

**PATENT, TRADEMARK AND  
COPYRIGHT JOURNAL OF  
RESEARCH AND EDUCATION  
VOLUME 15  
1971-1972**

PAGES IN THIS VOLUME  
ARE NOT NUMBERED CONSECUTIVELY

THIS VOLUME CONTAINS A SUPPLEMENT  
PAGINATED SEPARATE FROM THE VOLUME

VOLUME 15  
1971-1972  
PAGES 1 TO 696

CONFERENCE ISSUE  
1971  
PAGES 1 TO 116



# The Patent-Antitrust Spectrum of Patent and Know- How License Limitations: Accommodation? Conflict? or Antitrust Supremacy?\*

S. CHESTERFIELD OPPENHEIM\*\*

## INTRODUCTION

IN 1955 I PUBLISHED A LAW REVIEW ARTICLE<sup>1</sup> 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

---

\* This paper was delivered as an address before the Licensing Executives' Society at their Eastern Regional Meeting on April 21, 1970, at the Shoreham Hotel in Washington, D.C.

\*\* Adviser on Research, The PTC Research Institute; formerly Professor of Law, University of Michigan; Of Counsel, Howrey, Simon, Baker & Murchison, Washington, D.C.

<sup>1</sup> 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 *JPOS* 551 (1951).

perspective, the corpus of judicial decisions dealing case-by-case with the interactions of patent and antitrust public policies does not reveal substantial 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.<sup>2</sup> 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 anti-trust policy Rule of Reason applied to restraints beyond the rights of exclusion inherent in the patent grant.<sup>3</sup>

Apart from the dark cloud the dictum of Justice Black in *Lear v. Adkins*<sup>4</sup> 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 increased 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 Anti-trust Division's approach to trade secret or secret know-how license limitations, as announced by the head of the Division, Assistant Attorney General Richard W. 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

---

<sup>2</sup> 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 (Conference Number 1958).

<sup>3</sup> Elman, "'Petrified Opinions' and Competitive Realities," 66 *Col. L. Rev.* 625 (1966).

<sup>4</sup> *Lear, Inc. v. Adkins*, 395 U.S. 653 (1969).

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.

#### 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.<sup>5</sup> This is the position taken in the 1955 Report of the Attorney General's National Committee to Study the Antitrust Laws<sup>6</sup> and in the

---

<sup>5</sup> For collection of cases and commentaries on the American patent system and patent-antitrust issues, see Oppenheim and Weston, *Federal Antitrust Laws*, Ch. 13, (3rd Ed. 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); Bangs, "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.

<sup>6</sup> 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.

recent Report of the President's Commission on the Patent System.<sup>7</sup> 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.<sup>8</sup>

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.<sup>9</sup> 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.<sup>10</sup> 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

---

<sup>7</sup> The Report was transmitted to the President on November 17, 1966. The Commission was established on April 8, 1965.

<sup>8</sup> The Staff Report to the House Subcommittee No. 5, *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.

<sup>9</sup> See addresses cited *infra* note 10.

<sup>10</sup> 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 and 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, U.S. 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 (Conference Number 1966).

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<sup>11</sup> 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 in the unanimous Supreme Court opinion in the 1926 *General Electric* case<sup>12</sup> 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,<sup>13</sup> 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.<sup>14</sup> The basic distinction between intra-patent and

---

<sup>11</sup> McLaren, "Patent Licenses and Antitrust Considerations," *supra* note 10 at 63.

<sup>12</sup> *United States v. General Electric Co.*, 272 U.S. 476 at 490 (1926).

<sup>13</sup> *Motion Picture Patents Co. v. Universal Film Mfg Co.*, 243 U.S. 502 (1917).

<sup>14</sup> *Carbice Corp. of America v. American Patents Development Corp.*, 283 U.S. 27 (1931); *Leitch Mfg. Co. v. Barber*, 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).

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.<sup>15</sup>

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 17 years "of the right to exclude others from making, using, or selling the invention throughout the United States."

This limit time exclusiveness is the only way Congress has power to legislate because Article I, Clause 8, of the Constitution, in unequivocal terms, states that "The 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."<sup>16</sup> Congress can fix the limited term to less than the present 17 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

---

<sup>15</sup> 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).

<sup>16</sup> *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.



his patented invention, the patentee, acting individually, may refuse to license anyone. This is integral to his right to exclude. It includes his right to select his licensees. In that connection, Mr. McLaren properly stated that "it is desirable to preserve intact the patentee's power to grant licenses unilaterally, when and to whom he pleases."<sup>17</sup> Furthermore, the Patent Code affirms the divisibility of patent rights.<sup>18</sup> Hence, the patentee may license less than all of his rights and for less than the entire term of the patent.<sup>19</sup> In sum, the patent laws do not obligate the patentee to promote the kind and extent of competition demanded by the antitrust laws.<sup>20</sup>

The Antitrust Division's tests for determining whether to challenge a particular licensing provision unwarrantedly uses antitrust Rule of

<sup>17</sup> 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.

<sup>18</sup> For a depth analysis, see Powell, "The Nature of a Patent Right," 17 *Col. Rev.* 663 (1917).

<sup>19</sup> 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-Pollack Letters at 53 (1941).

<sup>20</sup> 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, should 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.

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 this 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 embodied 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.<sup>21</sup> Lower federal courts have clarified and sharpened these distinctions in a series of private patent-antitrust suits decided in the 1960's.<sup>22</sup> There are, of course, instances where the conduct of the patentee may transgress both the patent and antitrust laws. Factual situations involving the horizontal element of combination or conspiracy among patent owners or among their licensees are identifiable as "hard core" antitrust violations.<sup>23</sup> Likewise, patent license tying clause conditions are categorized as "hard core" patent misuse.<sup>24</sup>

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

---

<sup>21</sup> See Attorney General's Antitrust Committee Report at 254 (1955).

<sup>22</sup> *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).

<sup>23</sup> See cases cited *infra* note 25.

<sup>24</sup> See *Ethyl Gasoline* and *Univis Lens* cases, cited *supra* note 15.

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.<sup>25</sup> 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 borderline issues on which judicial clarification on patent license limitations is needed.<sup>26</sup> 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,<sup>27</sup> involving field-of-use restrictions, and the 1947 *Transparent-Wrap* case<sup>28</sup> 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

---

<sup>25</sup> *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).

<sup>26</sup> 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.

<sup>27</sup> See *infra* notes 31-34.

<sup>28</sup> See *infra* notes 39-42.

that some attorneys may be heeding the advice of Bruce B. Wilson, Mr. McLaren's Special Assistant, who said in a recent address:<sup>29</sup>

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.

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.<sup>30</sup> 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.<sup>31</sup>

---

<sup>29</sup> *Wilson, supra* note 10.

<sup>30</sup> 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.

<sup>31</sup> 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 such restraints are likely to arise where there is a substantial disparity in the value

Richard H. Stern, Chief of the Division's Patent Unit, speaking for himself, has articulated the Division's reasoning in some detail.<sup>32</sup> He begins by questioning the assumption that limiting the field of uses for which the licensee may sell the patented product is valid under the authority of the 1938 *General Talking Pictures* case.<sup>33</sup> 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

---

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.

<sup>32</sup> The two addresses of Mr. Stern to which my discussion refers, are cited *supra*, note 10.

<sup>33</sup> *General Talking Pictures Corp. v. Western Electric Co.*, 305 U.S. 124 (1938).

licensing in a manner which fails to distinguish patent law and anti-trust 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.<sup>34</sup> 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.

---

<sup>34</sup> 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).

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.<sup>35</sup> 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 unlike the case with nonexclusive licenses. Yet the Antitrust Division strays from such patent policy criteria of legality by emphasizing that nonexclusive 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 nonexclusive 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 the patentee.<sup>36</sup> 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<sup>37</sup> where the patentee receives his full price reward for

---

<sup>35</sup> *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."

<sup>36</sup> 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.

<sup>37</sup> *Supra* note 15.

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 a tying clause in his patent license to derive profits from unpatented parts or supplies.<sup>38</sup>

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<sup>39</sup> 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.<sup>40</sup>

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 nonexclusive 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.<sup>41</sup> It is ironic that the Division begrudges reliance on a Supreme Court decision in the *Transparent-*

<sup>38</sup> *Supra* notes 13, 14.

<sup>39</sup> *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.

<sup>40</sup> *Stokes & Smith Co. v. Transparent-Wrap Machine Corp.* 161 F.2d 565 (2d Cir. 1947), *cert. denied* 331 U.S. 837 (1947).

<sup>41</sup> 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.



*Wrap* case where Justice Douglas, a stalwart antitrust, and often charged with being hostile to patent rights, wrote the Court's opinion. Even though that decision is still the law,<sup>42</sup> the 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<sup>43</sup> 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.<sup>44</sup> 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.<sup>45</sup> The Division has also questioned quantity

---

<sup>42</sup> The lower federal courts have generally sustained grants-back, including assignment grants-back, absent proof of 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)

<sup>43</sup> *United States v. General Electric Co.*, 272 U.S. 426 (1926).

<sup>44</sup> 14 *IDEA* at 137-139, study cited *supra* note. 5.

<sup>45</sup> The following holdings have narrowed the permissive use of a first-sale price restriction 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

limitations in a patent license as akin to a price limitation<sup>46</sup> but the few court decisions on that point approve that limitation.<sup>47</sup>

#### 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. Roland W. Donnem has expressed doubt regarding the assumption that Section 261 of the Patent Code legalizes such limitations.<sup>48</sup> 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

---

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 the 1926 *General Electric* decision controlling.

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.

<sup>46</sup> 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).

<sup>47</sup> *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.

<sup>48</sup> Donnem, *supra*, note 10 at 39.

of the right of the patentee to place territorial restrictions upon his assigns or licensee within the United States."<sup>49</sup> As Committee Co-Chairman I concurred in that view. Two district courts have upheld such domestic patent license limitations.<sup>50</sup> 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 consideration.

#### 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.<sup>51</sup>

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

---

<sup>49</sup> 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.

<sup>50</sup> *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).

<sup>51</sup> 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.

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<sup>52</sup> 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 sublicense. The Antitrust Division is, therefore, correct in its position that only the patentee, acting unilaterally, may select his licensees.

#### TRADE SECRET OR SECRET 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*.<sup>53</sup>

Before discussing that dictum, a summation of Mr. McLaren's view and a resumé 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 elements of his advocated Rule of Reason approach to restrictions in know-how licensing as follows:<sup>54</sup>

---

<sup>52</sup> *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).

<sup>53</sup> *Lear, Inc. v. Adkins* 395 U.S. 653 (1969).

<sup>54</sup> 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 Com-

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.<sup>55</sup> The Restatement, Torts, Sections 757<sup>56</sup> and 758, sets forth the basic principles governing liability.

---

merce 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.

<sup>55</sup> For cases and comments on trade secrets, see Oppenheim, *Unfair Trade Practices*, 229-279 (2d ed. 1965; 1969 Supplement). Comprehensive texts are Turner, *The Law of Trade Secrets* (1962); and Callman, *Unfair Competition, Trademarks and Monopolies*, Ch. 14 (3d ed. 1968); Milgrim, *Trade Secrets* (1970). 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).

<sup>56</sup> 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 and that its disclosure was made to him by mistake.

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 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 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, 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.<sup>57</sup>

---

<sup>57</sup> *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 pre-

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 U. S. Patent Office. Lear thus obtained access to Adkins' idea 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 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.<sup>58</sup> 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

---

emptive 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.

<sup>58</sup> 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 courts 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).

federal agencies.<sup>59</sup> 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.<sup>60</sup> The Internal Revenue Code recognizes trade secrets as property subject to capital gains treatment.<sup>61</sup> Despite the alarm that the *Sears* and *Compco* decisions of the Supreme Court would be applied expansively, the federal and state courts have generally not applied that phase of federal preemption to deny protection to trade secrets.<sup>62</sup>

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.<sup>63</sup> 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

---

<sup>59</sup> 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).

<sup>60</sup> 18 U.S.C. §1905 (1964).

<sup>61</sup> 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).

<sup>62</sup> 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).

<sup>63</sup> 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).



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 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 fraudulent conduct rather than promoting the public interest in protecting valid trade secrets.

In *Painton & Co. v. Bourns*,<sup>64</sup> the district court applied the 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.\*

<sup>64</sup> *Painton & Co., Ltd. v. Bourns, Inc.*, 309 F.Supp. 271 (S.D.N.Y. 1970).

\* After this article went to press, the United States Court of Appeals for the Second Circuit reversed the part of the district court's order which declared the entire agreement invalid and directed a trial on the issue of contract interpretation. The court of appeals noted that this leaves the entire patent controversy, including the trade secret aspects, open for further consideration by the district court.

While recognizing that an ultimate decision for *Painton* on contract interpretation would for the most part dispose of the public policy issues related to the district court's denial of enforcement of the trade secret license, the court of appeals nevertheless discussed the policy issues. In sum, it concluded that (1) *Sears and Compco, supra* presented different issues not applicable to the instant case and (2) protecting trade secrets in advance of filing patent applications is not contrary either to public policy considerations generally or to federal patent policy.

Judge Friendly stated that "the district judge cited no data to prove that licensing of trade secrets had worked adversely to the public interest." The PTC Research Institute had taken notice of this absence of empirical evidence of harm. My discussion refers to some of the empirical studies on trade secrets the Institute has published. The Institute is presently planning an empirical survey on trade

*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 secret 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 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.<sup>65</sup> 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.<sup>66</sup> 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 accom-

---

secret licensing with reference to the public interest factors to which Judge Friendly expressly referred. It should be noted that the projected study is an outgrowth of the Institute's empirical study of domestic patent licensing limitations. See Openheim-Scott reports cited *supra* note 5.

<sup>65</sup> 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, "Patents and Trade Secrets: Instruments of Positive Competition," 12 *IDEA* 631 (1968).

<sup>66</sup> Behrman, "Licensing Abroad Under Patents, Trademarks and Know-How by U.S. 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 U.S. Economic Policy," 4 *IDEA* 150 (1960).

modation 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.



## FORUM

---

Although the primary purpose of *IDEA* is to communicate the research work of the Institute, it also serves as an educational vehicle for the exchange of informed opinion. The positions taken by the authors of papers and notes in this section are not necessarily those of the Institute. It is hoped that the material published in this section will stimulate researchers to undertake further study of the issues.

### Another View of the Antitrust Status of Territorial Limitations in International Licensing

HOWARD I. FORMAN\*

#### INTRODUCTION

THE PAPER BY RICHARD H. STERN on the "Antitrust Status of Territorial Limitations in International Licensing"<sup>1</sup> is a provocatively challenging pronouncement of a proposed new area of patent-antitrust conflict. Now, more than ever before, the industrial progress of our nation could greatly benefit from some clear-cut guidelines to the

---

\* Patent Attorney, Philadelphia; formerly Chairman, National Council of Patent Law Associations.

<sup>1</sup> *IDEA*, Vol. 14, No. 4 (Winter 1970-71), pp. 580-596.

location of the legal interface or line separating the patent and antitrust laws, so that patent licenses can be drafted with confidence that they will not become the bases of antitrust litigation. Instead, the propositions posed by Mr. Stern seem to suggest that the Justice Department's Antitrust Division, rather than seeking to establish that line of demarcation with requisite clarity, is expanding its concept of an amorphous interface on a global scale.

Mr. Stern's various propositions raise fundamental questions involving our national policy regarding the business community. They also may have a bearing upon certain aspects of our international relationships. As such, they deserve serious, even critical examination. The present analysis is intended to stimulate thought regarding a number of Stern's proposals, and possibly thereby to bring forth more comments concerning them.<sup>2</sup>

---

<sup>2</sup> As background information to a consideration of Mr. Stern's proposals it may be useful to recall abstracts from a study made some 30 years ago by the then Assistant Attorney General Thurman Arnold and his staff members of the Antitrust Division, U.S. Department of Justice.

One of Mr. Arnold's staff members, Joseph Borkin (Economist in charge of Patent Unit, Antitrust Division) in a paper entitled "Patents and the New Trust Problem," summarized an important phase of our patent laws thusly in *Law and Contemporary Problems* 75, 76 (Winter 1940) :

By judicial interpretation a patent right has come to include the power (1) to withhold the invention from use by anybody; (2) to use it exclusively; (3) to sell or assign with all rights; (4) to license its use or sale; (5) to sue infringers. This was pungently stated by the Supreme Court in the case involving the original Bell telephone patents:

"Counsel seemed to argue that one who has made an invention and thereupon applies for a patent therefor, occupies, as it were, the position of a quasi trustee for the public; that he is under a sort of moral obligation to see that the public acquires the right to the free use of that invention as soon as it is conveniently possible. We dissent entirely from the thought thus urged. The inventor is the one who has discovered something of value. It is his absolute property. He may withhold the knowledge from the public, and he may insist upon all the advantages and benefits which the statute promises him who discloses to the public his invention." (U.S. v. American Bell Telephone Co., 167 U.S. 224, 250 (1897).)

. . . In the case quoted above we have a legally primitive interpretation of patent rights. The decision has served as a ruling case in spite of an increasingly complex relationship between private and public rights.

Thus spoke Mr. Stern's predecessor in office in 1940. The judicial interpretation of the nature of patent rights which he labelled "primitive" is still the law of the land today. It may be, however, that Mr. Stern still holds to the same view as did Mr. Borkin.

In the lead article to the study, entitled "Antitrust Law Enforcement, Past and Future" (*Law and Contemporary Problems* 5, 14 (Winter 1940)) Thurman Arnold expressed his policy as follows:

Most important in the effective, constructive enforcement of the Sherman Act is the application of the Rule of Reason with respect to combinations in restraint of trade. This Rule envisages three situations in which a rigid application of competitive standards is not possible, under the economic necessities of a machine age:

1. Combinations which actually contribute to the efficiency of mass production should not be destroyed.
2. Concerted action on the part of groups of competitors in order to insure orderly marketing conditions should not be considered unreasonable.
3. Where competition has been destroyed mere imposition of penalties does not re-create it. Economic dislocation in great industries must be avoided.

It is to be hoped that Mr. Stern and his present-day cohorts have not lost sight of Thurman Arnold's statement of antitrust enforcement policy.

TERRITORIAL LIMITATIONS<sup>3</sup> AND PER SE RULE  
AGAINST DIVISION OF MARKETS

As Mr. Stern has said in opening his discussion of territorial limitations in patent licenses, "The central issue, around which all the others revolve, is the lawfulness of a division of domestic and foreign license rights."<sup>4</sup> Further, he states, "if they are illegal at all, [the illegality] is premised on the antitrust rule prohibiting the allocation or division of markets by actual or potential competitors."<sup>5</sup> He then poses the query

---

A third expression of antitrust policy was stated by Walton Hamilton (Special Assistant to the Attorney General, Antitrust Division) in his paper, "Common Right, Due Process and Antitrust" (*Law and Contemporary Problems* 24, 41 (Winter 1940)) who recalled these ancient, yet still pertinent judicial pronouncements regarding antitrust law:

A contract which imposes a restraint upon trade may be upheld or struck down. If upheld the reason is, as stated by a wise Judge years ago, "not because they are advantageous to the individual," but "because it is for the benefit of the public at large that they be enforced." (Baron Parke, in *Mellan v. May*, 11 Mees & W., 653, 665, 152 Eng. Rep. 967, 972 (1843).) Or, as another able jurist has put it, the agreement is reasonable if "the restraint is such only as to afford a fair protection to the interests of the party in favor of whom it is given, and not so large as to interfere with the interests of the public." (*Nordenfeldt v. Maxim Nordenfeldt & Co.* (1894) A. C. 535, 567).

Here, again, is a statement of antitrust policy that seems reasonable and just. It should be kept in mind in reviewing the Stern proposals regarding territorial limitations in international licensing.

<sup>3</sup> Throughout his paper Mr. Stern uses the terms "territorial limitations" and "territorial restrictions" interchangeably. In discussing his premises regarding them the same terms will be employed for ease of reference. However, it is worthy of note that Mr. Stern does not explain what he means by such terms, and without his explanation one cannot be certain what he meant to encompass by those expressions. To illustrate the quandry, Webster's *Seventh New Collegiate Dictionary* defines "restriction" as "a limitation on the use or enjoyment of property." In that sense, a statement in a patent license that the grant is effective in one or more specified countries is not a restriction because there is no limitation or restraint on the use or enjoyment of the property which is the subject of the license.

The licensor may own a patent in one country and grant a license permitting the use of the patent in a portion of that country. Or, the licensor may own corresponding patents in one or more other countries, and grant a license permitting the use of the patent in one or more, but not all, of those countries. In a negative sense—and perhaps this is what Mr. Stern meant by the term—these may be considered to be territorial limitations since they represent a "failure" to grant use of all of the licensor's patent rights world-wide. But they are not limitations, not restrictions, and not restraints on the use or enjoyment of the property that is licensed; the licensee can use the property licensed him without any material restriction being placed upon him. Of course, it is also possible that a patent license may contain an express limitation or restriction against practicing an invention in one or more specified countries where corresponding patents are owned by the licensor, rather than just omitting reference to certain countries, but this probably is a very rare practice if employed at all.

<sup>4</sup> *Supra* note 1, p. 581.

<sup>5</sup> *Id.* at p. 582.

whether this antitrust rule outlaws any licensing agreement by which an owner of a U.S. patent and a corresponding foreign patent grants a license under only one of them. To his credit, it seems to the present observer, Stern suggests that such agreements should not be viewed as a wrongful division-of-markets arrangement per se. Instead, he advocates that they be examined to determine "whether the economic effect is anticompetitive in the manner a division of markets injures competition."<sup>6</sup>

### *National Boundaries of Patent Rights*

Mr. Stern suggests that a possibly preferable way to view the matter is to consider the fact that a patent grant is effective only within the borders of the grantor state. Having suggested further that "a proper accommodation of patent and antitrust policies should take this distinction into account,"<sup>7</sup> Stern summarily dismisses this proposition by stating that the matter has scarcely been thought through enough to come to a final conclusion and goes on to another approach, one appeared to be based almost exclusively on the possible economic effects of territorial patent licensing.

It is submitted that the legal effects cannot be ignored, nor should they be subjugated to the economic effects, particularly if the laws of the foreign sovereign states which granted one or more of the patents in question favor the granting of licenses thereunder without regard for the economic effects in the U.S. as viewed by U.S. antitrust enforcers. If an American company A has one or a portfolio of U.S. patents and corresponding patents in France or Italy, and wishes to license a European company B under the European patents without including the grant of a license under the same patent rights in the U.S., our Justice Department may object but the French and Italian governments may favor the license; the French and Italians may be anxious to have the patents worked in their countries and the licensing of the patents to B may assure their being worked. It would seem that the French and Italian governments have a prevailing legal right; and company A has a legal privilege or duty to exercise its foreign patents, as permitted or required under the laws of the countries which granted them, without concern over the possible economic effects which such exercise, sans the

---

<sup>6</sup> *Id.* at p. 583.

<sup>7</sup> *Ibid.*



right in the foreign licensees to practice the invention in the U.S., may have in the U.S.

Mr. Stern, in skipping ever so lightly by the legal question to concentrate on economic issues, refers to the former as "the bare issue of national boundary of the legal right."<sup>8</sup> In doing so he somewhat shallowly disregards the fact that the patent right is a statutory right—a temporary legal grant or control over a carefully circumscribed piece of personal property which the patentee has conceived or devised—offered by grantor states as an inducement to disclose inventions for the benefit of their nationals. Through international licensing a U.S. company can effectively make its inventions available for use in those countries where it holds patents. Licensing may be the only way in which the company can make its inventions available in foreign countries, as in situations where it has neither the finances nor the technical manpower to develop and commercialize the inventions in those countries. If willing to grant such licenses, why should the U.S. company be compelled to license its corresponding patents in countries, such as the United States, where it wishes to do its own investing and commercial development of its inventions?

In many foreign countries the U.S. owner of patents which they grant is subject to a compulsory working requirement, the penalty for non-compliance being loss of the patent right. If the American patent owner is in no position to work the patent himself, the logical thing to do is to license some other party to do the working. If, by thus licensing one or more of his foreign patents the American owner is obliged—under threat of compulsion by U.S. antitrust action—to license his corresponding American patents, this would be tantamount to establishing a system of compulsory patent licensing in the United States. Congress has on a number of occasions considered and rejected the introduction of compulsory licensing into our statutes. Congress alone has the authority to change our laws to make compulsory licensing a provision of our patent laws. The Justice Department would be encroaching on the prerogatives of the Congress if it were to bring about the effect of a compulsory patent licensing statute through its misapplication of our antitrust laws to owners of American and corresponding foreign patents.

One cannot logically avoid the issue of "national boundary of legal right." Patents are statutory grants of nations and they do have territorial limits. To carry out Mr. Stern's proposals to their illogical extreme,

---

<sup>8</sup>*Id.* at 584.

the net effect of obtaining a patent in the United States and corresponding patents in many foreign countries would be to establish the equivalent of a "world patent." Not only would this wrongful superimposition of our antitrust laws upon our patent laws adversely and improperly affect the American owner of U.S. patents, it would tend to have the same effect upon foreign nationals who obtain U.S. patents corresponding to patents they obtain in their own and in other foreign countries.

Each country has the right to subject its patent grantees (and others doing business in the country) to its own antitrust laws. Each country has its laws regarding patent infringement. Each country has its own substantive law governing the style and form of patent claims it will approve. One cannot suppose that patents granted in countries outside of the United States, for one and the same invention as is covered by a patent granted in the United States, will be exactly alike in any respect except possibly the disclosures. In view of such great differences, to attempt to control the use and disposition of the patent rights in foreign countries by asserting a right against the holder of the corresponding U.S. patent would be to invite pandemonium.

In by-passing the legal effect in favor of the economic effect as a major factor to be considered, Mr. Stern is implying that if failure to license *both* U.S. and corresponding foreign patents should give the licensor an economic advantage the result would be the same as the wrongful effect of an illegal division of world markets.<sup>9</sup> Applying his economic yardstick Mr. Stern sets up five factors as bearing on the acceptability of international patent licensing provisions in terms of American antitrust law. They are:

- (1) The size of the licensors and licensees in their industries, and their degree of establishment in the market affected by the license.
- (2) Number of licensed products or product lines, the dollar value of the patented products, and the size of the package of patents that is licensed.
- (3) Term of agreement.
- (4) Existence of cross- or reciprocal licenses.
- (5) Restrictions on either party, in addition to one on territory.

---

<sup>9</sup> In this assumption Mr. Stern appears to be aligning himself with the thoughts of his predecessor, Mr. Borkin, ignoring the admonition of Thurman Arnold to avoid rigid applications of competitive standards where concerted action on the part of groups of competitors actually may contribute to the efficiency of mass production and/or insure orderly marketing conditions.

*Re Size of Parties*

Stern has taken cognizance of the argument made by some people that international patent licenses which contain clauses dividing domestic and foreign patent rights do not limit or eliminate competition, for in the absence of the licenses there may not be any manufacturing of the patented product by the licensees. This, he seems to agree, is reasonable justification for "a restrictive territory provision" where the licensor is a struggling newcomer seeking to get his patented invention firmly situated in one or more countries and wanted to bar his licensees from competing with him until he can better withstand the competition. Presumably, such a provision would also be acceptable where the licensee was a struggling newcomer on the theory that at least the arrangement made possible an entry into the market by one who probably could not have made such an entry without benefit of the license. However, contends Stern, if the licensor and licensee are major industrial factors in the U.S. and a given foreign country, and particularly if the parties have been actual or potential competitors in an industrial activity affected by the subject of the licensed patents, the arguments favoring the giving of help in the form of territorial restrictions to a struggling newcomer breaking into a market would not apply.

What difference should size and industrial status of the parties make? Take the typical case of a U.S. patentee, a U.S. corporate entity, which is willing to grant a license to one of its American competitors under corresponding German patents to practice an invention in Germany, but not to export the goods made thereby to the United States. Our U.S. patent laws permit the American corporate patent owner to refrain from licensing anyone under its U.S. patents, thereby reserving to the owner the exclusive right for a period of years to make and sell a product in the United States that is based on its patented inventions. This exclusive right is valid even against American companies of equal size and in the same field of business enterprise.

Now, if the American corporate patent owner wishes to license its American competitor—or some European competitor—to practice the invention under corresponding European patents, the licensor will benefit, the licensee will benefit, and the European consumers and countries in which the products are made and sold will benefit. Accordingly, it would seem to be good policy, public and private, to encourage such licensing. But if the Stern theory of the illegality of

territorial limitations applies, the American patent owner also would have to grant the licensee under its European patents a similar grant under its corresponding U.S. patents. Why should the American patent owner be forced to grant its competitors the right to flood the American markets in unrestricted competition with the patent owner? Rather than risk such economic suicide, the American patent owner most likely would refrain from licensing under its European as well as its U.S. patents. Who gains from this result? No one!

One must concede that the well established larger size prospective licensee normally is in a better position than the struggling newcomer to resist taking a license with any kind of restriction, territorial or otherwise. The old, established competitor can risk infringement, challenge patent validity, and invest in research and engineering to design around patents. Theoretically, then, the omission of rights to practice an invention in every country where the licensor owns corresponding patents—so-called “territorial restrictions”—should increase the likelihood of competition internationally among larger companies. In practice, however, such an effect is not always likely to occur because those companies are in a better position than the newcomer to steer their commercial activities so as to avoid conflicts, and they normally will avoid them if they can attain their commercial objectives in other ways. Instead of seeking an improvement by designing around patents, for example, those companies may settle for a “second-best” solution not involving the subject matter of the patents. If this should happen the net result could be a lessening of the efficiency of mass production of patented items on a world-wide scale.

Whereas an international licensing arrangement could insure orderly marketing conditions of the products made under the licensed patents, the absence of such an arrangement could deprive the people in some countries of the new technology, and otherwise adversely affect the marketing conditions even in countries where the technology is available. Such a net result surely would not support the premises of Mr. Stern based purely upon the size of the parties and their status in a given commercial field.<sup>10</sup>

### *Subject Matter of License*

Still operating under the presumption that only struggling new-

---

<sup>10</sup> Such a result would also be directly contra to the precepts of Thurman Arnold recited in note 2, *supra*.

comers need and are justified in being granted licenses with territorial restrictions in order to gain entry into a given market, Stern argues that such necessity is less plausible in cases where the licensed subject matter involves many different products. The same argument applies, he holds, as the dollar value and the number of patents in a licensed package increase. In such instances, he maintains, the licensee will have considerable incentive to try to enter the market by means of his own technology. If one takes a license with a "restrictive clause" under these circumstances, he argues, it more likely will be because of convenience than necessity. Stern's conclusion is that these various factors "indicate that the competitive impact of the territorial restraint" in a license agreement "is greater because of the greater economic importance of the subject matter,"<sup>11</sup> and that this is a prime factor in considering possible antitrust implications of the restriction.

Why? Why should the economic importance, size or value of the licensed package, or the relative need for the license govern the question of antitrust implications? The "necessity" argument is not the sole justification for territorial limitations, by any means. And what difference does it make if the licensee's entry into several product lines or activities is based upon convenience rather than necessity? If the licensee finds it convenient to take a license in one or more countries, for certain lines in certain countries and other lines in different countries, provided the licensing is done within the purview of the laws of the country or countries which granted the respective licensed patents, there is absolutely no logical reason why the enforcement of U.S. antitrust laws should be extended extraterritorially thereto. There is no valid legal reason, domestic or international; there is no valid economic reason.

### *Terms of Agreement*

In this section Mr. Stern suggests that struggling newcomers are entitled to some special exceptions such as territorial restrictions, but only for a finite term until the market has been "broken into." He envisages situations where know-how or technology related to the licensed patents is furnished, and if geared to continuation of territorial restrictions might lead to retention of those restrictions indefinitely. To prevent antitrust implications of such an arrangement Stern suggests that all territorial limitations on the use of patented technology

---

<sup>11</sup> *Id.* at 586.

be eliminated after five or ten years, otherwise the continuing flow-through of technology on broad product lines, subject to territorial limitations, would have the effect of dividing markets territorially. What justification is there in requiring the patent owner-licensor to limit his international licensing arrangement to a specified term of years less than the term of the patents? And why pick five years, or ten years? There is no meaningful justification for either term. It is a purely arbitrary proposal.

To follow Mr. Stern's suggestion would have the effect of reducing the terms of the licensed patents to five or ten years. What is the logical basis for such a result? The patents could be licensed for their full terms. Any technology or know-how that is agreed to be furnished could be supplied for the duration of the patent terms. Alternatively, a separate agreement could be entered into for the sale or license of the know-how over a stated period of years, without regard to the terms of the licensed patents.

### *Cross- or Reciprocal Licenses*

In discussing cross or reciprocal licenses subject to a territorial limitation, Mr. Stern alleges that they are probably more vulnerable to antitrust challenge than "one-way" licenses. If that allegation is based on his understanding of the operation or effect of such licenses, then his conclusion must be in error, for his explanation of the nature of such licenses is wide of the mark. He declares that, "By such an arrangement each party promises, in effect, to respect the other's territory and not to invade it, as part of the *quid pro quo* for the license."<sup>12</sup> That is not the case at all. By the cross-license each party is given the legal right to "invade" the other's patented territory; put another way, each party is given an immunity against suit for infringement of the other party's patent. Far from staying away from the other party's patented property, cross-licenses are like open doors with "Welcome" mats inviting the respective parties to walk in and make themselves at home in the other's patented territories.

Stern says that the presence of cross-licenses is not a decisive consideration, but it "tends to affect the antitrust prognosis adversely"<sup>13</sup> especially when combined with technology flow-through provisions for a long period. This conclusion can hardly be valid since it was based in part on an erroneous premise. Actually, cross-licenses can—and usually

---

<sup>12</sup> *Id.* at 587.

<sup>13</sup> *Ibid.*

do—have the effect of increasing competition as they tend to equalize the technological capacities and rights of competitors in a given field. If coupled with technological know-how, presumably exchanged by both parties, the competitive abilities of both are aided and abetted. Such aids to competition should tend, if anything, to lessen the chances of antitrust problems arising.

### *Relation of Factors*

Describing the extremes, Mr. Stern postulates that if all of the factors discussed above were adverse there would be a Sherman Act violation; if all were favorable there would be no problem to consider. He allows that it probably would be permissible to let the patent owner, at least in the case of a single and non-dominating patent, impose a territorial limitation (i.e. not grant a licensee rights under the American counterpart of a foreign patent).

It is the status of agreements somewhere between these two extremes that causes problems, says Mr. Stern, and he recognizes that the question is not one that readily admits of a clear-cut answer. Lacking a definite answer he advocates caution: do not, he urges, include territorial restrictions in licenses unless absolutely necessary. He suggests that the license be written so that product scope or the size of the licensed package be carefully tailored to the exact needs of the parties, as a means of lessening risks of probable antitrust violations.

It would seem that by merely stating the problem of indefiniteness as to the law on the subject, repeatedly saying the problem has yet to be thought through, and then urging that "conservative and careful drafting technique" be employed, Mr. Stern has pointed up the weaknesses of his entire thesis. If he would stick to ages-old principles, whereby the law of the land that grants patents is the law that should be applied to licensing agreements relative to those patents, there would be no doubts, no uncertainties. Instead, his attempt to mix law with novel economic theories must inevitably lead to confusion and uncertainties which will make the matter of international patent licensing a troublesome, difficult situation which will confound businessmen and lawyers alike.

### TERRITORIAL LIMITATIONS IN KNOW-HOW AGREEMENTS

It is not intended to discuss in this commentary, as was done with regard to Mr. Stern's proposals re territorial limitations in internation-

al patent licenses, each one of the points he makes regarding such limitations in know-how agreements. Such a detailed analysis will be made by the present writer in a future issue of *IDEA*. For the present it will suffice to observe that once the flaws in Mr. Stern's proposals re international patent licenses are recognized, similar flaws in his suggestions re know-how agreements will become apparent. Mr. Stern has postulated that to draw an analogy between licensing restrictions involving unpatentable know-how and those involving patents may be faulty,<sup>14</sup> and this may well be true with regard to a number of points of comparison. However, the analogy may hold up well when comparing the flaws in the reasons given by Mr. Stern in support of the so-called antitrust implications of international technology licensing, whether or not that technology is covered by patents.

Although it is not planned in these pages to discuss each of Mr. Stern's arguments, a brief word about his thesis regarding the international licensing of know-how may be in order. Mr. Stern visualizes the situation where an American owner of valuable know-how may want to sell or license it to a foreign buyer subject to a limitation that it shall not be used to make goods sold in the United States. He further visualizes that the ultimate rule of law the courts will decree in such situations is to proscribe all territorial limitations on the place of sale of goods made with licensed know-how. With this thought in mind he counsels the draftsmen of know-how agreements to avoid litigation by avoiding inclusion of territorial restrictions unless absolutely necessary, and then only if limiting their duration to the time necessary for the licensee to break into the market, among other factors which he specifies.

In making his point re know-how Mr. Stern seems to expect that his to by-pass, namely the "legal status" of patents. He indirectly concedes that his arguments re the international licensing of patents may not hold because patents are based on statutory or constitutional policy which would sustain an exception to the antitrust laws. This concession he appears to make by way of laying the groundwork for a case that no such exceptions are available in support of international know-how agreements with comparable territorial limitations. In making out his case Stern advances two arguments which, it is submitted, are both rather curious and self-defeating.

In Stern's own words, after describing patents as statutory monopoly-earlier premises regarding patents may founder on the footing he chose

---

<sup>14</sup> *Id.* at 589.



lies decreed by Congress and the Constitution as an exception to our antitrust laws:

A know-how agreement, even though the know-how might be substantial, valuable and secret, cannot rely upon any such statutory or constitutional policy which would sustain an exception to the antitrust laws. Moreover, since know-how does not have to follow the rules of the patent system—with regard to novelty, utility, inventive level, sufficiency and clarity of disclosure, and the like—the general public receives no *quid pro quo* of a substantial addition to the common store of knowledge, as it does after the expiration of the 17-year patent monopoly.

For these reasons, restrictions which might be tolerated in the case of a license under a valid patent, in order to accommodate the complementary policies of the patent system and the antitrust laws, might well be prohibited in the case of a know-how agreement. This does not compel the conclusion that know-how agreements may not be accompanied by any restrictions or limitations whatsoever. But it surely demands, at the very least, that the parties must do more than cite the analogy of permissible patent restrictions. Instead the parties would seem to be subject to the general law and policy governing all business agreements.<sup>15</sup>

The first point which is rather curious is the notion that, if there is to be any validity or propriety in international know-how licensing with so-called territorial limitations, the basis therefor would have to reside in the contribution the subject matter of the license makes to the commonweal. The fact that, unlike with patents, in the case of know-how licenses there is no guarantee of public disclosure of the know-how, seems in Stern's view to mitigate against the right of the licensor to insist on limiting use of the know-how to certain countries. Why should there be this distinction? Does the mere fact of public disclosure of new technology make proper what in Stern's mind might otherwise be improper, namely so-called territorial limitations in licenses involving that new technology? Such a justification is dubious. There are far more logical reasons supporting the proposition that international licensing with so-called territorial restrictions is proper.

The *quid pro quo* to which Stern makes reference is given to the public in return for the government's authorization to use its judicial power for a finite term to put an end to unlicensed infringers of patented technology. Since no such authorization can be given in the case of unpatentable know-how, the owner of such know-how is not obliged to give the public a similar *quid pro quo* and he must protect his technology as a trade secret as best he can. He does so under the general law of trade secrets applicable in this country or of such other country in which his agreement is to apply.

---

<sup>15</sup> *Id.* at 590-591.

If he enters into a license agreement relative to that know-how he and his licensee can only rely on those laws of trade secrets. If he enters into a license agreement involving the use of that know-how in France or any other country he and his licensee will be subject to the law of trade secrets in France or such other country. If an American owner of unpatented technology or know-how was, through separate agents in each of a half dozen countries, to license that know-how to a different individual licensee in each of those countries, would there be any plausible reason for our government to object to that practice? If the license was to be given to individual representatives in each country of a single party, would that make any difference insofar as the licensee's propriety was concerned? It cannot be seen why either practice would be objectionable. It naturally follows that there should be nothing wrong with accomplishing the same end result by a single license between the American owner-licensor of know-how and a single licensee relative to a number of countries in which the know-how is to be licensed.

The other point Stern makes is that, rather than depend upon analogous permissible territorial restrictions involving patents, in the case of international know-how licenses the parties will have to look "to the general law and policy governing all business agreements."<sup>16</sup> Precisely! That is the nub of the entire issue raised by Mr. Stern. Instead of trying to conjure up new and tenuous theories regarding international know-how licensing agreements it would be preferable to look to that "general law" for guidance. Keeping in mind that the "general law" has national boundaries, too, just as was pointed out in the discussion of international patent licenses it would be folly to try and make every international know-how agreement conform to American standards which may not fit into the pattern of applicable laws in foreign countries where the agreement is to be applied.

#### THE DIRECTION OF THE LAW

Mr. Stern concludes his rather challenging paper by stating that, in attempting to analyze the direction the antitrust laws will take in this area, he recognizes that today we are at too early a stage of understanding international technology agreements to know with certainty what will be considered right or wrong. He sees lawyers and their clients

---

<sup>16</sup> *Id.* at 591.

forced to take a case-by-case approach, calculating the risk of drawing litigation and the probable outcome thereof as best they can. He urges that all concerned act prudently without trying to see how close they can come to the Plimsoll Line until the courts have fully defined the law, suggesting that the courts will not treat lightly those who deliberately go perilously close to an area of proscribed conduct and take the risk of crossing the line.

Of course, by giving this gratuitous advice, Mr. Stern is, in effect, not leaving much doubt as to his confidence that he "knows" where that line will be or actually is today. One need not wait for a court decision to determine the location of that line. In fact, as Richard McLaren, Assistant Attorney General in charge of the Antitrust Division (and Mr. Stern's superior) stated when he testified re the Scott Amendments at the Hearings of Senator McClellan's Patents Subcommittee on May 11, 1971, if anyone has any doubt regarding any problems in the patents-antitrust interface, the Justice Department will gladly tell them the answer if they will but write in to the Antitrust Division and ask for its opinion.

