol-Myers Squibb, Cargill, Inc., Caterpillar, CheckFree, Cummins Inc., Dow Chemical Company, DuPont, Eastman Chemical Company, Electronics for Imaging, Eli Lilly and Company, Exxon Mobil Corporation, General Electric, General Mills, Genzyme, GlaxoSmithKline, Henkel Corporation, Hoffman-La Roche, Illinois Tool Works Inc., Johnson & Johnson, Medtronic, Merck, Millennium Pharmaceuticals, Inc., Milliken & Company, Motorola, Northrop Grumman Corporation, Novartis, Patent Café.com, Inc., PepsiCo, Inc., Pfizer, Procter & Gamble, SanDisk Corporation, Sangamo BioSciences, Inc., Texas Instruments, USG Corporation, United Technologies, Weyerhaeuser, and Zimmer.

You get the picture.

It is very difficult anymore to sort out exactly where the parties stand. This most recent version of the legislation is a compromise and both sides have gained and lost ground. There are a lot of issues addressed by the bill. The following are some of the "highlights."

The bill would change our system from "first to invent" to "first to file." "First to invent" means if you can prove that you invented first even though somebody has already filed, you will be granted the patent. The rest of the world uses "first to file." Historically, it was thought small businesses benefitted from "first to invent" because big companies had the lawyers and resources to file routinely. There has been some research recently that casts some doubt on that theory. (There is an interesting side debate as strict constructionists say the Constitution prohibits "first to file" because the Constitution refers to "inventor" and under first to file, the patent might be awarded to the paperwork-adept instead of the inventor.)

The bill would provide an administrative alternative to challenge a patent after it has been granted. At the present time, litigation is the only real option and it is difficult to have a patent registration reversed. The reform bill creates a post-grant administrative process to challenge patents.

Damages are a big issue in the patent world. There are two issues: what constitutes reasonable royalties, and whether someone is a willful infringer. There has been a lot of litigation over the standards used to make these determinations.

The argument on the reasonable royalties issue is that too much is included in the valuation of damages. Patent law requires that a patentee is entitled to, "in no event less than a reasonable royalty for the use made of the invention by the infringer, together with interest and costs as fixed by the court." One question that the courts wrestle with is whether the entire market value of the alleged infringer's product should be considered. The Congressional Research Service gives this example, "In some cases, the product or process that is found to infringe may incorporate numerous additional elements beyond the patented invention. For example, the asserted patent may relate to a single component of an audio speaker, while the accused product consists of the entire stereo system. In such circumstances, a court may apply 'the entire market value rule,' which 'permits recovery of damages based upon the entire apparatus containing several features, where the patent-related feature is the basis for consumer demand.'" The courts have been whittling away at the entire market value theory and specific language in the bill limiting its use has been dropped in favor of the "gatekeeper" compromise described below.

A second challenge for the courts is to figure out what constitutes "reasonable." Over the years, various "rules of thumb" have been used in litigation for estimating the amount of damages but not formally endorsed by courts. In a recent case, the key federal court for patent matters dismissed a commonly used "25 percent of profits" rule of thumb.

The criticism of the current litigation environment is that the damage determination process is largely a random event. You will hear that the pending bill creates a "gatekeeper" role for the courts regarding damages by requiring the establishment of methodologies and factors to be considered for damages up front by the court and then the court will control what evidence is introduced based on the methodology and factors. Hence the "gatekeeper" phrase.

With respect to willful infringer, under the patent law, courts "may increase the damages up to three times the amount found or assessed." These damages are assessed at the discretion of the courts and applied to willful infringers. There has been extensive litigation on what constitutes "willful infringement." According to the Congressional Research Service, "prior to the 2007 decision in *In re Seagate Technology*, Federal Circuit decisions emphasized the duty of someone with actual notice of a competitor's patent to exercise due care in determining if his acts will infringe that patent. In *In re Seagate Technology*, however, the Federal Circuit opted to 'abandon the affirmative duty of due care.' The court of appeals instead explained that 'proof of willful infringement permitting enhanced damages requires at least a showing of objective recklessness.'"

At the moment, the Senate bill leaves the current willful infringer standard intact.

The timetable for Senate action has not been announced and it is likely to be a contentious debate as the various coalitions will make more attempts to alter the bill on the floor. The belief is that the Senate will eventually pass the reform bill. The House will develop its own version of a bill, so there is still a long road ahead.