It is clear from such pronouncements that the direction of the law will be what the present Antitrust Division of the Justice Department thinks it should be—if their leaders have their way. By ever so carefully picking the cases they will wish to try, they will be seeking to get the courts to hand down rulings along the lines of "predictions" which they make in papers like Mr. Stern's on territorial limitations here under analysis. After all, the courts do not rule in vacuo; they rule only in actual cases, and in this area of patents and antitrust matters it is the Justice Department that institutes the suits that lead to the decisions which make the law.

This practice of carefully selecting cases to try in order to shape the course of the patent-antitrust law, and the practice of writing and lecturing widely as to what that law should be, is what set off the furor which led to the Scott Amendments on patent licensing in general. In indulging in such practices Mr. McLaren and Mr. Stern seem to give the impression that they not only fail utterly to understand what a patent is and what a patent does, but also fail to appreciate the many problems confronting a businessman who wishes to become either a licensor or a licensee under one or more patents. Perhaps if they did not lose sight of the true nature of the patent grant some of the thoughts advanced by Mr. Stern re international patent license restrictions or limitations may not have been presented. Similarly, if he could appreciate the country-by-country legal problems involved in know-how licens-

ing he might not suggest his simple "cure" for alleged ills in that type of licensing.

For one thing, although certainly Mr. Stern knows better, he gives the impression of believing that patents granted in various countries are of equal status in terms of their scope, their coverage, the rights and obligations appertaining thereto, et cetera. Since no two countries have truly identical patent laws, no patents on even one and the same invention necessarily cover the same legal ground or have the same legal effect.

The patent coverages in different countries may be completely different one from another. The type of claims can vary. The scope of the claims can vary. The terms of the patents can vary. The laws governing invalidity or infringement of the patents can vary. As a result, a party licensed under a patent in country A may be prepared to attack validity or defend against infringement in country B where he is not licensed, because in B the patent may be invalid or not infringed. This may be simply because the scope of the claims or the limitations put in the claims in the patent granted by B are different from those in the claims in the patent granted by A. The licensee under the patent in country A may not wish to obtain a license under patents granted by other countries. He should not be forced to take a license in countries where he is not interested in practicing the invention. By the same token, the licensor should be able to decide in what countries he wishes to grant licenses and in what countries he wishes not to grant licenses.

Obviously, in a typical situation the patent owner-licensor will not have corresponding patents in every country which may be of interest to a prospective licensee. But in countries where patents are obtained the owner frequently will wish to increase his income through royalties by licensing a capable operator in each such country. In doing so the patent owner is making it possible for the patent to be worked, frequently in cases where he is unable to work the patent himself. This may lead to new products, new industries, and inevitably to new competition in each country where the patent is worked.

To make such licensing attractive to the licensee, the patent owner may grant an exclusive right to work the patent in one country to M, in another country to N, and in still another country to O. In fact, such a restriction is the only way in which licensing can be effective and, if forbidden, will very much reduce licensing abroad. In doing so the licensee in each case is given assurance of an opportunity to recoup its investment and make a profit, just the same as the licensor would under the patent laws of each country if he were able to work his patent

himself. Each licensee is thus given the maximum opportunity to succeed in the absence of competition from other licensees in the same country. The country in which the licensee operates will benefit by the new investment and development of technology. The fact that the owner of the patent rights in the various countries sought to maximize his royalty return by granting separate licenses in the different countries, to separate licensees deemed best able to operate under the licenses, should not mitigate against the logic and the benefits of such a plan to all concerned.

Mr. Stern may consider such an arrangement the same as the allocation of territories or a division of markets, but if so it is hardly an arrangement that can be considered improper from the antitrust view of restricting competition. Granted that in a given country each licensee operates exclusively under its patent license, but this is within the normal nature of the patent grant in each country, and after the patent expires in each country the subject matter of the patent is completely open to competition. In the meantime, of course, each licensee is not licensed to go into the territory of another licensee or of the patent owner's unlicensed territories, but this also is within the normal operation of the patent laws of each country that may have granted the patents in question.

In suggesting that territorial restrictions in international patent licensing may be improper Mr. Stern overlooked the fact that patents are granted for terms of different duration in different countries. If a patent owner was required to license in all countries where he owned corresponding patents the licenses may be for different periods of grant.

Patents may be invalid in some countries and valid in others. For example, a patent may be invalid in Germany because of a publication in the United States, whereas the patent may be valid in the United States if filed within one year of the publication date. As another illustration, Germany and the United States have requirements for full disclosure of the invention, which is not the case in some other countries. There are, of course, other such examples of differences in the patent laws of the various countries.

Different parties in different countries may be licensed for different products. Why should a license for all products or fields be forced on a licensee (i.e. block-booked) who wants a license for only one product or two products, and who may want to be free of royalty obligations on other products, or may even want to challenge the applicability of the patent with respect to other patents? According to some authorities it is

wrong to require block-booking of some sorts. Ironically, according to the Justice Department viewpoint it may be wrong *not* to block-book when it comes to international patent licensing.

Rather than try to bend the law to require that a license granted under a foreign counterpart patent also be granted under the U.S. counterpart patent, it should be realized there are benefits which all may derive if licenses are not granted in some countries. For example, as pointed out previously, the lack of a license in certain countries may encourage the making of new developments to avoid patent infringement and thereby benefit the public at large. This is a form of competition, and if it should develop it may be one of the most fruitful of all forms of competitive endeavors, particularly if the new developments prove to be as good or better than the patented invention that spurred the research which led to them.

It may be that to license different people in different countries, or to license a particular party in only certain specified countries, will have the same effect as a restriction or limitation excluding one or more of them from certain other countries to the extent that patents exist in those other countries. But this is the result of the normal, proper exercise of the patent grant in each country, namely the legal, constitutional right to exclude others from practicing the patented invention. It is not the result of an illegal or extra-legal restriction. Thus, failure to license in a particular country is not a positive prohibition with a coercive objective, but merely serves to make the action of another party subject to the laws of the other country, in this instance the patent laws or more specifically the patent infringement laws.

#### CONCLUSION

In conclusion, it must be observed that it would be perilous to adopt Mr. Stern's approach to territorial limitations in international licensing. It is not plausible to apply antitrust standards established for domestic purposes to situations involving patents granted and maintained under the laws of foreign countries where the standards may be totally different. In the international field there are many diverse problems and conflicts affecting the granting of patent license rights, and each must be dealt with under the laws of the individual country where they arise. In Europe, under the Common Market, and in Japan under its tightly government-regulated economy, the governments themselves are in effect partners with their nationals in many

business enterprises, and those governments have an interest in the use of inventions patented in their countries.

It has been pointed out that even the pioneers in the enforcement of U.S. antitrust laws have recognized the need for applying the Rule of Reason when considering the effect of combinations that may appear to be in restraint of trade. Based upon the economic necessities of the times there may be situations where this Rule favors a flexible application of competitive standards to the end that the efficiency of mass production is not destroyed, orderly marketing conditions are insured, and economic dislocations of great industries are avoided. If the legal bases of foreign governments—viz. the national boundaries of the patent rights which they grant—are to be ignored in favor of economics, at least those who choose thus to brush aside the laws of other nations should give some consideration to the possibility of killing the economic goose that lays the golden eggs of productivity and commerce. Before tampering with the normal, proper exercise of one's legal patent rights, and the licensing of those rights under the laws of each country which grants such rights, the Antitrust Division should be careful to weigh the possible adverse economic consequences in this country as well as in countries throughout the world where American industry does business.

# A Brief Reply to Some Criticisms of the Patent System

GEORGE E. FROST\*

IN ONE WAY OR ANOTHER, every patent system has involved the concept of what is "prior art" and some standard of accomplishment, in relation to the prior art, required to support a patent. These requirements seem inevitable if the patent is to be a right, and not simply an award given at the pleasure of the sovereign. The matter was well put by the Supreme Court in *U.S. v. American Bell Telephone Co.*, 167 U.S. 224, 250 (1897), where it is said:

. . . He [the inventor] does not determine the measure of his rights. The legislative body, representing the people, has declared what the public will give for the free use of that invention. . . . No representative of the public is at liberty to negotiate with him for a new and independent contract as to the terms and conditions upon which he will give up his invention. He must come under the dominion of the statute, and take that which the public has proffered its willingness to give. As the lawmaking power has prescribed what the public will give, specified the terms and conditions of purchase, indicated the time and methods of determining the right of compensation, he on his part has an absolute legal right to avail himself of all the provisions thus made. . . .

Almost every person—inventor, businessman, or lawyer—who has been concerned with patent protection has encountered instances

---

\* Patent Attorney, Detroit, Michigan.

*Editor's Note: We have asked several highly regarded patent attorneys to participate in a "Forum" to be published in IDEA directed to common criticisms of the patent system. They were asked to write brief replies to these criticisms, covering essentially two questions (1) Is the problem a real one—that is, is this issue real, significant and pervasive? (2) What remedies are proposed? As an example of the criticism, we referred the attorneys to an article by Frank M. Buttrick of the National Twist Drill & Tool Company, published in Industrial Research; however, we suggested that the replies published in Forum need not necessarily respond to Mr. Buttrick. This is the first of the series of comments by patent attorneys.*



where the prior art has frustrated attainment of what seems to be a proper reward. One recent example is the article by Frank M. Buttrick in *Industrial Research*, bearing the title "Are Patents Worth Their Cost?" (October 1970).

Mr. Buttrick, as many have done before him, deplors both the uncertainties and expenses involved in patent proceedings. He is not wholly kind to patent lawyers. But he does bring out the items that are beyond control of the lawyers, including the extent that effective patent rights rest on the fortuitous absence or presence of close prior art and the extent that it is not feasible exhaustively to examine the art at the early stages of patent proceedings.

There are at least two alternatives: One is an award system. On August 18, 1787, James Madison proposed to the Constitutional Convention a provision to authorize the Congress to "encourage by premiums and provisions" the making of inventions. The Congress has in fact done this in the Atomic Energy Act, which specifically provides for monetary rewards. It seems clear, however, that a general award system extending across all patentable subject matter entails too many administrative problems for consideration at present. See, e.g. Kaysen and Turner, *Antitrust Policy* (Harvard, 1959), p. 162.

The other alternative is government-financed research. Again, this has been done in specific fields. Congressional interest in aviation was reflected in the support given to Langley's experiments. In World War II, and since, government-financed military research has been enormously important. In many phases of agriculture, state and federal government financed research has been predominant for many years. Again, however, the alternative has its limitations. Most importantly, experience has demonstrated time and time again that the government aid does not necessarily go to the successful inventors, and that motivated individuals working without government support are often most productive. After all, it was the Wright brothers, not Langley, who made the first successful airplane.

And so we return to the patent system as the most generally applicable way to encourage the making and marketing of inventions. And until some creative individual comes forth with an alternative we will continue to face the problems of prior art.

The situation is not necessarily as dismal as it sounds. True, the President's Commission correctly emphasized the "exploding technology" in 1966. But this does not mean that the quantity of the prior art has some immediate prospect of wholly defeating the patent system. In my own experience, prior art seldom "pops out" from nowhere after

a reasonable search. It is important to distinguish what the facts are and what involved individuals think the facts are. Inventors often do not see what they don't want to see. Businessmen frequently share this failing. The result, too often, is that interested parties ignore the voices of caution—and fail to study adequately the prior art that is relatively handy. Not only this; but there is an almost irresistible tendency to seek patent claims that are too broad, coupled with refusal adequately to assess the true place of the invention in the art that is available. Inventor frustration with the patent system as it exists may have justification. But this does not demonstrate that there would be any less frustration with any feasible alternative.

## EDUCATIONAL ACTIVITIES

---

*We are bringing the following paper on management problems in the development of an invention to the attention of our readers to provide information on the experience of a leading development laboratory.*

### The Development and Management of University-Derived Inventions\*

JOHN L. GRAY\*\*

THE SUBJECT OF THIS PAPER is a discussion of the management problems during the phases involved in the development of an invention from its conception to a final useful product, based on our experience over the years with inventions from universities as well as other sources. It is important to remember at the outset that we are primarily concerned with two things—inventions and human resources. The inventions are extremely fragile in their embryonic condition; and, they need much loving, tender care to be converted, over a necessarily long

---

\* Talk given before the Council for Research Policy and Administration of the National Association of State University and Land Grant Colleges on November, 10, 1970, in Washington, D.C.

\*\* Vice President and General Manager, Battelle Development Corporation.

period of time, into a strong, mature, and useful condition. As the invention matures, the human resources involved, having differing skills and personalities, must be applied at precisely the proper period in the development. Thus, the true management role is the skilled application of these human resources to the maturing idea at certain critical periods in its development.

It must also be remembered that we are concerned with an extremely high-risk activity. A Booz, Allen & Hamilton study some years ago, which I believe is still valid today, indicated that for every 47 ideas that are funded for development by American industry, two reach the marketplace some seven to 15 years from the start, and one becomes a successful product.

This brings us to the time period involved. It is much longer than many people appreciate. James R. Bright, Professor of Technology and Associate Dean at the Graduate School of Business of the University of Texas, has written extensively on this subject and studied a number of different cases. As he so ably points out, the development time is usually upwards of ten years from conception to successful market penetration, and a quarter of a century is not uncommon. Professor Bright cites Xerography as an example of an invention requiring a quarter of a century from conception to successful market acceptance. Since this was a development of Battelle Development Corporation, we can corroborate the fact that it was approximately 25 years from Chester Carlson's conception of the basic invention of Xerography until the time that fairly large sums of royalty income were received by BDC and the inventor.

One of the most promising university inventions with which we are involved at the present time is Wirand\* Concrete. It was invented by Professor James P. Romualdi of Carnegie-Mellon University about eight years ago. This is a new material of construction and the field-trial period tends to take longer than might otherwise be the case. But, at the end of eight years, we are just starting to receive significant license fees. Earned royalty income may still be years away; and, the large use of this invention for highways and airport runways is probably as much as five to 15 years away. While these are just two examples in our own experience, I know that there are many others. Professor Bright has documented 30 or 40 cases which he has studied fairly carefully and which corroborate this time period.

The phases involved in the development of an invention can be

---

\* Trademark of Battelle Development Corporation.

described as including conception of the invention, reduction to practice, development of a prototype, arrangements with industry, commercial introduction, and widespread adoption. These phases are particularly pertinent to university-derived inventions. I intend to discuss the management activities during each of these phases, not differentiating whether the management is provided by a university, an organization such as Battelle Development Corporation or the ultimate industrial organization.

The conception of an invention is a mental act, usually depending upon the recognition of a need which must be satisfied. From a university management standpoint, one of the earliest things that must be done is to recognize that, in fact, an invention has been made. Many times the inventor will not appreciate that he has made an invention. Ideally, therefore, continuing surveillance of the creative work of the university in the areas likely to produce inventions, such as in the physical sciences, by one having an adequate level of skill in identifying inventions, is desirable. Record-keeping at this stage is of considerable importance also. Disclosures, preferably kept in a bound laboratory record book, witnessed and dated by someone who can understand the technology involved, is of extreme importance for possible future patent activity. Premature publication is another important factor to keep in mind in connection with university-derived inventions. While there is a one-year grace period in the United States from the time that a publication has been made to the time that the patent application must be filed, this is not generally available in the more important foreign countries where publication any place in the world prior to the filing of the patent application is an absolute bar to obtaining patent protection. On the other hand, if a U.S. patent application can be filed first followed by the publication in an appropriate technical journal, then foreign patent applications can be filed under the International Convention in most countries of interest within one year from the filing date of the U.S. patent application.

Whether the patent application is filed shortly after the invention is conceived is dependent upon whether sufficient information is available to enable the patent attorney to draft an adequate application. In a continuing development, quite often a patent application is filed as early as possible, and then additional information strengthening the inventive disclosure is added by means of a continuation-in-part patent application.

From a management standpoint, an additional consideration at this phase of the development of the invention is the question of ownership.

If the funds of certain government agencies or other organizations have been involved, it is quite possible that the ownership of the invention will be determinable at this time.

The next major phase involved is the reduction to practice of the invention. This occurs when the mental act of invention conception has actually been reduced to some sort of physical form which involves the practice of the invention. Again, dated, witnessed records are of considerable importance for later patent activities. Also, again depending upon the source of funds used in reducing the invention to practice, a determination of ownership could be made at this time. Usually, it is now appropriate to evaluate the invention to determine its ultimate commercial potential although such an evaluation can occur earlier or later, depending upon the nature of the invention. Since the university must necessarily have an invention conceived by its staff enter the marketplace through an industrial manufacturer, licensing is the usual mode employed, and patentability becomes of considerable interest. Therefore, in evaluating an invention, the scope of patent protection likely to be obtained is of extreme importance. Also considered at this time is technical-economic feasibility in its broadest sense. Tied in with this is the market—whether the size justifies the necessary future investment, how the market can be penetrated, and what competition, if any, exists. These are the three major categories reviewed in evaluating an invention.

For the past several years, BDC has been evaluating approximately 1,000 inventions annually, and has spent about \$200,000 each year doing this. This expenditure is purely for evaluation and does not include developmental funding or patent prosecution.

In actually performing these evaluations, BDC draws on the four Battelle laboratories with a total staff of about 6,000. Most of the technical disciplines are available in-depth in these laboratories; and, where they are not, we have arrangements with numerous consultants. Staff patent attorneys, as well as outside patent counsel, are retained. BDC can draw also on the technical-economic groups of the laboratories, as well as outside market specialists. BDC's extensive contacts with industry are very useful in getting a real-world fix on the value of the invention, as are the comments of consultants on occasion.

The next major phase involves the development of a prototype. The extent of this activity and the cost of funding in developing a prototype will depend directly on the invention. The objective of the university, or some other development organization such as BDC, is to develop technical information and assurance of ultimate patent protection to

the point that the invention can be licensed to industry, because industry is the vehicle by which this product is to be made available so that the public can buy and enjoy it. The kind of people that become involved in the development of the invention can change at this point. Sometimes it is desirable that the inventor no longer be involved. Quite often his lack of objectivity and emotional attachment to the invention, which is really "his child," prevents the successful development of the prototype. However, sometimes a combination of the inventor working with persons having more of an applied research outlook is desirable. For example, we have an invention involving the use of a classical herbicide which, when applied in minute subtoxic quantities, increases the protein content of forage crops instead of having a lethal effect, especially in cases where the soil is not particularly fertile. In order to obtain appropriate application rates of the material, new concepts in slow-release technology had to be developed. A cooperative program was developed with greenhouse and field work in various parts of the world directed by the inventor, while the complementary project on methods to achieve controlled-release rates, which may be important to the ultimate practical success and adoption of the invention, was carried on in Battelle's Columbus Laboratories.

Project management becomes important at this stage. People who think in applied-research terms and who have experience in this area are needed. Research planning and management is needed. Goals and schedules must be established and kept. Performance must be measured.

During this period, arrangements will either have been made or negotiations will start with industry. Consequently, these phases may overlap. Historically, BDC has usually invested between \$35,000 and \$600,000 before it consummates a business arrangement with an industrial organization for the further development and ultimate manufacturing and marketing of the subject matter of the invention. The nature of the arrangement varies depending upon the nature of invention, stage of development, and the continuing investment that must be made. In some cases, nonexclusive licenses are employed, in some cases exclusive licenses, and in some cases an equity position. I will discuss all three alternatives.

In the case of a fully developed invention, nonexclusive licenses usually result in the greatest possible use of the invention and the greatest return to the inventor. The licenses are easy to negotiate and, in some cases, a printed form may be used. A nonexclusive license is not at all practical if there is a significant, continuing developmental phase involved. Exclusive licenses quite often are used:

- (1) Where there is still a certain amount of risk involved in the development of the invention;
- (2) Where a large, further investment is required on the part of the licensee; and
- (3) Where nonexclusive licenses would not be attractive to prospective licensees. Even here, however, quite often the licenses are limited as to period of time.

In some cases, an equity position is desirable. One of the most difficult things to do in the development of a new technology is to have the life of the basic patents commensurate with the useful enjoyment of the invention. For example, the basic patent on the electropolishing of stainless steel, invented by Dr. Charles Faust and owned by the Battelle Development Corporation, expired at about the time large-scale usage of the invention was realized. Perhaps the most dramatic return to the inventor or university is obtained when a new technology is injected into an existing corporation which radically changes the size and profitability of that corporation, and payment is made in the stock of that corporation. This, of course, is the story of the Haloid Corporation, later known as the Xerox Corporation. Sometimes the technology is so new and the payoff is so far away that the only organizations with the money and management available are large companies. In such a case, the patent owner would not be interested in obtaining an equity position in the large company because there are too many other factors which could affect the price of the equity other than the invention being brought to the company. In this case, it sometimes is desirable to create a new corporation whose value would be tied directly into the success or failure associated with the invention in question. It is difficult, but important, to inculcate into the management of this corporation the same commitment and desire that might be found in a smaller, existing corporation.

Commercial introduction is the next significant phase in the development of the invention, and the interface between applied research and development and commercial production is an extremely difficult one to bridge. The technologists who are applied-research oriented hate to let go of the development because they know they can always improve it even though with diminishing value. Different personalities and different skills are needed at this stage, and this is probably one of the most radical periods of change in human resources in the entire development of the invention.

The next phase involves the widespread adoption of the invention. As I mentioned, it is important to have this occur within the life of the



patents. Even in the case of xerography, the basic patents had only a few years of life remaining when the major market acceptance was reached, but the secondary patent structure was of considerable value.

Lastly, in those cases when success is achieved and income is received on university inventions which have been developed under an invention development agreement with the Battelle Development Corporation, a percentage of the income received immediately goes to the university. The university may designate that the inventor shall receive all or part of this percentage. The same percentage is retained by BDC, and the balance is used to reimburse BDC for its expenditures. After BDC has been completely reimbursed, the remaining income is divided equally between the university and BDC.

In summary, therefore, the development of inventions and their management involves the nurturing of fragile ideas, through the effective use of people with differing skills, to a stage where they become products or processes useful to society. The time span is long and the risk is high, but the rewards, both in financial return and in the sense of achievement, can be great.



## STUDENT PAPERS

---

---

By making available student papers, students will receive an incentive and our readers will appreciate the evidence of scholarly development in the fields of interest. These papers are carefully reviewed by the Editorial Committee and other specialists, and helpful suggestions are made to the students as part of the educational function of *IDEA*. The Research Institute invites educational and research institutions to submit informative student manuscripts on the patent, trademark, copyright, and related systems.

### Shapiro, Bernstein & Co. v. Goody Revisited: Judicially Sanctioned Restraint on Alienation and Double Satisfaction\*

JOEL M. FREED

#### INTRODUCTION

In *Shapiro, Bernstein & Co. v. Goody*,<sup>1</sup> the Second Circuit Court of Appeals addressed the problem of liability in the distribution chain of unauthorized<sup>2</sup> phonograph records and concluded that "a seller of unauthorized records of copyrighted music, although *having no con-*

---

\* This paper was chosen to represent Georgetown University in the 1970 Patent Office Society Student Award Competition, which is conducted annually under the aegis of The PTC Research Institute. It has also been awarded Georgetown University Law Center's first prize in the 1970 Nathan Burkan Memorial Copyright Competition which is sponsored annually by the American Society of Composers, Authors & Publishers. The author is a member of the firm of Burns, Doane, Swecker & Mathis, Washington, D. C.

<sup>1</sup> 248 F.2d 260 (2d Cir. 1957) [hereinafter cited as *Goody*], *rev'g* *Miller v. Goody*, 139 F. Supp. 176 (S.D.N.Y. 1956), *cert. denied*, 355 U.S. 592 (1958).

<sup>2</sup> This paper deals only with the *Goody* litigation insofar as statutory protection is afforded in connection with unauthorized records.

nection with the manufacturer,<sup>3</sup> is an infringer and liable for damages which the Act<sup>4</sup> provides,<sup>5</sup> and that “[s]ince the liability of [manu-

<sup>3</sup> There appears to be at least some question under the facts of *Goody* as to whether the seller was in any way “connected” with the manufacturer, if the word *connected* is deemed to have “good” or “bad” faith connotations. See the opinion of the court below in *Miller V. Goody*, 139 F. Supp. 176, 178 (S.D.N.Y. 1956). Nevertheless, both courts felt that this point was not relevant to a decision.

<sup>4</sup> The Copyright Act, 17 U.S.C. § 1 *et seq.* (1964) (hereinafter referred to as the Copyright Act or the Act), provides in relevant part as follows:

§ 101 *Infringement*

(e) *Royalties for Use of Mechanical Reproduction of Musical Works.*—Whenever the owner of a musical copyright has used or permitted the use of the copyrighted work upon the parts of musical instruments serving to reproduce mechanically the musical work, then in case of the infringement of such copyright by the unauthorized manufacture, use or sale of interchangeable parts, such as discs, rolls, bands, or cylinders for use in mechanical music-producing machines adapted to reproduce the copyrighted music, no criminal action shall be brought, but in a civil action an injunction may be granted upon such terms as the court may impose, and the plaintiff shall be entitled to recover in lieu of profits and damages a royalty as provided in section 1, subsection (e), of this title: *Provided also*, That whenever any person, in the absence of a license agreement intends to use a copyrighted musical composition upon the parts of instruments serving to reproduce mechanically the musical work, relying upon the compulsory license provision of this title, he shall serve notice of such intention, by registered mail, upon the copyright proprietor at his last address disclosed by the records of the copyright office, sending to the copyright office a duplicate of such notice; and in case of his failure to do so the court may, in his discretion, in addition to sums hereinabove mentioned, award the complainant a further sum, not to exceed three times the amount provided by section 1, subsection (e) of this title, by way of damages, and not as a penalty, and also a temporary injunction until the full award is paid.

§ 1 *Exclusive Rights as to Copyrighted Works*

(e) To perform the copyrighted work publicly for profit if it be a musical composition; and for the purpose of public performance for profit, and for the purposes set forth in subsection (a) hereof, to make any arrangement or setting of it or of the melody of it in any system of notation or any form of record in which the thought of an author may be recorded and from which it may be read or reproduced: *Provided*, That the provisions of this title, so far as they secure copyright controlling the parts of instruments serving to reproduce mechanically the musical work, shall include only compositions published and copyrighted after July 1, 1909, and shall not include the works of a foreign author or composer unless the foreign state or nation of which such author or composer is a citizen or subject grants, either by treaty, convention, agreement, or law, to the citizens of the United States similar rights. And as a condition of extending the copyright control to such mechanical reproductions, that whenever the owner of a musical copyright has used or permitted or knowingly acquiesced in the use of the copyrighted work upon the parts of the instruments serving to reproduce mechanically the musical work, any other person may make similar use of the copyrighted work upon the payment to the copyright proprietor of a royalty of 2 cents on each such part manufactured, to be paid by the manufacturer thereof; and the copyright proprietor may require, and if so the manufacturer shall furnish, report under oath on the 20th day of each month on the number of parts of instruments manufactured during the previous month serving to reproduce mechanically said musical work, and royalties shall be due on the parts manufactured during any month upon the 20th of the next succeeding month. The payment of the royalty provided for by this section shall free the articles or devices for which such royalty has been paid from further contribution to the copyright except in case of public performance for profit. It shall be the duty of the copyright owner, if he uses the musical composition himself for the manufacture of parts of instruments serving to reproduce mechanically the musical work, or licenses others to do so, to file notice thereof, accompanied by a recording fee, in the copyright office, and any failure to file such notice shall be a complete defense to any suit, action, or proceeding for any infringement of such copyright.

In case of failure of such manufacturer to pay to the copyright proprietor within thirty days after demand in writing the full sum of royalties due at said rate at the date of such demand, the court may award taxable cost to the plaintiff and a reasonable counsel fee, and the court may, in its discretion, enter judgment therein for any sum in addition over the amount found to be due as royalty in accordance with the terms of this title, not exceeding three times such amount.

The reproduction or rendition of a musical composition by or upon coin-operated machines shall not be deemed a public performance for profit unless a fee is charged for admission to the place where such reproduction or rendition occurs.

<sup>5</sup> 248 F.2d at 264 (emphasis added).

facturer and seller] is several and independent, it follows that the [seller] may not claim that any part of [the manufacturer's] payment . . . reduces [the seller's] liability. . . ."<sup>6</sup> However, the court limited recovery against the seller to 2 cents per record and declined to recognize the possibility of an additional "discretionary allowance not to exceed the royalty trebled."<sup>7</sup>

It is the purpose of this paper to explore each of the above holdings and to examine their validity from the standpoint of public policies against multiple recovery<sup>8</sup> and restraints on alienation,<sup>9</sup> as well as to determine whether the relevant statutes are amenable to a construction<sup>10</sup> consistent with these policies.

### THE BASIS AND RAMIFICATIONS OF THE DECISION

It is interesting to note that both the district court and the court of appeals based their irreconcilable decisions upon the duty of a court to refrain from legislating.<sup>11</sup> Application of the well settled rule that where the terms of the statute are clear, there is little if any room for interpretation may not have ever been undertaken in circumstances wherein a statute was more ambiguous than the one involved in the subject litigation. In connection with a consideration of a suggested statutory interpretation attempting to resolve this apparent ambiguity, a closer look at the meanings ascribed to the allegedly "clear" statutory terms by the two courts involved may be worthwhile.

---

<sup>6</sup> 248 F.2d at 267. It is important to note that although the court did not deem it relevant to its decision, there was a question as to whether the total amount of the plaintiff's settlement with the manufacturer, or any part thereof, was classifiable as a royalty paid by the manufacturer. Compare *id.* at 262 with *id.* at 268. See notes 51-53 *infra* and accompanying text.

<sup>7</sup> 248 2d at 266.

<sup>8</sup> See notes 46-59 *infra* and accompanying text.

<sup>9</sup> See notes 60-68 *infra* and accompanying text.

<sup>10</sup> See Conclusion *infra*.

<sup>11</sup> Judge Kaufman stated that:

Where the legislative mandate is clear, as is the case here, judges are bound to follow the law scrupulously regardless of personal preference, and the rule of strict adherence to the statute is never so necessary as where the legislature has established what it considered to be a comprehensive regulatory scheme as it did in the case of mechanical reproduction of music. For a judge to attempt to qualify or amplify the rights Congress delineated in such detail would be both imprudent and improper. 139 F. Supp. at 186-87.

Judge Hincks, writing for the court of appeals, agreed with Judge Kaufman that:

[I]t is only for Congress to decide whether the protection and control afforded the proprietor is "fair" or "adequate" either from the private or the public viewpoint, or is the best possible balance between private and public interests. 248 F.2d at 268.

The relevant facts of the *Goody* case may be capsulized as follows: Joseph Krug, an original defendant not involved in the litigation at the appellate level, commenced unauthorized manufacture and sale of records, including copyrighted selections, and failed to file a notice of intent to use and to make payments of statutory royalties as required by the Copyright Act, 17 U.S.C. §§ 1 (e) and 101 (e). The dealer-defendant, Sam Goody, became a customer of Krug. Whether or not Goody was aware of non-compliance by Krug with the statute is disputed.<sup>12</sup> The copyright proprietor commenced action against Krug and Goody for copyright infringement, the former proceeding ending in a monetary settlement releasing Krug and specifically reserving rights against all others.<sup>13</sup>

The plaintiffs thereafter sought, through motion for summary judgment, recovery under § 101 (b) of Title 17 of the United States Code.<sup>14</sup>

### *The Lower Court Opinion*

Noting that the Copyright Act of 1909 did not in any way affect the holding of *White-Smith Music Publishing Co. v. Apollo Co.*<sup>15</sup> that a record is not a "copy" within the meaning of the copyright statute, Judge Kaufman went on to discuss the protection accorded copyright proprietors in the area of records by reason of 17 U.S.C. § 101 (e).

<sup>12</sup> See note 3 *supra*.

<sup>13</sup> The monetary settlement was stated in terms of compensation for "costs and expenses incurred by the plaintiffs . . . in their proceedings" against Krug. 248 F.2d at 267; 139 F. Supp. at 179.

<sup>14</sup> 17 U.S.C. § 101 (b) (1964) provides:

(b) *Damages and profits; amount; other remedies.*—To pay to the copyright proprietor such damages as the copyright proprietor may have suffered due to the infringement, as well as all the profits which the infringer shall have made from such infringement, and in proving profits the plaintiff shall be required to prove sales only, and the defendant shall be required to prove every element of cost which he claims, or in lieu of actual damages and profits, such damages as to the court shall appear to be just, and in assessing such damages the court may, in its discretion, allow the amounts as hereinafter stated, but in case of a newspaper reproduction of a copyrighted photograph, such damages shall not exceed the sum of \$200 nor be less than the sum of \$50, and in the case of the infringement of an undramatized or nondramatic work by means of motion pictures, where the infringer shall show that he was not aware that he was infringing, and that such infringement could not have been reasonably foreseen, such damages shall not exceed the sum of \$100; and in the case of an infringement of a copyrighted dramatic or dramatico-musical work by a maker of motion pictures and his agencies for distribution thereof to exhibitors, where such infringer shows that he was not aware that he was infringing a copyrighted work, and that such infringements could not reasonably have been foreseen, the entire sum of such damages recoverable by the copyright proprietor from such infringing maker and his agencies for the distribution to exhibitors of such infringing motion picture shall not exceed the sum of \$5,000 nor be less than \$250, and such damages shall in no other case exceed the sum of \$5,000 nor be less than the sum of \$250, and shall not be regarded as a penalty. But the foregoing exceptions shall not deprive the copyright proprietor of any other remedy given him under this law, nor shall the limitation as to the amount of recovery apply to infringements occurring after the actual notice to a defendant, either by service of process in a suit or other written notice served upon him. [Exemplified amounts omitted.]

<sup>15</sup> 209 U.S. 1 (1908).

Plaintiff had argued that since manufacturer Krug did not file the requisite notice under § 101 (e), the general infringement portions of the statute (particularly the minimum damage section 17 U.S.C. § 101 (b)), became applicable.<sup>16</sup> The court's negative response to this position involved two points.

First, insofar as records are concerned, infringement as defined in § 101 (e) referred to "unauthorized manufacture, use, or sale" in the same phrase. Assuming that a seller who became an infringer by reason of § 101 (e) was liable under § 101 (b), the same would necessarily be true of an infringing manufacturer, thereby reaching the result of giving "to the musical copyright proprietor a greater choice in his type of recovery than is given to any other copyright holder."<sup>17</sup> As pointed out by the court: "Such a conclusion would be wholly inconsistent with the legislative purpose of giving only limited rights against mechanical reproduction of music."<sup>18</sup>

Secondly, since § 1 (e) and § 101 (e) note circumstances in which a royalty in connection with unauthorized recording may be trebled, any initially possible inference that Congress intended such infringement to be treated under § 101 (b) is negated. As the court concluded, those clauses would have been unnecessary; Congress, if it desired the result urged, would merely have had to call a recording a copy or to provide for compulsory licensing, with non-licensees being liable for ordinary infringement.<sup>19</sup>

Of more particular interest, by reason of the fact that at the appellate level the plaintiffs prevailed in the theory that §§ 1 (e) and 101 (e) justified recovery against the seller of unauthorized records, is the treatment by Judge Kaufman of the abstract question of liability in connection with unauthorized sellers. The defendant had apparently argued that § 101 (e) should be construed as applicable only to unauthorized manufacturers. Plaintiffs responded with the argument that such a construction would effectively eliminate the words "use or sale" from that portion of § 101 (e) referencing "infringement of such copyright by the unauthorized manufacture, use or sale of [records]."

This dilemma was never reconciled by Judge Kaufman.<sup>20</sup> Neverthe-

---

<sup>16</sup> 139 F. Supp. at 184.

<sup>17</sup> *Id.* at 185.

<sup>18</sup> *Id.*

<sup>19</sup> *Id.*

<sup>20</sup> Apparently Judge Kaufman's failure to attribute any meaning to the terms "use or sale," appearing in the portion of the statute referring to "manufacture, use or sale," strongly influenced the reversal by the Court of Appeals. See text accompanying note 38 *infra*.

less, he determined that the defendants were not liable primarily because

[h]ad there been no consent decree, and had Krug subsequently become a compulsory licensee, the records sold by defendants herein would have lost their status as infringing records. Indeed, by the terms of plaintiffs' own argument, had Krug filed notice and not paid the royalties, the records would still have lost infringing status at least to the extent that the only protection against them would then be that accorded under the mechanical reproduction sections and limited to recovery from the manufacturer. It is difficult to believe that Congress intended to hinge such huge differences in consequence on a paper distinction; moreover, Congress could hardly have intended to create a seller's liability totally dependent on the manufacturer's surface intent. It would be illogical to rule that a seller may at any time be sued as an infringer when he has no control over the status of the records involved. The copyright law must be read to have general application, and if it had been intended ever to apply to a non-manufacturing seller it would provide, as a matter of good drafting, for a set point in time when the seller does become liable, and set conditions for suit would be prescribed which would not rest wholly upon the actions of others. Clearly, the type of liability formula necessary is one which would have to be devised by the legislature, not imposed on an ad hoc basis by the judiciary, and to impose liability against sellers generally without some such formula would be contrary to Congress' clear purpose to impose primary [if not sole] liability on the manufacturer of infringing records.<sup>21</sup>

It is thus clear that Judge Kaufman's decision in this regard was based on concern with two issues. First, even though there was some question as to the innocent intent of the seller under the facts of the case before him, he was unwilling to construe the statute in a manner which would treat innocent sellers in the distribution chain in the same manner as those with tainted backgrounds. As will be discussed below, the court of appeals felt quite differently on this issue, analogizing the situation to the general copyright infringement rule that treats the question of infringement separately from the question of intent.

However, Judge Kaufman, in noting that the case before him was a proper one for summary judgment, stated that

[t]he two dealer defendants herein admit in their brief that "the sale or vending of an unauthorized copy of a copyrighted article by anyone is an infringement of the copyright irrespective of the position of the vendor in the distributive process, his bona fides, his innocence, or the unknown peril to which he may have been subjected." And this is undoubtedly the law.<sup>22</sup>

Although this statement appears superficially to make Judge Kauf-

---

<sup>21</sup> 139 F. Supp. at 184.

<sup>22</sup> *Id.* at 180 (citations omitted).



man's opinion internally inconsistent, it must be recognized that Judge Kaufman was not stating that innocence relieved one from liability for infringement. Rather he was stating that since it would be inequitable to treat the innocent seller as an infringer in *all* cases, some other construction of the statute is required, *i.e.* one which at least necessitates first instance recourse to the manufacturer in the case of unauthorized records.

The second and somewhat related point implicit in Judge Kaufman's position, relates to the statutory proscription against restraints on alienation at least where a manufacturer files a notice of intent to use.<sup>23</sup> It is thus apparent that in his due concern for the innocent vendor of unauthorized records, Judge Kaufman cleared the way for the bad faith vendor to interpose himself in the chain of distribution of unauthorized records with impunity since, by his own admission Judge Kaufman stated that the innocence of Goody was immaterial.

Furthermore, through his concern over restraints on alienation, Judge Kaufman left the copyright owner totally without a remedy in instances where the manufacturer was unavailable.<sup>24</sup>

### *The Court of Appeals Opinion*

For convenience, the court of appeals opinion shall be analyzed in the same order of consideration of issues as set forth therein. The relevant facts are set forth above.

---

<sup>23</sup> Judge Kaufman construed the statute as proscribing restraints on alienation also in instances wherein a notice of intent to use is filed subsequently to manufacture of the records. The court of appeals, however, noted that:

[t]o declare that a royalty payment frees the record from further contribution (§ 1(c)) is a far cry from saying that the payment exonerates any and all prior infringers from liability already accrued. 248 F.2d at 265. See note 32 *infra* and accompanying text.

<sup>24</sup> The only contrary indication negating this conclusion is the previously quoted statement concerning "Congress' clear purpose to impose *primary* [if not sole] liability upon the manufacturer of infringing records." 139 F. Supp. at 184 (emphasis added). Judge Kaufman's subsequent discussion reconciling §§ 1(e) and 101(e) with § 101(b) does, however, clearly show that his opinion was broader based than requiring only first instance recourse to the manufacturer. For example, he later stated that:

According to plaintiffs' construction, the proprietor may recover royalties and damages from the infringing manufacturer, and then minimum damages or actual damages from any distributors of the infringing records, no matter how innocent their intent. This is basically the protection accorded against copying. . . . *Id.* at 185 (emphasis added).

Since this appears to have strongly influenced Judge Kaufman's decision, it bears some further analysis. It is believed that, at least today, this is a misstatement of the law. See text accompanying note 51 *infra*.

Judge Hinks, writing for the court of appeals, stated the question presented as follows:

Does . . . the Copyright Act . . . provide copyright owners with a remedy against non-manufacturing sellers of unauthorized phonograph recordings of copyrighted songs?<sup>25</sup>

As a starting point, this question seems to suffice. Unfortunately, after answering the question in the affirmative, the court of appeals felt no obligation to explore whether or not that remedy applied against *all* non-manufacturing sellers: regardless of their position in the chain of title, regardless of the status of their intent, and regardless of prior remedies. As discussed below, one of the major faults of the decision lies in this failure.

Prior to a detailed analysis of the positions of the parties, the court of appeals noted that § 101 (e) discusses infringement in connection with “unauthorized manufacture, use, or sale” and

directs “any person” who in the absence of a license agreement, intends to use the copyrighted music, once it has been licensed to another, to serve notice to that effect on the copyright owner thereof and the copyright office;

without further ado, it was stated that

[a] natural reading of these sections leads us to the conclusion that a seller of unauthorized records of copyrighted music, although having no connection with the manufacturer, is an infringer and liable for damages which the Act provides.<sup>26</sup>

The basic issue before the court insofar as it is affected by the term “manufacture, use or sale” is subsequently treated. At this point, it is helpful to note that the court’s reference to “any person” as utilized in § 1 (e) fails to stress that the “any person” referred to is statutorily specified as “any person . . . *relying upon the compulsory license provision of this Title. . .*” This provision § 1 (e), specifies that:

[W]henever the owner of a musical copyright has used or permitted or knowingly acquiesed in the use of the copyrighted work . . . any other person may make similar use of the copyrighted work upon the payment to the copyright proprietor of a royalty . . . *to be paid by the manufacturer. . .*<sup>27</sup>

---

<sup>25</sup> 248 F.2d at 262.

<sup>26</sup> *Id.* at 264.

<sup>27</sup> 17 U.S.C. § 1 (e) (1964) (emphasis added). In a subsequent portion of the opinion, the court, seemingly inconsistently, strongly implies that since the “any person” referred to in § 101 (e) must be a manufacturer, the remedy which is found to exist in connection with sellers does not include royalty trebling provisions. See text accompanying note 40 *infra*.

It seems relatively clear, that the term "any person" as used in § 101 (e) is not inclusive of sellers or users to the extent that manufacturing activity is not involved. As such, the term does not lend such support to the ultimate conclusion as the court would seem to imply.

Nevertheless, the court was quite correct in emphasizing that the statute, by its terms, includes users and sellers as infringers.

Appellee's argued that the word "sale" must be eliminated from the statute as inconsistent with the basic purpose of the compulsory licensing scheme, by reason of the injustices that may ensue from a failure to do so. In response, the court cited *F. W. Woolworth, Co. V. Contemporary Arts, Inc.*<sup>28</sup> for the proposition that the absence of control by sellers over their suppliers' compliance with the Copyright Act does not relieve the seller from liability. Recognizing that records are not copies within the meaning of the act, the court refused to depart from its characterization of the *Woolworth* holding since § 101 (e) specifies unauthorized sale as infringement. It suffices to say, at this juncture, that the hereinafter suggested statutory interpretation is not at odds with the court of appeals position on this point. However, as hereinafter discussed, the establishment of an infringing act does not automatically result in monetary liability of the infringer.<sup>29</sup>

Appellees, relying upon Judge Kaufman's opinion, argued that since a filing for compulsory license by the manufacturer would free the records from their infringing status, "it would be anomolous to hold the seller liable."<sup>30</sup> The appellate court, however, was of the opinion that:

To declare that a royalty payment frees the record from further contribution (§ 1 (e)) is a far cry from saying that the payment exonerates any and all prior infringers from liability already accrued.<sup>31</sup>

Insofar as the quoted statement may be interpreted as indicating (1) that statutory royalty payment by a manufacturer does not affect his liability in connection with previously manufactured records not authorized, or (2) that a payment for previously manufactured and unauthorized records does not erase a previous *infringing act* of a seller, the statement appears undoubtedly correct. Nevertheless, insofar as it is implied that monetary liability of a seller is mandatory (regardless of prior recovery by way of settlement or otherwise from the manufacturer or from other sellers), the statement is inconsistent with

---

<sup>28</sup> 344 U.S. 228 (1952).

<sup>29</sup> See text accompanying notes 51-53 *infra*.

<sup>30</sup> 248 F.2d at 264.

<sup>31</sup> *Id.* at 265.

basic public policy against restraints on alienation and basic public policy against double recovery.<sup>32</sup>

Regarding appellee's argument that a remedy against a seller of unauthorized records is applicable, if at all, only by the way of injunction, the court stated that:

[T]he reference in § 101 (e) to the "royalty as provided in" § 1 (e) was intended to limit not the class of potential defendants but only the amount of the royalty.<sup>33</sup>

The correctness of this conclusion was supported by the fact that the unauthorized manufacturer-defendant under § 101 (e) could never be the same person as the authorized manufacturer-defendant under § 1(e). Thus, the term "royalty as provided in" § 1 (e) necessarily had reference to amount rather than particular defendants. Moreover, that phrase follows words of recovery in the statute rather than words of liability. This reasoning<sup>34</sup> leaves little room for argument.

Appellant's next contention gave rise to the sole substantial point upon which the court of appeals agreed with Judge Kaufman. In determining that recovery against a seller of unauthorized records must be measured under § 101 (e), if at all, rather than under § 101 (b), the court considered that since § 101 (e) was specifically directed to records, any conflict arguably presented by § 101 (b) should be resolved in favor of the specific and chronologically later statutory section.<sup>35</sup> Moreover, the court noted that § 1 (e), to which § 101 (e) has reference as a measure of recovery,

was a form of statutory compensation which by its very nature measures the damages resulting from its non-payment. . . . Since, under

---

<sup>32</sup> See section on "Public Policy Objections—" *infra*.

Although the court's position is unclear as to whether a record is freed from contribution only in cases wherein the statutory royalty was paid pursuant to a compulsory license in the absence of a suit for recovery, it is possible to interpret the court's opinion as indicating that a belated payment of royalty by the manufacturer frees the record from all *future* (compare the statutory term "further" in § 1(e)) contribution even though it may not be considered as extinguishing liability for past infringement. 248 F.2d at 267. Although future restraints on alienation are thereby eliminated, the absence of retroactive effect on past sales is tantamount to authorizing restraints on alienation insofar as the copyright infringer may await ultimate consumer purchase before commencing suit at which time each seller (and presumably the ultimate user because the statute defines use as infringement) may be held liable for 2 cents per record. Imposing such liability for alienation is, of course, indistinguishable for present purposes from authorizing its restraint.

<sup>33</sup> 248 F.2d at 265.

<sup>34</sup> *Id.*

<sup>35</sup> *Id.* at 266.

the statutory scheme recovery of the statutory royalty afforded the measure of compensation which Congress contemplated for the owner, the difficult problem of proof which is presented in cases [under § 101 (b)] not controlled by a royalty does not arise and there is hence no need in such cases for the application of . . . [the] § 101 (b) [provisions]. . . .<sup>36</sup>

While clearly illustrating the correctness of the court's conclusion as to the non-applicability of § 101 (b), the court's delineation of the provisions of § 1 (e) as "a form of statutory compensation" that ends the question of "damages" establishes, without specifically intending to do so, what is believed to be the primary argument against its sweeping holding: that all sellers of unauthorized records are not only infringers but are monetarily liable in all cases for that infringement. It appears that at least in instances where that statutory damage has been satisfied—and admittedly there was a question in *Goody* as to whether the settlement with Krug constituted, in part, satisfaction of the damages—a subsequent recovery of that damage is improper. This point is discussed more fully below.<sup>37</sup>

The court dismissed the question of settlement having effect on recovery against the seller by characterizing the seller's liability as "several" rather than "joint."<sup>38</sup> Reliance for this characterization was placed upon the use of the alternative "or" in the definition of infringement by unauthorized "manufacture, use or sale." As herein-after pointed out, such characterizations are, in the opinion of the Supreme Court, irrelevant to the issue of satisfaction.

It is interesting to note that in addition to holding that a seller is liable regardless of settlement with others, the court limited recovery against the seller to 2 cents in answering the following question:

Does the owner's recovery against the seller, like his recovery against the manufacturer, include in addition to the 2¢ royalty a discretionary allowance not to exceed the royalty trebled, or is it limited to the 2¢ royalty?<sup>39</sup>

The court's treatment of the issue is best examined with reference to the following quotation:

As to this, we hold that the recovery against a seller is limited to 2¢ per record. Certainly in the first part of § 101 (e), which casts liability for infringement upon sellers, there is no provision for addition to the award of a sum comprising the royalty trebled: the provision therein contained for allowance against the seller of "a royalty

---

<sup>36</sup> *Id.* at 265-66 (emphasis added).

<sup>37</sup> See text accompanying note 57 *infra*.

<sup>38</sup> 248 F.2d at 267.

<sup>39</sup> *Id.* at 266.

as provided in section 1, subsection (e)" points solely to that part of § 1(e) which creates a statutory royalty of 2¢, not to the next to the last paragraph in § 1(e) which gives the court discretion to increase the award by the royalty trebled. The language providing for a recovery against the seller of "a royalty" is scarcely adequate to provide a recovery of a sum amounting to the royalty plus the royalty trebled. Moreover, the proviso which comprises the second part of § 101(e) is limited to a person who "in the absence of license agreement, *intends to use* a copyrighted musical composition upon parts of instruments . . . , relying upon the compulsory license provision of this title." The language of this limitation is apt for application to a manufacturer, but scarcely applicable to a dealer who generally does not *intend to use a composition upon the parts of instruments*, etc. Indeed, if the enlarged recovery created by the proviso was intended, like the remedy provided in the first part of § 101(e), to apply to sellers as well as to manufacturers, the limitation of the proviso, quoted above, would have been entirely redundant.<sup>40</sup>

An analysis of this reasoning must begin with a note that it seems strange that the court did not seek an interpretation of the statute which would permit the trebled discretionary allowance as against bad faith sellers.

As to the court's reasoning, it will be recognized that the reference in the first part of § 101(e) to the statutory royalty of 2 cents as set forth in § 1(e) may have been just as readily interpreted as applicable to the financial consequences for failure to pay the royalty as well as to the royalty itself. Although such consequences are worded in terms of failure of a manufacturer to pay the royalty, the court had previously found that the use of the term manufacturer in § 1(e) did not place a limitation on persons liable by reason of § 101(e).<sup>41</sup>

Moreover, the court's subsequent statement that the language "a royalty" should be deemed inadequate to include the royalty trebling provisions (presumably on the basis of strict construction of statutes where penalties are involved) failed to account for the fact that the trebling provision is discretionary in § 1 and would be discretionary if carried over into § 101. This would obviate any rigid applicability in instances of good faith sellers. Strict construction of statutes against penalties should be limited to instances where such a construction would absolutely, and not discretionarily, render a presumably "innocent" party liable for the penalty.

Finally, it was possible for the court, without rendering the Act

<sup>40</sup> *Id.*

<sup>41</sup> See text accompanying note 34 *supra*.

ambiguous, to apply the proviso trebling provisions of § 101 (e) to bad faith sellers. Their choice to refrain from so doing on the ground that the language is applicable to manufacturers "but scarcely applicable to a dealer" is somewhat puzzling. Neither a manufacturer nor a dealer really intends to "use," as the court interprets the word, the copyrighted musical composition upon parts of instruments serving to reproduce mechanically the musical work since the word "reproduction" as used throughout the statute seemingly does not refer to the "reproduced" records, but instead refers to the reproduction of the music.<sup>42</sup> The dual statutory placement of the word "use" before "the copyrighted work" or "copyrighted musical composition" supports this proposition.<sup>43</sup> At any rate, even if the language by its terms appears to extend only to a manufacturer, the previous construction of the first portion of § 101 (e) as incorporating the trebled provisions of § 1 is still applicable.

As the court indicated, there might be a redundancy in the statute if the proviso was intended to cover sellers as well as manufacturers.<sup>44</sup> This apparent redundancy could be eliminated by interpreting the proviso as extending permission to sellers to file a notice of intent to use so as to escape liability regardless of the manufacturer's nonpayment.

#### PUBLIC POLICY OBJECTIONS TO THE APPELLATE DECISION

##### *Double Recovery*

As previously noted, the appellate decision in *Goody* specifically authorizes at least a double recovery of 2 cents per record that it terms as "a form of statutory compensation which by its very nature meas-

---

<sup>42</sup> Compare *White-Smith Music Publishing Co. v. Apollo Co.*, 209 U.S. 1 (1908) with the language of §§ 101 (e) and 1 (e).

<sup>43</sup> If the phrase "upon the parts of instruments serving to reproduce mechanically the work" appearing in the statute is read as modifying the nouns "composition" or "work" (i.e. the copyrighted composition is "upon the record," which is a part of the instrument serving to reproduce the work) and not as modifying the term "use," (in which case "use" would mean use of the copyrighted work and not merely use of the physical property of the record) the language of the statute could be reconciled. With such a construction of the term "use" the court would be able to reconcile its finding of a remedy against sellers based upon the phrase "any person" in the statute. See note 27 *supra* and accompanying text.

<sup>44</sup> 248 F.2d at 266.

ures the damages resulting from its non-payment."<sup>45</sup> Such a permissible recovery is believed to be totally inconsistent with the Supreme Court's position in *Aro Mfg. Co. v. Convertible Top Replacement Co.*<sup>46</sup>

In *Aro* the Supreme Court was faced with a situation wherein a patentee brought suit against the Convertible Top Replacement Co. for contributory infringement. Involved in the litigation were sale of convertible tops both prior to and subsequent to an agreement between the patentee and the manufacturer of the original car equipment. This agreement purported to run only in favor of the manufacturer with reservation of rights against future and past vendors of replacement fabrics.<sup>47</sup>

As to activity that occurred prior to the settlement agreement between the manufacturer and the patentee, the court held that

Whatever the agreement's effect on the amount recoverable from Aro . . . it cannot be held in the teeth of its contrary language and intention, to have erased the extant infringement.<sup>48</sup>

To this extent the appellate opinion in the *Goody* case is consistent with Supreme Court pronouncement.<sup>49</sup> This opinion was based upon the repudiation by the Supreme Court of the common law rule that release of one tortfeasor even without satisfaction, releases others.<sup>50</sup>

---

<sup>45</sup> In *Harms, Inc. v. F. W. Woolworth Co.* 163 F. Supp. 484, 485 (S.D. Cal. 1958), this reading of the *Goody* case was adopted. The court in *Harms* felt there was implicit approval of the *Goody* ruling in the denial of *certiorari*, at 355 U.S. 592 (1958).

It will be remembered that the basis of the *Goody* holding was that the seller and manufacturer are severally, rather than jointly, liable. In a copyright infringement action not involving records, *Dan Kasoff Inc. v. Palmer Jewelry Mfg. Co.* 171 F. Supp. 603 (S.D.N.Y. 1959), this reasoning of the *Goody* case was relied upon to support an award of statutory damages against both a manufacturer and seller in an amount, the total of which may very well have exceeded the actual damages of the plaintiff. *Id.* at 604, 607. To the extent that this award was not attributable to profits, albeit profits not provable, it is believed that the decision was erroneous for the same reasons as applied to the *Goody* facts.

<sup>46</sup> 377 U.S. 476 (1964).

<sup>47</sup> As to future sales, the court held that the authorization of the manufacturer to use the structure also authorized future repair of that structure without liability, regardless of the intent of the parties. 377 U.S. at 497, 498. This decision was based upon the fact that insofar as subsequent to the agreement there could be no direct infringement by reason of authorization, well settled law established that contributory infringement could not exist in the absence of direct infringement. 377 U.S. at 500.

<sup>48</sup> *Id.* at 500.

<sup>49</sup> See text accompanying note 31 *supra*.

<sup>50</sup> 377 U.S. at 501.



It is important to recall at this point that the joint tortfeasor, whose release the contributory infringer attempted to rely upon, was that of the vendee of the convertible top car. This vendee may be classified as a "use" infringer and the contributory infringement of the defendant contributed only to the vendee's "use" infringement and not the car manufacturer's "make" and "sell" infringement. There was no attempt to rely upon the release of the original manufacturer for release of the defendant.

This distinction may be clarified by viewing the *Aro* case as involving two infringements, one by the manufacturer as a "make infringer" and one by the consumer (together with the defendant contributorily) as a "use infringer." Conventionally, the make infringer and the use infringer are deemed to be severally rather than jointly liable, independently of any consideration of the joint liability of the use infringer and the contributory infringer for the use of the patented invention.

When analogizing this state of affairs with those existing in *Goody*, it will be remembered that the *Goody* court also deemed the manufacturer and the seller of unauthorized records as severally liable and based its decision on that fact. However, regardless of this identical characterization of liability, the Supreme Court, in *Aro* went on to quote the rule:

Payments made by one tortfeasor [there a "make infringer"] on account of a harm for which he and another [there a "use infringer"] are each liable, diminish the amount of the claim against the other whether or not it was so agreed at the time of payment and whether the payment was made before or after judgment. . . .<sup>51</sup>

As the court pointed out:

Indeed, if "actual damages" or "full compensation" paid by a maker-and-seller can have the effect of releasing a user, as was indicated in *Birdsell*,<sup>52</sup> such a result should follow *a fortiori* where, as here, the damages paid were expressly stated to be compensation for use of the device, and the person subsequently sued is a contributory infringer liable merely for contributing to the same infringing use. In such a case full payment by or on behalf of the direct infringer leaves nothing to be collected from the contributory infringer.<sup>53</sup>

Although the *Aro* decision may be distinguished on its facts insofar as it ultimately involved compensation for the damages caused by the use infringer causing release of one contributing to the same infringing

---

<sup>51</sup> 377 U.S. at 503, quoting Restatement of Torts § 885 (3) (Bracketed portions inserted for clarity).

<sup>52</sup> *Birdsell v. Shaliol*, 112 U.S. 485 (1884).

<sup>53</sup> 377 U.S. at 503.

act,<sup>54</sup> the compensation test of the *Birdsell* opinion referred to by the Supreme Court cannot be so distinguished insofar as it applies to *severally* liable parties.<sup>55</sup>

Remembering the *Goody* court's characterization of 2 cents per record as "a form of statutory compensation which by its very nature measured the damages resulting from its non-payment,"<sup>56</sup> one may conclude that a single payment of that statutory damage by the manufacturer should have released the unauthorized seller on the grounds of full satisfaction of the statutory damage. Therefore, the court in *Goody* should have at least determined whether the settlement agreement involved any compensation for the statutory damage of 2 cents per record from the manufacturer. To the extent that it did represent such compensation, the seller's liability for damages is extinguished.<sup>57</sup>

An attempt to distinguish the unauthorized record situation from the *Aro* fact pattern may be based on the alleged differences between the copyright law and the patent law. It is characteristically clear that

<sup>54</sup> Although the court's decision in *Goody* was seemingly broad enough to permit double recovery for even the same infringing act where two parties were involved, the Second Circuit Court of Appeals retreated from that untenable position in *Shapiro, Bernstein & Co. v. H. L. Green Co.*, 316 F.2d, 304 (2d Cir. 1963).

<sup>55</sup> *Birdsell* recognized full *satisfaction* as extinguishing the property in common law trespass actions and analogized the situation to intellectual property statutory actions.

<sup>56</sup> 248 F.2d at 265.

<sup>57</sup> It should be here noted that the statute involved in the *Aro* case permitted recovery of damages only and not profits, 377 U.S. at 505. Since the statute involving unauthorized recordings permits only recovery "in lieu of profits and damages" and substitutes a "statutory damage" the statutory scheme is similar. Cases such as *F. W. Woolworth Co. v. Contemporary Arts, Inc.*, 344 U.S. 228 (1952) relied upon in the *Goody* opinion and in *Harms, Inc. v. F. W. Woolworth Co.*, 163 F. Supp. 484 (S.D. Cal. 1958), for the proposition that total recovery may exceed actual damages (and therefore presumably statutory substitutes therefor) are inopposite insofar as they involve a portion of the statute apparently permitting recovery for damages and profits cumulatively. A detailed discussion of this provision of the statute is beyond the scope of this paper. See generally *Nimmer on Copyrights* (1970), §§ 151-154. However, even in situations where profits come into play, the rule is clear that one is not liable for profits that another made from the same infringement. *Elizabeth v. Pavement Co.*, 97 U.S. 126, 139-40 (1877) (patent case); *Washingtonian Pub. Co., Inc. v. Pearson*, 140 F.2d. 465-67 (D.C. Cir. 1944).

It is interesting to observe that although a totally different problem was involved in the *Goody* situation (i.e., one of satisfaction, rather than one of penalizing infringement by permitting recovery of damages as well as profits) the *Goody* opinion was cited as supporting the proposition that cumulative recovery and not alternative recovery is appropriate under § 101 (b). *Peter Pan Fabrics, Inc. v. Jobela Fabrics, Inc.*, 329 F.2d, 194, 196 (2d Cir. 1964). The failure to distinguish these situations was the precise cause of the erroneous decision in *Goody*.

in the copyright law an exclusive right to vend is involved; moreover, in the case of unauthorized records, unauthorized sales are delineated separately from manufacture and use. The separate mention of these acts does create separate torts. Such an attempted distinction should, however, fail in view of the fact that the patent grant includes "the right to exclude others from making and using, or selling the invention. . . ."<sup>58</sup>

Thus, in the patent area, separate acts of infringement are also involved.

Furthermore, in *Bauer & Cie. v. O'Donnell*<sup>59</sup> it was held that the terms "vend" and "vending" as used in the patent and copyright statutes existing at that time have exactly the same meaning. It is thus doubtful that any distinction could be today drawn on this point even though the term "sale" is used in connection with records. This is not surprising since the problem is not one of infringing activity, but one of satisfaction.

### *Restraints on Alienation*

The second major public policy militating toward a disposition of cases such as *Goody* in a manner different from that undertaken by the court of appeals involves a policy against restraints on alienation. This policy is not entirely foreign to the copyright law as is evidenced by the "first sale doctrine" which prohibits qualification of future title once the first sale is made, even in instances where the sale is made with notice of that qualification.<sup>60</sup> The unstated common law reason militating against restraints on alienation is the prevention of control of property that has once passed into "commerce."

Although the doctrine is worded in terms of "first sale" it is clear that the first sale which deprives the copyright owner of further control of the work can consist of some recognized form of compulsory transfer and need not be truly voluntary.<sup>61</sup> Keeping this in mind, and keeping in mind the fact that the copyright statute under discussion involves compulsory licensing, it becomes relevant to consider the underlying rationale behind giving a copyright owner the right to vend under any circumstances.

---

<sup>58</sup> 35 U.S.C. § 154 (1964). (Emphasis added.)

<sup>59</sup> 229 U.S. 1 (1913).

<sup>60</sup> See, e.g., *Bobbs-Merrill Co. v. Straus*, 210 U.S. 339 (1908).

<sup>61</sup> *Platt & Munk Co. v. Republic Graphics, Inc.*, 315 F.2d 847, 854 (2d Cir. 1963).

According to Professor Nimmer,

[G]ranting the exclusive right to vend . . . is a necessary supplement to the prohibition on copying in order to make fully effective the copyright owner's right to prevent public distribution of his work. (Footnote omitted).

This rationale becomes inapplicable in the situation where the copyright owner first consents to the sale *or other disposition* of copies of his work. In such circumstances the copyright owner wishes still to prevent unauthorized copying, but it is no longer for the purpose of preventing distribution . . . since by hypothesis he has already consented to such disposition of his work. Therefore the right to prevent unauthorized vending at that point (although still no doubt desired by the copyright owner) is no longer a necessary supplement for the purpose above described . . . , but it is rather primarily a device for controlling the disposition of the tangible personal property which embodies the copyrighted work. Therefore, at this point the policy favoring a copyright monopoly for authors gives way to the policy opposing restraints of trade and restraints on alienation. (Footnote omitted.)<sup>62</sup>

Although in the situation involving sellers of unauthorized records the copyright owner has not consented to the particular sale of the particular tangible personal property, in most cases he has consented to disposition of the records in some other manner. Otherwise, the compulsory licensing provisions of § 1 (e) would not come into play.<sup>63</sup>

Having so consented (and in fact being under a duty to consent to the disposition of records by others where they seek to take advantage of the compulsory licensing provisions), the rationale of giving the copyright owner the right to vend is, according to the logic of Professor Nimmer, inapplicable and should give way to the policy opposing restraints on alienation.<sup>64</sup> Although Professor Nimmer qualifies his analysis of priority of the policy against restraints on alienation over the right to vend by limiting its applicability to instances in which wrongful copy is not involved, i.e., instances other than those involving infringing copies, the importance of this limitation

lies . . . in the practical consideration that the copier may be unavailable or financially irresponsible so that the vendor of the infringing copies may be the only party against whom the copyright proprietor may obtain meaningful relief for the infringement of his work.<sup>65</sup>

---

<sup>62</sup> *Nimmer on Copyright* (1970), § 103.31. (Emphasis added.)

<sup>63</sup> Situations where the compulsory licensing provision does not come into play are beyond the scope of this article. In such instances the public policy implications of the rationale of the court in *Goody* may be quite different.

<sup>64</sup> To the extent that an objection may be based on the quality of the copies, Congress has seen fit to ignore this problem in the case of records.

<sup>65</sup> *Nimmer on Copyright* (1970), § 103.31.

Referring again to the *Goody* fact situation it is clear that the court's decision authorized a restraint on alienation to the extent that it subjected the vendors, even innocent vendors, of unauthorized records to liability despite full satisfaction of the statutory damage of 2 cents per record.<sup>66</sup> One may agree with the court's analysis that the vendor of unauthorized copies is an infringer. However, as noted above, even in the area of infringing activity, the policy against restraints on alienation should take precedence over the right to vend (or the right to prevent unauthorized sale in the case of records) in instances wherein the infringer is not the only party against whom meaningful relief is obtainable. Clearly that is not the case where the manufacturer has already paid the 2 cents.

As earlier noted, the *Goody* case is unclear as to whether or not a restraint on alienation is imposed as to subsequent disposition of the record once compensation has been received from an unauthorized manufacturer who filed a late notice of intent to use. Insofar as the opinion may be construed to authorize this particular restraint, it is *clearly* contrary to the statutory scheme which provides that payment of a royalty shall free the record from any *further* contribution.<sup>67</sup>

To summarize, even though the copyright owner has not consented to the particular sale of a particular record, if the compulsory licensing clause has come into play the alienation of a record—even prior to payment by any party—should not be permitted to be restrained until such time as it appears that the only meaningful remedy is against that party. The fact that an authorized sale is not involved in a manner which would bring the “first sale” doctrine into play in its classic sense, is immaterial. Particularly where “it may fairly be said that the copyright proprietor has received his reward. . . .”<sup>68</sup>

It is arguable that the policy against restraints on alienation as urged above should not be recognized where Congress has provided a notice and payment route which, if followed, would by statute preclude restraints on alienation and obviate any further worries about that subject. A similar argument, in the damage area, may be made on the basis that unless the statute is scrupulously followed, there is no reason to prevent a double recovery, particularly where a plaintiff may never

---

<sup>66</sup> See note 32 *supra*.

<sup>67</sup> *Id.*

<sup>68</sup> *Burke & Van Heusen, Inc. v. Arrow Drug, Inc.*, 233 F. Supp. 881, 884 (E. D. Pa. 1964); *cf. Blazon, Inc. v. DeLuxe Game Corp.*, 268 F. Supp. 416, 433 (S.D.N.Y. 1965). See also *U.S. v. Masonite Corp.*, 316 U.S. 265, 278 (1942) (patent case).

have been satisfied in the true sense of the word, i.e. his *actual* (not statutory) damages were not recovered.

Both of these arguments, however, beg the question somewhat insofar as they begin with the proposition that Congress by statute has authorized restraints on alienation and double recovery in certain circumstances. It is doubtful that this is the case; and, in instances where the statute is in doubt, an interpretation should be attempted which reconciles well settled public policy doctrine with the terms of the statute.

In further response to the latter, damage, argument, it may also be pointed out that regardless of the actual satisfaction in "real life" terms, the statute granted protection in an area where such protection was not previously available in any terms. In such instances, an argument on statutory construction may be made along the lines that the statute should not be construed to grant any more than specifically stated insofar as it is derogation of prior law.

#### CONCLUSION

The asserted faults of the two *Goody* decisions and some public policy considerations deemed applicable to the fact pattern under consideration having been explored, it remains to examine briefly a submitted statutory construction which attempts to reconcile the words of the statute and these public policy considerations. Primarily, this construction is aimed at giving meaning to every term in the statute, a basic consideration of the court of appeals in its opinion, while providing a meaningful remedy taking into account the subjective intent of the seller of unauthorized records.

Little if any consideration need be given to the plaintiff's original claim that recovery should be under § 101 (b) as opposed to §§ 101 (e) and 1 (e). Both courts reached what appears to be a correct contrary conclusion. However, a major area of court dispute involved whether any right of action exists at all as against the seller of unauthorized records. The lower court by effectively reading out the terms "use" or "sale" from § 101 (e) concluded that no such right of action exists; the appellate court concluded that such an action must lie, or else the terms "use or sale" in § 101 (e) would be without meaning.

This conflict could be resolved in several ways. First, it may be argued that the alternative "or" in § 101 (e) gives rise to a cause of action against an unauthorized manufacturer, user *or* vendor, but only

against one of them.<sup>69</sup> Alternatively, an interpretation similar to this may recognize a cause of action against the seller, but only in instances where the manufacturer is unavailable. In other words, first instance recourse to the manufacturer might be required.

Nevertheless, it is believed that the initial holding of the appellate court was correct if limited to mere recognition of a possibility of a cause of action. Infringing activity by manufacture, use or sale seems explicit in the statute and should be recognized. However, from the standpoint of recovery, recovery should be permitted against a user or seller only to the extent that 2 cents per record, or any part thereof, has not been received from any other infringer by way of settlement or through satisfied judgments. This would attribute meaning to all terms of the statute while eliminating double recovery and obviating any restraints on future or past alienation in instances where recovery was once obtained.

In this connection, it should be only the recovery of the initial 2 cents per record that is so restricted. The statute should be so construed that bad faith sellers are liable for an additional 6 cents regardless of whether or not the initial 2 cents damage has been satisfied.<sup>70</sup> Injunctive relief should be applicable only against bad faith sellers and then only if no recovery of the initial 2 cents has been obtained. This limits restraints on alienation to situations where the copyright proprietor has not received his reward.<sup>71</sup> It might also be desirable to require first instance recourse to the manufacturer, at least in the instances of good faith sellers.

Through the above application of the statute, bad faith sellers would be adequately treated in all instances and recovery against good faith sellers would be minimized and possibly limited only to instances where the manufacturer is unavailable.

---

<sup>69</sup> Ascribing significant meaning to the term "or" is not foreign to the appellate court insofar as they did so in connection with their reasoning that a cause of action existed. See text accompanying note 38 *supra*.

<sup>70</sup> See text accompanying notes 39-44 *supra*. This interpretation should be applied even where 6 cents was recovered from the manufacturer who failed to file notice. Recovery in such instances from the manufacturer seems to be automatic. *ABC Music Corp. v. Janov*, 186 F. Supp. 443, 447 (S.D. Cal. 1960); citing *Goody*. Insofar as the added recovery against a seller represents damage by reason of necessitating a suit, a double recovery problem is not involved; insofar as it represents a penalty, the double recovery problem is also absent.

<sup>71</sup> Cf cases cited in note 68 *supra*.





# International Trademark Protection: Private Interests and Public Programs

## TABLE OF CONTENTS

INTRODUCTION	81
CLINIC PARTICIPANTS	82
INTRODUCTORY REMARKS	<i>Director L. James Harris</i> 84
THE INSTITUTE'S TRADEMARK RESEARCH PROGRAM; CONCLUDING SUMMARY AND OBSERVATIONS	<i>Moderator Joseph M. Lightman</i> 87
KEY PRESENTATIONS	
NATIONAL LAWS AND INTERNATIONAL TREATIES:	<i>Francis C. Browne</i>
IMPLICATIONS AND INTERACTION	88
Origin and Function of Trademarks	89
Bilateral, Regional, and International Arrangements	91
MULTIPLE-COUNTRY FILING:	<i>Anthony R. DeSimone</i>
MADRID AND ITS ALTERNATIVES	97
Functions of Present Madrid Agreement	97
Proposals for Changes	99
TRADEMARK PROTECTION AND ENFORCEMENT	<i>Paul Hoffmann</i>
ABROAD	131
Strategy for House Marks	134
Strategy for Product Marks	135
Other Strategy Aspects	136
UNFAIR COMPETITION IN TRADEMARKS ABROAD	<i>Stephen P. Ladas</i> 140
Situation in Civil Law Countries	141
Situation in Common Law Countries	145
Particular Problems in Japan	147

## GROUP DISCUSSION

Acquisition and Enforcement Strategy	138, 151, 159
Boycotts and Trademark Rights	168
Consumer Interests, Advertising, and U. S. Laws; Unfair Competition and Passing-Off	124, 171 148
Corporate Management Practices Regarding Selection and Administration of Trademarks	126
Class Registration Problems	157, 161
Concurrent Use and Registration	168
Cost Factors in International Protection	120, 124
Eastern European Trademark Laws	172
Licensing and Control of Trademarks	150, 154, 159, 161
Madrid Agreement Problems Regarding U. S. Adherence and Proposed Changes	105, 118
National and Regional Connotations in Registration	123, 130, 166
Non-Use and Abandonment	116
Non-Use and Registration	157
PX Trademark Usage	154, 156
Proposed U. S. "Intent to Use" Trademark Legislation	104
Regional Agreements	95
Tradename Protection	166
Service Mark Protection	139

# International Trademark Protection: Private Interests and Public Programs

## INTRODUCTION

AS A PART OF THE INSTITUTE'S CONTINUING CLINIC SERIES, the Clinic on "International Trademark Protection: Private Interests and Public Programs," took place at the Institute's headquarters in Washington, D.C. on January 27, 1971.

As in previous Clinics, a team of invited experts from industry, government and education participated. The Moderator of the Clinic was Joseph M. Lightman of The PTC Research Staff and an International Economist in the Bureau of International Commerce of the Department of Commerce. Director L. James Harris opened the Clinic and was followed by four key speakers: Francis Browne, Senior Partner, Browne, Beveridge & De Grandi; Anthony DeSimone, Trademark Counsel, Merck and Company, Inc.; Paul Hoffman, Trademark Counsel, General Electric Corporation; and Stephen P. Ladas, Senior Partner, Langner Parry, Card and Langner. The statements of these principal speakers and the ensuing discussion which they engendered are reported in the Proceedings below.

Previous Clinics held by the Institute and reported in *IDEA* were on Statutory Requirements of Companies for Protection of Intellectual Creations, Volume 8, Number 4; Computer Software Protection, Volume 13, Number 3; The Patent Cooperation Treaty, Volume 14,

Number 1; Trade Secrets, Volume 14, Number 2; and Unfair Trade Practices, Volume 14, Number 3.

### Clinic Participants

Mortimer Altin	—Trademark Counsel, American Home Products Corporation
Francis C. Browne	—Senior Partner, Browne, Beveridge & DeGrandi
Horace B. Cooke	—Special Consultant, The PTC Research Institute
Anthony R. DeSimone	—Trademark Counsel, Merck & Co., Inc.
L. James Harris	—Director, The PTC Research Institute; Professor of Law, The National Law Center, The George Washington University
Paul Hoffmann	—Trademark Counsel, General Electric Company
Harold M. Knoth	—International Coordinator, Deere & Company
Stephen P. Ladas	—Senior Partner, Langner, Parry, Card & Langner
Joseph M. Lightman	—International Economist, Foreign Business Practices Division, Office of International Investment, Bureau of International Commerce, U.S. Department of Commerce
R. J. McCloskey	—Patent Attorney, Eaton, Yale & Towne, Inc.
George M. Murphy	—Assistant Trademark Counsel, International Telephone and Telegraph Corporation
Helen W. Nies	—Partner, Pattishall, McAuliffe & Hofstetter
S. Chesterfield Oppenheim	—Adviser on Research, The PTC Research Institute; formerly Professor of Law, University of Michigan
Donald Panek	—Patent Counsel, Valeron Corporation

- W. Glasgow Reynolds —Trademark Consultant, E. I. du Pont de Nemours & Company
- Irving H. Siegel —Consultant, The PTC Research Institute; Independent Economic and Management Consultant
- Rene D. Tegtmeyer —Director, Office of Legislative Planning, U.S. Patent Office
- G. von Thury —General Patent Counsel, Borg-Warner Corporation
- Gerard J. Weiser —Research Associate, The PTC Research Institute; Partner, Dechert, Price & Rhoads
- Olin E. Williams —Patent Counsel, Koppers Company, Inc.

## Proceedings of the Clinic

**DIRECTOR L. JAMES HARRIS:** On behalf of The PTC Research Institute of The George Washington University I welcome you to the Clinic. First, I'd like to tell you a little bit about the purpose of the Clinic. We've been developing this instrument, the Clinic, to provide a more effective means of communication, as a way of implementing our other media of professional education. In the Clinic we deal in depth with frontier problems. We try to surface generally inaccessible information and explore new approaches to these current problems. We consider this a part of our research program; an activity in the public interest. We invite—these meetings are by invitation only—a team of leading specialists who represent a range of disciplines. The invitees are selected for their experience and for their position. We hold these deliberations in confidence and until you all have had an opportunity to edit your remarks there will be no publication of the proceedings.

As a research tool, we are employing the Clinic to diagnose the problem, to learn the symptoms and to find remedies. But first we've got to understand the disease. We've got to find out what's wrong, where it hurts, just like a doctor does. Then, perhaps, we can come up with some practical remedy. To do this, we've got to let our hair down. We don't want any company secrets, but we must tell ourselves the facts. We've got to have a maximum of trust among professionals. We've got to have frank and open discussion and this, of course, should best be accomplished under the aegis of a Research Institute. I want to repeat that the publication of the proceedings will be made only after you have had an opportunity to edit your remarks. I emphasize this because I know how important it is for frank discussion.

Why are we having this Clinic now? We are impressed with the increasing attention being paid to the role of trademarks in international trade. There are important developments going on in international conventions and treaties, such as the Paris Union, Benelux, Madrid, et cetera and a press of current problems relating to interna-

tional trademarks that affect U.S. interests, such as foreign protection, enforcement practices, et cetera.

How will we proceed in this Clinic? From experience we found that we have to run each Clinic on an ad hoc basis, depending on the subject under study. This Clinic on international trademark protection will begin with a presentation by Francis Browne of Browne, Beveridge and DeGrandi. Mr. Browne is going to talk on National Laws and International Treaties: Implications and Interactions. Then we'll have a brief period for cross-questioning to clarify points. After each presentation, if we need it, we'll have brief cross-questioning of the speaker for two reasons: one, the papers were not distributed before the meeting and, two, some of the speakers are talking from notes and not from papers. We wanted to give the speakers as much leeway as possible with the method of presentation. Consequently, in order to enhance communication, you might want to ask a few questions for clarification.

The second paper will be presented by Anthony DeSimone of Merck and Company. He's going to talk on Multiple-Country Filing: Madrid and Its Alternatives. The remainder of the morning session will be devoted to open discussion.

You can of course, bring up any relevant subjects you want to. These key papers are only intended to start the ball rolling and to point up directions for fruitful inquiry. We should also explore those areas you feel are important and should be of interest to the group.

The third paper will be given after lunch by Paul Hoffmann of General Electric. He will talk on Trademark Protection and Enforcement Abroad. The final paper will be presented by Stephen Ladas of Langner, Parry, Card and Langner, and he will address Unfair Competition in Trademarks. The remainder of the afternoon session will be devoted to open discussion.

The Moderator-Commentator is Joseph Lightman, a member of the Research Staff of the Institute, an International Economist in the Bureau of International Commerce, Department of Commerce. I want to make it clear that our meeting is different from a conference, different from a seminar, different from a workshop. This type of meeting is intended to generate a mutual confidence to encourage participants to let their hair down. The specialists have been invited for their particular expertise and after the subject matter is discussed in depth it will be edited, published and distributed to the general public, without any cost or effort on its part. This is a new type of learning and teaching instrument that we've been developing, which also results in an educational package comprising a distillation of the actual experience and frank opinion of relevant experts.

Luncheon will be served at 1:15 at the Adams Rib Restaurant, on the ground floor of the Joseph Henry Building, 21st and Pennsylvania—two short blocks from here. We'll break at 12:45, the Clinic will reconvene between 2:00 and 2:15, and will run until 5:00.

At the completion of the Clinic, Mr. Lightman will make some brief concluding observations in the nature of a summary.

There's one very important item I want to emphasize. Please identify yourself before speaking, so that we can make an accurate transcription. I know that in the heat of discussion, you may forget, but, whenever you possibly can, please identify yourself. Also, keep the discussion informal so that we can retain spontaneity. It's important for a productive and fruitful Clinic to create an atmosphere of informal, uninhibited give and take. However, we want to encourage a maximum of interaction to make the give and take as creative of new ideas as possible, so keep your questions and observations as brief as you can.

Before turning the meeting over to Mr. Lightman, I want to repeat: you will all have an opportunity to edit your remarks before publication. Until you do, your remarks are to be considered confidential.

Let us go around the table and have the participants identify themselves for the record. Irv?

DR. SIEGEL: Irving H. Siegel, Consultant to The PTC Research Institute; independent consulting economist, also working now with the American Chemical Society.

MR. COOKE: Horace B. Cooke, Special Consultant, The PTC Research Institute.

MR. KNOTH: Harold Knoth, International Coordinator, Deere and Company.

MR. REYNOLDS: W. G. Reynolds, Trademark Consultant to E. I. du Pont de Nemours and Company, Wilmington, Delaware.

MRS. NIES: Helen Nies, with the firm of Pattishall, McAuliffe & Hofstetter, here in Washington.

DR. LADAS: Stephen Ladas, Langner, Parry, Card and Langner.

MR. HOFFMANN: Paul Hoffmann, Trademark Counsel, General Electric.

MR. LIGHTMAN: Joseph M. Lightman, member of The PTC Research Institute research staff; International Economist with the U.S. Department of Commerce.

DIRECTOR HARRIS: Jim Harris, Director of The PTC Research Institute.

MR. BROWNE: Francis Browne, partner in the firm of Browne, Beveridge and DeGrandi, Washington, D.C.



MR. DESIMONE: Anthony DeSimone, Trademark Counsel, Merck and Company.

MR. ALTIN: Mort Altin, Trademark Counsel, American Home Products Corporation.

MR. TEGTMEYER: Rene Tegtmeyer, Patent Office.

MR. VON THURY: Geza von Thury, Trademark Attorney, Borg-Warner Corporation.

MR. PANEK: Don Panek, Patent Counsel, Valeron Corporation.

PROFESSOR OPPENHEIM: S. Chesterfield Oppenheim, Adviser on Research to the Institute.

DIRECTOR HARRIS: Joe, I turn the meeting over to you.

#### JOSEPH M. LIGHTMAN

Thanks, Jim. Before calling on our key speakers, I will mention briefly a few aspects of the research program the Institute now has underway in the trademark field. Currently, our approach is centered on the economic role of trademarks in U.S. corporate management operations, consumer experiences, and international trade relations. Studies recently completed and published have delved into subjects involving trademarks as market penetration tools, into quantitative goodwill evaluations inherent in trademarks, and into trademark aspects of growing service industries in the United States.

In international contexts, our research has been concerned with trademarks as income factors in U.S. licensing and export operations. And we have also published the results of research on the role of trademarks in East-West trade relations, and in commercial aspects of other regional industrial property activity, particularly in Latin-America, the Middle East, and Asia.

As you know, our research is objective. We take no preconceived positions. Our basic purpose is to emerge facts, to educate, and to inform. So, today's Clinic is an important element in our efforts to surface problems of deep concern to business, legal, and other professional groups interested in the international trademark field. And then, we also want to develop new insights that will be useful to such groups in their activity. Also, we are anticipating from today's discus-

sion new avenues of approach that might be blended into our on-going research activities.

Although I am with the U.S. Department of Commerce, I am appearing today as a member of The PTC Research Institute staff, and of course as Moderator of this Clinic. I believe that I have a very easy job today because, actually, I don't have to say anything substantive. All I have to do is call on people to speak. Nevertheless, any comments or questions I may have are strictly my own and not necessarily those of the U.S. Department of Commerce. Francis, is that a good disclaimer that will stand up in any court?

FRANCIS C. BROWNE: I think you can depend on that.

MODERATOR LIGHTMAN: This morning's session, as Jim mentioned, will be devoted to national and international frameworks of trademark protection and as the first speaker, I call on Francis Browne, senior partner of the firm Browne, Beveridge and DeGrandi. His subject will be National Laws and International Conventions and Treaties: Implications and Interactions. Francis.

DIRECTOR HARRIS: Before you do, Francis, may I ask Mr. McCloskey to identify himself.

R. J. MCCLOSKEY: I am from Eaton, Yale and Towne, Incorporated, Cleveland.

DIRECTOR HARRIS: Welcome aboard.

MR. MCCLOSKEY: Thank you.

MODERATOR LIGHTMAN: Francis.

## FRANCIS C. BROWNE

Thank you, Jim and Joe. To say that I am presenting a paper is probably an overstatement, and to say the least, flattering, because, what I am about to say is not in the form of a paper in the academic sense. My guidelines and instructions, when I was invited to participate in this discussion, were that it was to be rather informal, anything that was said was subject to revision, I could retract anything that I say that may be found to be in error, or something that I wish I hadn't said. With that as an introduction, let me plunge directly into the merits of the topic which has been assigned to me because we'll find that the time

will run all too short if we cover all the subject matter that we have to cover on the agenda.

The subject of National Laws and International Conventions and Treaties: Implications and Interactions, presents a subject of such broad scope that I couldn't possibly do justice to it in the time allotted here. Therefore, my treatment will be more in the nature of an outline, with the possibility that, when it comes time for elaborating or extending my remarks, I may want to fill in some of the gaps in the outline. But I'd like it at least to be a framework for discussion, and, if I may plagiarize some of the points that come up in the discussion, I will try to identify them in the edited remarks as to their source, but please forgive me if I fail to give proper recognition to someone who contributes something of substance in the course of the discussion which may appear to be part of my dissertation. How much time am I allotted?

DIRECTOR HARRIS: Approximately 15 minutes. If you need more time, I am sure the Moderator will be considerate.

MR. BROWNE: Let's start with the historical origin of trademarks themselves, for the setting. It's too academic to go into detail as to the historical origin, nature and function of trademarks before a group like this. But I must, since these remarks will be published, have a frame of reference for the subsequent remarks.

The origins and functions of trademarks (I would rather refer to "trade identification" rather than trademarks) is deep-rooted in history. All of you know the function of heraldic symbols, indicating affiliation with or origin from a particular family. The plaids of the various clans of Scotland and Ireland perform a similar function. When you come to the commercial side of things, you have the hallmarks of the artisans, indicating membership in certain Guilds and then, ultimately, you have symbols indicating origin in a particular commercial enterprise. This brings us up to the time of the industrial revolution and subsequent thereto.

We have a broadening of trade identification in more recent years to identify services, as distinguished from goods, by means of trade origin indicating symbols or devices.

It would seem at the outset that the nature, purpose and function of trade origin indicators would not present any great problem as far as jurisprudence is concerned. The fact of the matter is, the difference in the jurisprudence applicable to the protection of trade origin indicia in the world today is the greatest line of division between the various countries of the world in the field of industrial or intellectual property

rights. We have the Anglo-Saxon common law concept of protection of those symbols arising out of use. We have the code approach, where the right arises out of the sheer fact of registration. As we go on in our discussion, we'll see how this dichotomy of jurisprudence leads to severe obstacles to bringing about interaction by way of international conventions or treaties.

Let us take the common law approach, where you have an inherent right, just as you have with your own surname, to be protected against someone else representing himself to be you, by use of your name. He may do other things (which we're not concerned with in this topic at the moment) to lead others to believe that he's someone other than who he really is—let's call it "passing off"—but I'm talking now only about trade origin indicia, I think Shakespeare deserves credit for being a harbinger of our present jurisprudence when a good many years ago he said something to the effect that: "He who steals my purse, steals trash, but he who takes my good name, takes all." This is an indication that back even as far as the time of Shakespeare the name was a sacred thing, and, in more recent times, in the Supreme Court decisions, I believe it was Chief Justice Hughes in one of his opinions, who said that "a trademark is a fragile thing, and it must be protected under the law, if it is to preserve the function which it was intended to perform."

At this point, let us consider *who* the trademark is intended to serve. Too often, those of us in practice and those who are the proprietors of a trademark think that the law is intended to protect the *owner* only. The fact of the matter is, there is an equal public interest if the trademark is to serve its intended function and purpose and that is to enable the *public* to distinguish between sources or origins of goods or services. This is a fact which is very often overlooked in judicial decisions.

I'm glad to say that most recent decisions are taking more cognizance of the consumer interest—the public interest—in determining whether or not a newcomer should be allowed to encroach upon another's trade origin indication by whatever means he may do it, whether its using a similar script, using a phonetically similar designation, or using something that has a similar connotation.

I believe that, as far as the development of the common law is concerned, the consumer protection aspect is equal in importance to that of protecting the right of the party whose goods or services are identified and distinguished by that device.

I'm afraid that in the statutory law countries the emphasis is not on

protection of the consumer. As you all know, by the sheer fact of registration, certain rights are purported to arise on behalf of the registrants under that system of jurisprudence. The right arises even without an examination of the preexisting registrations to determine how close the latecomer is to another party with respect to sound appearance or significance of his mark.

So, if we have the right—any right—arising out of sheer registration, it doesn't seem, in my opinion, to take sufficiently into consideration either the matter of public interest or the protection of the right to which the trademark is supposed to be entitled—the right of the public to be free of deception on the one hand, and, on the other, the right of the user of the mark to be free from encroachment upon his identification by his competitors. (If I may add a little footnote—not just competitors—but those who would seek to trade on that goodwill or, as it's sometimes called, taking a free ride on a preexisting goodwill—reaping where he has not sown.)

With this background of dichotomy of jurisprudence, I think it becomes evident that international arrangements are not likely to come about, even on a bilateral basis, unless there is a homogeneity or uniformity of jurisprudence with respect to the trademark *right*. I think this accounts for the fact that at least France and Italy, in recent years, undertook to have a bilateral arrangement whereby registration in either country would extend protection to the other country automatically. I think the experience of those of us who have dealt with that situation—and I think Dr. Ladas, here, is in a good position to comment on the effectiveness of that arrangement—hasn't been too effective. There still is a certain amount of national pride, I'm afraid, which makes one country reluctant to give full faith and credit to the administrative action which takes place in another country, even though there may be a treaty which purports to give a right equally to the citizens of both countries.

So much for the bilateral arrangement. Now let's go to the next step of regional arrangements. I think again you must have homogeneity or uniformity of the jurisprudence (and, to the fullest extent possible, similarity), if not identity, of national laws in order to make regional trademark arrangements fully effective.

The Benelux arrangement which we are most recently familiar with, and the Malagasy Union arrangement, I think, exemplify what I'm referring to now. On the one hand, the Malagasy Union has certain economic ties which make it easier for the members to give reciprocal privileges to the single registrant arising out of a single registration

applicable throughout the Union. It's a little more difficult taking the Benelux countries, each of whose histories and origin have been somewhat different. But yet, there's a compatibility among the Benelux countries which, I think the future will show, will work out more successfully, perhaps even than the French-Italian arrangement, which existed and still exists, as far as I know.

Another regional approach was made many years ago, as you all know, on a hemisphere basis, in the Inter-American Treaty. I think the arrangement which was worked out at that time was probably 50 maybe even 100 years ahead of its time. The principle upon which the Inter-American arrangement was based was sound but there were practical considerations which prohibited it from being fully effective. Let's take, for example, the provision for the establishment of two Bureaus, one in Havana and another in Rio de Janeiro which was contemplated by the arrangement for deposit of marks and registration of marks. The system never really got off the ground—but it was mainly practical considerations which prevented it from doing so. I don't think it was anything by the way of dichotomy of jurisprudence because, I think, for the most part the jurisprudence was homogeneous among the Latin members of the arrangement.

Let's shift now to the world-wide scope of international arrangements. I'd say that, by and large, the Paris Convention has been very effective insofar as it provides for "national treatment" under its broad terms. It also provides for priority, which becomes important in the registration countries whereas it's not quite so important in the use countries. Furthermore, the Paris Union extends beyond just the trademark or trade origin indicating subject matter to other acts which constitute acts of unfair competition. The treaty provides that each of the participating countries also must provide effective protection of trade names, even without registration. This is a part of the Paris Convention which, I think, has frequently been overlooked by practitioners as well as governments when it comes to enforcing the rights of foreign nationals in a Paris Union country. There are a few cases of record—I don't have the citations right now—but there are significant instances where the trade name protection clause of the Paris Union has been invoked successfully. It's more apt to be invoked successfully in those cases where famous or well-known marks—marks having world-wide renown—are involved.

If we are going to approach the problem of affording adequate protection to both the consumer and the owner on a world-wide basis, we run full circle into the problem of dichotomy of jurisprudence. The

efforts made under the Paris Union through the Madrid Arrangement to bring about some form of universal protection have not been successful largely because of this dichotomy of jurisprudence. The United States cannot adhere to the Madrid Arrangement in its present form because of that dichotomy. If the Madrid Arrangement is modified to accommodate the Anglo-Saxon jurisprudence or if a separate treaty is drawn up (perhaps even outside the framework of the Paris Union but under the auspices of WIPO) then maybe you can start reconciling the differences in jurisprudence and come up with a workable system for central registration to which trademark owners may turn to determine whether they are likely to encounter obstacles in using their mark in various parts of the world.

However, such an arrangement is not likely to provide that protection for consumers and the public which I believe should be provided, very firmly and definitely, if trademarks are to perform their real intended function. What probably would come of it is that, like in the Paris Union, there would have to be some provision which would state that each signatory country would afford effective protection of the trademark registered internationally; I may even go so far as to phrase that in such a way as to say that they will afford effective protection of the trademark in such a way as to assure protection of the public interest. At some of the meetings that I've attended in the past few years, I've had an opportunity to raise this point obliquely. It seems to be a new point—it hasn't been given much thought—and I must say that this is not peculiar to trademarks. I find the same thing to exist in discussions of international arrangements in the case of patents. It seems as though the participants in the international discussions are more concerned with protection of the right of the party *owning* the property or seeking to obtain a patent than they are about the role of the patent system generally in the *public interest* to promote the progress of science and the useful arts *after the patent has expired*. They look only up to the time of grant and try to work out a lot of different ways of getting the patent. Very little is said about enforcing the rights of the patent during its enforceable life and nothing seems to be said about utilization of the technology (which is free to the public) after expiration of the term.

Now, as far as trademarks are concerned, I think the thing that has been neglected in trademarks is a reflection of the consumer interest in the role of trademarks on an international scale because of our present speed of communication and transportation. When you can go from here to Tokyo in a matter of 12 hours (and if we have the SST, you

will get there even faster) there is less of a geographical difference than there was between Washington and Chicago in the days of rail transportation. All I'm doing is trying to illustrate that, with our speed of communication and transportation today, it's almost as if you never left home. When you go to a foreign country and see trademarks and trade indications or devices, they'll bring up ideas and notions that you connect with things back home—and vice versa. This is equally applicable to foreigners coming to the United States. Therefore, the *consumer* interest has to be given consideration in future international arrangements, so that the effective protection that we talk about will extend to the protection of the *consumer* against being defrauded, as well as protecting the right of the trademark *owner* in his right to free and fair competition.

I think this probably summarizes all of the thoughts that I have at the moment as an outline which bears on the question of National Laws and International Conventions and Treaties: Their Implications and Interactions, without going into detail as to what certain national laws provide and what certain treaties provide. I've tried to paint this in an outline form with a fairly broad brush, again hoping that the people who will raise questions and discuss this matter will fill in many of the gaps. It is my firm belief that as time goes on we will have more and more opportunity to discuss the problems of international registration and protection of marks and protection of consumer interests on an international scale.

Now, let me just digress with a footnote. This really doesn't belong in the body of the text, I don't think, but, because the administration of trademark systems in most of the countries of the world is placed in the hands of agencies which are also responsible for the administration of the patent systems, many misunderstandings and misconceptions arise. Let's take, for example, this matter of availability or registrability of a mark, as compared with patentability of an invention. In most countries, prior patenting anywhere will bar the issuance of a patent later on in the country in which you apply. This means that the country—practically every country—has to have an information bank telling what patents exist in *every* country in the world. Now this is good from the patent system's standpoint because, again, carrying out the purpose of the patent system each country should have available for its citizens this fund of technical knowledge to draw upon, particularly when it passes into the public domain. Also they may draw upon it on a royalty basis while the patent is in force and even while it is pending.

With trademarks we have a different problem. Because of the nation-



al scope of the right, we don't have an "anticipation" test in trademarks. In other words, the right is geographical in scope by its very nature. At the outset we have a totally different juridical approach to trademarks than we do to patents. If you want to go into a comparison or contrast between trademarks and copyright, I think you may see a closer analogy between trademark and copyright than you can between trademark and patents. Copyright is more similar to trademark rights because the copyright—the so-called common law copyright—arises under the same common law concept of jurisprudence as the right arising out of the use of a trademark. It's the property of the party who first uses in the case of trademark: it's the property of the author in the case of someone who creates a work, whether it be a painting, sculpture or writing. Therefore, there's probably more fundamental similarity between trademarks and copyright than there is between trademarks and patents.

We might give consideration to these comparisons and contrasts in international arrangements with respect to trademarks. Let us be sure not to restrict our angle of vision to just those conventions and treaties which relate to "patents or trademark," but broaden our angle of vision and see what we can learn and benefit from such things as the Berne Convention on Copyright as contrasted to the Universal Copyright Convention. If we can profit by anything we learn from the efforts to reconcile the differences between those Conventions, it'll be all to the betterment of both the trademark and copyright systems. Thank you.

**MODERATOR LIGHTMAN:** Thank you, Francis. In keeping with our procedure, we will devote five minutes to clarifying and amplifying questions and then call on Mr. DeSimone, before getting into broader discussion. Are there any factual-type questions that anyone would like to ask Mr. Browne'at this point?

**STEPHEN P. LADAS:** Francis mentioned the French-Italian agreement, bilateral agreement of a few years ago, and then the African Malagasy Union agreement. Of course, he knows very well that the former was simply a formal agreement under which a registration in France extended automatically to Italy—not quite so automatically because Italy still has to issue a certificate itself of registration—but there is nothing but that formality. In other words, the validity of the registration in each country derived from the registration in each country is dependent on its national law, whereas the African and

Malagasy Union is a single, uniform, unique law for all the 13 African Republics, which covers all subjects of trademark law. It's quite different.

I think Francis could have mentioned, I'm sure, but time limitations prevented him from doing so, the Scandinavian example, where you have a uniform Scandinavian—practically uniform—trademark law in all four countries. There is no registration in one which extends to the others. Still, registration in every country is necessary. It's another form of regional agreement, if you will, which preserves the registration procedure of the country but unifies the law, and this absolutely unified law in four countries is very important.

**MODERATOR LIGHTMAN:** Dr. Ladas, do the reciprocal recognition benefits of the French-Italian agreement, pertain to foreigners who apply for a trademark in either country?

**DR. LADAS:** It was thought so. An amendment was made only recently under which it is limited to nationals, and the real worry now is: does that apply to past registrations. We hope that it does not change whatever has been done in the past.

**MR. BROWNE:** On this point, Dr. Ladas would you let us have your comments with respect to the Common Market arrangement and the accessibility with respect to trademarks. We've heard a lot about accessibility of patents, but what comments do you have regarding the trademark aspects of the Common Market plan?

**DR. LADAS:** Mr. de Haan had prepared a general draft trademark law for all the Common Market in 1963, but, in view of the efforts for the common patent law, the draft has remained as a project and nothing has been done. I'm sure in my own mind that it will be taken up again immediately as soon as the common patent law for the six countries is completed.

**MODERATOR LIGHTMAN:** Before continuing our discussion, I should introduce Gerry Weiser who just arrived. Gerry, do you want to identify yourself and corporate affiliation?

**GERARD J. WEISER:** I don't have much to say except that I'm an attorney in Philadelphia. I've been engaged in international patents and trademarks.

**DIRECTOR HARRIS:** And a member of the staff of The PTC Research Institute.

**MR. WEISER:** And I'm awfully sorry to be late.

**MODERATOR LIGHTMAN:** I now call on our second speaker, Anthony R. DeSimone, Trademark Counsel of Merck and Co., Inc. Tony is also an immediate Past-President of the U.S. Trademark Association and a

member of its Board of Directors. Last year he was a member of the U.S. Delegation to Geneva at a meeting of experts on the Madrid Arrangement. Tony's subject will be the Madrid Arrangement and its Alternatives.

#### **ANTHONY DeSIMONE**

Thank you, Joe. When Joe called and asked me if I would be on this program, I asked him what subject I would be assigned. He said, "Madrid and its Alternatives," and I said, "Well, Joe, I've done a little work on it, so I can probably handle it without doing any more work," and I hope I don't regret that decision before the day is out.

In any event, I was interested to hear Francis talk about homogeneity of laws and dichotomy of jurisprudence and so forth, because I suppose that the ideal arrangement for international registration would be the one proposed by Sidney Diamond which would be some kind of a supranational registration which would function somewhat like the Afro-Malagasy Union, where the application would immediately relate to all of the countries involved and so would the registration, but, as Francis said with respect to the Pan American Convention that it was a hundred years ahead of its time. I think the type of international arrangement I mentioned just now would probably be a hundred or two hundred years ahead of its time.

We fall back, then, on what we have and consider the possibilities of improving it. For this reason, although I'm sure most of you are familiar with it, I thought I might just review some of the substantive aspects of the present Madrid Agreement because they do relate to subsequent activity. The present Madrid Agreement grew out of Article 15 of the Paris Union and went into effect about 1892. At present, 21 countries adhere to it, mostly the continental European countries except for Scandinavia and Turkey, which withdrew about ten years ago, and some of the North African countries, like Tunisia, Morocco, and the UAR and also Vietnam because of the original relationship with France.

The present Madrid Agreement requires that a person seeking an international registration must first obtain a registration in his own

country. This is then deposited at Geneva as an international registration, where it is treated, more or less, as an international filing in each of the countries that are members of the Agreement. Each country of the Agreement accepts this international registration as a filing and treats it in accordance with the laws of its own country. If it is an examination country, like Spain or Germany, or the Netherlands, that international registration will get a rather vigorous examination. If it is a country like Belgium or France or Italy, where they don't have examination as to likelihood of confusion, the examination is pretty much pro forma and the application becomes, in effect, an international registration in that country. The United States has never been a member of the Madrid Agreement.

To go back a minute, I would like to mention one other aspect of the Agreement. Since each international registration was predicated upon a national registration, if a prior registrant could cancel a later registrant's home country registration, then that later registrant's international registration, which was predicated upon its home country registration, would fall, and he would lose his rights in all of the countries to which the international registration extended, which, at that time was all of the countries of the Agreement. The Agreement was modified at Nice, and the Nice Arrangement went into effect in 1966. The Nice Arrangement made some very important changes in the Madrid Agreement and I'd like to mention at least two of them.

The first is that, under the Nice Arrangement an international registration becomes independent of the home country registration after the expiration of five years. So, if you want to bring an action to cancel the entire international registration, it must be brought within the initial five-year period. Otherwise the person seeking cancellation has to go into each individual country with an action. This is a significant change in the Madrid Agreement.

The other important change is the provision relating to territorial limitation. Under the old Agreement, you filed your domestic registration at Geneva, and if it passed the examination in all of the countries concerned, it became an international registration in all of the countries. The Nice Arrangement has a provision called Article 3*bis* under which a country may elect that an international registration will not extend to that country unless the international registrant specifically requests that it be extended and pays a fee for having it extended. Thus an international registration does not automatically extend to all of the countries. It will not extend to the countries which have selected the Article 3*bis* provision unless the registrant selects those countries for

his registration. I don't recall, offhand, just exactly how many countries have now adopted the territorial limitations provision—I think, perhaps, about half of the 21 countries.

Subsequent to the Nice Arrangement which, as I say, was December, 1966, virtually the beginning of '67, the Office of International Affairs in the Patent Office, the government, in effect, began to look at the Madrid Agreement again and at the possibility of having the United States become a party to it. Some discussion apparently went on out of which BIRPI, the administrative office for the Treaty, prepared a document which had some proposals in it relating to changes that might be made in the Madrid Agreement to make it more attractive to nonmember countries. I think they were thinking, in large part, of the United States, the United Kingdom, and the Scandinavian countries and perhaps Japan and other countries that are not presently members of the Agreement.

These BIRPI papers were circulated throughout the world and, of course, they were circulated in the United States. Virtually all of the associations that deal with trademark matters—the USTA, the ABA Patent, Trademark and Copyright Section, the APLA, the International Chamber of Commerce, and a lot of the regional and local patent law associations studied the proposals and at the request of the Commissioner of Patents, submitted comments which he had asked for with the thought that it would be useful for him and for the government delegation to know what the thinking of the private industry groups and associations in the United States was with respect to these matters.

BIRPI then called a meeting of the Madrid Agreement countries to which it invited several nonmember countries, including the United States, the United Kingdom, the Scandinavian countries, Japan, and Russia. The meeting was held in April 1970 and, I think, all of the nonmember invitees showed up except Japan. The Russians had a delegation, and the Scandinavian countries had delegations, the United Kingdom, and the United States had delegations. Perhaps the most important proposal, which had achieved rather unanimous acceptance and support in the United States, was the concept that an international registration agreement should be based on a direct filing of an international application with an international government organization, such as the BIRPI organization in Geneva, and that it should not be dependent upon a home country registration.

This idea didn't set very well with the Madrid Agreement countries, so, immediately on the first day, we knew we were in for trouble. They talked a great deal about the concept of having an international regis-

tration based on a home country registration, that this was important, and we couldn't figure out why it was important because, while under the Paris Union many countries had a requirement for a home country registration, most of them had eliminated this requirement. Now I think virtually all of the European countries, except Portugal, no longer require a home country registration. Any national can go in and file an application in any one of these foreign countries without presenting a home country registration. Yet, when they talked about the Madrid Agreement, it suddenly became very important to have a home country registration.

There was only one valid reason, that we could see, why they might want the home country registration. This related to the possibility under the Nice Arrangement, and even under the earlier provisions of the Madrid Agreement, of canceling the home country registration and thereby canceling all of the other international registrations, what we now have come to term the "central attack theory."

They said, "What happens to the central attack theory if we don't have a home country registration to serve as a basis for this central attack." Well, as far as central attack is concerned, I would point out that, under the Nice Arrangement, the central attack provision only exists for five years, which is quite a change from the London text, which was 20 years. Other matters were considered that had been brought up in the original paper but the really basic question, which was the question of dependence or independence, stymied the proceedings so that we never really got to discuss in detail the other questions such as user or non-user and so forth.

And so, at the close of that meeting, Commissioner Schuyler thanked them all and stated that although there had been some useful communication, he was a little disappointed in the outcome. He suggested that perhaps the matter should be brought up before a broader and larger forum, namely, the Paris Union itself. So, in September of 1970 there was another meeting in Geneva at which Commissioner Schuyler raised the question of whether there should be a revision of the Madrid Agreement or whether there should be a new treaty. I think this gave some of the Madrid countries pause for thought because most of them, though not all of them, then expressed the feeling that maybe some accommodation could and should be found under the Madrid Agreement, and that perhaps revisions could be made. This suggests that perhaps there has been some change in thinking since the April meeting and perhaps more of the Madrid Agreement countries are receptive to some of the thoughts that we expressed at that meeting.

In any event, as a consequence of the September meeting, the WIPO organization decided that they would invoke another meeting, but this time would invite all of the Paris Union countries. But they decided that before they held that meeting, which they planned to hold in October 1971, they would hold a preliminary meeting in February. So there will be two meetings, one in February and one in October. A number of association representatives have been invited to the February meeting, the thought being that the WIPO people would like to give industry—the private sector—an opportunity to express its views about any possible arrangements.

In preparation for the February meeting WIPO wanted to get out a working paper again, and, before doing so, it sent a representative to the United States. At the request of Commissioner Schuyler the USTA organized an ad hoc committee meeting with the WIPO representative in New York City to which a number of trademark lawyers interested in the subject came. Dr. Bogsch from WIPO was present, and we had an all-day discussion with him so that he could get the views of the different lawyers and company representatives here concerning the important questions. He then went back to Geneva and drafted a document which, he felt, reflected to a large extent a lot of the views he had heard expressed at the New York meeting. This document has now been circulated among the industry people and Commissioner Schuyler has asked for comments concerning it prior to the meeting to be held in February.

This new document again raises the question of dependence versus independence, and we still support the view that the best choice, from our point of view, is independence—direct filing of the registration with the intergovernmental agency.

The second problem then becomes the question of central attack, and Dr. Bogsch tried to work out a formula for central attack which is expressed in the document. Very briefly it offers the possibility that a person seeking to cancel a later registration would go into the defendant's home country or the place where he has his principal place of business and bring his cancellation action there. If the marks don't conflict in that country (because of the territorial limitation provision) so if the plaintiff doesn't have the applicant's mark—conflicting with his mark in the applicant's home country—then the plaintiff may have a conflict in his own home country.

However, if the two marks do not conflict in either the defendant's or the plaintiff's home country, can the plaintiff bring the action in any country where the marks conflict?

These are some of the thoughts that have been expressed with respect to the handling of central attack. Also, the suggestion that the period during which central attack might occur would be reduced from the present five-year period to a lesser period—maybe three years, or even two years, which would improve the situation:

Perhaps the basic question of whether or not we can or should get into the Agreement is the question of user, because, as Francis said, our common law rights in this country are predicated upon use and everybody's thinking is oriented toward use, whereas in every other country of the world the rights to registration arise prior to any use of the mark. This concept is so ingrained in virtually all of these countries that it's doubtful, to me at least, that you could persuade them to accept a use concept.

But, with respect to use, I think that, if we are going to get into an international arrangement, we have to reorient our own thinking a little bit about use. For one thing, I think that economic conditions, market conditions today, make our concept of use prior to registration a sham. There's hardly any sizable business in the country that can really honestly get a trademark into commercial use in time before it seeks a registration, and this has led to this token-use concept. I think that, more important, really, than use, is the concept of non-use. By that I mean that, if you let a person have a registration in which he represents an interest in a trademark for a particular purpose, the important thing is that he use it at some time, and that it doesn't have to be, or it shouldn't have to be, before he files his registration. More realistically, I think it should be within some reasonable time limit even after he seeks his registration, so long as he has indicated his intention to use that mark. And he should lose his rights in the mark if he does not use it within a reasonable time rather than be required to use the mark before he can claim any registration rights in it.

Even at the present time, we have an accommodation to the Paris Union, under the Lanham Act, which provides that a foreign registrant can file an application to register his trademark in the United States based upon his home country registration. He will be granted a registration in the United States and the Act says he does not have to allege use in commerce. Now, many registrations are being issued every day to foreign registrants who have no use in the United States at all. What kind of a registration is this individual receiving? Nobody really knows, but we go on granting the registration. Now, there is a conflict of opinion as to whether these registrations are valid, or invalid, because these registrants are really not using their marks in the United States.



You get the argument that these people don't have a trademark unless they're using it somewhere—whether in the United States or abroad. The present position of the Patent Office (there's been no judicial decision) is that a foreign applicant must submit specimens showing use somewhere in the world. This view is contrary to an earlier view expressed by Daphne Leeds in a case which I recommend to all of you, the *Merry Cow* case which was decided in 1955 in which she argued that there are two types of registration in the United States, one based on use, and the other based on the treaty power which does not require use.

Now, if we adopt a position where we say, "Well, we can have rights based on intent to use, as long as there is some use within a reasonable time," then you can get into the treaty. Otherwise, we are going to have great difficulty trying to get into the treaty.

As far as right based on intent to use, I don't pretend to be a Constitutional lawyer. I studied Constitutional law so many years ago that I remember very little of it, but I do remember that during the period I was studying Constitutional law, there was a great expansion of thinking about what the Commerce Clause embraced, and what powers Congress had under the Commerce Clause, and the Court started taking jurisdiction in situations where it said, "Well, it isn't *in* commerce, but it is a burden on commerce." Maybe I'm wrong, but, why can't the concept of intent to use support a registration for a limited number of years in the sense that this does affect interstate commerce—because the person is representing that he intends to ship goods in interstate commerce under this trademark. Now, if he fails to do that within two or three or five years, then he loses this right. But, it seems to me that you could conceivably support a registration based on intent to use even under the Commerce Clause—you just stretch the Commerce Clause a little bit. It's been stretched before.

So, when we go to Geneva in February, we are going to have to face up to the question of what kind of rights are we going to give to the foreigner under the Convention. Now, the proposal here suggests granting a foreigner a registration based on non-use for five years and then if he doesn't use it within the five years, his registration will fail. And, perhaps, that term can be reduced from five years to four years or three years. But you're going to have to offer them something not predicated upon use in the United States, and perhaps not even predicated upon use anywhere, but predicated upon an intention to use. Otherwise there's going to be great difficulty in getting the United States into an international arrangement of any kind. Thank you.

MODERATOR LIGHTMAN: Thank you, Tony. I want to ask a question. You talked about the "Paris Union" treaty power registration, where certain foreign parties can register in the U.S. based on non-use. Is such registration possible on the Principal or Supplemental Register?

MR. DESIMONE: Principal.

MR. BROWNE: It is my understanding that every organization in the United States having anything to do with trademarks approves in principal the enactment of legislation providing for intent to use registration or application at least, and, in fact such legislation has been pending in Congress. The administration—both the previous administration and the present—has approved this, but Congress has not seen fit to enact the legislation. Do you have any information to the contrary? In other words, is it true that everybody in the United States favors—when I say everybody, everybody who has voted—favors the Intent to Use Act?

MR. DESIMONE: Well, I don't think you can state it that broadly. There is an intent-to-use bill which has been in the Congress in one form or another for many years and great efforts are being made to get it to committee hearings. Now, I'm sure, myself, that when it comes to committee hearings, there will be some opposition to it, but I agree that probably the greater majority of people would support and do support the intent-to-use legislation. And, the intent-to-use legislation, I think, suggests the kind of thinking that I'm talking about, because it means that we are now getting away from the pure use before you file, and are thinking in terms of rights based on intent to use. Now we're being very, very cautious about how we're approaching it, and just how extensive these rights are going to be, but at least a step and a start is being made in that direction. The intent-to-use bill would require that the registrant, or rather, the applicant, must use his mark within six months of the publication date of the application before his registration will issue. There again, you see, you are talking about periods of time. So, if it can be six months, why can't it be two years, or three years, or whatever you feel is rational and reasonable. And I think it would make all of us more honest in the trademark field if we could have a right in a trademark for a limited number of years which would give a person an opportunity to really get into commerce and have it on the market, and if you don't do it in that time, then forget it. And you have to bear in mind that even under this concept, there's something on the record. No one is really being hurt because he sees the mark on the register, and there's no reason why he has to adopt the same mark or a confusingly similar mark. He's got a record of it.

PROFESSOR S. CHESTERFIELD OPPENHEIM: Perhaps this might need clarification. I am interested in your comment on the Commerce Clause of the United States Constitution. Congress has plenary power over interstate commerce and it has not yet exhausted all of the power it now has. Mere intent to use a mark should be coupled with actual use after a reasonable time has elapsed. A small company intending to use a mark should be allowed a reasonable time to plan for the marketing of the product bearing the mark—especially a small company with limited resources to make a market test.

MR. DESIMONE: The right will be lost.

PROFESSOR OPPENHEIM: If a mark is on the Register but is not in use, this does place a burden on interstate commerce in the sense that the registered mark will tend to deter others from using it or using a confusingly similar mark. To the extent that others are reluctant to get into an infringement suit, the unused registered mark does affect interstate commerce. That should be sufficient under the present expanded interstate commerce concept.

MODERATOR LIGHTMAN: May I introduce two people who just came in? Mr. Murphy, would you please state your full name and affiliation.

GEORGE M. MURPHY: George Murphy from ITT. I'm actually here in place of Don Goodell who is the Chairman of the USTA International Trademark Committee, but who is in Europe on a ski vacation. I offered to trade places with him.

DIRECTOR HARRIS: Perhaps I ought to repeat at this point that our remarks here this morning are completely confidential until the participants have had an opportunity to edit them. In order to surface otherwise inaccessible information, it is necessary for us to be as frank and open as we can—professionals speaking to professionals.

MODERATOR LIGHTMAN: Dr. Ladas?

DR. LADAS: I would like very much to direct attention for discussion to a very central point. Shall we persist in trying to change, to revise the Madrid Agreement or shall we give up quickly and try to make a new arrangement on filing? It seems to me that we must stick to the first effort primarily, because the Madrid Agreement as it works today has many evils and we want to correct those evils—and evils for us, for Americans. Territorial limitations, for instance. Perhaps most of you know that about one-third of international registrations are Swiss registrations. The reason for that is this: under provisions of the Swiss law, Swiss applicants can register a trademark either in the Swiss Patent Office or in the International Bureau. And therefore since either registration is good for the Swiss, he goes to the International Bureau

because at the same time he can get the international registration. We struggled in the International Chamber of Commerce for many years to change this. We changed that by making this provision which Mr. DeSimone mentioned about an applicant having to specify the countries to which he wishes to extend the registration, but the Swiss who are, as you know, quite stingy, arranged so that the extension to one country cost only \$6. Therefore, it is very easy for a Swiss registrant to pay another \$60 and get registration extending to ten countries. As a matter of fact, the experience with this so-called specification of countries—the experience so far—of these three years, it that very few international registrations are really limited. They may be limited so they may probably exclude three or four countries, but generally they cover quite a bit. And this is because the cost is so cheap. The important factor to limit the territorial extension of international registration is to increase those fees.

And, of course, we have the factor that there is now a general, I hope, recognition that every international registrant who will select a country where he wants the international registration to extend, must pay the filing fees of that country, or the registration fees of that country, which would, of course, increase cost considerably, and discourage wide extension.

So, it seems to me, that it is important to try to change the Madrid Agreement so as to limit the territorial extension because this is bad without any question. I don't know if you know—as I will have an opportunity to say later—the big problem today is to find new trademarks. The number of trademarks in the world has increased tremendously. The advertising people have sold us a bill of goods, that you have to have for every product a new trademark. I know of a company that had one trademark for 75 years and now has 60 trademarks. I know of another company that had two trademarks for about 50 years, now it registers 6 to 12 marks every year—new marks!

Where are you going to find those marks? There is a tremendous dearth of available marks and so people may register the same trademark or very similar marks and this is not intentional, deliberate, misappropriation. It's just because they come across the same trademark. Therefore, getting an international registration which automatically extends to 20 countries for a small fee of \$6 is bad, unless you need it for all those countries. And when a little Swiss fellow, a little company, registers a trademark in the International Bureau instead of in the Swiss Bureau, he usually has no intention to use it in 21 countries. So,

that's why I go back to the idea that we must change, if possible, the existing Madrid Agreement rather than to seek a new one.

Another problem on which there is a great debate is the question of independence. Independence means that you don't have to have a home registration before you can obtain an international registration. We are at a disadvantage, because it takes us six months, 12 months, and maybe a few years to get a registration in the United States. Companies such as I have mentioned to you, who are anxious to register six or 12 marks every year, cannot wait for that. They have to go out and register immediately. Therefore, they are deprived of the privilege of getting an international registration because they don't have a U.S. registration. It is important, therefore, to get rid of that requirement of home registration.

Germany agrees with us. I reminded them why that Agreement had been made originally. It's very curious. You know, many times a law has been passed for some reason and through the times, by accretion, other reasons come up. The requirement of home registration was originally inserted in the Agreement because the French at that time were afraid of German registered marks which were French-sounding marks or were French appellations of origin for which France, as you know, has always fought. So, they imposed the requirement of home registration because then the German Patent Office would prevent registration of a French mark in the German Patent Office and therefore that mark would not be extended internationally.

In other words, they wanted the German Patent Office to do the work that they would have to do themselves. That is the reason that the requirement was put in. Now, of course, gradually there developed other reasons. And one of the reasons I will now mention is the central attack problem. In other words, if you object to an international registration, you go ahead and cancel the home registration and therefore the international registration goes by the board. Now, I would like very much today, here with people of experience, to see what is our experience about it. Is there any validity to that central attack problem? From my own experience of nearly 40 years, there are very few cases where I resolved this problem by cancelling the basic home registration. Usually, you resort to negotiations and after you oppose successfully or cancel in some countries, where you have the best advantage, then the owner of international registration comes around and there is a settlement. That is my experience. Therefore, there is not really much validity for the need of a central attack. Then, always remember that this is a two-edge sword—it will be used against us—because anyone can come to

the United States, cancel the registration here and thereby cause the loss of the right in 30 or 40 countries. Why should you lose such a right? It is an unfair position, because in some countries you may have a perfectly good right whereas in other countries you may have to yield.

After the recent decision in England, where the G.E. trademark registration has been cancelled after it had been on the Register since 1907, you see that cancelling the registration in the home country thereby causing cancellation in all the countries can be a very unfair thing. So, therefore, it seems to me that we should stick to the demand that there should be an independence.

I am not going into the question of use. I think, as Mr. DeSimone has suggested, non-use is much more important. In other words, if we stick with this discussion for a while and don't rush with a new arrangement, my conviction is that we should try to change the Madrid Agreement and make it more workable and more useful to ourselves.

MODERATOR LIGHTMAN: Thank you, Dr. Ladas. Paul Hoffmann has some comments.

PAUL HOFFMANN: Well, Dr. Ladas is always a hard act to follow. I support Dr. Ladas completely. He really said all I wanted to say on the subject. I am particularly concerned with the swamping of the Register. I've said this for the last four years. I am most concerned that in the papers I have seen in the last year coming out of Geneva and after listening to people who have been there, and the Commissioner, I haven't heard a word about the problems the new applicant will experience. You know we've been talking about dependence and all kinds of problems, but I haven't heard a single word—maybe somebody else has and can correct me—about this really most important point, the swamping of the Register with unwanted registrations. Now, if you can extend registrations to the U.S. for \$6 or \$10—inflation goes on—very soon the cost will mean nothing. People will register in the United States as a matter of course.

Last year, I just saw the figure last week—14,000 international registrations were obtained. Some of them are multiclass—and even if you go to the international classification, you may end up with 10-15,000 registrations more in this country, and you're going to increase the work of the U.S. Patent Office by 50 percent. Somebody is going to pay for this, not only in hard cash as far as supporting the Patent Office, but somebody also is going to pay for it in not getting marks. As I will say in my statement on Protection and Enforcement, there is a bit of international blackmail going on in the trademark area. A company by obtaining registrations easily will be able to block others and extract some

concessions for a consent. And I don't like that. This is why I support Dr. Ladas' view.

On the question of the central attack, again, I agree with Dr. Ladas. In my experience I have had only one or two cases—but that is a problem that can get a bit sticky. I'm not worried about the situation where a known company is not using its mark, there is somebody I can put my hands on. I remember a case, Turkey used to be a member of the Madrid Agreement, and this person had extended the mark to Turkey and we really needed it. It turned out he was dead, and his registrations were blocking others in 21 countries. Now, if this arrangement continues and we have 40 or more member countries, and the registrant has disappeared what do you do then? So, this is the real problem, I think.

MR. DESIMONE: Do you know of 40?

MR. HOFFMANN: There's a tendency to cut the term of registrations to ten years, this will help. I think the importance of a central attack is really not at the beginning of the term, but rather at the end, you know, when companies have disappeared. This is not something that really disturbs me; a solution will be found and if we can't find it now, we'll find it five years from now once we are participating in an arrangement.

Finally, on intent to use, I agree with Mr. DeSimone. Most people know that I have supported intent to use for the last ten years and I would like to see it. On the other hand, I often think that, whatever happens eventually, we will have to find a way to define what use is—is it token use—or is it sufficient, like in Holland, to publish a one-inch advertisement offering the goods under the mark. Nobody cares whether or not the offer is legitimate. I think, it is really not too hard to define. For instance, "commercial use," may be a reasonable definition.

MODERATOR LIGHTMAN: Thank you, Paul. Horace?

HORACE B. COOKE: Before I get to my question, I couldn't help remembering a time when my company just started moving into Oregon. We discovered an old state registration; someone had registered the trademark, Gulf. And the state was just about to pass a new law which on its face provided that any old registrations under the old law could automatically be renewed. We found this man, but he died from a fishbone in his throat just three days before the time his old registration expired—so sometimes those questions solve themselves.

I wanted to ask a silly question, perhaps, of Dr. Ladas. I wonder if, in filing in some country where a "home" registration is required, any United States resident without a federal registration ever tried to rely

on a state trademark registration. It is a "home" registration, and I would assume that the foreign statute probably calls for a federal registration. But I wonder whether that is actually the case in some countries.

DR. LADAS: I don't know of any case. I think we tried it sometimes, but only in some Latin American countries.

MR. HOFFMANN: I am in the process of trying it in Denmark now, where you don't need a home registration, but I am trying to show that we do have registration in the United States—not in the Patent Office, but in certain states. I don't know the result as yet.

MR. COOKE: I don't know whether the USSR republics provide home registration.

DR. LADAS: They don't require home registration anymore.

MR. COOKE: I meant whether the individual republics in the Soviet Union are treated as separate republics or just as part of the national organizations.

DR. LADAS: There is only one registration.

MODERATOR LIGHTMAN: Mr. Altin had a question.

MORTIMER ALTIN: I wanted to make some remarks. We've had two speakers this morning; Mr. Browne, who was talking more, I think, about substantive law, with emphasis upon what he considered the importance of protecting the interests of the public, and Mr. DeSimone was talking about the Madrid Agreement and possible alternatives which are mainly procedural dealing with the filing of applications.

Although harmonization of substantive law may be our eventual goal, there are presently such vast differences in substantive law around the world that it would be very hard to devise a system that would reconcile these differences. I think that after we have had a few years experience with the Benelux law, which is a harmonization of substantive law, some of us may want to stop thinking about harmonization for the present, at least. I anticipate so many complicated questions of prior rights and conflicting jurisprudence that many of us visualize a real nightmare in trying to sort these rights out.

However, if we concentrate on trying to form some kind of international procedural arrangement for registration, eventually there is going to be more and more harmonization of substantive law.

For example, in various discussions concerning the possibility of United States adherence to a treaty for the international registration of trademarks, much pressure has been and will be placed on the United States to change its substantive law to provide for registration based solely upon intention to use, eliminating the requirement for any use



prior to registration. This pressure is arising out of efforts to establish an arrangement that is primarily procedural.

Eventually, changes like this are going to creep into the national laws of all countries in order to facilitate joining a procedural convention or treaty which will help the registration of trademarks. Francis Browne was talking about the difficulty of harmonizing the theory of the protection of public interest depending upon whether the country's law was based upon the common law, and the Anglo-Saxon system of law as contrasted with the code law countries. Actually, I don't think the question of protection of the public interest as well as the proprietor's right in trademarks depends at all on whether it is a code or a common law system, because you will find that there are many code countries where the public right is taken into consideration. For example, there are several countries where, in the registration procedure, if a trademark of another party is cited, a consent given by that party will automatically remove the reference trademark.

There are other code countries, on the other hand, where consents are not accepted and the reason given is that the public right not to be confused must be protected, not primarily the proprietor's right. A couple of countries that are examples of this are Venezuela and Brazil, and I know there are a number of others. So I don't think the question of public right depends upon whether it's a code country or a common law country.

**MODERATOR LIGHTMAN:** Mr. Murphy.

**MR. MURPHY:** Tony, one of the objections that always comes up with reference to intent to use is that possibly there may be a greater influx of applications. In this connection as to the U.S. we have always talked about a six-month period to initiate use, but you were talking generally about swamping the International Register, and as to the U.S. you are talking about a two or three-year period to initiate use. I just wonder if this wouldn't provide businesses with a greater temptation than they currently have. As a practical matter, I have men in the field call me up and say, let's register X, Y and Z in the U.S. and in b, c, d and e for this or that, and then we say, well, of course, in the United States you have to have use. And there are many difficulties involved in arranging with field personnel even a use sufficient to make application for U.S. registration. So that the businessmen concerned probably whittle themselves down to one mark or to one mark and an alternate.

I am just wondering if you had an extended period to initiate use in the U.S., and if you've got a go-go business man involved, which I think may be the case in many U.S. companies, whether or not there would

be a danger of cluttering the U.S. Register for a period of two or three years with marks that really don't belong there, and thus subsequently of adding to the problem of swamping the International Register if the U.S. were to become a member of the Madrid Agreement.

MR. DESIMONE: Well, George, first of all, when intent to use was first proposed, about ten years ago, I was probably one of the very few people who didn't like it, particularly for the reason you mention. I felt that it wouldn't get rid of the token-use activity—that it would probably encourage more token-use activity because if somebody has filed an intent-to-use application, and it's been published and so forth and has gone through a lot of the mechanics of screening, then, when its time for you to put it into use or lose your rights to register, you're going to make a token shipment. But that takes me back to what I said earlier. I think the real problem is that the six-month period is inadequate—that if our thinking was adjusted to perhaps a two or three-year period, which is a very realistic period for putting a product on the market, then you could abolish token use by actually demanding commercial use and not recognizing anything other than commercial use. So, if you get into trouble with a registrant, you can ask him, "When did you use the mark? Where did you sell it? What stores? What's the volume of sales," and so forth, and you've got a real situation. But, otherwise, yes, I do think that intent to use might encourage more token-use activity.

But now, you have two questions, really, because you are talking about intent to use swamping the Register but, also, since we're talking about international matters and Steve and Paul brought up the question of swamping the Register, I would like to make a comment about that, because I think that what is happening very often is that we are looking at individual aspects of the international convention rather than the whole thing in the total context of the convention. As far as swamping the Register is concerned, if you're talking about a United States registrant, just consider: first of all, the international applicant comes into the United States, and he has to face the U.S. examining procedure, *ex parte*, and opposition procedure, just like any other applicant in the United States Patent Office. So, that's a substantial hurdle. Secondly, at the end of five years, he has to file a use affidavit. Now, the present Section 8 says "use," and that could be amended to say "use in commerce." So then it says, "use in commerce," which means that the foreign registrant, under the agreement, has to get his product—his mark—in use in interstate commerce within five years or he loses his registration.

Now, just these two things, I think, are serious deterrents to a foreign

registrant even under the Madrid Agreement. Steve mentioned something else—the possibility of higher fees. So you do have at least three deterrents to swamping the Register.

MODERATOR LIGHTMAN: Mr. von Thury?

G. VON THURY: I want to comment on, I think, a basic and primary concept in connection with international registration. Dr. Ladas suggested that we should stick to the revision of the existing Madrid Agreement. I was just wondering whether any consideration was given as to how to accomplish this revision. As a footnote, as you probably all know, the Madrid Agreement countries are not in agreement on one minor aspect, not even whether there are 21 or 22 countries. Some recognize East Germany as a member, some deny. So how can we expect from this Madrid Agreement nations that they will revise in accordance with the wishes of other prospective new members. Therefore, in my view, a new treaty would be much more realistic than the revision of the existing Madrid Agreement. Now, it's possible that this could be accomplished by a revision, but I am very pessimistic knowing that this is one aspect—how many countries are the members—21 or 22?

Now, other alternatives, just reading this new proposal, IRM GG 1, from WIPO, it occurred to me, what would happen if we would proceed with a new treaty and then wait until the Madrid Agreement could be revised, and if not satisfactorily revised or if satisfactorily revised, whether there couldn't be a merger just accomplished between the two systems as we merge two corporations, and assume or accept whatever they have, the facilities, the experience, and add the new provisions of a new treaty. That could be, I think, accomplished within the frame of the new WIPO organization. But I would appreciate if Dr. Ladas would comment how he thinks that the revision could be accomplished.

DR. LADAS: I would not be as pessimistic as you are, because judging from the discussions which we have on this, and judging from the discussions within the international association for the protection of industrial property, we have agreed on many revisions. For instance, even the territorial limitation and paying the government fee for each country, even that has been agreed upon. We have agreed to limit the registration to two or three classes only and pay an extra fee for additional classes. As you know, now there are international registrations covering all 34 classes without having to pay a fee. So we agreed on those things.

I think the main disagreements today are really two: first, this question of central attack—*independence and central attack*. And sec-

only, the question of whether the Madrid Agreement may impose on applicants the requirement to file evidence of use or later on to file an affidavit of use or non-use. These are the questions which are really now being debated, and I should hope that an agreement can be reached.

Going back to Mr. Cooke now, Mr. Cooke's point about the controversy on the general question of use in the United States before application in the framework of the Madrid Agreement that really doesn't come up. In other words, the only question that comes under the revised agreement is, should we insist on an international applicant producing specimen labels to show that he's using the mark anywhere. That's the only issue and on this there has been disagreement in the Patent Office. The matter has never been to court yet and conceivably an interpretation under which you don't have to have use, provided that there is a bona fide intention to use the mark would be sufficient.

Another answer to the question is the British system. All of the British countries, as you know, do not require use. Bona fide intention to use the mark is sufficient. And, leaving aside India at this moment, (because that's a special case) generally bona fide intention to use a mark has been accepted of traders that are in international commerce.

One time I was trying to find out what the British courts have decided on bona fide intention to use. I checked all cases where they denied bona fide intention to use the mark. And I found only five or six cases, and those cases are specific cases where there was in fact, really, no bona fide intention to use the mark. But the international trader who ships his goods all over the world would generally, in British law countries, seem to have a bona fide intention to use the mark. And there has been no cluttering of the Register in those countries because of what Mr. DeSimone has said: there's a severe examination, there is opposition and the requirements for registrability are very high, so that the number of marks which are being registered are kept down.

MODERATOR LIGHTMAN: Mr. Reynolds?

W. GLASGOW REYNOLDS: I would like to make an observation about two things. The first is directed to Dr. Ladas' comments upon the proliferation of trademarks in modern commerce. Today there are developments going on of a technological nature which are spurred by massive scientific research in which we find that American companies as well as foreign companies are generating new products at a phenomenal rate. In my own organization, for example, over 25 percent of today's products were not in existence ten years ago. And as a handmaiden to that, we have a terminology in the chemical business, and also in the pharmaceutical field, in which we are saddled with a scientific jargon

that is almost unpronounceable. Typical of this development are terms such as "hexahexachlormethane"; and "decahydronaphthalene." Rather than market products by these names we have felt compelled to adopt simplified five-letter words as alternates, and that is our excuse as well as our reason for having so many trademarks in the chemical and pharmaceutical industries. I thought that I had to say something along this line because I blushed to think that my principal client owns over 600 trademarks when Dr. Ladas commented upon the growing multiplicity of terms held by some organizations.

IRVING H. SIEGEL: They weren't four letter words.

MR. REYNOLDS: No sir. Now the second thing that I want to comment on is central attack. The consequences of central attack that concern me most start with its basic premise that the entire network of foreign trademark protection under the Madrid Agreement will automatically collapse, domino-style, with a successful assault by an infringer in just one of the many market areas in which the registrant may be operating in international trade.

It may help to illustrate the extent of my concern if we consider for a moment the escalated consequences that the court decision in our *Cellophane* case would have brought about had this nation been a party to the Madrid Agreement at the time it was handed down. (*Du Pont Cellophane Co. v. Waxed Products Co.*; 85 F2d 75 (CCA 2nd 1936) modifying 6 F. Supp. 859 (1934) cert. den. 299 U.S. 601, 81 L. Ed. 443, 57 Sup. Ct. 194 (1936).) In that case the evidence contained market surveys showing that the "Cellophane" trademark was in general use as a generic term in the United States. As a result the courts struck down the covering domestic registration of the mark. They did not disturb any of the covering foreign registrations. But, had Du Pont confined its foreign coverage to a single filing under the Madrid Agreement, that coverage would have automatically collapsed under the principle of central attack the moment the American courts terminated that U.S. registration. Moreover, that global collapse would have occurred even though the evidence had disclosed that the word "Cellophane" had not become a generic term in a single signatory nation apart from the United States.

Now when you start to translate that into practicalities you come up with two very disconcerting results. The first is that when you lose a registration by central attack you lose more than some little handy identification. With it you sacrifice all your past dollar investments in advertising and promoting public acceptance of that identification. And here you not only lose accumulated capital expenditures in your

home market but in every market area of the world connected with this Madrid treaty. In the case of cellophane, those expenditures would have totaled many millions of dollars.

The second disconcerting result is the high cost of insuring oneself against such a financial catastrophe. Common sense dictates that the best hedge against that would be to undergird your Madrid filing with a host of local registrations in each nation where your goods are distributed. But this could also become extremely expensive considering the likelihood of litigation involved in such local registration efforts. And that, in turn, prompts the sad afterthought that such expenditures would more than wipe out all the savings in multiple fees that advocates of the Madrid Agreement now foresee as an economy argument for embracing it.

In the face of these practical considerations, one is tempted to conclude that the Madrid Agreement is not the answer to standard legal protection for trademark licenses and franchises in modern commerce. A more realistic answer would seem to lie in a completely new treaty sans central attack and all related threats to the advertising and promotion investments which have become the *sine qua non* of today's competitive world.

DR. LADAS: Gentlemen, I think these are very valuable observations that have been made and I may only say there is no question about the technology problem in new products and so on, that have come into the market. But I don't think it's always that.

MR. REYNOLDS: I agree with you.

DR. LADAS: An American company bought a company in France, which makes just two kinds of products. You know how many trademarks they had? 265 marks! I sought to convince the American company to abandon many of them—not only because it would simply be foolish to maintain so many marks and to defend them—but also on the philosophy that I think it's really not right to monopolize too many marks.

MODERATOR LIGHTMAN: Mrs. Nies has a comment.

HELEN NIES: I wanted to comment that I think the suggestions on non-use are very practical and that we need more thinking along these lines in this country. I also have a question, and I hope I'm not displaying too much ignorance. Do you know of any case that has ruled on whether the presumption of abandonment under the Lanham Act, that is non-use for two years, applies to a foreign registrant?

MR. DESIMONE: I don't think that has ever been a case.

MRS. NIES: I hadn't seen a case on that point and it seems to me that the presumption does apply, and that you probably could cancel a

registration of a foreign registrant if there's been no use in this country for two years, unless, of course, there are circumstances explaining away the non-use. In other words I think the registration of a foreign registrant is subject to the same provisions as any other registrant's.

DR. LADAS: But it's not the same in this country and it's not true. Abandonment is always a very difficult one to prove.

MRS. NIES: Oh, yes.

DR. LADAS: Intention to abandon as well as the fact of abandonment.

MRS. NIES: But I think we have a principle that use is required to maintain a registration.

MR. DESIMONE: You just made a statement. You said they're subject to the same provisions as anyone. They're not. They have a registration and they haven't used it in the United States. But they have a registration. No one else in the United States has a registration when he hasn't used the mark.

MRS. NIES: I was referring to the remaining provisions of the Act being applicable to that registration.

MR. DESIMONE: Well, what I meant was that once he gets his registration, what does it give him? You just mentioned that I might be able to cancel his registration if he hasn't used it within a reasonable time.

MRS. NIES: You were speaking in terms of five years, and I was considering whether we didn't have a shorter time provision now.

MR. DESIMONE: That's possible, but the point I was making was that I don't think the foreign registrant really knows what he does have when he gets his registration, and the only time he's going to find out is if somebody sues him, say, on two years' abandonment, or somebody sues him for non-use, or whatever, but meanwhile the registrant is holding a United States registration. And perhaps he thinks it's just as valid as anybody else's and maybe it's not.

MODERATOR LIGHTMAN: Mort, do you have a comment?

MR. ALTIN: Yes, I have some comments to make. I'd first like to make a comment on the discussion of non-use and abandonment. I think too many trademark attorneys—and this is a world-wide question—tend to equate non-use and abandonment where actually they are not necessarily the same thing, particularly under our theory of law. More is involved in abandonment than non-use. How this affects the question of the United States adherence I don't want to go into now.

I want to make a few comments about the central attack theory. I'm sitting on the fence on this issue because there are very definite advantages to central attack and very definite disadvantages; also I'm afraid I feel "you're damned if you do and you're damned if you don't." But I'm trying to evaluate the relative advantages and disadvantages.

The advantages of having central attack are primarily a matter of saving money because where you have a central filing system you can still proceed under national law, and you always have the opportunity of attacking a mark in any country individually. Of course, the financial burden could be a fairly tremendous one. Assuming that the same conditions exist in every country and that you would have to cancel in every country, I would imagine that in most cases there are very few countries where you would really find it necessary to bring cancellation. Although there are 21 countries in the Madrid Agreement, I would assume that if there was a mark that I wanted to attack I'd probably be interested in six or seven countries, at the most, probably not in all 21.

On the other hand, the thing that really frightens me about a system of central attack as it exists now in the Madrid Agreement is that you might have started using a new mark and perhaps after two years be fairly well established in ten or 12 different countries. If, for example, particularly under U.S. law, somebody who is making use of a mark but who doesn't have a registration can come "out of the woodwork," so to speak, and cancel your home country registration whether it's a "home country" or whether it's some other method of choosing a central registration as a source of central attack. You can be left without a trademark in ten or 15 countries. This can be particularly difficult in countries where all rights depend upon registration and not use. Frankly, I think the latter problem is worse than the problem of having to attack a mark in each country separately. However, in many, many discussions that have taken place recently about this problem, there have been several compromises suggested which might be reasonable ones, such as for example, finding some method of limiting the causes for central attack. In other words, if somebody is terribly worried about a situation like the one that existed a few years ago where Mr. Aries registered internationally famous trademarks in Monaco, perhaps if the grounds for central attack were limited to reasons of fraud or something of that sort rather than mere conflict between two trademarks, maybe we would be in a better position to accept central attack. Also if central attack were limited to countries where the same conditions exist, in other words, if such attack were based on a prior trademark, if the cancellation could take place only in those countries where the two trademarks co-existed or something of that sort, then there might be some possibilities, but I feel that without some of these limitations central attack as it exists today, to my mind, is unacceptable.



DR. LADAS: Mort, as a matter of practical experience, what does it amount to exactly? Under the Madrid Agreement, after you cancel the home registration, the International Bureau will not cancel the international registration unless you can prove the mark is no longer protected—not registered—protected in the home country. Therefore, the cancellation of the home registration does not necessarily bring about cancellation of the international registration. You have still to prove that the mark is no longer protected in that country.

Secondly: If an international registration is independent and is owned by a Frenchman, and you cancel his French registration and enjoin the use, and therefore he's not able to apply the trademark in that country, why would he be interested anymore in the international registration? He cannot export from France. In other words, theoretically the problem of central attack looks like it's very important, but practically it doesn't really amount to much.

MR. ALTIN: Well, there are very many products, Dr. Ladas, that my company, either through a subsidiary or licensee, sells in many countries in Europe that we do not sell in this country at all. Or if we do sell the same product, sometimes it is under a different trademark. We are not concerned solely with an export situation.

MODERATOR LIGHTMAN: I think Oppie, you've got a question.

PROFESSOR OPPENHEIM: Listening to the discussion, I have been made aware of the problem of "swamping" the register with marks in foreign countries. I gathered from the discussion that the registrants, for example, small companies, may get broad territorial protection of their registered marks in countries other than the one in which the mark is actually being used by "swamping" the registers in countries other than their home country.

This raises, in my mind, antitrust questions which might apply in the U.S. or possibly abroad. If there is overly broad territorial protection of the mark this may create barriers to competition. It is also a possible paradox if, for example, small companies "swamp" the registers in various countries with their marks and thus foreclose large scale companies from using those marks. The large companies may be the only ones with sufficient resources to use the mark but may be blocked from doing so.

I would like to ask Stephen Ladas if, in his experience in attending international conferences, the antitrust implications I have mentioned are considered so as to avoid excessive protection of registered marks.

DR. LADAS: There hasn't been any. Even the Common Market Commission hasn't really dealt with that problem yet. I think obviously the

problem you mention exists. But the little fellow who ties up the big company by the easiness of an international registration extending to 20 countries will generally be satisfied to make a deal and the question resolves itself into the issue of how much you want to pay rather than try to select a new mark. Depending on how important is the market behind the mark for both the little fellow and the big company, the one or the other solution will be found.

MR. HOFFMANN: Well, the price always goes up if my company is involved. That's why I feel so strongly about the swamping of the Register. I am afraid the safeguards which Tony mentioned such as examination by the Patent Office, are not of too much value. How many marks are really rejected, anything goes on the Register here these days. Well, it is really not the Patent Office. The CCPA with some of its decisions made it very difficult for the examining operation to reject marks for descriptiveness. If we are going to try and reduce the number of marks through oppositions, that's very good for the lawyers, but expensive for the clients. In the United States, we are much more inclined to say "What do we really need—in a particular country—not what can I do to block other people." And then, so many companies will say "We can get a registration in the United States cheaply, let's do it." I'm very concerned with the effects of all this. Maybe I'm wrong. If the treaty comes into force, maybe I'll be proven wrong, but I'm concerned.

MR. VON THURY: This is in connection with the central attack. I was just wondering whether I am right, or maybe Dr. Ladas will correct me. There is a provision, or was—I don't know whether this was already changed—that you could convert an international registration into a national registration in a given country. So, in this connection, if there is a central attack I could imagine that while the home registration is in effect, I could convert my other international registrations in the other 20 countries into national registrations.

DR. LADAS: It costs a little money, but you can do it.

MR. VON THURY: Yes. And therefore, if we are talking about central attack, I am undecided whether yes or no. I think this conversion should also be considered, because this might frustrate the central attack.

MODERATOR LIGHTMAN: Mort?

MR. ALTIN: I wanted to make a remark. Mr. Oppenheim mentioned the interplay of antitrust and he talked about the small companies, proliferation coming from them. Well, this is very true. One of the interesting things that occurred to me is that when the talks first started

in the United States, about our possibly adhering to the Madrid Agreement, I can't recall who said it, it may have been you, Joe, that the main reason why the United States Government decided to start looking into adhering to Madrid was for the benefit of small companies, to make it easier for them to register; they couldn't afford to register individually in foreign countries. These are the companies that were to use Madrid.

**MODERATOR LIGHTMAN:** I don't know whether this was the main reason. However, it is an important aspect of the Bureau of International Commerce's activities in export trade promotion. Small and medium size companies have said to us "We need trademark protection abroad badly, but we can't afford it. Is there some way we can get a wide area of trademark protection and at the same time minimize our costs." It is difficult to advise them, outside of stating that we are exploring the possibility of U.S. adherence to the Madrid Agreement.

**PROFESSOR OPPENHEIM:** It is alright, Joe, if they use the mark, but if they are simply saying—we're small companies and we want to get on the various registers, then the "swamping" of the registers with small business marks may create potential barriers to competition of other companies faced with trademark infringement suits over a broad territorial area.

**MODERATOR LIGHTMAN:** Oppie, we are trying to encourage these companies to enter into or expand exports. They immediately point out that their trademarks are valuable and need to be protected against piracy. Their basic problem is that they cannot afford to register and enforce their marks abroad. That's all I'm saying.

**DR. LADAS:** Of course, you have to look at the other side. Look at the small companies in the other countries. Take Japan, for instance. If we go into a separate treaty and Japan becomes a part of the treaty, God help us! Japan files 90,000 trademark applications a year, 90,000! And 95 percent of all industry in Japan is small industry, with less than 300 workers or employees. Intense competition is the result, and out of this the misappropriation of foreign marks about which I'll talk a little later. If it is easy to register internationally, at little cost, you may have at least 25,000 of that 90,000 applications extended to the United States.

**MR. VON THURY:** More work for trademark attorneys.

**DR. LADAS:** Well, I'm thinking of industries.

**MR. BROWNE:** On this matter of proliferation of registration and congested Register, it seems to me as though an effective examination system will cure that problem. I don't see any threat at all. I think there should be an effective examination system in every single country. And

if there is, you may have a lot of applications, you may put a burden on the Patent Office, but you will not congest the Register.

Second, I wanted to comment a moment on this central attack idea. I think everyone would be opposed to a central attack which was unlimited in its scope. If there is any kind of central attack, it would have to have certain limitations. A thought that has occurred to me since this question has come up in other meetings and here today is that the compromise might be an application of the rule of the comity. So that, if you do want to do some forum shopping, pick out a jurisdiction in which the registration exists, get a ruling in that country, and then all other countries who are signatories to the treaty could determine whether, under the rule of comity, they would give recognition to that decision provided it was not inconsistent with their own national law.

**MR. VON THURY:** A different set of facts.

**MR. BROWNE:** That's not comity. It has to be the same set of facts. In other words, it would lend itself very easily in our own country to the application of summary judgment. If the same facts and the same issues are presented here, why go through all the discovery period, the testimony period, briefs, final hearing, and wait two and a half years when all those facts have been considered and a competent juridical body has made a determination in one country. If that decision is not inconsistent with our law, I don't see why our Trademark Trial Appeal Board, on summary judgment, couldn't adopt that same decision in this country.

**DR. SIEGEL:** This would be along the lines already proposed by Mort with respect to the procedural harmonization.

**MR. BROWNE:** It ties in very directly with that.

**MR. ALTIN:** On that point I'd hate to have the United States courts or the Patent Office give comity to the decisions of the Japanese Patent Office.

**MR. BROWNE:** Well, you may be able to find more examples than that. As a matter of principle, if they are fit to follow, why shouldn't we follow it?

**MR. HOFFMANN:** You say, "effective examination." There are only two countries that really have effective examination. One is England and the other Japan, if you are an American applicant.

**MODERATOR LIGHTMAN:** May we hear from some other company representatives; Mr. Knoth, Mr. Williams?

**HAROLD M. KNOTH:** I don't have any comments because I think we're so far away from even coming close to Madrid that we're buying a lot of horses and we haven't got the wagon yet.

**MODERATOR LIGHTMAN:** Mr. Williams?

OLIN E. WILLIAMS: Our experience has been that the Japanese examination and plethora of marks is a fact situation and that this does not interfere at the time that you register (and hence is not a situation that would be improved by the Madrid Agreement). We are playing right now a very expensive game trying to find out what mark can be used in certain areas of machine manufacture. We have yet to find one. We had a communication from a Japanese gentleman saying that he's willing to talk business. Unfortunately, we haven't had several thousand dollars to offer for sale. Paul, didn't you say it was a little higher for your company than that?

MR. HOFFMANN: It always goes up when we are involved.

MODERATOR LIGHTMAN: Mr. Murphy?

MR. MURPHY: Mr. Oppenheim isn't here right now, but I just didn't want to let pass a comment on his observation dealing with the problem of swamping of the Register by small companies getting registrations for marks which are actually not going to be used by such companies in X number of countries, and of whether or not such action by small companies is a competitive barrier. I think it would be a mistake to fasten on that type of terminology ("competitive barrier") in connection with trademarks because it may have a very great reverse spin on it. Dr. Ladas has talked about the doctrine of accession. You may fasten on something for one purpose and you may later find out that it also has other ramifications which are less appealing, and in this particular case, I think, the dangers inherent in characterizing trademark registration in that particular fashion ("competitive barrier") are extremely great.

MODERATOR LIGHTMAN: Dr. Siegel.

DR. SIEGEL: I just want to ask a question for information about the Japanese law. Do most of the words tend to be preempted in the sense that they are, say, always in recognizable English and therefore possibly competitive—from the viewpoint of other companies desiring to use somewhat similar names? Or is the word often more distinctive, in the sense that it is inherently Japanese and therefore possibly prevents an American company from mimicking a Japanese cultural veneer? In short, I'm curious as to whether the competition is intrusive into the verbal domain of American companies or seeks to fence out American identification with oriental cultural accomplishments.

DR. LADAS: They are very intrusive into Americans' cultural veneer. Mostly they pick up the American word or they pick up Katakana characters corresponding to the sound of the American mark.

MR. BROWNE: From my experience, there are cases where American companies adopt marks in the United States which have a "ring" which is not just Japanese but it may be Scandinavian, it may be French, it

may be German, depending on the nature of the product. Furniture—Scandinavian; wines, perfumes—French; chemicals, German; maybe radios and that sort of things—Japanese. So I think we're just as guilty in that respect in trying to avail ourselves of the connotation of regional origin by the nature of the mark itself as the Japanese are. American marks are usually imitated because of the goodwill which the mark itself symbolizes rather than the nature of the mark.

MODERATOR LIGHTMAN: Mr. McCloskey.

MR. MCCLOSKEY: I would like to comment on something that Dr. Ladas raised earlier. Many divisions in our company believe they must generate a new trademark every time a new product is developed. This feeling prevails even where the new product is similar to those which have been marketed in the past. Our filing procedure is to file trademark applications initially in the United States. A review is then made to determine whether corresponding applications should be filed in foreign countries. Many times this review does not occur until after the U.S. mark is registered.

One of the first questions always asked concerns cost. In other words, our divisional people inquire about the cost of filing a trademark application in the several foreign jurisdictions in which they are interested. Usually the number of applications filed is determined by filing cost. In the event it would be possible to file in several countries for a nominal fee such as \$5.00 or \$6.00, I am sure that the question would not be raised and countries would be flooded with our trademark applications. In many countries the trademark would never be used.

MODERATOR LIGHTMAN: Harold?

MR. KNOTH: I wanted to ask a question of Mr. Williams, if he cares to answer it. What kind of price did you run into? We're in about the same boat—we're trying to find out a price.

MR. WILLIAMS: Between \$5,000 and \$10,000.

MR. KNOTH: You see, our problem is that we have to deal with about four people because of overlapping classifications of the same mark. There's another thing about Japan—if you have any animal mark like we have, any kind of an animal like ours, we can't register, we can't use it. So our mark, as you know, is the leaping deer, but standing deer or sitting deer are still references.

MR. VON THURY: I would like to comment on Mr. Browne's statement concerning the interests of the consumer. I think this is a very interesting and very important aspect and I hadn't heard this before, particularly since I come from a civil law country, my education is based on a civil law system and, since you mentioned there has been no

consideration given in the past to the rights of the consumer in connection with trademarks but primarily it recognized the registration in civil law countries as protecting the trademark owner—it is a proprietary right.

I think if we adopt that concept, we should also give some attention to the right of the consumer and the public. I am afraid, because of the civil law system concept, everything is codified. And this will not be possible under the trademark registration. We try to consolidate and think under a common rule our own concepts of trademarks used and concepts of registration. I think this would be an area which should be explored whenever this comes up in connection with international conventions and negotiations: what is the primary aspect of the registration? Just to protect the proprietary rights of the trademark owners or to protect the consumer?

MR. BROWNE: Consumer protection.

MR. VON THURY: That's right. Maybe this should be covered and somehow consideration should be given whether this aspect can be somehow unified so that whatever our interest is this will be protected under the civil law system. I think I was very much interested in that aspect the first time that it came up.

MODERATOR LIGHTMAN: This is a research project now on the Institute's drawing board: the question of consumers and trademark protection. Also, I want to mention that most countries now have provisions against registration of generic terms as trademarks. So in that sense, I think some progress is being made in the area of consumer protection in trademark laws.

MR. VON THURY: But it's still in the interests of the trademark owner.

PROFESSOR OPPENHEIM: May I ask you, Francis, in speaking of the coalescence of the trademark with unfair competition, are you thinking also, for example, of the present wave of consumer protection against false and misleading advertising, using the mark as a vehicle for such advertising?

MR. BROWNE: That's right. I wasn't confining myself to trademark statutes as such. But when we're talking about a treaty, we are talking about giving effective protection. I was talking about giving effective protection of the *function* which the trademark is supposed to perform, namely, a means of indicating origin or, at least, distinguishing one origin from another in the eyes of the *consumer*. After all, you don't adopt a trademark solely for the sake of the trademark owner.

PROFESSOR OPPENHEIM: I was thinking more of the tarnishing of the

mark that comes from, let us say, false or misleading advertising, rather than the use of the mark as such. I am thinking of the Federal Trade Commission's recent complaints against companies owning nationally known and advertised trademarks and which are being charged with misleading advertising in violation of Section 5 of the FTC Act. As you know, this is part of the recent attention being given to consumer protection.

I am not judging the merits of these complaints. My point is that perhaps this increases the responsibility of trademark counsel to advise management regarding the impact that such FTC charges may have in reflecting adversely on valuable trademark assets of the nationally known and advertised products or their housemarks. I am wondering whether the advertising agencies that persuade management to engage in certain advertising promotion might unwittingly contribute to a tarnishing of the trademark if the FTC issues a complaint which is publicized. Even if the matter is settled by a consent settlement or goes to trial, it seems to me that it may be difficult to counteract the disparagement of the mark in the public mind. If the advertising which is being attacked is carried on television or radio or in other national media, it will have such an impact that it will be difficult to correct any misleading advertising and thereafter convey to the consuming public the elimination of the representations which the Commission believes are misleading.

Again, I emphasize I am not judging the merits of these complaints, but I do know that the FTC is now determined to correct misleading advertising of products bearing nationally known marks. The Commission also is attempting to correct such advertising by requiring the company to admit that its past advertising was false or misleading and then admit to the public that this has been the case. The FTC thinks it has authority to do that as an effective remedy.

I think we should bear in mind that as far back as 1938 Justice Black, in his opinion in the *Standard Education Society* case, said that the FTC has authority to protect the consumer who is unsuspecting, gullible and ignorant, as well as the reasonable and prudent purchaser. It seems to me, therefore, that it might be well to recognize that we are now in a period when consumer protection is in the ascendant and the Supreme Court might well support the FTC in striking down advertising claims which years ago were not being challenged.

DR. SIEGEL: I just want to raise one other point before we are required to break. Mr. McCloskey mentioned the overzealousness, perhaps, of company people in pursuing the generation of trademarks and



their registration. I'm wondering if there is a tendency of companies to reward unduly this type of energy. Is the activity regarded in the same way as patent generation? Is it tied in, possibly, to the patent system? Do people want to identify an original contribution in addition to generating a patent?

MR. McCLOSKEY: We have a patent award system which is in no way connected with trademark selection.

DR. SIEGEL: What is the technique for generating trademarks? Is there a committee?

MR. McCLOSKEY: Well, it's been rather informal. It's been on a divisional basis, or a subsidiary basis, whatever the case may be.

DR. SIEGEL: Is there competition, then, among divisions?

MR. McCLOSKEY: It varies among divisions. Some divisions actually run contests for their employees. For example, a division may announce a new product and solicit ideas for a new trademark to identify the product. Incidentally, many times incorrect terminology is applied by our divisions. Frequently, a trademark is also called a copyright or patent. Four or five marks are then selected by a party in charge of the contest and submitted to our department for clearance. This, however, is the exception. Very few divisions have done this and in most divisions a trademark is selected by the advertising or marketing people without a contest and submitted to us for clearance.

At the present time, our company is in the process of establishing a corporate identity program. One of the reasons for establishing a policy of this type is to eliminate the many, many unimportant trademarks which we own. It is our feeling the better use of our advertising money and budget will result in the event it is concentrated on a few of the important trademarks of our company. A considerable contribution to EYT's growth and to our trademark rights has been through acquisition. Unfortunately, a program has never been implemented in the past to phase out many of the trademarks which are secondary and tertiary. As a result, our trademark rights have multiplied substantially over the past 10 or 15 years. Many of the products associated with these trademarks, however, are related or similar. We have presently established a committee of which I am a member with our advertising people and management personnel to implement a program that will:

- (1) Determine the primary marks that we have;
- (2) Determine which marks should be abandoned immediately;
- (3) Determine which marks should be phased out over a period of years;
- (4) Determine a policy for selecting future trademarks.

DR. SIEGEL: It would be company-wide in scope?

MR. MCCLOSKEY: Yes.

DR. SIEGEL: Would a company like Du Pont have this problem?

MR. REYNOLDS: We've just completed a long range reorganization of our trademark activities at Du Pont which, like your own, has been an adjunct of growth and evolution in a broad based and heavily diversified product structure. In the first stage we reduced the number of our trademarks from 1700 down to 600 over a period of nearly 12 years. This was accomplished partly through gradual retirement of our weakest symbols, and partly by grouping closely related goods for sale under a single "family" trademark.

In the second stage of our long range reorganization we evolved a loose leaf "Du Pont Identification Manual." This contains a host of guidelines for our entire organization to follow in displaying the name Du Pont, our Du Pont oval house mark, our company-wide slogans as well as those 600 product trademarks. As for new additions to that roster we spell out in great detail the criteria which each department should follow in coining new product trademarks. Because of this manual we feel no need for a formal committee to do our selecting. Our organization is well aware of the fact that the manual cannot be altered as to institutional trademarks without approval of the top management of the parent company and as to product trademarks without approval of our middle management.

In the third stage of our reorganization we turned over the house-keeping and monitoring jobs on our trademark structure to the lawyers. The task of mothering our registrations and files is handled by a thoroughly competent Trademark Registration unit of our Legal Department. The monitoring is done by a group of 25 lawyers that sit at the elbow of every departmental head in the parent company, and at strategic geographical points from Montréal to Geneva where they can be readily accessible to subsidiary heads and closely affiliated operations.

One interesting point about these 25 lawyers is that they are not patent lawyers. They are generalists usually trained in the field of trade regulation. As such they are experts in sensing, contesting and containing abuses of trademarks and franchise operations which our system of free competition seems to breed incessantly both inside and outside the framework of every large corporation. In short, they are more consumer-oriented than they are laboratory-inclined.

By the way of a wrap-up on this long range reorganization, we believe it has produced these results (a) we have discarded years of

accumulated deadwood from our trademark portfolio; (b) we have provided our organization with a workable set of guidelines for self-administration; (c) we have generated a classic managerial system in which our trademark activities are highly centralized at the policy level of the parent company and widely decentralized at every operating level throughout the world; (d) we have oriented our housekeeping activities into the most modern electronic and computer equipment known to today's technologists, and (e) we have staffed our organization with watchdogs that are best trained to service our trademarks in keeping with greater consumer protection and sterner regulation of international trade.

**DR. LADAS:** I have also some experience with the so-called regional mark of which Mr. Reynolds said something before. But in view of this fact that there is such a tremendous dearth of trademarks and there are conflicts, unavoidable conflicts, you may find that you can register a trademark pretty well in Africa but not in Europe or in Latin America or the Far East, and conversely.

And I am coming to the conclusion that many times it is practically impossible to have a trademark that you can hope to register all over the world, unless you are prepared to buy out anticipations. So you may come to think of different marks for different groups of countries which are separable commercially or market-wise. We may have to come to this kind of policy of thinking of the world in regions, rather than in world-wide view.

**MR. REYNOLDS:** When my people think in those terms, I keep calling up the trademark image which Professor Oppenheim mentioned earlier; namely, we must think increasingly of the universal consumer when we approach trademark management. We dare not partition today's customers into an African consumer, a Far-Eastern consumer and so on. That would compel us to set up separate little advertising campaigns tailored to each of these little pockets. The resulting waste of advertising dollars simply makes any such partitioning a prohibitive matter. I am fearful that the range of today's advertising has far overshoot the regional, sectional or jurisdictional bounds that are tied by inertia to outmoded trademark registration customs and procedures.

**MODERATOR LIGHTMAN:** Mr. Cooke.

**MR. COOKE:** Oppie brought up the question of the consumer situation, the atmosphere into which we are moving very rapidly. I note that those who were at the APLA meeting on Monday at luncheon heard the Commissioner of Patents of Canada, state it as his opinion that Canada considers itself a consumer country, and I think this is sound in

view of the fact that a relatively small number of Canadian patents are issued to Canadian inventors and I assume a relatively small number of Canadian trademark registrations may be likewise registered by Canadian companies. He pointed out that within two years he expects the Canadian patent law to be pretty substantially modified, as he put it, away from what he called the American strong patent system to a weaker patent system in which there would be a greater opportunity for opposition, for effective government licensing, compulsory or otherwise, with priority on a first-to-file basis and so forth.

Now, there's no doubt that that same trend is going to be felt in trademarks sooner or later, although perhaps not as immediately as in Canada, and I would certainly think in many of the countries in the world which are consumer countries, there is considerable doubt that there is as much value in having foreigners take out and maintain strong trademark positions as there might be. I think it's something that everyone has to face. I would hope, incidentally, this afternoon there will be some discussion of the question of whether foreign trademarks should be held by subsidiaries or parents. I think these are two closely related questions that are important.

**MODERATOR LIGHTMAN:** Gentlemen, we have time for one more question.

**DIRECTOR HARRIS:** It will have to be a quickie.

**MODERATOR LIGHTMAN:** Mr. Murphy.

**MR. MURPHY:** I just want to make an observation on Japan with regard, at least, to housemarks. We found out that with the rampant piracy that often exists, it is more economical in the end to obtain a blanket coverage in both English and Katakana characters in all classes in Japan than it is to go in piecemeal with various applicants from time to time and spend, let's say, in the neighborhood of \$5,000 to \$10,000 to buy out an applicant in an important class. Recently, we had an instance with Avis where someone had filed for the AVIS mark in the class which included buttons and the like—and, of course, Avis was using and uses buttons and like goods in its promotional campaigns. We received outside opinions that a registration based on this application might cause us difficulty in connection with use by Avis of the AVIS mark on promotional buttons, and that even if we were to prevail it would cost us an awful lot of money. We bought this particular application from the pirate and immediately decided that it was to Avis' benefit to get the blanket coverage referred to above, which we feel for an important house mark is absolutely necessary, and in the long run economical, in Japan.

**DIRECTOR HARRIS:** Gentlemen, I hate to interrupt, but we are due for lunch at the Adams Rib, which is on the ground floor of the Joseph Henry Building—that's the large new building on the corner of 21st and Pennsylvania. I hope you will devote your luncheon conversation to non-doctrinal topics and keep your best doctrinal ideas for the afternoon session. We will return here, hopefully, at approximately two o'clock.

## **Afternoon Session**

**DIRECTOR HARRIS:** Gentlemen, we are reassembled and to save time, we'll start at once. Mr Lightman.

**MODERATOR LIGHTMAN:** This morning we heard speakers on the subjects of international treaties, and laws, and on the Madrid Agreement and its alternatives. This afternoon's session will be devoted to the practical problems of what you have to do and watch out for in protecting your trademark rights abroad. As the first speaker, I call upon Paul Hoffmann, Trademark Counsel of General Electric Company. His subject will be "Trademark Protection and Enforcement Abroad," Paul.

### **PAUL HOFFMANN**

When Joe called me suggesting that I act as one of the discussants talking about "Trademark Protection and Enforcement Abroad," my first question was: "To what kind of an audience will I be speaking?" And when he told me, I said, "Oh, no! That's not a subject for these people. These are all experts. What can I tell them?" He insisted that I think about it and he said, if you want to, look up the last two clinics in *IDEA*. I couldn't lay my hands on them so, like a man who jumps into a pool without looking whether there is water, I said, "Yes." Two weeks ago, he sent me the two copies and then I knew there was no

water. And, having listened this morning, I'm sure there was no water.

But, picking up my bones I decided, well, I'm going to do it and while I am quite sure that I can't tell you anything about how to protect trademarks and their enforcement, maybe you'll find it interesting to hear how we at General Electric Company do it.

DR. SIEGEL: Your remarks will not be out of order.

MR. HOFFMANN: In order to understand our trademark philosophy, two points need to be kept in mind. We are primarily a one-brand company, and we are decentralized. The use and administration of trademarks at General Electric is governed by a rather detailed policy issued by the Vice President of Public Relations. It deals with the ownership and functions of the two primary trademarks, which are owned everywhere in the world by General Electric Company.

MR. COOKE: By the parent company?

MR. HOFFMANN: By the parent company. The GE monogram and the signature mark, GENERAL GE ELECTRIC. The policy also deals with the ownership and subordinate function of secondary trademarks, which are also owned by the parent company—anything that is originated here in the United States we own around the world. There are some exceptions, but the rule is, the parent company owns all marks.

The policy determines under what circumstances marks may be licensed and what approvals are required, use of the trademarks by dealers, the administration of the trademarks, and this is where we lead into the area of protection and enforcement. The housemarks are administered by the corporate trademark counsel, both in the United States and overseas. In effect he has world-wide responsibility for the housemarks. But, just as a lawyer in private practice has to have a client, the company lawyer requires the approval of an operating executive before getting involved in a major controversy regarding the housemarks.

Secondary trademarks are under the jurisdiction of the Product Departments which originate them. Each department registers its own mark in the United States, and the corporate trademark counsel functions only in an advisory capacity. He also is consulted prior to the institution of contested proceedings. The foreign protection and enforcement of secondary trademarks lies with the trademark attorney of the International Division who functionally reports to the trademark counsel, but acts only under instructions from the departments, since only they can really know to what extent protection is required.

Having laid the ground work, I can now go into the strategy which is being used in the protection of the marks as well as their enforcement. While this strategy is to a considerable extent tailored to the needs of

my company, I believe that it can probably be used by many other companies.

Strategy is defined by the dictionary as "the science and art of employing political, economical, psychological and military forces to achieve a maximum result." I try to work on a plan for protecting and enforcing trademarks based on economic, psychological and, of course, legal considerations.

**DR. SIEGEL:** No military?

**MR. HOFFMANN:** No. Faced with 160 countries and territories in which trademarks may be registered and classification systems that require several registrations in each country demands a total assessment of the business needs today, tomorrow, and 25 years from now. And I know that some chickens come home to roost when they're 25 and 60 years old.

Obtaining trademark protection is in some ways like buying insurance. The real question we all wrestle with is how much is enough? Insuring against fire or burglary, the main criterion is the value of the property, but the distance from the nearest police and fire station, and the effectiveness of the police and fire departments (when they're not on strike) also need to be considered. Thus, in the case of trademark protection, one must take into account the effectiveness of the trademark laws and the sophistication and reliability of the courts of a country before deciding whether it is worthwhile to register there.

In planning trademark strategy, I consider the following factors:

- (1) Is it a housemark or product mark: Obviously the housemarks require greater protection.
- (2) The nature of the product: Producer goods which are products normally sold to industrial customers, need generally less protection than consumer goods. The amount of protection is inversely proportional to the size of the product. Trademarks for locomotives and generators need less protection than those for transistors.
- (3) The law of the country where protection is sought: We are all aware of the differences in the amount of protection required in first user or first applicant countries.
- (4) The attitude of the law and the public towards trademarks: The jurisprudence of various countries differs in sophistication and reliability. Piracy may be more or less prevalent.
- (5) The commercial importance of the country: It is not necessary to register a trademark used on nuclear fuel in an underdeveloped country where its manufacture is not a real possibility.

And here I want to deviate from my text, because I saw yesterday, or the day before, a publication in the *Russian Gazette*, for Tootsie-Rolls, for the Tootsie-Roll package. I just wondered what kind of reasoning went behind registering the Tootsie-Roll trademark in Russia in English.

Finally, point (6) Cost: One must take into account not only the out-of-pocket expenses of obtaining registrations, but also of maintaining what could eventually be an excessive number of marks.

As to the protection of housemarks: The more famous a mark, the more protection it deserves. If cost is no limitation, strategy is simplified. Register the mark in all countries in respect of all goods for which registration can be obtained, irrespective of their immediate interest and without considering whether or not such registrations can be enforced. I know that this approach has found favor with some trademark owners, but I do not advocate it, not only because cost can be very substantial, but also because enforcement of unnecessary registrations may be the cause of unfavorable publicity for the trademark and its owner.

What is the alternative? I believe the solution lies in protecting your housemark in the most important countries in respect of all goods of actual, possible and peripheral interest even if a multitude of registrations is required, the number of registrations being in direct proportion to the importance of the country as an existing and potential market. Obviously, in those countries where one registration can cover more than one class I advise registration of the trademark in respect to a very broad list of goods without going outside the sphere of interest of the trademark owner.

As you know, European firms—and, I suspect, some American firms—use the strategy of registering both their housemarks and product marks, in respect to all goods. This has, of course, the advantage of deterring new applicants from adopting a similar mark, even in a far-removed field. If a new applicant asks the prior registrant for a consent to the registration of his mark, the registrant can and often will extract concessions which may be of some value in the future in a foreign country.

I personally disapprove of this strategy because I believe that trademark owners, like everybody else, should consider the public interest in their actions; I recall we talked about it this morning. The Register is very crowded in nearly all countries and it is difficult enough to adopt and find new marks. There is no need to make it more difficult. Fortunately, the concept that a mark must be used to remain valid is



gaining ground everywhere, so that there is reason to hope that this legitimate form of extortion will fall into disuse.

To sum up, I recommend the following strategy for the protection of housemarks:

- (1) Register in respect to the most important products in every country in which registration is possible. We do and we are registered, I think, for electrical goods wherever we can.
- (2) Register in respect to all goods of actual, possible and peripheral interest where this can be done with one registration.
- (3) In key countries, even if it means obtaining many registrations, register for all goods of actual, possible and peripheral interest. For instance, in Germany we have a very, very wide registration, but not for food, for instance.
- (4) In commercially less important countries, register only in respect to goods of interest, keeping in mind what steps the competition is capable of taking in imitating your products.

Now, as to product marks: The protection of product marks requires a different type of approach which really calls for more planning than that for housemarks. While a business has usually only one or two housemarks, it may have five hundred or more different product marks. If you adopt the same strategy of registering in each country, you come up with the fantastic figure of 80,000 registrations. Add that to the fact that an active company may originate 20 new marks or more a year, and the need for a strategy becomes obvious.

I know that I am whistling in the dark in advocating a strategy in accordance with which a trademark in the United States will not be adopted until its availability has been checked out in foreign countries. Unfortunately, this procedure of coordinating the United States and foreign effort is hardly ever followed, in part because it is too time-consuming and requires planning too far ahead, not to speak, of course, of cost. As you know, usually a mark is being selected, taken into use in the United States, and protection overseas is sought thereafter—frequently only after the mark has become fairly well known in the United States. Thus, our strategy must be tailored to this *modus operandi*.

The easiest approach is, again, a blanket approach, a plan under which every new product is applied for in a large number of countries. Again, I don't recommend this strategy because it leads to a great amount of waste and dead wood since only relatively few products are so successful that their trademarks merit registration in all countries. If you stop to think of all the registrations you have, and all the American

products that really have world-wide significance, you'll be surprised how few you come up with.

On the other side of the spectrum is the approach which is very parsimonious with registrations. The justification for this strategy often is, particularly in the area of industrial products: "Well, the other party will not know about it; we will never be found out." Another argument is that it is really not necessary to register a trademark in a country where rights are determined by first use, since you can normally prevent a latecomer from adopting a similar mark. I don't favor this approach either, because enforcing a mark based solely on first use is infinitely more difficult and costly than enforcing a registration.

I favor a course of action which lies between the two extremes, and which I call the "key country and concentric circles" strategy. Which countries are key-countries depends on the area of primary commercial interest of a company and the product. But once registration has been obtained in these countries, the mark has really become a rare and important property. At that stage I would advise extending registration to another 10 to 15 less important countries. It is true that possibly in the meantime the mark may have been stolen or infringed innocently in one of the commercially less significant countries in which protection had not been obtained. However, there are always ways to recapture a mark, such as paying for a consent or buying the other mark, and let us be realistic, the incidence of piracy is relatively small in Zanzibar or Fiji.

Having registered your mark and set up a watching service to help you enforce it, what is the strategy to be used in the enforcement of trademarks? The basic question, as in the protection of trademarks, is how much? Should a trademark be enforced rigorously against any and all similar marks in any and all countries, and if not, how selective can enforcement be without impairing the value and validity of the mark? There are a number of criteria that I apply in deciding whether or not to enforce a trademark:

- (1) *The nature of the mark.* Obviously a mark like KODAK is easier to defend than GE.
- (2) *The commercial importance of the mark.*
- (3) *Dilution.* Sometimes famous marks are used by imitators on unrelated goods. I think that attorneys should search their souls to determine whether such a use is really harmful to their client's mark, or whether they are just engaging in legal niceties. I for one would not particularly worry if GE were used on lollipops in Hongkong.

- (4) *The law of the country where the infringement takes place.* The laws of the country concerned have to be taken into consideration. In certain countries it is more important to defend a mark than in others. For instance, if the jurisprudence does not take into account similar marks by third parties in a trademark opposition or an infringement action, it is less important to enforce a mark against a similar one than in a country such as Germany where the so-called "distance theory" applies.
- (5) *The nature of the action.* In some countries a trademark can be opposed or cancelled through administrative proceedings at the Patent Office, while in others a full-fledged court action is required. There is an understandable tendency to prefer an administrative proceeding over a lawsuit, not only because of the lesser cost involved, but also because the final effect is less drastic than that of a judicial adjudication.
- (6) *Cost.* Last but not least, the benefits to be reaped from very strict enforcement must be balanced against the cost.

Based on the foregoing, what is the recommended strategy? The housemark must be defended at all cost against clear-cut infringements. Enforcement should be attempted even if no sales are being made in the country where the infringement occurs. Permitting a third party to adopt your mark, even if not of immediate commercial significance, could lead to serious consequences in the long run.

If the offending mark is only similar, and there is apparently no intent to imitate, I advocate enforcement by administrative action if at all possible. Courts are usually much more difficult to convince of the confusing similarity of two marks and are also not bound by the technical consideration governing in Patent Offices which, in most countries, favors the first registrant. And, of course, I also always will try, if at all possible, to negotiate, before I take any legal action and I have found that to be the most effective way of doing business.

As to product marks, while some product marks are nearly as important as housemarks, I generally feel that enforcement should be somewhat less stringent and expenditures more controlled. One lawsuit may cost more than the profits made from the product bearing the mark over a period of years. I'm sure we all have tales to tell on that score.

There is one other and very important aspect which a company needs to consider in protecting and enforcing its trademarks, and that is the image which it projects by its actions in this area. Just as in other fields of endeavor, companies acquire a reputation, depending upon how

strictly and honestly they protect and enforce their marks, and how sound and accommodating they are in dealing with others. All companies would like to have a reputation for reasonableness and firmness. Consistent attitudes and actions over a number of years will promote such a favorable image. Once established, this will in turn be most helpful in carrying out a company's trademark policy and strategy.

I believe that when you heard I would speak about trademark protection and enforcement, you thought that I would discuss our case in England. But this is strictly not an enforcement problem, unless you represent the English General Electric Company, which is enforcing its marks against us. As to protection, it is true that I am protecting our marks from attack, but I don't think the topic included this kind of protection strategy, which can only be planned on a case-by-case basis. However, if you want to discuss this case, I'll be happy to talk about it. Thank you.

MODERATOR LIGHTMAN: Thank you, Paul. In keeping with our procedure, we will devote about five minutes to any clarifying or amplifying questions. Harold?

MR. KNOTH: I have three simple questions, Paul. When you say, you seek protection wherever you can, do you rely on cautionary notices and extensions of UK registrations?

MR. HOFFMANN: Well, as far as cautionary notices are concerned, hardly. As to extension of the UK registration, I'm having a problem right now. The UK registration is very limited.

MR. KNOTH: Do you try to register the GE and the circle as well as the GE alone?

MR. HOFFMANN: No, just the GE in the circle.

MR. KNOTH: Number three is, what kind of watch service do you have? Local or international?

MR. HOFFMANN: We use a New York firm.

MR. KNOTH: World-wide?

MR. HOFFMANN: World-wide.

MR. KNOTH: I may ask you after a while what kind of firm that is.

MR. HOFFMANN: OK.

MODERATOR LIGHTMAN: George?

MR. MURPHY: Paul, I wanted to ask a question in reference to ownership of marks. I think you indicated that product marks for products which originated in the United States stand in the name of the parent company in foreign countries. How do you handle situations

where a product originates with one of your foreign manufacturing subsidiaries rather than in the United States, and is first sold in a foreign country by your local subsidiary but is subsequently also manufactured locally by other of your foreign subsidiaries in other countries? For example, I don't know what your situation is, but assuming that there's a GE manufacturing company in one European country which originates a product and, subsequently, there are GE companies in other European countries which also will be manufacturing that product—how do you handle ownership in that kind of situation?

MR. HOFFMANN: If the mark is locally originated, like in Brazil or Mexico, it will be registered in the name of the local subsidiary which pays for it. We will be kept advised because central records are kept in my office. To the best of my knowledge, we have had only one situation where the Venezuelan company adopted a service mark and now the Mexican company is using the same mark and each company registers in its own name.

MR. MURPHY: I don't think it's the type of situation which would come up so much in South America as it would in Europe, where markets are more closely related, but maybe your situation is different.

MR. HOFFMANN: Yes, that is right. We do not have very many manufacturing subsidiaries in Europe.

MR. MURPHY: And also I wanted to ask, in naming your foreign subsidiaries, is General Electric included, as a policy, in the names of such subsidiaries?

MR. HOFFMANN: Not as a policy. Approval of the Chairman of the Board is required and approval is ordinarily not given unless we own sufficient shares to change the name and we observe very strict procedures to protect ourselves. This is really the toughest problem right now. In all cases there is a desire to use the name. We've come to the conclusion we can't have different names all over the world, so the best is to try and take as many legal precautions as we can. We have tradename agreements, provisions in the articles of incorporation, et cetera.

MODERATOR LIGHTMAN: Paul, I want to ask a question with respect to service marks. Take a country such as Japan, which has no service mark classes, but yet, under the Convention, is obligated to protect service marks. How do you protect a service mark in Japan?

MR. HOFFMANN: I haven't done so. We have registrations for all of the goods that GE is interested in in Japan, but we haven't really tried to fight the battle.

MODERATOR LIGHTMAN: Later on, I'd like to go into this further.

MR. VON THURY: I may have just a suggestion. In case of service marks in countries where you have no service mark provision, you can register, say, as printed material in another class. Of course, I don't know how the enforcement will be. But I think in Japan and in Great Britain—I think in Great Britain, Class 16, which is the class for printed material, you register your service mark.

MODERATOR LIGHTMAN: One more question before we continue.

MR. McCLOSKEY: In defending or protecting house marks in foreign countries, are the charges borne by the corporation or the division which manufactures the particular product covered by the mark?

MR. HOFFMANN: No. When it comes to the housemark, the corporation pays the charges.

MR. REYNOLDS: What you're also doing, Paul, I assume, is to preserve all indicia of title, by which I mean all tangible evidence of the legal title to your mark strictly within the parent company. And it would be my further bet that you do this despite your key system of cost allotment among organizational units and subsidiaries so that you will have your records straight when you come to these obit cases.

MODERATOR LIGHTMAN: The next speaker is Dr. Ladas, who will discuss the subject of Unfair Competition in Trademarks Abroad. Dr. Ladas?

#### STEPHEN P. LADAS

The title of this presentation necessarily limits the question of unfair competition to this particular angle. In other words, how far unfair competition relates to the protection of trademarks.

We are prone to say many times that unfair competition is the broad principle of which trademark law is only a particular application or a particular aspect. That may be in theory, but in practice it isn't really so—the trademark law and unfair competition law are two separate legal compartments. The reasons are several:

First, the conditions of production, distribution and advertising of merchandise in the tremendously large markets in the present times have greatly affected the old primary function of a trademark as an identification of origin of goods. In the present economy of complex manufacture and distribution, the mark primarily enables a manufac-

turer or trader to distinguish his goods from those of others, and it also enables the consumer to make an informed choice. This function is strongly emphasized through constant repetition by impression on the consumer's mind by advertising and by symbolizing through the mark the actual or assumed value of the products.

Secondly, in this present function, the trademark has become an asset of tremendous value, the secure ownership of which to a manufacturer or trader is an economic necessity of paramount importance. Hence, there has been a nearly universal adoption of statutory law on trademarks based on registration as a basis of ownership and protection. It would be a contradiction to this idea for one to resort to unfair competition law to nullify the operation of a statute, the requirements of which have not been complied with.

Third, trademark law, because of its largely technical regulation, has reached a stage of maturity suitable to the exigencies of our modern society. Unfair competition law has evolved more slowly, and it is still full of uncertainties particularly when the legal materials at hand do not afford enough elasticity and the remedies available are not adequate.

As a result of these reasons, unfair competition law in a substantial number of countries today has a limited meaning or application to a variety of unethical or fraudulent trade practices, such as imitation of trade names, false or misleading advertising, industrial espionage, misuse of trade secrets, interference with contracts, dishonest marketing methods involving unfair exploitation of the public's credulity or ignorance, et cetera. And there are numerous countries in which there is no unfair competition law in the sense that the civil law of torts or civil wrongs has not been made to apply either by legislation or by court decisions to unfair competitive activities. In these countries only fraudulent activities coming within the scope of crimes punishable by a penal court may be reached in this domain.

Leaving these countries aside, since the subject we are concerned with has no application at all to them, I should like to discuss two groups of countries and the effect of their law of unfair competition on the protection of trademarks.

Before doing so, I would remind all of you that we have this very important stipulation in the International Convention, Article 10*bis*, which provides, particularly for our purposes here, in the first paragraph, the broad principle that any act of competition contrary to honest practices constitutes unfair competition and must be suppressed. This affirms the foundation of fair competition as being "honest prac-

tices," and is predicated on the assumption and on the hope that "honest practices" is a notion that has a theoretical universality and that there is an evolving aspiration to their realization in all countries. In fact, this realization is far from being widely fulfilled. Some of the reasons for this failure are:

- (1) The tort in unfair competition is part of the general law of torts of the national systems of law and therefore it is deeply rooted in the legal traditions of the particular countries.
- (2) Morality which is the source of the law of unfair competition is a simple notion in theory only. In fact, it reflects customs and habits anchored in the spirit of a particular community. There is no clearly objective standard of feelings, instincts, or attitudes towards a certain conduct.
- (3) The pressures existing in the various countries for the suppression of unfair competition differ greatly. Generally, the development of the law of unfair competition depends on active and intense competition in the marketplace by competing enterprises. It is the pressure of conflicting interests which leads to the establishment of clear rules. This pressure is not uniform. Then,
- (4) The question is asked: Where does lawful competition end and unlawful competition begin? The fact that a competitor may derive a profit from his act of competition or cause monetary loss to another is not in itself unlawful. The dictum "no one should reap where he has not sown" requires delicate application. Progress would be paralyzed and monopoly would be generalized if we should attempt to prevent persons from using the work or experience of others. We must encourage people to compete in the same trade or industry for the custom of the people on the most favorable terms. The issue is whether the means employed in competing are fair and lawful. On the other hand, a trader must be able to use devices by which he impresses his identity and that of his product on the mind of the public, and must also guard the benefits of his labor and his investment by preventing interference with the relationship he has established.

Thus, the law of unfair competition, like that of trademarks, is an ordering of interests, individual and public, growing out of the relationship of competitors among themselves and with the consuming public, in an effort to reconcile and satisfy all these interests. If the legislator has chosen to demand of the trader compliance with certain



legal formalities or requirements in this effort at reconciliation of his interests with those of his competitors and with the public, it is not wrong for the law to refuse to hear the trader who fails to comply.

Now, may I consider those two groups of countries I mentioned. One group of countries is, of course, the civil law countries particularly in Europe, which have developed a remarkable body of case law of unfair competition by evolving it generally from a general principle of a Civil Code or from supplemental legislation.

The best example of this is France where the whole gamut of acts of unfair competition has been brought by the courts under the general principles of articles—two articles in the Civil Code concerning Civil Liability. By a remarkable power of adaptability, the French courts were able to create a full-bodied case law. Civil law countries that have copied the Napoleonic Civil Code have followed the French courts in this development of unfair competition law, such as Belgium, Luxembourg, Italy, Netherlands, and Switzerland.

Germany had also similar principles in its Civil Code, but for a long time the courts refused to apply these to acts of unfair competition. This caused the government to enact the famous Act against Unfair Competition of 1909, and this has been copied by 10 other European countries: Scandinavia, Austria, Switzerland, and so forth. Since then, the German courts have done one of the finest jobs in developing unfair competition law and have influenced similar evolution in all of Europe.

A number of other countries which had developed a case law of unfair competition found it advisable to fix certain positions quite clearly by legislation—for instance, Italy, Belgium, Luxembourg, and Switzerland now have legislation—statutory legislation—on unfair competition in addition to the civil general principles that I mentioned before. But the result of that has been that it is now clearly assumed that an act of creating confusion by misappropriation or simulation of trademarks is not always covered by the unfair competition law.

In France, the new law of 1965 now provides, after one century of a different law, that registration is the only basis for acquiring ownership of a trademark. Thus, a mere prior user of a trademark in France can no longer avail himself today of the law of unfair competition in order to dispute the right of a prior registrant, except in certain qualified cases. And the owner of an unregistered trademark in France can only protect himself against a third party other than the registered proprietor or his licensee. Similarly, the Benelux Trademark Law, which went into effect on January 1, 1971, establishes the same position for the three countries. Article 12 of this law is sweeping in its effect. It reads:

Whichever the nature of the instituted action may be, no one shall have the right to lay claim to a sign, which is to be considered as a trademark in the meaning of this law, if he has not effected proper registration of such sign.

Thus, the prior user of a trade name, of a title of establishment, of a distinctive package, may avail himself of the protection of the unfair competition law, but not the prior user of what is technically a trademark.

In Germany, side by side with the right which has applied by registration only, there is also the possibility of acquiring trademark rights by user under the provisions of Section 25 of the Act which protects the so-called *Ausstattung*, which is "get-up," and in Germany get-up does include registrable trademarks as well as unregistrable trademarks. But in order to obtain the protection of that particular Section of the Act, one must produce very convincing proof that the relevant trade, the relevant class of consumers and traders, recognize that mark as a result of long and extensive use, as being a distinctive sign of an enterprise.

Similarly, the Scandinavian Uniform Trademark Laws protect both registered and unregistered trademarks, but the unregistered trademarks which they protect are marks "established" in the marketplace, and proof of such "establishment" by long and extensive use must be shown.

In Japan, also, there is a provision in the trademark law that protects the prior user. But the prior user must prove that his mark was "widely known in the territory of Japan," and "widely known" means exactly what it says, in the sense that the Tribunal will require a very large number of trade declarations and affidavits testifying to such wide knowledge. Very rarely may this onus of proof be discharged.

The conclusion is that in civil law countries where the principle has been established by statute that registration is the basis of ownership of a trademark, the unfair competition law will not, in the ordinary case, enable the owner of an unregistered trademark to succeed in ensuring protection. This is subject, of course, to specific exceptions:

- (1) The advantage that can be taken of Article 6*bis* of the Paris Convention if one can prove that the mark is well known in the territory.
- (2) Another advantage which can be taken by the new Article 6 *septies*, of the Convention when the registrant is the agent or representative of the proprietor of a trademark and applies for or registers, without proper authorization, the trademark of his principal.

- (3) When special provisions exist in a particular country, such as the German Act I mentioned and the Scandinavian laws.

However, the Unfair Competition Law in civil law countries may be availed of for the protection of registered trademarks as a supplement to the Trademark Act, particularly in cases of extended protection beyond the scope of registration. This is where the true character of the law of unfair competition exhibits itself in Europe.

In British law countries—this is the second group of countries I would like to talk about—there is no protection of unregistered trademarks as such by a common law trademark infringement action. Protection of unregistered marks is afforded only by the law of passing-off, and this is quite different from what we understand as common law of trademarks. At this point, may I suggest respectfully that we should be very careful when we talk about common law countries and civil law countries. There is no such thing as common law countries in this field. It's United States law and foreign law. That's what we have now.

The principle of the law of passing-off in British countries is that no person can represent his goods or his business as the goods or the business of another. The issue then is whether the defendant's misrepresentation is such as is likely to deceive or mislead the public into believing that his goods or his business are those of the plaintiff, when they are not. The plaintiff must not only establish his ownership of the mark by adducing evidence of prior use, but he must prove such use of the mark for such time and in such manner that the goods have become known in the market by such mark.

In a passing-off action in order to succeed, a plaintiff must establish that the defendant is selling or threatening to sell his goods in a manner which amounts to a false representation as to origin. And in determining whether the defendant is doing so, all the surrounding circumstances have to be taken into consideration, including not only the resemblance between the two trademarks involved but also the similarity or differences between the get-up of the goods, the price of the goods, the geographical areas covered by the trades of the two parties, the outlets, and so on.

Thus, the fact that the plaintiff has always used a distinctive package or label is very relevant. The defendant in a passing-off action is entitled to rely on all these differences in support of his contention that he has adequately distinguished his goods from those of the plaintiff.

On the contrary, in an action based on a trademark infringement which can involve only a registered trademark of the plaintiff, the necessity of introducing evidence is irrelevant. The probability of

confusion or deception existing *in fact* is not a necessary ingredient of the infringement action, the sole question being whether there has been any infringement of the statutory “monopoly right” derived by the registration. If two marks are confusingly similar in themselves, a registered trademark and the defendant’s mark, and the goods are alike, there is such infringement of the monopoly right.

At this point, I would like also to add this: This difference must be very much kept in mind, and one must not voluntarily and easily, as in this country, sue for infringement and for passing-off, because of the burden of proof, circumstances of which are entirely different—if some of you would like to know, to read carefully about it, because it’s a tremendously important point in enforcement rights, I would ask you to read the judgment of Justice Romer in *Lever Brothers, Ltd. v. Sunniewite Products, Ltd.* 1966, 66 R.P.C. at page 89, starting from line 7 to page 90, ending in line 43. It’s a most illuminating discussion.

Basically, then, a passing-off action in England is concerned with interference with a competitor’s goodwill rather than with the deception of the public. Indeed, the *Spanish Champagne* case is the first case in England where the court expanded the theory of passing-off to apply to a case where the act complained of was essentially a dishonest act which would mislead the public. And this comes back to what Francis Browne said before: British countries are worse than civil offense countries from that point of view, when it comes to whether you protect the property right or protect the public against deception.

Most impressive in this connection are the words of Justice Cross in the *Sherry* case, referring to the decision of Justice Dankwert in the *Spanish Champagne* case: I’m going to read these few lines because they are tremendously important. This is what Cross says about Dankwert:

He uncovered a piece of common law or equity which had until then escaped attention—for in such a case there is not, in any ordinary sense, any representation that the goods of the defendant are the goods of the plaintiff; and evidence that no one has been confused or deceived is quite beside the mark. In truth, the decision went beyond the well-trodden paths of passing off into the un-mapped area of unfair trading or unlawful competition.

Listen to that: un-mapped area of unfair competition. The British court talking that way!

Now, I may end by considering the practical question how far unfair competition exists with respect to misappropriation of trademarks in the world. I should say from my experience of 40 years that generally it is less now than it used to be in earlier years. This is due particularly to

the fact that American enterprises have realized the basic differences of foreign law from our law with regard to ownership of trademarks, and do generally understand the need or advisability of early registration of their marks.

The real problem today, as I said before, is to find and be able to register new marks in a wide number of countries. Multiplication of business and products have created a real dearth of available marks.

But there are, of course, many examples of misappropriation motivated by dishonest competition. I am sorry to say that the majority of these cases occur in a country in which I have many friends, and which I am sure these friends also deplore—and this is Japan. There is a certain explanation for this, as I mentioned before. Japan is a country of small industry. There is tough competition and there is a constant seeking for well-known foreign marks to adopt or imitate, usually in equivalent Katakana characters, but also in the original English. Often this taking of another's marks is too blatantly unfair and dishonest.

The latest example which I may cite is this one—and I cite it because it may be important for several of you who represent corporations here:

Here is a case where an American company joined to a Japanese company to create a joint venture. As you know, you have to file the agreement of the arrangement with the Bank of Japan and MITI for approval. The American company wanted particularly the joint venture to use the American marks, and because it insisted on that provision, it was allowed to have an investment of less than 50 percent for that reason. As you also know, I'm sure, the competent Ministry (in this field of food products the competent Ministry is the Ministry of Agriculture and Forestry) consults associations, trade associations, and even competing firms, and asks for their opinion or observations about the arrangement which is being submitted to them for approval. This happened in this case. The negotiations started in the middle of 1969. The application was communicated by the Ministry to the various associations about November or December. From November 1969 to March, 1970, nearly 30 marks of the American company were registered by competing firms. The question is how can you get those marks back in case the American company had no registrations in Japan, or the wide use required by Japanese law.

I have discovered certain things I am going to submit to you because you might want to use the example. You know the Japanese Unfair Competition Law won't help you, because it requires that, in order to protect your trademark, it must be widely known in the market. There is a provision in the Trademark Act, Article 4, paragraph 10, which

says that the mark shall not be registered if it is in confusion with a similar mark widely known in the market. That also doesn't help. But there is also another provision, in paragraph 5 of Article 4, which says that a mark shall not be registered if it is against good morals and public order. That the misappropriation I mention is against good morals is obvious, because this is absolutely dishonest blatant misappropriation of trademarks to prevent the joint venture company from using American marks. And it is also against public order, I claim, in the sense that, if the court is going to allow that kind of dishonesty to be established in the marketplace, the public order of Japan is threatened. Japan is bound by the International Convention, by Article 10*bis*, to protect against dishonest acts in trade. Here is an opportunity to hold that this paragraph 5 of Article 4 is an intent to legislate in Japan in accordance with the stipulation of the International Convention.

I thought this would be a good example to end the talk with.

MODERATOR LIGHTMAN: Thank you, Dr. Ladas. Francis Browne has to leave and would like to comment.

MR. BROWNE: First of all, I would like to congratulate my colleagues on the panel, Tony DeSimone, Paul Hoffmann, and Steve Ladas on their fine papers. It surprises me no end how these papers dovetailed without having had any previous conversation among ourselves as to what the contents were going to be and how this was going to develop. I'm deeply flattered to be in this august company and I'm deeply pleased to be among so many good friends. And I'm sorry that I do have to leave for my prior commitment, but at least you're free to talk about me after I leave.

MODERATOR LIGHTMAN: Thank you very much.

DIRECTOR HARRIS: Thanks for participating.

MODERATOR LIGHTMAN: The floor is now open for discussion—questions?

MR. HOFFMANN: Well, I'll start on that final question regarding passing-off. You may find it interesting to know what happened in England. The English General Electric Company lodged three actions against GE. Two for trademark infringement and passing-off by our subsidiaries and the third action to expunge our mark from the Register. The reason for this action was that a registered mark cannot infringe another registered mark, so as long as our mark is on the Register we cannot infringe. Thus, our opponents would be left with a

passing-off action against the two subsidiaries, and they would have a very difficult time to prove it. While a court may find similarity of the marks it couldn't possibly find passing-off, because we didn't pass-off. All our advertising on labels bore the legend "Not connected with the English Company of a similar name." How can you pass-off, when you say you are not connected? This is why the case to expunge has become the main case.

**MODERATOR LIGHTMAN:** Dr. Ladas, you mentioned that you are going to try to seek corrective action in a trademark piracy case under provisions of the Japanese Trademark Law pertaining to public order and morals. I certainly hope you succeed. In our office, we have continuing complaints from U.S. firms faced with Japanese copying of their unregistered well-known marks. If you can get a favorable decision on this aspect of the Japanese Trademark Law, our life in Commerce Department, with respect to assistance to the businessman operating abroad will be much easier.

Mort Altin has a comment.

**MR. ALTIN:** Why, yes, we've had a very similar case where we've had a practically world famous trademark registered in Japan for only part of one class and it surprises me, but a very big, well-known Japanese company has registered the same trademark for the rest of the class. And they would be confusingly similar goods, I would think, in trade. And, when approached as to why they did this, they very frankly said, "Well, you know, one of your other divisions is opposing one of our other marks. If you'll withdraw that, we'll give you your mark back." But so far, it's just straight outright piracy.

One of the things I wanted to mention while I have the floor is, Dr. Ladas, there are these provisions of the International Convention, the Paris Convention, but I know I haven't had broad experience in trying to enforce them. I know that there are certain provisions with regard to registration of trademarks, "telle quelle" provisions, and so on.

One of the big problems that I find is that there are many countries that will join conventions and obtain all the benefits of conventions and yet when it comes to relying upon the provisions of the convention they say, "Well, in our country, international treaties are not self-executing and we have never passed the enabling legislation to make it in force in our country." Would you have some comments on that?

**DR. LADAS:** I think, Mort, there is now more and more compliance with these treaties. When I wrote my book many years ago, I believed and argued for the self-executing character of the Paris Convention. I do not press this now. Not because theoretically that is not true but

because, as a matter of practice, governments now change their law to bring it into conformity with the Convention.

As an example, Israel, as you know, has Section 11 which provides for the *telle quelle* principle of Article 6*quinquies* of the Convention. Israel gives effect to this Article by the decisions of the Patent Office contrarily to the previous system based on British practice.

Also, in the Scandinavian countries, if you have a U.S. registration and you submit a certified copy of it, you will obtain allowance notwithstanding the domestic law.

MR. ALTIN: But none of the British countries will do that.

DR. LADAS: British countries—no. It is the principle of British law that when a treaty concerns private right or concerns matters that have been covered by legislation, the treaty is never self-executing. You have to wait for the change of the law and none of them has changed the law to give really effect to Article 6*quinquies*.

MODERATOR LIGHTMAN: Dr. Ladas, have you ever known of a case where Article 6*bis* has actually been enforced in any country with respect to a complaint involving unauthorized registration of another's well-known mark? In such complaints we receive involving U.S. household marks that have been pirated abroad, many such marks are not household words in the countries of another's registration.

DR. LADAS: That's true.

MR. REYNOLDS: We have recently detected growing activity in that field of products liability known as "enterprise liability." This is beginning to raise questions in our minds whether a parent company—via its name alone—is likely to incur new legal exposure at the hands of subsidiaries who also use a world like "Du Pont" in their corporate titles or on their letterheads. Do you at General Electric now take this development into consideration in drafting your license agreements extending the GE mark to your subsidiaries?

MR. HOFFMANN: Not yet, but I've just written a memorandum on that point, the criteria you must consider when licensing and one of the things that I mentioned is the case down in Texas.

MR. REYNOLDS: That's the *McCain* case. (*E. I. du Pont de Nemours & Co. vs. McCain*, 414 F2d 369 (1969).)

MR. HOFFMANN: Yes. And it has, of course, even further implications in this country because you can't really prevent people from using your trademark on their product if they use a component or an ingredient, such as silicone, made by you. I have made the point that it may increase our liability. Our policy states that subsidiaries will get a license. The real problem we are now facing, is, can we or should we license the housemark to non-subsidiaries.



DR. LADAS: You are talking about manufacturing licenses. You can provide in any manufacturing license for liability due to defects of the products being borne by the licensee?

MR. REYNOLDS: I suppose that under the law of contracts if you are in an arm's length negotiation you can pretty well write in anything that the other party will buy in a manufacturing license. But I have technical reservations as to whether or not a wholly owned subsidiary or even a majority held subsidiary can ever be in an arm's length bargaining position with its parent company. So we approach these arrangements with subsidiaries as if they were primarily an exercise in accounting.

Accordingly, in our licenses with subsidiaries we will reserve title to the trademark, we will license it to them, we will specify the qualities of the goods, we will make periodic tests of their production for conformity with our specifications but since we do not have actual physical control of their production at all times, we will balk at the final step when it comes to underwriting their product liability. This is a risk which we think should remain with the subsidiary and non-subsidiary alike. To make certain that the sins of the sub will not be visited upon the parent by way of some trumped up theory like conglomerate osmosis, we spell out the sub's production responsibilities directly in the boiler plate clauses of the agreement.

MR. HOFFMANN: This is a salient point. What we have in the agreement is that if we are not satisfied with the product they will take it off the market and hold us harmless for all damage due to the defective product.

MR. REYNOLDS: You mentioned this *McCain* case, Paul, this case in Texas. For the benefit of those who haven't yet seen that decision it concerned the explosion of an end-product of one of our customers. We were supplying a very small ingredient to these people and we permitted them to mention our name in that context when they printed up their labels for the final formula. The Fifth Circuit Court of Appeals held us jointly liable for injuries caused by the explosion in question. It charged us with permitting our name to be used upon a product manufactured by another without determining the safety hazards of the end product.

MR. VON THURY: I would like to comment in connection with Mr. Hoffman's statement and recommendations concerning enforcement. I know that many of you are aware of the service which the U.S. Trademark Association gives helping registrants to oppose certain trademarks. We have just had an occasion in Japan—because we are talking about Japan—where one applicant applied for "Full-automata" for trans-

mission, and we found out that our Borg-Warner automatic transmissions are popularly referred to in the trade in Japan as "full automatic." We opposed. As a matter of fact then I reported to USTA, to Dorothy Fey, and I don't know what the service is.

MR. DESIMONE: Well, the service is that if the USTA is satisfied that the term is generic it will transmit the information to Joe Lightman's office who will then make representation to the State Department. But the USTA will not bring opposition. In the case you mentioned, I doubt that the USTA will take any action.

MR. VON THURY: As a matter of fact, the Embassy regretted the practice and thus far we received very civil reaction from the Japanese examiner. We filed a formal opposition. Of course, the opposition is based only on the contention that our products are popularly and generally referred to as "full automatic." And if the Japanese are to obtain this registration for the expression "Full automa" for the same product, there will be damage—injuries. So, the Embassy made representations, and I received a copy of that, too—and our opposition apparently was thus far favorably considered by the examiner—at least verbally he promised that he would refuse the Japanese application.

MODERATOR LIGHTMAN: Geza, I'm sure the Embassy made a diplomatic representation based on our instructions. But, I want to emphasize that representation against generic word applications is strictly through diplomatic channels. It is not in the form of an opposition proceeding.

MR. VON THURY: No, no—I meant this was in support—

MODERATOR LIGHTMAN: The U.S. Department of Commerce coordinates the Generic Word Protection Program with USTA strictly through diplomatic channels abroad. Our program does not involve opposition proceedings which must still be made by the interested party.

MR. VON THURY: I want to point out that this helps enforce our rights.

MR. KNOTH: Joe, this also has to be done before the mark is registered.

MODERATOR LIGHTMAN: Yes. Sometimes if the opposition period has expired, it might be a good idea to get a letter in the foreign patent office file, at least to go on record that the U.S. Government is against the generic term as a trademark. But the U.S. Government objection is based on the overall trade picture. We don't operate on behalf of any one company. Our interest is in seeing that U.S. exports are not impeded by registration of generic terms on trademarks abroad.

MR. KNOTH: Geza, how did you learn of this registration or attempted registration?

MR. VON THURY: From my Japanese associate.

MODERATOR LIGHTMAN: Gentlemen, the floor is open for discussion on any subject.

MR. COOKE: I was very much interested in Mr. Hoffmann's paper—in fact, all the papers. I remember that not too many years ago I suddenly found myself, with almost no trademark experience, in charge of the world-wide trademark operations of the Gulf companies. I started out with the premise that the housemark, the Gulf mark,—the major mark—should always belong to the parent company. That was all very well, except that we found that some of our subsidiaries had already registered some of our marks in their name. I think one of the most interesting solutions that we found in that case in Belgium was that we finally persuaded the Belgium registrar to take the position that, although our subsidiary had registered our name brands in Belgium and registered the names, they really did it for our benefit and therefore they were permitted to transfer the mark to us, so it came out much better than I thought it would.

I might add that I don't know whether this is just true of the oil companies, but there are some special problems of the oil companies to which I could refer, but I really found, as time went along, that when we did have some licensees outside who were non-subsidiaries, they were often a little easier to control and handle than our subsidiaries were themselves. This was because most of our subsidiaries had been in existence before they became our subsidiaries. They had their own staff, their own people and they had very little comprehension of our world-wide interests as distinct from their national interest.

I did want to mention a rather interesting problem. I suppose it is peculiar to the oil industry and I remember discussing this with Dr. Ladas before I retired. I think the problem has to a certain extent disappeared, for Gulf at least, because we've gone into more countries. But this is it: In many—in fact, almost all maritime countries—there has been for centuries an established maritime custom of having stockists at various ports. Not necessarily an open port—any port. They are supplied by Gulf or one of our subsidiaries with our products. They are not sold at that port by the stockist to anyone who comes along, but only to what were called “contract vessels.” A ship comes into the port with which one of our companies, or Gulf itself, has made a contract. The captain then says to the stockist, “We want so many barrels of this, so many barrels of that. Put it on board.” And eventually the billing

would come around and they'd get a bill for the goods. They weren't paid for then, nor were those goods available to anyone else unless under a similar contract.

The goods entered the port in bond. They did not go through customs, they were not subject to customs or tariff at all. From that standpoint, they never entered that country and they were not for sale to people in that country—only to the “contact” ships in passing. The question came up before we were actually selling otherwise in these countries, whether our registered marks were being used, whether this constituted use. I remember discussing it with you, although I don't know that I can quote your answer exactly, in London, way back at one of the Congresses.

That's an extraordinary situation. And I don't know if there are any other similar situations—it would be pretty much a maritime situation: fuel oils and lubricants. It might include machinery—I don't know.

MR. HOFFMANN: Like in a PX.

DR. LADAS: PX is a different problem. The thing that you mention relates to free ports and transshipments. Decisions in West Germany and in Holland have established this distinction. If the goods are consigned to a particular port and they stay there for transshipment, alright. But if they become a subject of commercial transaction, in other words, if someone takes possession of the goods and then disposes of that possession by some transaction, then it is an act done within the territory of the country and therefore amounts to infringement or amounts to use.

MR. COOKE: Well, it's halfway between those two positions. There's no original consignment. The ship comes in and says, “I didn't think I'd need it, but suddenly I need some more.” So the stockist supplies it and it goes on the contract.

DR. LADAS: Who supplies it?

MR. COOKE: The stockist who holds the goods gives that ship anything that's within the contract terms. But there's no specific consignment of that goods in advance.

DR. LADAS: Does he pay for it?

MR. COOKE: Not there. No. The shipping company pays Gulf rather than the stockist. The stockist is reimbursed by Gulf.

DR. LADAS: Well, I would like to see all the facts. What you have to find is whether there is a transaction—a commercial transaction.

MODERATOR LIGHTMAN: George?

MR. MURPHY: Paul, I wanted to ask a question on your licensing. When you license your GE mark to your various subsidiaries, is your

licensing done by virtue of a separate trademark license agreement, which only covers that subject matter?

MR. HOFFMANN: Yes.

MR. MURPHY: In other words, you don't have it under any type of a general relations agreement.

MR. HOFFMANN: In about 95 percent of the cases, we have a separate trademark agreement. I think that this is a separable situation. It is easier from an administrative point of view.

MR. MURPHY: What about your product marks. Are they also—you may have a number of them that would be in one license—the subject of license by formal agreement?

MR. HOFFMANN: Yes.

MR. MURPHY: In those trademark licensing agreements where you're dealing with your subsidiaries, is there any type of a royalty consideration?

MR. HOFFMAN: Well, that is a very, very difficult problem. We have been wrestling with this for years. You know, the difficulty in the problem is really Section 484 of the Internal Revenue Code. You've got to deal with the subsidiaries at arms length. What we do is this—the compensation for trademarks is part of that for technical know-how and patents so that there's a total lump sum of X percent for industrial property. This is logical because in some countries the know-how may be worth more and in others the trademark. Some companies will need and use more know-how than others.

MR. MURPHY: Well, I know it's a problem that cuts two ways because in one sense you're supposed to have income to meet the Internal Revenue Code Section and in another sense there are a number of countries where once you attribute income to trademarks you will not be allowed to get that income out of such countries.

MR. HOFFMANN: Like in Brazil, for instance, so we don't provide for a trademark royalty there.

MR. MURPHY: But it seems that at least as far as Internal Revenue Service is concerned, your answer would be that there is some package compensation here. Is there any provision or language in your trademark license agreements, since these are separate agreements, which could support your position from the very face of these agreements?

MR. HOFFMANN: Yes, "in consideration of the compensation provided for in the technical assistance agreement," and in the technical assistance and patent agreement it says "for patents, trademarks, and know-how."

MR. MURPHY: So that in wording the agreements—

MR. HOFFMANN: They all tie in.

MODERATOR LIGHTMAN: Mort, I think, has a comment.

MR. ALTIN: Yes, there was some mention in recent discussion about ownership of trademarks. And I just thought I would mention something that hasn't been mentioned up till now, and that is that in earlier years it was always easy to adjust the ownership of trademarks between parent and subsidiaries back and forth, depending upon changing circumstances. But for the last eight years, since the amendment to the Internal Revenue Act of 1962, there are very serious problems with the U.S. Internal Revenue if you want to transfer a trademark from parent company to subsidiary, or back, or the other way around. And this always has to be looked into.

And I'd like to go on and ask one question of Dr. Ladas. There was some mention made of PX cases. Now, this has come up a number of times. Is there any sort of generalization that can be made as to how the various countries in the world treat that as use?

DR. LADAS: Generally, the question has come up for other reasons, because the authorities and the interested parties don't know what is going on in the PX's. But if you wish to take advantage of sale of goods in the PX bearing your mark, then I think you should theorize as follows: We are talking sometimes that there is an extraterritoriality involved. During the time of war and military occupation there is extraterritoriality, but in peace time there is no such thing. The place where the PX is located is not territory of the United States. It is just absurd to think so. It is legally the territory of the country concerned.

We have arrangements with the governments concerned wherever we have military bases in foreign countries. And the arrangements are arrangements which really are to save us, to relieve us, from administrative control, from interference by the government of the country in which the PX's are located. It is a matter of courtesy, of absence of embarrassment.

So, therefore, if the mark is being used there, this is local use. You have sold the goods with the mark to the PX or to the organization who sells to the PX. The PX sells the goods to the military or civilian personnel whom the PX store supplies. These are transactions taking place in the foreign countries, not in the United States. There is use of your mark and there may be infringement of a local mark, although it may not be discovered.

MR. ALTIN: So these cases could come around two ways? There could be cases where—

DR. LADAS: Infringement.

MR. ALTIN: Infringement or, on the other hand, trademark use.

MR. DESIMONE: You could always find one or two black market operations to extend the use into the country.

MODERATOR LIGHTMAN: Oppie?

PROFESSOR OPPENHEIM: This is for my own enlightenment. You experts know the answer, but Mr. Hoffmann has been talking about the criteria or strategy in connection with a single registration covering various classes of products, as against a more selective approach to registration. Mr. Hoffmann, does that mean that you would be interested in having a registration, for example, covering all electrical products?

MR. HOFFMANN: Well, we go into many classes in addition to electrical. The chemical class, for instance, because we have a chemical division, medical instruments.

PROFESSOR OPPENHEIM: I don't want to use the word "conglomerate." I see that you are referring to diversification of products.

MR. HOFFMANN: Yes.

PROFESSOR OPPENHEIM: This is what I am getting at. Suppose you have a genuine case of diversification—a very broad product mix that you now have or that you contemplate having. Then I would suppose there wouldn't be any adverse effect on the public interest attached to a broad registration covering the various types of products. Trying to get such a registration not only takes care of the products you now produce, but also, in a rapidly diversifying enterprise, the registration would cover other new product lines. You might then justifiably say, "well, we had better have a very broad coverage." I am not versed in what that means. To what extent should a single registration cover many classes of products?

MR. HOFFMANN: Well, that depends on the country. In some countries, like Germany, you can get one registration for all classes.

MR. DESIMONE: It's bad philosophy because you have to be very honest with yourself as to whether or not you really have an intention to use this mark in the various classes, otherwise, again, you see, you're proliferating trademark registration into classes where you're really not going to use them.

PROFESSOR OPPENHEIM: I suppose the analogy is found in the cases we've had in the U.S. on territorial protection of a mark where a party tries to preserve a broad territory as his own, instead of getting protection only in areas where there is a reasonable probability of expansion of his business using the mark.

MR. DESIMONE: That's right. The minute you get into the question

of classes, the trademark right should be associated with its use, and you should lose your trademark rights within a reasonable time through non-use, and one of the problems is that if you get into too many classes you're going to have non-use. Of if you have non-use in many of those classes for a long period of time you may not then do anything about it, you know, because many of these registrations run for 14 years or 10 years—so you've got a mark now on the register in a class where you're really not using it, and in all honesty, it shouldn't be there.

**PROFESSOR OPPENHEIM:** I agree with you and that is the choice I would like to see taken, namely, there should be a reasonable likelihood or some evidentiary basis to show that a company is likely to expand its business with actual use of the mark. I don't think that a conglomerate enterprise, for example, should be able to stake out any area it pleases for protection of any kind of a product mix.

**MR. DESIMONE:** I wouldn't accept that premise, because then almost any company can use this as an excuse for going into other classes but if you are guided more by, "What do I intend to use the mark on at the time I'm filing my application"—then you will find many, many fewer classes that you're really interested in.

**PROFESSOR OPPENHEIM:** I must agree with you. It is a matter of public policy.

**DR. LADAS:** It may help you for a while. In other words, you might do it. But when it comes to a question of non-use, you may be in difficulty. In Germany, the law has been changed now. It provides in an opposition case, for instance, if you question the fact whether the opposer has used his trademark, he has to introduce proof of use and, insofar as he does not prove use for particular goods covered by his registration, he cannot win.

**PROFESSOR OPPENHEIM:** That's why I distinguish, for example, a situation like General Motors Corporation. Years ago General Motors was accused of being a conglomerate. In my mind, General Motors is far removed from the usual meaning of "conglomerate." For example, the General Motors electric refrigerator, with the trademark "Frigidaire" is technically and functionally related to the art of motors. Therefore, Frigidaire refrigerator is really a product extension which is functionally and technologically related to the areas of General Motors' main enterprise. General Motors developed a fractional motor for its Frigidaire refrigerator because it had been found that prior to that time the motor in its refrigerator was not adapted to the size and the capacity of the body.

I still agree, however, that there ought to be some kind of a criterion



to limit registration so that it covers only products which are within the proper area of the product expansion of the company. In other words, I do not think that a registration should be allowed for every potential type of product which might possibly be produced in the future.

MR. DESIMONE: Well, in addition, I approve of non-user provisions and I'm glad that Germany is soon getting one. I think more emphasis should be put on the non-user provision concept. You'll be alright for a while, but after five years, or three years, or whatever the non-user provision, unless you can prove use you're in trouble. The only difficulty is that in most countries someone has to attack the mark after that five-year period.

DR. LADAS: Or file a similar application.

MR. DESIMONE: There has to be created a confrontation. Otherwise the registrant has got this mark sitting on the Register in a particular class and it's fine.

PROFESSOR OPPENHEIM: As I said earlier, I think that there should be some kind of a statutory period to avoid registration of marks which are not being used or which are not likely to be used. I think it is good public policy to require the registrant within a certain statutory period to show that he is actually using the registered mark.

MR. DESIMONE: Right.

PROFESSOR OPPENHEIM: In other words, an attempt to use within, let us say, five years, would be a good way to prevent someone from keeping on the Register a mark which is not being used over a long period of years and thus preclude others from making actual use of the same or similar mark.

MR. DESIMONE: Right, and we get rid of a lot of dead wood.

DR. LADAS: My experience in a variety of companies is, they don't make any abuse in these countries of the registration system by going into classes in which they are not concerned.

MR. DESIMONE: No, they don't, in fact.

PROFESSOR OPPENHEIM: I was simply trying to get some more knowledge about what is happening in the international trademark field.

MODERATOR LIGHTMAN: Mr. Williams?

MR. WILLIAMS: I would like to ask Mr. Hoffmann—if I can enlarge his comments a little bit—what he says about the trade name, the names of their subsidiaries. Now you say, I believe, that you don't license anybody to use the housemark unless you have 75 percent of it.

MR. HOFFMANN: Our policy says majority control as far as a trademark is concerned, except with approval of the Chairman of the Board,

and we must have enough voting control to be able to change the name, and generally not less than 75 percent.

MR. WILLIAMS: That applies also to the trade name?

MR. HOFFMANN: To the trade name, yes.

DR. LADAS: This is because in foreign countries under the Companies Law, usually you cannot change the name with mere majority of the stock. You have to have more than a majority. Therefore, that explains the reason for providing in the name clause of the licensee that the name has been adopted by special permission which is revocable at the discretion of the licensor.

MR. HOFFMANN: What we say is, such approval will not ordinarily be granted to use the tradename, unless General Electric owns, directly or indirectly, at least 75 percent of the subsidiary's voting stock, but may be granted, in special circumstances, if the company owns sufficient voting stock to change the subsidiary's name. There are countries where a vote of two-thirds or even less of the voting stock is sufficient to change the name.

MR. WILLIAMS: This gives rise, I think, to a couple of other questions. One is: Is there any effectiveness, Dr. Ladas, in overcoming this rule contractually when the subsidiary is set up by requiring that the trade name be returnable when, for example, the parent loses majority control; and, second, if the parent loses control, can he successfully resort to the courts to have the permission revoked?

DR. LADAS: I know of a company that doesn't use 75, but insists on this: First of all, the foreign company must be organized under a neutral name if it's a newcomer. Or, if it's an oldcomer that has already a name, there must be a special meeting of stockholders at which the name clause of the company is changed to read somewhat as follows: "The name of the company shall be (I'm going to use your name) General Electric Company of Ireland, permission having been granted by the owner of the trademark, General Electric Company of New York, and so on, for the change of such name with the clause that the company shall have the right, at all times, to require that the name be changed." That is part of the statute, so that stockholders, creditors or the State have notice of the fact that the word General Electric, if that's the name, is not their asset. It's an asset of someone else which they use by permission and that permission is revokable at will.

MR. HOFFMANN: We do that. We have such provisions in the statutes but, of course, nothing helps you in the final analysis. Because, if eventually you have lost control without changing the name, and the shareholders tell you, "We are very sorry, but we are not going to

change the name," the only thing that I think can help you is, to make a contractual arrangement and set a penalty of \$1000 a day, or something like that, from the day you've said, now you change it and they don't.

DR. LADAS: The courts will not enforce that in a number of countries.

MR. HOFFMANN: It depends on each country. You have to do that country by country, and we have done this in all kinds of ways.

MR. WILLIAMS: I once asked a French attorney the following question: "If you have entered into such a provision by the articles of the corporation providing that the right to use the trademark reverts, but the mark was never used in France before use by a dissident majority that was originally a minority shareholder, and this shareholder would then say that there was no real consideration in the original contract (the trademark then having no value), but through their efforts this subsidiary has enriched the foreign parent's name and it now has a trade value, will the courts in France force the subsidiary to give this up? Can the parent get an injunction in such an instance to tell the subsidiary he can't use the name anymore?" The French attorney replied, "I doubt it very much. I think that the argument that the subsidiary had put all the goodwill into the mark would probably prevail."

MR. HOFFMANN: I think it is really quite an insolvable problem. The best case and the only one that I really know is the *Columbia-Nastri* case. It was written up in the *Trademark Reporter*—where the Italian subsidiary had taken over the name and would not relinquish it after it ceased to be a subsidiary. The Italian company sued the parent in the U.S. for reimbursement of royalties paid. The court in effect said, "Well, thieves shouldn't sue," and the American company succeeded in having the judgment upheld in Italy. There are very special facts here, but it is the one situation where the question of an appropriation of the name of the former parent has been litigated.

MODERATOR LIGHTMAN: Mort, do you have a comment?

MR. ALTIN: Yes, I want to get back to the question of the multiclass registration of a trademark. I think all of us must keep in mind that this has to be a flexible matter depending upon the jurisprudence of the country that you're talking about. In a country like the United States, where the test of infringement is whether a similar trademark is used on goods which would be likely to cause confusion, we say multiclass registrations aren't necessary. But when you get to countries where infringement depends upon infringement of an exact stated product which is mentioned in a registration in one particular class, then it

becomes necessary, particularly for well-known trademarks, to have defensive registration. Now many countries with laws of that type do provide for defensive registrations which are in other classes and will be associated with the main mark and, when used in one class, will constitute use in all classes, so they can't be cancelled. There is a very definite value and need for such registration where the jurisprudence is such that you have a very limited position in an infringement action.

MR. DESIMONE: Well, these countries you refer to have express provisions statutes relating to defensive registration. The criteria are recognized: First that you don't use the mark in that class if the class differs from the class that you are interested in, and secondly, it has to be an important mark.

MR. ALTIN: No. I'm just saying that it's got to be a flexible thing. If jurisprudence has to be taken into account together with requirements for use, and so on, to make a strict requirement that a mark that is registered must be used on this and that class otherwise it has to be cancelled, is not necessarily a realistic one.

MR. DESIMONE: It must be used—it should be used eventually in the class in which you're filing it, unless you're filing it as a defensive registration under an express provision of the statutory law of that country, which provides for defensive registration.

MR. ALTIN: Well, some countries don't label it that specifically.

MR. DESIMONE: They don't recognize it. They assume that your application for registration is in the class where you plan to use the mark.

MODERATOR LIGHTMAN: Go ahead, Gerry.

MR. WEISER: I assume your reference to licensing applies only to wholly owned subsidiaries and not to joint ventures where the law of the country would not permit you to have a majority controlling interest.

MR. HOFFMANN: Oh yes, we do have a few here and there but then we have management control. I think there's one exception now. But, of course, are you talking about the name or the—

MR. WEISER: The name.

MR. HOFFMANN: No, the name, not so far. And I don't think we will have that situation except under very exceptional circumstances—the trademark is another matter.

MR. WEISER: Do you feel the effects of your control of the trademark on the products on a non-controlled candidate? Let's say in Europe.

MR. HOFFMANN: Well, we do not have such situations as of now.

MR. WEISER: Is that, do you think, typical of the industry at this time or atypical?

MR. HOFFMANN: Well, of the industry, no. Westinghouse has a number of licensees who have no stock or management control. But of course, there's a difference whether your trademark is Westinghouse or General Electric. I asked Joe to have a study made, if possible, as to how the industry—not only the electrical industry, but generally—how companies look upon licensing their housemarks to non-controlled companies. The business pressures become very strong where a company wants to sell in a particular country but cannot do so because the product doesn't fit or there are import restrictions and a local company offers, "Well, sure, we'll make the product and we want your know-how, but we can't sell unless we have your trademark, because nobody knows us outside our area." So the pressures for that become very great and that is why I asked Joe to study—

MODERATOR LIGHTMAN: This is a project on the drawing board now.

DIRECTOR HARRIS: This would be GE? The housemark itself?

MR. HOFFMANN: Yes, General Electric.

MODERATOR LIGHTMAN: Paul, there's another problem that is quite serious with respect to trademark licensing. And that's in certain Far Eastern countries, such as Taiwan, where you have difficulties trying to get a trademark licensing agreement approved in the first place.

MR. HOFFMANN: Well there you don't even start them.

MODERATOR LIGHTMAN: But the situation is easing somewhat. I might add, some countries have been loosening their regulations a bit.

MR. VON THURY: I've come up with a piece of information that is exactly in connection with a policy in tradename and trademark. We have—Borg-Warner—I mention the name so it might go on the record—has a policy, probably similar along your line, your company's line. We distinguish between tradename and trademark. As far as our tradename is concerned, our policy is that we permit other companies abroad to use Borg-Warner if we own 100 percent. Nothing but 100 percent. Anything less than 100 percent (there was one exception, in Australia, 75 percent), we permit use of divisional names. So we have in Germany Brown-Boveri-York, GmbH. So that's the second stage, the divisional name. But a corporate name, only if 100 percent.

With trademarks, we're a little bit more liberal, more lenient because there we license—and, in connection with Mr. Murphy and the licensing, I may mention that we have a package agreement. But when we have a trademark agreement, in most instances we do not prefer to submit the main agreement because I had bad experience that the first

thing is that in the British countries the submission of the main agreement is asked where we have commercial and royalty indications that we don't want to disclose to competitors. Of course, we can submit and ask that it should be treated as confidential, but in registered user countries you don't have to refer to the main agreement.

MR. HOFFMANN: No, you don't have to.

MR. VON THURY: Therefore I think it is very wise to keep the trademark agreement separate from any package agreement where in the package agreement patent, know-how, and trademarks, and technical assistance are lumped together, and there are the royalties. For Internal Revenue purposes, that's enough.

MR. HOFFMANN: A policy of 100 percent control of a name is very simple and easy to exercise until you are told by a foreign government, "How about selling 10 percent to the public." At that stage of the game, are you going to take the name away or not? and, of course, you can't, because if you do you're going to face serious business problems. Our policy is written with this experience in mind. I think where voting control goes 75 percent or below, where we really no longer have enough shares to change the name, we would consider the matter very carefully.

If you are rigid on 100 percent ownership, you may face grave difficulties in certain situations.

MR. VON THURY: Yes, but Paul, there is one aspect that we should bear in mind. In some countries where the State takes over the company, what happens? And that's a possibility in many countries, particularly in Latin America

MR. WEISER: Is that involved in Zeiss marks?

MR. VON THURY: Zeiss marks? You mean their latest decision here? That's again whether something is illegal from our point of view. Of course, this follows something in the Swiss decision previously where they decided that expropriation by East Germany is not recognized.

MR. COOKE: Dr. Ladas, if I can go back to the oil industry again: it's always been axiomatic that you didn't have to actually make the goods yourself. You could have them made for you to your specifications, and that was alright. This question has been a bit controversial in connection with the oil industry on account of gasoline trading, which goes on pretty much around the world. If an oil company were going into a new country before it had a refinery there, it would probably buy its goods from another company. Is there any sign anywhere throughout the world that that action is beginning to weaken the trademarks; that the trademark should stand for more than just whatever products you offer; that it should stand for yourself in a more personal way?

DR. LADAS: Well, so long as you are not required to have any use of a trademark before you register, so long as registration gives you ownership, that requirement is quite diluted.

MR. COOKE: I have two things in mind. Well, the thing that called it to my mind is that I had occasion to buy some tools the other day. I was very much surprised that when I bought Stanley tools they were made in England now. They can have them made for them in England and get them over here through customs and everything else cheaper than they can make them in this country. Well, they're not Stanley tools in the sense that we thought they were good old New England tools. Now they're good old British workmanship.

But the use problem is serious. It isn't the easiest thing in the world to just walk into a new country and sell gasoline. You just don't do it in a day. I think it took us—Gulf had been talking about selling gasoline in Germany as long ago as the time I went out there as Patent Counsel in 1952—but I think its just been between the last three to five years they're actually selling gasoline in Germany. They'd been trying to do it ever since. You just don't walk in and sell gasoline. Lubricating oil and allied products are easier. I suppose the same thing is true of many products where there's a governmental regulation or ruling of some kind that you can't sell certain goods in that country until they're approved by their Department of Agriculture, or whoever it may be in charge of drugs. So I would think that a sound user provision ought to have some qualification for special conditions.

MODERATOR LIGHTMAN: George, you had a question?

MR. MURPHY: I have another question for Paul, again on licensing. When you license your housemark to your wholly owned subsidiaries, do you limit the products by definition? You may have a lamp subsidiary with only lamp products, but I'm sure you also may have a number of subsidiaries which are in a variety of fields and such companies may be growing and offering additional products and services, in which case you would have to consistently amend from time to time if you had a limited product definition to begin with. Do you have any type of a carte blanche license agreement in such cases, wherein all products and services are covered?

MR. HOFFMANN: Where we do have broad based companies, the agreements are practically carte blanche, but as a general rule I try to avoid anything carte blanche. I usually ask, "What are you doing now and what do you think you are going to do within the next few years? Let's put that in." After that, it's a useful management tool to be able to say to your subsidiary when it wants to extend its product base, "Well, you haven't got a license for the trademark." And this is one way

of exercising control. It is very simple for us to amend and add some new goods. The philosophy is to make the agreement as broad as is reasonably needed today and three to five years from now.

MR. MURPHY: As a practical matter, sometimes subsidiaries may run (I know management in the U.S. is supposed to be omniscient, but sometimes it's not) with the ball and be engaging in a number of product and services offerings and little sidelines here and there, and may be doing this for a number of years without knowledge of U.S. parent company management, and you wouldn't have had a license covering such situations due to narrow initial definition of licensed products and/or services. As a practical matter, I think this problem can arise.

MR. VON THURY: This may be handled practically. In the first page in the paragraph, I indicate for a second paragraph, second page, "The goods as listed in Schedule A as amended from time to time" so whenever there's a new one, I just amend the schedule. And this is practical because, if they then say leave the whole agreement recorded, I don't have to file a new registered user agreement, just amend the schedule. Is that possible, Dr. Ladas?

DR. LADAS: Yes.

MODERATOR LIGHTMAN: This morning there was one question I wanted to ask. If I may change the subject for the moment. Dr. Ladas, you mentioned the Common Market and draft agreement also the Benelux Agreement. What happens to the Benelux Agreement when the Common Market Trademark Agreement comes into effect?

DR. LADAS: That's about five or ten years from now. We can worry at that time, I think.

MODERATOR LIGHTMAN: That answers my question.

MR. WILLIAMS: Dr. Ladas, I seem to be coming back to this trade-name situation. Because, when you get a housemark it seems to get so blended between company name and product and, of course, your clients or your bosses never know the difference, and they bandy them back and forth. It seems to be easy to keep things in order, at least from a documentary point of view—from what you say—trademark licenses, separately drawn and kept apart.

For example, in Europe, does this go back to the name? For example, it is a GE subsidiary name and some government, say the Belgium government, says, "Well, you've got to sell 50 percent of that stock to nationals." Where does that jurisdiction lie? Do Europeans think of tradenames as trademarks? Do they think of the tradenames as housemarks or do they ignore jurisdiction until it comes to the courts by un-



fair competition, or do they have something like our state State Departments, where we go in and register a corporate name?

DR. LADAS: No, there are different things. First of all, in a number of countries you can actually register a tradename as a trademark. In some other countries, you can avail yourself of special laws on trade names. France has a certain law of that kind. In the rest of the countries, you protect tradenames by unfair competition law. But when it comes to licenses to use your tradename, since you have licensed it, the question becomes one of contract law. And then, of course, you have the problem as I just pointed out, how far that contract obligation of the licensee to change the name can actually be enforced, in view of any public law to the contrary.

In other words, the tradename problem is really dangerous in two cases. One is where your management decides to sell the foreign company you have, and the counsel must be aware of the fact that someday he may be called by the president who says, "I've sold the company in France." Counsel of the company will have had to foresee that possibility and therefore have taken some precautions so that that name can come back to the company. You sell the assets of the company but you don't sell the name.

The second case is this problem of nationalization of the company which you have today in Peru and Chile, and you may have, probably, in other countries. There is nothing you can do about it. If you have allowed the name to be used, whether the company is a wholly owned subsidiary or 75 or 50, it's just gone so far as that government is concerned because the government exercises this kind of action.

We have to weigh those possible risks with the great advantage of having a multinational corporation. And there is going to be, I foresee, changes of law, taxation law, company law, in the future for such multinational corporations. And you don't have, really, multinational corporations unless your companies in the various countries have more or less the same name. So, whether you are willing to risk having the tremendous benefit of a multinational corporation that uses the same name in so many countries, or whether you are going to be very cautious is extremely difficult to weigh. I think this is something that top level management has to determine for itself.

MODERATOR LIGHTMAN: In terms of basic protection of a tradename, Dr. Ladas, I have the impression that the "Paris Union" Convention, doesn't quite mean what it says. Article 8 says that tradenames can be protected without registration. The complaints we've been getting, especially regarding Spain, for example, indicate that you've got to go

through some kind of formality to register that name, either in a corporate register or somewhere, to protect it.

MR. VON THURY: Those are commercial establishments.

MODERATOR LIGHTMAN: But the point is, do countries, do all countries under the Convention protect the tradename without registration?

Mr. von Thury: You find out when you try to enforce it.

DR. LADAS: You mention Spain. There are at least six Supreme Court decisions protecting a name of American companies without registration. And many countries in Europe do likewise—Germany certainly does. Switzerland is a case apart, because Switzerland insists either you do business in the country or you have the name registered. In Switzerland there are three kinds of protection for tradenames: Federal Register, Cantonese Register, and Unfair Competition. You have to satisfy one or the other of those requirements. So it's a little complicated. But generally speaking, Article 8 has worked out. The main question of Article 8 is this: Can you protect your name even though it has not been used in that country? If it has been made known only in that country they know about your name from international advertisements and so on. That is the real issue. And recently, in the Madrid meeting of the AIPPI, we have adopted a new suggested text for the change of Article 8 which I think is very good.

MODERATOR LIGHTMAN: Are there provisions in certain foreign laws for concurrent use? In other words, if somebody else has registered your mark and you can't get that cancelled, and yet can prove that in certain respects you are the rightful owner, can there be concurrent use?

DR. LADAS: Concurrent use or concurrent registration?

MODERATOR LIGHTMAN: Both.

DR. LADAS: Concurrent registration, in British countries generally.

MODERATOR LIGHTMAN: How about Japan?

DR. LADAS: Japan, no. In concurrent use the problem is this: If you have begun using a mark before registration by another, can the owner of the registration stop you. The general rule in those countries is that you can continue having a personal use of the mark.

MODERATOR LIGHTMAN: Harold?

MR. KNOTH: I'd like to get off on something a little more fundamental. I just wonder whether anybody had any experience with the Arab boycott—whether there's any way to get around it.

MR. DESIMONE: Just sign the affidavit.

MODERATOR LIGHTMAN: And report it to the U.S. Commerce Department.

DR. LADAS: There is nothing you can do.

MR. HOFFMANN: I think one of the best ways to get around a boycott is when they need what you have.

MR. KNOTH: Yes. But if you want to register your trademark, they don't give a damn.

DR. LADAS: No. They won't accept your application. They won't issue a certificate of registration, won't allow you to file an opposition, and so on.

MR. KNOTH: Well, now—suppose you swear falsely. That's going to affect your trademark adversely.

DR. LADAS: If you do what?

MR. KNOTH: If you swear falsely. If you sign the affidavit and what you say is not true, that's going to affect the validity of your registration.

MR. DESIMONE: Well, its illegal anyway. Why would you swear falsely?

DR. LADAS: If you have a boycott, it doesn't make any difference. You don't have a chance to file an affidavit. If you are boycotted, you're boycotted. That's all.

MR. DESIMONE: No, but you're talking about the affidavit. If Adam Smith is satisfied to sign the affidavit. There is an affidavit that you can sign.

DR. LADAS: If you have not been boycotted.

MR. DESIMONE: You're referring to whether you should sign the affidavit or not?

MR. KNOTH: Yes.

MR. DESIMONE: Well, it depends on the circumstances under which you are doing business in Iraq. There are circumstances where you can honestly sign the affidavit.

MR. KNOTH: Even though you're dealing with Israel too?

DR. LADAS: The question as now asked is much more specific than before.

MR. DESIMONE: And we've got them to eliminate the portion as to whether there are any Jews on your Board of Directors and that, so you've got—

MR. KNOTH: How did you do that?

MR. DESIMONE: Well, I think it was pressure from many American groups—

MODERATOR LIGHTMAN: But Harold's basic question as I understand it is—suppose a company does business with Israel and signs an affidavit saying it does not. Is that correct, Harold?

MR. KNOTH: That's one point.

DR. LADAS: Well, how do you do business with Israel? Have you an establishment there?

MR. KNOTH: Yes.

DR. LADAS: Have you an agent there?

MR. KNOTH: Yes.

MR. DESIMONE: And your trademarks are used there by you? It's your label?

MR. ALTIN: You're in trouble.

MR. DESIMONE: I don't see how you can sign the affidavit.

MR. KNOTH: Well, suppose you sign the affidavit truthfully? Is that all they want, for you to sign the affidavit?

MR. DESIMONE: They'll apply the boycott. If you're doing business in Israel, they'll apply the boycott.

MODERATOR LIGHTMAN: But just bear in mind that this request by the boycott countries has to be reported to the U.S. Commerce Department.

MR. DESIMONE: What's the form number, Joe? Fourteen?

MODERATOR LIGHTMAN: I don't know. But there are regulations.

MR. KNOTH: But is it not true that we can do it once a year or once each occasion?

MR. MURPHY: I don't know whether you can solve the problem in this particular way at this time; I don't know what the questions are on the required affidavits at present. But what we did at my former company of employment in this situation was to drag out a very remote and lifeless foreign subsidiary which applied in its name for the registration and which, in fact, did not make any false statement. Some form of protection was thus obtained, and the registered mark could then be licensed to the parent company. Now, this was a device, but it was felt that we should have some form of protection in the Arab states for an important product mark, and there had been a tremendous amount of infringement of that mark in such areas. How worthwhile a mechanism this was or may be now, I don't really know. But it was simply utilizing a shell foreign company which did not have the corporate housemark in its name and could not be connected on its face with the U.S. parent company to obtain some degree of trademark protection in the Arab world.

MR. DESIMONE: I don't know what you mean. The affidavit is trying to find out if you are doing business in Israel, as I recall, and if you say, "Yes, I'm doing business in Israel," you'll be boycotted.

MR. KNOTH: Yes, but sometimes the affidavit depends on the purchaser. If he wants the goods bad enough, apparently the government

lets him fill out some questionnaire that's very simple, such as, "Is this liner insured by an Israel company" and you can easily say, "No."—

MR. HOFFMANN: I think you have to distinguish between the affidavits which you require for trademark registration purposes which—

MR. DESIMONE: Well, that is the one I'm talking about.

MR. HOFFMANN: And between—and the actual boycott. As far as the actual boycott is concerned, they will close one or both eyes if they want what you have.

MR. DESIMONE: Yes, if you're selling something they want.

MR. HOFFMANN: You know, like Hilton, there's one Hilton hotel in Cairo and one in Israel. When it comes to registering your trademark you either fill out this form or you don't fill it out.

MR. KNOTH: The ones we've got are pretty tough and its pretty hard to answer.

MR. HOFFMANN: We don't fill them out. I just don't register.

MR. COOKE: I'd like to do a little crystal balling, again. I might start by going back to a few years ago. The company had just made a slight change in the form of use of one of its gasoline trademarks and decals were going on the pumps. So we got a hurry call from Florida and the next call I got was from the Vice President for Sales who said, "Haven't we registered our trademarks in Florida?" And I said, "Yes." "This particular trademark?" "Certainly. We've got a state registration." Well, we had just shut down our pumps. And they said something about registration.

Well, what had happened was that the night before we had changed the decal, it was still basically the same trademark. We found that when the inspector came around, he saw the decal and said, "You haven't registered the octane number of that gasoline with the state authorities and you can't sell under that decal until you do."

And today, you know they are moving toward a requirement that all gasolines shall be sold under specified octane numbers. And the only way they can do that is, I believe, to identify the specific grades and the brands, the trademarks the gasolines are sold under. And what I am looking forward to, in some distant future, is the sort of thing in a good many industries, such as food industries, and probably drug industries, and others. There will be a tendency to require—I don't know how to put it exactly—but to require a certain specified quality to use a certain mark. In other words, this will be an official requirement that when you use a particular trademark the goods so marked must stand up to certain standards. I think that is developing, and perhaps it's bound to develop in a consumer economy. And a trademark is a handle by which

that kind of power can be exerted. So I just leave that thought with you.

MODERATOR LIGHTMAN: We want to finish up fairly soon now. Are there any further questions?

MR. MURPHY: I just have one further observation on a possible explanation of Paul's citation of the Tootsie Roll application in Russia. It's something that I've found to be getting very bothersome. We talked about how the advertising people and promotional people are taking over and causing a lot of problems in connection with swamping the Register and in other areas. There may be some promotional value to the Tootsie Roll people, and I don't mean this in a jocose fashion, in being able to cite in their advertisements that their mark is registered or owned from such and such a removed geographical area to such and such a removed geographical area. Registering a mark for the gimmick value of the fact of such registration is becoming more common, and I wouldn't be surprised if this type of thinking hasn't arisen because advertisers and their agencies are becoming more and more aware of all areas affecting trademarks and of the many ways in which trademarks can be used, sometimes valuably and unfortunately sometimes detrimentally, in advertising and promotion.

MODERATOR LIGHTMAN: Pertinent to Mr. Murphy's comment, I note that the Institute has published a book entitled *Nurturing New Ideas: Legal Rights and Economic Roles*. The book contains an article on "Trademark Protection in the Soviet Union" giving a number of reasons why it might be desirable to seek trademark protection in that country.

Gentlemen, I would like now to wind up and summarize briefly the basic subject matter covered in today's Clinic.

Francis Browne discussed the subject of national laws and treaties. He emphasized the basic differences in trademark jurisprudence between the common law and civil law countries. He also pointed out that the basic purpose of a trademark system should be not only to serve proprietary interests of trademark owners but to serve consumer interests as well. He noted that consumer protection in trademark contexts was more feasible in the common law countries than in registration countries.

Tony DeSimone talked about the present Madrid Agreement, describing its salient provisions including the prior home registration requirement. Only after five years does a registration become independent with respect to the so-called "central attack" procedure. He also discussed new proposals to make the Madrid Agreement more attrac-

tive to nonmember countries, such as the U.S., U.K., Scandinavian countries, Japan and the Soviet Union. He noted that a proposal for an independent central filing was pretty well shot down last April at the Committee of Experts meeting for a number of reasons. A new proposal to be discussed at a forthcoming meeting in Geneva will deal further with this feature, a new central attack provision, and provisions with respect to user requirements. Tony emphasized that in order to become eligible for adherence to an international filing arrangement, the U.S. would have to do some intensive exploration about revisions of the use requirements in our law.

In the afternoon session, Paul Hoffmann discussed trademark strategy, distinguishing between protection of housemarks and product marks, giving us his views on the type of approach that should be taken. In the case of product marks, he would proceed between the overall blanket approach and the so-called parsimonious approach. He also discussed enforcement strategy, setting forth certain criteria with respect to decisions that a company should make based on the nature of the mark, i.e., commercial importance, dilution factors, and, of course, the law of the country and the nature of the action, whether it could be accomplished by administrative or judicial proceedings. And cost factors, of course.

Dr. Ladas discussed questions of trademarks and unfair competition. He pointed out that trademark laws in our lifetime have now reached the stage of maturity—this isn't necessarily true of unfair competition statutes, which have limited meanings in many countries vis-à-vis trademark practice; in many countries there is no law of unfair competition.

Dr. Ladas also mentioned Article 10*bis*, the unfair competition provision of the "Paris Union" Convention, noting that each country interprets Article 10*bis* in terms of its own jurisprudence and statutes. He also distinguished between the civil law countries, such as those in Western Europe which have a good body of case law in the unfair competition field, particularly France, and Germany. In most of these countries, the first registration governs and the unfair competition law generally will not override any rights that are acquired through first registration. He then mentioned the situation in British law countries where protection of unregistered marks in the unfair competition area emanate from protection based on statutes and case law against passing-off and misleading trade practices.

That's basically a broad brush summary of the papers that were presented from which our discussion emanated.

I want to thank all of you for being here and contributing to a most

informative, comprehensive and provocative session. The views and facts surfaced today will certainly be of value to the business, legal and professional groups concerned with international trademark activities.

DIRECTOR HARRIS: I want to thank the speakers, the Moderator-Commentator, and all you participants on behalf of the Institute. I've been very much impressed by the number of new ideas that have been surfaced. I am also impressed by the extent of the probing the participants have engaged in. I think this has been a very successful meeting. You will have an opportunity, of course, to edit your remarks before publication. We have already emphasized their confidential nature until you have reviewed them. We will send you your remarks shortly. Please edit and return them expeditiously so we can meet our press schedule.

Thank you again. The meeting stands adjourned.



## NOTES

---

### Fifteenth Annual Conference Scheduled on Enterprise Under Stress: Changing Premises and New Responses

The Fifteenth Annual Conference of The PTC Research Institute will explore the responsibilities and opportunities of government and private enterprise to meet the evolving demands of society. It will feature the possible contributions of invention, innovation, and industrial property. The compatibilities and incompatibilities of the antitrust and unfair trade practice laws will be highlighted. The Con-

ference will be held on Wednesday, October 20, 1971 at the Shoreham Hotel, Washington, D.C. The fee, including luncheon, is \$65.

Speakers of prominence will make the main presentations that provide the basis for discussion. The full proceedings will not be published. Publication will be limited to the principal papers. The program follows:

#### *Enterprise Under Stress: Changing Premises and New Responses*

- A. New Context for Research
- B. New Circumstances for Industrial Property  
LUNCHEON: Kettering Award Address
- B. (Continued) New Circumstances for Industrial Property
- C. New Setting for Antitrust and Unfair Competition

The Conference will consider risks attendant on the introduction of new products and the social requirements for enhancing the quality of life and the material welfare and leisure of our people. Attention will be directed to national and international problems due to technological hazards such as pollu-

tion of the environment, and to consumer protection. Emphasis will be placed on the role and potential of R&D, industrial property and competition in meeting these current and emerging challenges. Notice will be taken of the new constraints on R&D and on industrial property.

## Billy M. Horton Receives Inventor of Year Award

Billy M. Horton, inventor of the fluid amplifier which triggered a whole new fluidics industry, was chosen as the 1970 Inventor of the Year. The Institute presented the Award to Mr. Horton on May 20, 1971.

Born in Bartlett, Texas, Mr. Horton studied physics at the University of Texas where he received his B.A. in 1941. He served as a radar officer during the war with training at Harvard and M.I.T. and service in Europe. After the war, he joined the staff of the Naval Research Laboratory, working on sliding electrical contacts, fluorescence, and nuclear radiation detectors. In 1949 he received an M.S. in physics from the University of Maryland. In 1951 he transferred to the Ordnance Division of the National Bureau of Standards, now known as the Department of the Army, Harry Diamond Laboratories, of which he is the Technical Director.

Mr. Horton's invention, which is basically an amplifier used as a control mechanism, utilizes fluids or gases in lieu of conventional electri-

cal current, thereby having no moving parts or conventional elements to wear out or change values. Among its many applications in use or under development are jet engine controls, air-conditioning systems, stabilization and control of aircraft and rockets, control of diesel locomotives, control of numerous chemical and industrial processes, laboratory construction of digital and analog computers, and an entire family of medical life-saving and life-support devices such as heart pumps and respirators.

Other awards received by Mr. Horton are the Arnold O. Beckman Award of the Instrument Society of America, 1960 and the John Scott Award in 1966. In 1969 he became a Fellow in the Institute of Electrical and Electronic Engineers.

Previous recipients of the Institute's Inventor of the Year Awards were Chester F. Carlson, 1964 (xerography); Samuel Ruben, 1965 (batteries); Gordon K. Teal, 1966 (silicon transistor); Robert Adler, 1967 (electronics); Jay W. Forrester, 1968 (computer memory); and Stanley D. Stookey, 1969 (glass).

## Institute Holds Special Conference of Invited Experts on R&D, Technological Education and Industrial Property

"R&D, Technological Education, and Industrial Property: Policy Correlations for the 1970's" was the subject under discussion at the Institute's Special Conference held on May 20, 1971 at the Twin Bridges Marriott in Washington, D.C. The Conference explored how national priorities will have to be reordered and implemented to overcome the plight of the "knowledge industry"—that is, R&D and higher education, especially science and engineering—due to such factors as the reduction in research funding, poor business conditions, unemployment among scientists and en-

gineers, decline in graduate school support, dim prospects for new crops of graduates, the information explosion, and the great increase in employee mobility. A better understanding emerged from the Conference of the role and potential of industrial property, taxation and competition in meeting some of these challenges to the "knowledge industry." The proceedings of the Conference will be published as a monograph.

The program of the Conference, including the speakers, is presented below:

### *Welcome*

L. James Harris

Director, The PTC Research Institute; Professor of Law, The National Law Center, The George Washington University

### *Introductory Remarks*

Conference Chairman

James S. Cole

President, Research Corporation

### *New Conditions and Problems of the "Knowledge Industry," National and International*

Speakers: Henry David

Executive Secretary, Division of Behavioral Sciences, National Academy of Sciences

Lawton Hartman

Special Assistant to the Director, National Science Foundation

George D. Summers

Manager, Biomedical Programs, Fairchild-Hiller Corporation

Cross-questioning and comment by Panel

*New Challenges to Patent, Know-How, and Other Industrial-Intellectual Property Rights*

Speaker: Sidney Carter

Patent Attorney, General Motors Corporation

Cross-questioning and comment by Panel

General Discussion

LUNCHEON

Master of Ceremonies: O. S. Colclough

Chairman of the Advisory Council, The PTC  
Research Institute; Director Emeritus of the  
Institute

Inventor of the Year Award Presentation

Recipient: Billy M. Horton

Technical Director, Harry Diamond Laboratories

Luncheon Speaker: James Wakelin

Assistant Secretary of Commerce for  
Science and Technology

*Antitrust and Competition Policy in R&D Setting*

Speaker: Richard E. Day

Professor of Law, Ohio State University

Cross-questioning and comment by Panel

*Emerging Needs in Tax Policy Concerning Research and Education*

Speaker: Arthur B. Hanson

Senior Partner, Hanson, O'Brien, Birney & Stickle

Cross-questioning and comment by Panel

General Discussion

## Stacy Jones Authors New Book

In view of Stacy Jones' efforts over the years to bring the story of the patent system to the lay public and to prospective careerists, and his contributions to several of the publication programs of the Institute, we are bringing his most recent book, *The Patent Office*, to the attention of our readers as an *IDEA* note. The brief statement on the book jacket describes the contents so well, we quote from it:

"Stacy V. Jones, whose 'Patents of the Week' column has been a popular feature of the *New York Times* since 1952, tells the complete story of the Patent Office, from the early days, when amendments to the 1790 patent law opened the doors wide to fraud, to the present, when this overworked agency struggles daily with the swelling volume of patent applications and the growing complexity of modern technology in a valiant attempt to shorten the time between application and issuance of a patent (average time: 2.5 years; longest pending time on record: 36 years, 9 days!) . . .

"The inventor, the student, the patent attorney, the government official, and the merely curious will find this book a mine of information on the basic categories of pa-

tents; the rights conferred by a patent (or a trademark); how patents are applied for, issued, and sometimes fought over in the courts; and a score of related matters. Famous patents are covered (the telephone, the flying machine, the rocket) as are patents for devices that lie just this side of insanity (diapers for parakeets, to cite one example).

"In his concluding chapter, the author predicts the shape of patents to come and forecasts improvements in the present system, including that dream of all patent officials—a workable automated retrieval system for tracing patents. The appendixes present the basic features of the labyrinthine patent law, discuss career opportunities in the Patent Office, and describe the law of trade secrets, which is defined as the 'common law corollary of statutory patent law.'

"THE AUTHOR: Stacy V. Jones is well qualified to write about the Patent Office. In addition to writing his weekly column for the *New York Times*, he contributes articles on patents to *Science Digest* and is the author of several books, including *The Inventor's Patent Handbook*."



Joint Ventures Abroad: Industrial Property,  
Taxation, and Competition

**An Institute Clinic**

# Joint Ventures Abroad: Industrial Property, Taxation, and Competition

## CONTENTS

INTRODUCTION	184
CLINIC PARTICIPANTS	185
INTRODUCTORY REMARKS	<i>L. James Harris</i> 187
BUSINESS ORGANIZATION FOR JOINT VENTURES	<i>Felix Klass</i>
Objectives	191
Motivation	191
General Criteria for Type of Joint Venture	193
Legal Form	194
Who Runs It	194
Role of People	194
JOINT VENTURES AND THE PATENT, TRADEMARK, AND KNOW-HOW LAWS	<i>Homer O. Blair</i> 202
Joint Ventures Defined	202
Proprietary Assets as Contribution to Joint Venture	202
Territorial Limitations in License	204
Trademark Licensing Caveats	204
Clearance Required for Sending Technology Abroad	205
Initial Filing Costs for Patents and Trademarks	206
PRESENTATION OF FOUNDERS DAY AWARD TO P. J. FEDERICO	232
JOINT VENTURES AND THE ANTITRUST AND UNFAIR COMPETITION LAWS	<i>Sigmund Timberg</i> 235
Antitrust History of Joint Ventures	235
1—"Prehistoric gestation" period	235



2—"Sherman Act era"	235
3—"Era of cultural diffusion"	237
4—"Clayton Act age"	239
Business Motivation Underlying Joint Ventures	241

**JOINT VENTURES AND THE TAX LAWS** *Chester C. Hilinski*  
242

Two Primary U.S. Tax Law Concepts Relating to Joint Ventures	243
Tax Implications of Know-How Transfer	244
Industrial Property That Qualifies for Tax-Free Exchange	245
Tax Law, Other Than Income Tax, Involved in Joint Ventures	249

**GROUP DISCUSSIONS**

Amount of Equity Shareholding of Partners	197
Joint Venture Defined	199
Incentives and Deterrents for Establishment of Joint Ventures in a Country	199
Technology As Contribution to Joint Ventures	199
How to Prevent Joint Venture from Exporting Technology to Countries Restricted by U.S. Government	207
Control of the Joint Venture	208, 252
Compulsory Licensing	211
Territorial Limitations in License	213, 261
Governmental Review of Licensing Arrangements	216, 260
License Arrangements with Soviet Union and Eastern European Countries	218
Types of Legal Agreements and Provisions Utilized in Setting Up Joint Venture	227
Clayton Act Exemption for Investment As Applied to Joint Ventures	252
Rule of Reason Applied to Foreign Commerce Joint Venture	253
Conflict Between Patent and Antitrust Policy	254, 263
Trend of Antitrust Law in Europe	258
Comparison of U.S. and European Antitrust Law	260
Comparison of U.S. and Foreign Tax Law	262
Meaning of "Given in Perpetuity" to Qualify for Tax-Free Transfer of Industrial Property	263
Planned EEC and European Patents	264
"Toe-Hold" Theory of <i>Bendix-Fram</i> Case	266

# Joint Ventures Abroad: Industrial Property, Taxation, and Competition

An Institute Clinic

## INTRODUCTION

A CLINIC ON JOINT VENTURES ABROAD: Industrial Property, Taxation, and Competition was held on March 31, 1971, at the Institute's headquarters in Washington, D.C.

This Clinic, as previous ones in the series, was by invitation and consisted of a team of experts representing a broad spectrum of disciplines from industry, government and education. Gerard J. Weiser, Research Associate of the Institute and Patent Attorney with Dechert, Price and Rhoads, moderated the Clinic. Introductory remarks by L. James Harris, Director of the Institute were followed by the four principal speakers: Felix Klass, Director of Licensing of Celanese Corporation; Homer O. Blair, Director of Patents and Licensing, ITEK Corporation; Sigmund Timberg, Antitrust Specialist in private practice; and Chester C. Hilinski, Attorney, Dechert, Price and Rhoads. These presentations and the subsequent discussions comprise the Proceedings reported here.

Previous Clinics published in *IDEA* are Statutory Requirements of Companies for Protection of Intellectual Creations, Volume 8, Number 4; Computer Software Protection, Volume 13, Number 3; The Patent Cooperation Treaty, Volume 14, Number 1; Trade Secrets, Volume 14, Number 2; Unfair Trade Practices, Volume 14, Number 3; and International Trademark Protection, Volume 15, Number 1.

## **Clinic Participants**

- Homer O. Blair —Director, Patents & Licensing, ITEK Corporation
- Betty Bock —Director of Antitrust Research, National Industrial Conference Board
- Rupert Brady —Patent Attorney, Brady, O'Boyle and Gates
- Horace B. Cooke —Special Consultant, The PTC Research Institute
- O. S. Colclough —Chairman of the Advisory Council and Director Emeritus, The PTC Research Institute
- Arved Deringer —Attorney, Deringer, Tessin, Herrman & Sedemund, Cologne
- P. J. Federico —Consultant on Patent Law, Cushman, Darby and Cushman; formerly Examiner-in-Chief, U.S. Patent Office
- Marcus B. Finnegan —Patent Attorney, Finnegan, Henderson & Farabow
- John C. Green —Project Leader, International Trade and Development Studies, The PTC Research Institute; Scientific Communications and Research Consultant
- L. James Harris —Director, The PTC Research Institute; Professor of Law, The National Law Center, The George Washington University
- Chester C. Hilinski —Attorney, Dechert, Price & Rhoads
- Felix Klass —Director of Licensing, Celanese Corporation
- Jean Paul Marty-Lavauzelle —Attorney, Office Gide Loyrette Nouel, Paris
- Andrew L. Ney —Patent Counsel, Standard Pressed Steel Company
- Thomas I. O'Brien —Patent Counsel, Union Carbide Corporation

- S. Chesterfield Oppenheim —Adviser on Research, The PTC Research Institute; formerly Professor of Law, University of Michigan
- Walter H. Palmer —Director of International Operations, Grove Manufacturing Company
- Irving H. Siegel —Consultant, The PTC Research Institute; Independent Economic and Management Consultant
- Lanty Smith —Attorney, Jones, Day, Cockley & Reavis
- Charles D. Snead —Vice President, Eastman Chemical Division, Eastman Kodak Company
- Richard F. Sperring —Director of Planning and Development, PPG Industries
- Sigmund Timberg —Attorney, Antitrust Specialist
- Gerard J. Weiser —Research Associate, The PTC Research Institute; Patent Attorney, Dechert, Price & Rhoads
- Taggart Whipple —Attorney, Davis, Polk and Walter

## **Proceedings of the Clinic**

**DIRECTOR L. JAMES HARRIS:** I welcome you to the Clinic on behalf of The PTC Research Institute of The George Washington University. First I'd like to tell you about the Clinic purposes.

We're developing this instrument for a more effective means of communication and of professional education. What we want to do is deal in depth with frontier problems and also to develop generally inaccessible information. We encourage new approaches to current problems. This is part of the Institute's research function in the public interest. To accomplish this purpose we invite a team of experts, leading specialists representing a range of disciplines. You are the team selected for this Clinic based on your experience and your position.

We hold these deliberations in confidence. They are confidential until the participants have had an opportunity to edit their remarks. We emphasize this because it is extremely important in this type of gathering to let your hair down. The Clinic is a research tool. What we are trying to do is to diagnose, instruct and if possible to remedy. As I have said at previous Clinics, we utilize a kind of medical approach. What we want to do is to understand the disease, what is wrong, where it hurts, and perhaps come up with some kind of a remedy. And to do this, I emphasize, we have got to let our hair down. We don't want any company secrets, but we've got to tell ourselves the facts. We've got to have a maximum of trust among experts. We believe this frank and open professional discussion can best be accomplished under the aegis of a Research Institute. I repeat, the publication of the proceedings will be made only after all of the participants have had an opportunity to edit their remarks.

What we want to do—based on our experience—is to create an atmosphere, an informal atmosphere, an uninhibited give and take. We want to encourage a maximum of interchange. We want to make the give and take as creative of new ideas and new approaches as possible.

What can we all do as participants to accomplish this? First, against the dropback of our own ideas and our own experience, we've got to listen to and evaluate the notions expressed by others. Second, if our own viewpoint seems to be unrepresented, by all means, contribute to the discussion. Third, let us keep our observations and questions as

short as we can so that the benefit of the discussion will be maximized for everyone—in other words, so everyone participates. When we get a group of a certain size, or beyond a certain size, we find that there is a tendency for people who are more outgoing to monopolize the discussion. That may be good operating procedure for a Conference, but this is not a Conference. It's an "all hands" Clinic, and in order to get the most out of it, everybody should participate.

The Moderator, in order to make it your Clinic, will intrude minimally—and only to keep the trend of the discussion clear and to elucidate important points that might get short shrift. The value of this exercise depends entirely on the quality of the input of all the participants. We have found that as a teaching and a learning instrument this method is unique. It has been an unusual experience for our past participants.

Why are we holding this Clinic now? Most of you are aware, I know you are aware, of the spreading internationalization of business—seeking raw materials and low wages abroad, global promotion and development, the spread of advanced technology throughout the world; also there is the increasing nationalistic parochial politics in some places, trade restrictions of all sorts, the growing interest in the quality of life and economic well being of all people all over the world, and the proliferation of the joint venture in almost every conceivable field as the most advantageous way of penetrating foreign markets. Increasing attention is being paid to industrial property in international trade, developments of relevant international conventions and treaties, the press of current problems concerning international aspects of industrial property that affect U. S. interests, particularly relating to antitrust and tax policy, and to international competition in R&D. Notice is also being taken of the growing inroads of foreign producers in important domestic markets and U.S. markets abroad.

In this Clinic we are going to follow a procedure that we have found successful in our other Clinics. We will commence with a broad presentation on Business Organization for Joint Ventures to key us into the total picture. This first presentation will set the tone. It will be made by Felix Klass, Director of Licensing of the Celanese Corporation. For a brief period thereafter we will have cross-questioning to clarify points. We will follow the same procedure after each presentation, because you haven't had copies of the papers in advance of the presentations—you haven't seen them before. Therefore, we will devote five minutes or so to any clarifying questions on each paper before we go into general discussion.

The second paper will follow the first paper, after the points are clarified. The second paper will be presented by Homer O. Blair, Director of Patents and Licensing of ITEK Corporation on Joint Ventures and Patent Trademark, and Know-How Laws. The remainder of the morning session will be devoted to open discussion. The third paper—there are four papers—will be given after lunch by Sigmund Timberg, an antitrust specialist in private practice, on Joint Ventures and the Antitrust and the Unfair Competition Laws. Mr. Timberg, we learned this morning, had to attend a hearing in court and will be here for lunch. Since his will be the first paper given after lunch, I would suggest that we reserve our antitrust questions for that period, when Mr. Timberg will join us.

The final paper will be presented—after the five-minute period for cross-questioning—by Chester C. Hilinski of Dechert, Price and Rhoads on Joint Ventures and the Tax Laws. The remainder of the afternoon session will be devoted to open discussion, after the five-minute period for cross questioning on Mr. Hilinski's paper. The Moderator-Commentator is Gerard Weiser, a member of the Research Staff of the Institute, a patent attorney associated with Dechert, Price and Rhoads. At 12:30 we will have a brief ceremony honoring the 1971 recipient of the Institute's Founders Day Award for Distinguished Government Service. Luncheon will be served at 1:15 in the Adams Rib Restaurant on the ground floor of the Joseph Henry Building at 21st and Pennsylvania—that's two short blocks from here, the building in which we were previously domiciled. The Clinic will reconvene between 2 and 2:15 and will run until five o'clock. At the completion of the Clinic Mr. Weiser will make some brief concluding observations.

Please identify yourself before speaking, and speak loudly and clearly so that we can make an accurate transcription. I know that in the heat of discussion you might forget, but when you do remember, repeat your name. It is very important to repeat so the transcriber can get used to your voice and identify you accurately. If you speak from notes, please let us have a copy. This will be helpful too. Before turning over the meeting to Mr. Weiser, let's go around the room and identify ourselves. My name, as you know is Harris. I'm the Director of The PTC Research Institute.

MR. KLASS: Felix Klass, Director of Licensing, Celanese Corporation.

DIRECTOR HARRIS: Mr. Timberg isn't here. Oppie hasn't arrived yet. He's probably waiting for Betty Bock. They will come together.

MR. WHIPPLE: I'm Taggart Whipple, a lawyer in Davis, Polk and Walter in New York City.

MR. SNEAD: Charley Snead, Vice President, Eastman Chemical Division of Eastman Kodak Company.

MR. SPERRING: R. F. Sperring, Director of Planning and Development, PPG Industries, Pittsburgh.

MR. LAUVAUZELLE: I'm Marty-Lauvauzelle, a lawyer from the firm of Gide Loyrette Nouel in Paris.

MR. GREEN: I'm John Green. I have a consulting firm here in the city and I'm associated with the Institute.

DR. SIEGEL: Irving Siegel, private economic consultant and also I'm associated with The PTC Research Institute.

MR. FEDERICO: P. J. Federico, presently teaching at G. W. Law School and doing a little consulting work.

DR. SIEGEL: Formerly?

MR. FEDERICO: Formerly, a member of the Board of Appeals at the Patent Office.

MR. SMITH: I'm Lanty Smith from Cleveland, Ohio of the law firm of Jones, Day, Cockley and Reavis.

MR. COOKE: Horace Cooke, former Patent Counsel, Gulf Oil Corporation; now Special Consultant to The PTC Research Institute.

MR. PALMER: Walter Palmer, Director of International Operations of Grove Manufacturing Company.

MR. BRADY: Rupert Brady, a patent attorney with Brady, O'Boyle and Gates, Washington, D.C.

MR. FINNEGAN: Marcus Finnegan, a patent lawyer with Finnegan, Henderson and Farabow in Washington, D.C..

MR. DERINGER: Arved Deringer, a lawyer in Cologne, West Germany.

MR. NEY: Andrew Ney, Patent Counsel, Standard Pressed Steel in Jenkinstown, Pennsylvania.

MR. O'BRIEN: Tom O'Brien, Patent Counsel, Union Carbide Corporation, New York.

MR. HILINSKI: Chet Hilinski, a lawyer in Philadelphia with the firm of DeChert, Price and Rhoads.

MR. BLAIR: Homer Blair, Director of Patents and Licensing, ITEK Corporation, Lexington, Massachusetts.

PROFESSOR OPPENHEIM: S. C. Oppenheim, formerly Professor of Law, now Adviser on Research to the Institute.

MODERATOR WEISER: And I'm Gerry Weiser. Before I came here I felt in very good health and after Lou explained to us the purpose of this Clinic, I think I feel much less healthy now; but I hope that at the end of the afternoon we will all have found the remedies and the new approaches which Professor Harris has suggested that we ought to look for. Mr. Klass, would you like to start to tell us what you have prepared.



FELIX KLASS

I feel a little bit like a fish out of water here. The outline of the Clinic on joint ventures that I received spoke of industrial property and taxation and competition, and emphasized the legal aspects. I'm going to talk about a different part of joint ventures—the business aspect. Specifically the Business Organization for Joint Ventures. To narrow my field a little bit, I'll talk about those arrangements in which a U.S. company together with a limited number of foreign partners, usually one foreign partner, and more usually a foreign corporation, establishes a joint venture company to carry on a business in a country foreign to the United States. Most usually again the foreign partner is resident in the country where the joint venture is being established. I'll focus on those cases where the U. S. company brings technology or more broadly some industrial property rights to the joint venture as is set out in the outline of the Clinic that I received.

I would like to approach my topic in a very positive sense. Looking toward the things that the joint venture can do and that the partners can do that will help it to fulfill its basic function which, for the purposes of the discussion today, I take to mean that the joint venture should be profitable. The other speakers here will discuss industrial property, antitrust and taxes. These are all areas where there is certainly an opportunity to achieve many things; but primarily it is an area where one is concerned and must take care to avoid running afoul of the law. The reach of the law has become very wide, especially the antitrust law in the United States. But one word of caution or hope, if I may. The antitrust laws and to a lesser extent the tax laws of many of the foreign countries are growing very quickly, especially in Europe. They are catching up and, possibly like technology, it won't be very long before the antitrust laws of Europe are equal to and possibly even ahead of ours, I suggest that the antitrust and tax laws of foreign countries will impose more restrictions than what we now have under U. S. law and impose more limits on how we can do what we want.

Now the motivation for joint ventures in my experience falls into two general areas. In one area, a U. S. company going abroad wants a joint venture for what the joint venture partner can bring to the venture. In some cases the partner brings marketing skills and a marketing organization in a foreign country. In other cases the partner brings a manufacturing organization that can undertake the manufacture of a product in an economic manner, whereas the manufacture of a product in a completely separate company would turn out to be

uneconomic. In still other cases the partner brings financial strength to the organization which the joint venture partner in the States is unable or unwilling to put at risk in a given foreign country. The partner can bring many other strengths, but these seem to be some of the more important. That's one kind of joint venture, if you will, where both parties—the U.S. company and the foreign company are willing to participate in the venture.

There is another category of joint ventures, however, with which we are faced in this world. That is, we must have a joint venture not necessarily because we want it, but because the law or regulations of a country where we are proposing to establish a business do not permit a wholly owned subsidiary. One example I'm sure that has been brought to the awareness of all the people here is the case of Japan, where it is essential to obtain the approval of the Ministry for International Trade and Industry (MITI) to establish a subsidiary. In many industries you cannot obtain the approval for the establishment of a business if you own more than 50 percent of it. In some cases it is even very difficult to obtain approval where you have a partner and want to own 50 percent. MITI has recently liberalized its regulations and has even provided for foreign ownership in some industries of 100 percent of a company. For the most part, these are industries in which no U. S. companies would want to participate.

Another example of where one must take a joint venture partner is in Mexico—where under the petrochemical law, if you are in what is designated a petrochemical industry which covers a large part of the chemical industry, you cannot have more than 40 percent ownership by companies foreign to Mexico. A new place where we are going to run into laws of this nature is in the ANCOM nations, the Andean Common Market countries, where a proposed regulation has been published which provides that only a local company would obtain all the benefits of the duty-free arrangements among this group of countries. A local company is defined as one owned 49 percent or less by people outside of the ANCOM nations. A company where there is more than 49 percent foreign ownership would not obtain benefits of the absence of duty. It would also not obtain certain preferential financial arrangements and would be in a far less advantageous position to continue to operate there. The most important industrial country in ANCOM is Colombia and there are many joint ventures, many subsidiaries of U. S. companies there which will have to decide whether to reduce their ownership if the ANCOM treaty and the ANCOM regulations become effective. Keeping in mind the foregoing as well as

many other factors, what we have to do in organizing a joint venture is to establish a business that will be able to operate well and be successful in the country where it is established. You have to have an effective manufacturing organization or an effective service organization, if this is the type of business you have in mind. You also have to achieve an effective marketing organization. And you have to have an effective administration to pull the pieces together and do the job. Depending upon the nature and size of the business, you may, in the joint venture, want to have a technical organization to do research or development or at the very minimum provide for technical service of the products that you make and sell to your customers.

Where you are establishing a large organization—and large depends on the industry and the country and so forth—but where you are establishing a large organization, the joint venture can do its own manufacturing and marketing, and have its own administration and do these economically. In many cases, however, the size of the operation is so small that you cannot effectively undertake to set up your own manufacturing, marketing, and administration. So what you can do, is call upon your joint venture partner who is situated in the country where you are going to operate to help you to do these things. It may make a great deal more economic sense to have the joint venture partner do one or more of them. I have personally seen joint venture organizations that are exclusively marketing organizations with the manufacturing conducted by the joint venture partner. I have seen joint venture organizations where the joint venture puts up a plant and produces a product, and this product is added to the entire product line that the joint venture partner sells in the markets where he is experienced and where he can do a job. I have seen in many cases where the joint venture partner supplies all the administrative overhead to oversee personnel and to manage salary, patent and legal problems because the partner is staffed to do it and can do it inexpensively and economically for the joint venture as compared with the joint venture doing it for themselves. In fact, carrying things to a bit of an extreme, I'm familiar with a rather successful joint venture which is a set of books and a board of directors. The joint venture partner does everything else and I guess in one sense of the term this is a way of getting the profitability of the venture divided among the joint venturers without needing to set up a separate organization, a separate manufacturing company.

Now, here I would suggest that none of these arrangements can be considered permanent. That is, you may start today and set up a joint

venture which is a set of books and a board of directors. In five years, it may make a good deal of sense with growth and with the possible addition of new products to have the joint venture start to pick up its own manufacturing, marketing, or administration, or possibly even all three of them. I guess the motivation of people and the way to get the best job done by them is something we will always continue to work on. But one aspect of dealing with people impresses me very strongly and is relevant here. If you put a man at the head of an organization or some part of an organization and say "you are responsible for its profitability, and you'll get a pat on the back and some reward if you are successful, and a boot in the rear if you're not," you tend very much to get a more effective organization. You get something which has a great deal more drive, and a great deal more success is usually achieved. So that when you bury a little organization in a big one that offers the efficiency of size you can be successful. However, if you can pull it out and identify people and make them responsible for what goes on, it is my belief that you can be even more successful and you have to balance these two factors.

As to the legal form of the business, you just have to fit into the country where you are going to operate. We normally employ a corporation or its equivalent. We do take advantage in some places of what is known as a private company in Great Britain. The GMBH in Germany is pretty much the equivalent. It's designed for a company in which there are only a limited number of stockholders. It offers the advantage of considerably more flexibility in what you can do. It offers the advantage of considerably greater privacy in that you have to publish few or no reports of your results and do very little else that would bring you to the attention of the public. There is a comparable type of company in Japan. A private company.

In starting to work in Japan and getting some perspective as to available courses of action there I became aware of this type of company and tried to persuade some people in Japan with whom we were establishing a joint venture to consider it because it seemed to offer a tremendous number of advantages. I was very interested in the response which was "Well, that sort of a company is O.K. for the noodle maker on the corner who runs a one-man business, maybe with a boy delivering the noodles on a bicycle, but that's not a real business for a company." I've never heard of anyone using it. I'd be intrigued to try it and see if we can't break some new paths.

Another very important aspect of setting up a business as a joint venture is to determine who runs the business. Who really is going to

run the show? I've heard some pretty hot arguments about it and I've developed a perspective about it which makes getting an answer fairly simple for me, although not everyone agrees with it. To begin with, when you have two good-sized companies getting together to form a joint venture, neither company is going to give the other the final say in what happens if there is a real row between them. I think it is unreasonable to expect one company or the other to say "Well, look if we have a disagreement you can do it your way." So I don't try to answer the question of what happens if there is a real final knock-down battle because I can't develop an answer which is acceptable now, and I can't anticipate all the problems that will arise in the future.

On the other hand, I think it terribly important that the day-to-day operation of the joint venture be left to the people who are on the job and running it. You cannot run a joint venture across an ocean. Not well. You have to have the people there responding to the day-to-day needs of the business. If we have the day-to-day needs of the business being taken care of by the people who are there under the general guidance of the board of directors or equivalent, and we get into a really difficult argument—one where no solution seems possible and that goes to the fundamental nature of the business—I guess you just have to sit there and continue to argue it out until you come up with an answer. Or if that's not possible, I have heard a few horror stories where a joint venture was actually being hurt so much as the result of the conflict between the joint venture partners, that eventually, in order to save it, since it was a large operation, they hired an independent manager and told him "You run the business—we will not say anything." Or in one or two other cases, one side or the other has purchased the business in order to eliminate the argument.

To my knowledge these problems do not arise very frequently. I've heard of three or four of them in a great many years of exposure in this part of the business. There are many I'm sure that do not come to the public eye. But there are many, many more joint ventures that operate successfully without such problems.

Let me talk very briefly about one other subject—people. Particularly expatriates from the United States moving into the foreign company. Transferring technology can best be done by moving people. No matter how many blueprints and drawings, and instructions manuals you write, still the final element of technology is in the heads of people. Transferring marketing skills is very much the same thing. It's in the heads of people. But while technology for running a chemical reaction or building an electric motor can be done pretty much the same in any

part of the world marketing of products has to be adapted to the local scene. It has to be adapted to the way marketing is done locally. Under those circumstances, I think to get the best possible job done, at the outset you have to train people from the joint venture and you have to transfer some people into the joint venture.

It has been our policy, and I think it has operated successfully, to move the expatriates out of the joint venture as quickly as possible—as soon as local management, local technical talent, and local marketing talent can be trained. With one exception. As a routine matter, we like to keep one or possibly two people in every major joint venture to act as a good pipeline back to the people in the United States. No matter what the organization chart of a company, you have to know the people and you have to know who to go to to get the right answers or who can get the answers for you. We have found it extremely helpful to have one technically oriented individual in every major joint venture and use him as the way to get the questions funnelled back to the United States and to get the answers and to ride herd on the people in the United States to make sure that the answers come back promptly and quickly.

For the last several years, looking at, I am sure, a very unrepresentative group of annual reports and comments about the result of business, I find that the percentage of earnings of U.S. companies from overseas has been increasing significantly. Maybe the Institute would like to do some studies on that. Certainly in the company that I work for this percentage has gone up year after year after year. What we have been able to do, if you will, is to take the benefit of the work we have done to satisfy the domestic market: the research we've done, the development work we have done, the marketing skills we have developed, we have transmitted at relatively little additional cost to other parts of the world. We have satisfied the needs of the people in other parts of the world. And as a result we have profited further ourselves. I think it improved the economies of many less developed countries and provided better things made locally, for their people.

**MODERATOR WEISER:** Thank you, Mr. Klass. If some of you want to ask Mr. Klass to clarify some of the points made in his paper, this will be a good time to do so. Mr. Snead.

**CHARLES D. SNEAD:** Mr. Snead. Mr. Klass, why do you assume that antitrust restrictions will in a little time in the future be even more

severe in Europe than those in this country? Would you enlighten us a little on that?

MODERATOR WEISER: Can we note this question and leave it for this afternoon because we might go into a long discussion on antitrust. I'm sure it is going to come up again and I'll definitely make a note of it and we'll bring it up again this afternoon. Actually one of the points that appears interesting from Mr. Klass' statement, as I see it, is that, underlying this Clinic, is a strong trend towards mergers and towards joint ventures. And we identify already some differentiation, some stemming or some controls that might prevent the continuation of this trend and perhaps make it more selective, either with respect to size of the joint venture, the countries or products. We might as we go along try to identify this further. Any other questions that you have for Mr. Klass? Mr. Lauvauzelle.

JEAN PAUL MARTY-LAUVAUZELLE: Mr. Klass, it seems that you have assumed in the joint venture which you have described that the two partners have equal interest. Could you comment on your experience as to the point—should partners have equal interest or, on the contrary, in your experience have you made more ventures where one of the partners was a leading one and, in fact, made the decisions?

MR. KLASS: Most of the joint ventures with which I have personal experience are those in which the equity shareholding is not even. There is a disparity. One partner has a majority share and the other partner has a minority share. But it is a very large minority—40-45 percent. What we normally have provided is that, acting on the board of directors or its equivalent, the partners have an equal voice, even though their shareholding is not identical. The thought on that is that a large company owns better than 40 percent of the business. A large company is not willing to make that significant an investment without having a say in how the business will be run.

MODERATOR WEISER: Mr. Finnegan.

MARCUS B. FINNEGAN: Marcus Finnegan. Felix, in your experience, are most of these joint ventures just two-company joint ventures, or do you sometimes get into multiple-company joint ventures?

MR. KLASS: In my experience, most of them are two-company joint ventures. Where I have heard of three-company and four-company joint ventures has primarily been in Japan where the tendency is to have your customer, if you will, or your raw material supplier, participate in the joint venture.

MR. FINNEGAN: I have one other question. I believe you said that

joint ventures tend not to be permanent arrangements. Could you elucidate on that a little?

MR. KLASS: I said, Mark, that the specific arrangement of the joint venture tends not to be permanent. It may grow. It may decline in relative size. I'd say the chances of it lasting forever are somewhat less than if you had a wholly owned subsidiary. There are many that have gone for a long period of time with continued success. When they become unsuccessful, they tend to die.

IRVING H. SIEGEL: Your main point seemed to be, when you were speaking, that they, the joint ventures, are evolutionary in nature; that there may be new and changing circumstances that should lead to a reconsideration of the initial arrangement.

MR. KLASS: I would agree with that. If the joint venture continues to grow in size and in product line, there is no reason why it should not build and become more successful. If, as may be the tendency, the joint venture starts up with one product and stays that way, I think that like any company that only has one product and stays that way, there is some tendency for it to gradually decline and wither.

MODERATOR WEISER: Oppie, you had a question?

PROFESSOR S. CHESTERFIELD OPPENHEIM: Aside from antitrust considerations, assuming that a foreign country does not bar an acquisition or even a wholly owned subsidiary, what kind of business considerations have you experienced in making a decision as to whether to attempt a merger or an acquisition for a product or market extension as against a joint venture?

MR. KLASS: The financial demands that were made, and the expectation of success. If you need a marketing organization for some line of plastics, for example, and you have one new plastic coming in, you might have to make an acquisition of a company whose sales were many, many times the expected sales of the product you are going to make in order to get a good enough marketing organization with a wide enough spread to do the job for you. You don't like to invest \$10 to support the one dollar. You might make an acquisition for the sake of moving into a new business in a certain part of the world. But it's not to put a new product in. In the outline of the Clinic there was some emphasis on where the U.S. company brings technology to the joint venture.

MODERATOR WEISER: Mr. Deringer.

ARVED DERINGER: How narrow or how broad do you define the term joint venture? Do you mean only those situations where you set up a joint business organization, company or corporation like this, or do



you even include licensing arrangements, or even distributorships.

MR. KLASS: I tried to define joint venture at the beginning of my paper as those arrangements where we have a legal relationship, a new company formed with a small number or probably in most cases one other partner and it is usually a corporation. That's all I'm talking about.

MODERATOR WEISER: I'd like to bring something out from your paper at this point. What type of products would you associate ideally with a type of joint venture or what type of other products would you associate with a different type of joint venture. Either in terms of finished products—I'm attempting to distinguish processes from products—manufactured products, chemicals from finished chemicals, electrical or other. Would you treat a synthetic fiber differently from an insecticide or process to make an insecticide. Is there a type of joint venture which lends itself better to one type of product than to the other?

MR. KLASS: This is an area where I have no reaction. I haven't had any experience there. I would say simply that the joint venture, in most cases that I'm familiar with, has to bring something new to the country where it's going. It is possible but very much more difficult simply to enter the market of another country without something new, some advantage—a new proprietary process, a new proprietary product—a better way of doing things that can be protected. You have to have some advantage to come into the new country. Once you are established there you can bring in a routine product, but to get established there you must have an advantage.

MR. FINNEGAN: Felix, when you say you must have an advantage, are you talking about the U. S. partner in the joint venture? For example, say you're talking about Germany—do you mean you should have a German patent covering the initial product that you plan to market in the joint venture and that that patent would belong to the U. S. partner?

MR. KLASS: Again, I went back to the outline of the Clinic where it said the U. S. partner was normally bringing technology. My experience suggests that if you want to come into the German market to make sulfuric acid, which normally anyone can make and normally anyone can make as economically as you can, you are not going to be successful unless you have some unique advantage in cost and ability to manufacture. Thus if I were looking to a joint venture to come into a country like Germany which is highly industrialized, I would want a product on which I had patent protection. Or I would want a secret process which

is 12 percent better in manufacturing cost than anything else available. I want an advantage to go in and establish a business onto which you can then hang other things. But without that advantage, you have an extremely heavy burden.

Now there are some companies who have taken the burden. They have come in with a tremendous investment—a couple of hundred million dollars, ten years of patience—and then it begins to pay off. That is a very heavy demand to make on a company, and therefore I think the place where you ought to start is where you have some advantage. If you go into a less developed country and you bring in a good technology, whether protected by patents or not, you have the advantage that there is no one else in the country who is practicing that technology and therefore you can achieve the same beneficial results.

**RICHARD F. SPERRING:** Sperring of PPG. Could you comment on this item that you have just finished discussing with respect to special process, special advantage, and how you can translate that into some measure of equity value in forming the initial venture?

**MR. KLASS:** I'd hesitate to get into it except to say that in the outline of the tax talk there is a specific comment on how you get a tax-free equity position—that I'm sure will be covered under the tax talk. It can be done. It's got some interesting quirks and I'm certainly no tax expert.

**MR. SPERRING:** Then may I rephrase my question? You sound as if this is a difficult approach. Therefore I'm to imply that in approaching a joint venture with another foreign corporation there is a large measure of equity input that must go with the unique process that you are entering the market with.

**MR. KLASS:** No, I think it can be done taxwise. It's difficult for me because I get into the tax area, and they are people in a world all their own, with all due respect. (Laughter)

**CHESTER C. HILINSKI:** In orbit.

**MR. KLASS:** But it takes a bit of time. It can be done. It takes some extra work and you just have to work with the tax people and work out with them the right approach. We've been quite successful in coming into many joint ventures with our equity being the contribution of patents or know-how.

**MR. HILINSKI:** I think what you are asking about is whether, if you are a U.S. organization and you have some secret process, some formula that is capable of transmission and use to advantage in a foreign country, whether you can transmit that and have the foreign organization then put in whatever else is necessary. This is possible.

**DIRECTOR HARRIS:** What do you do specifically to protect your investment in the foreign market?

**MR. KLASS:** I put it this way. We look to foreign countries to establish a subsidiary or a joint venture with a criterion that here is a market in which the joint venture can operate and be profitable. We live by the law of the country where we operate. We have no choice. I can visualize and I know of some countries where we have elected not to go because it seemed too difficult for the reward. As for protection, I don't know of any way to insure success. I guess no one in business really does. But to come to Japan where we have several joint ventures that are highly successful, one of which is close to 15 years old now, I guess what we do is try to determine that the market is actually there, try to determine that the economics of what we are trying to do are hopefully a bit better than anything anyone else can do. We try to find a good partner. The Japanese partner is equally interested in the joint venture and in our cases anyway he has the money end. He has provided the cash equity in contrast to our know-how and patent rights structure.

Then I guess the last thing we do is continue to work very, very hard both in guiding the company through its board of directors and in helping the company on a day-to-day basis wherever we have something we can offer them. Like any other company, some years have been better than others, but at least in Japan they have always been good. We've had some cases where we have gone in and the joint venture just hasn't worked. In retrospect you can identify all your mistakes, or at least a good many of them. And you try to avoid repeating those mistakes when you work the next one.

**MODERATOR WEISER:** Are you saying that your experience does not bear out the failure of the joint ventures mentioned.

**MR. KLASS:** I don't think that I would say that the joint venture has anything in it which makes for failure or success for that matter, as compared, for example, with a subsidiary.

**RUPERT BRADY:** Rupert Brady. Can you point out any one country from your experience where you may have had more difficulty than in other countries, or had more failures with joint ventures?

**MR. KLASS:** Not really. You know you can feel frustrated when you wait 20 some odd months to get MITI approval in Japan. But that is just sitting there waiting. You get frustrated about the wait but it is no particular great difficulty. Sit there and wait, and if you have to wait too long you just terminate. We've never been successful in setting anything up in India. And the rules are getting tougher there all the

time. I still would like to set up a joint venture with an Eastern European country but haven't had the opportunity so far.

JOHN C. GREEN: You spoke about the foreign partner bringing research, development, technical services to the activity. Would you distinguish between highly industrialized countries and developing countries. It has been my experience that in a developing country the technical services are important. The development is limited to adaptation to the environment, and the research is usually disappointing.

MR. KLASS: I would agree with that comment and say, simply, that to do research you must be in an environment that lends a tremendous amount of support for the research. You get that support in Japan, in the United States and in parts of Europe. Realistically, I can't think of any other place in the world where you can get that type of support. It makes more sense to do the research in those countries where it can be done economically and effectively than the less developed countries should buy the results. It will be cheaper and you can buy the successes and forget about the failures. In most of research, of course, there is failure.

MODERATOR WEISER: Gentlemen, we will go back to asking questions of Mr. Klass later on. I've put some aside myself. Mr. Blair would you like to tell us about the patent aspects of joint ventures?

#### HOMER O. BLAIR

I was a little concerned when Mr. Harris said we were supposed to let our hair down because I was going to be in real trouble here. (Laughter) In my comments I'd like to use the term joint venture a little more broadly than Felix did and include arrangements between partners which might include licenses as well as a separate organization. First I'd like to comment on patents, trademarks, and know-how together as proprietary assets, and then make a few comments on each of them separately.

I believe the most important aspect of these proprietary assets and one that was touched upon by Felix, is that you can use these assets as part or all of your contribution to the joint venture. Every company that I've ever been associated with always has a number of demands on

their investment funds. They have many things to do with their money and there is never enough money to go around. If you can, in effect, use some of your proprietary assets in place of this money in establishing a joint venture, you're that much ahead and you'll get a better return on your investment.

One thing that must be emphasized is that you have to be extremely careful in choosing your partner whether it's a partner in a joint venture or it's a license. Sometimes companies have stars in their eyes. They see all the money that's going to come in from their arrangement and they don't really evaluate the capability of the other partner. If we take a situation where a United States company is putting technology into the arrangement and the other party doesn't really have the capability to use the technology, to manufacture the product, or market it, even though he may have the best of intentions and have the nicest people working for him, you're going to be in trouble. Thus, you must critically analyze your prospective partner in a thorough way.

You have to use your proprietary assets in a way that will be in your best interests. You can use them initially in establishing the venture as part or all of your equity. You can also use them, in addition to this initial establishment to get a return on a continuing basis by means of a license to the joint venture from the United States partner. In that way you may participate both in the profits of the venture and in the royalties from the license of your proprietary assets.

Often when you start into a joint venture you might decide to be a little cautious and put just a part of your proprietary assets or your technology into the joint venture because either the country, or the technology, or the other partner or the market he handles may be unfamiliar. Possibly you might wish to start out with one product or one product line and have the arrangement with the joint venture include a license which might be renewable or which may be quite limited in one way or another. If all goes well and you are able to work well with the other partner and he contributes in an appropriate fashion, you can renew the license or add additional technology from time to time. Of course in this arrangement you have to keep in mind the realities of the market place and you can't sit on the technology until the market has passed by or the competition has come out with an improved product.

In many countries, as Felix mentioned, you can't establish a fully owned subsidiary. Japan is certainly one that comes to mind. There are others. In this case you can use your proprietary assets to help you. You are going to be in an arrangement where you're not going to have

complete control or have all the profits. You will have to share these. But if you are going to get into this market you will have to work out some sort of arrangement, and your proprietary assets may be the lever to get you in there. The other partner certainly is looking to you for something of value to him. If you have technology that is protected by these proprietary assets, that is useful and will form the basis for the product that the joint venture will sell, you have something he needs and the proprietary assets may be the key.

As you know, patents and trademarks are only effective in the country in which you have them. The United States patent is only effective in the United States. You have to get another patent for Germany, England, et cetera. Depending on the current views of the U. S. Department of Justice and, as Felix indicated, the views of other countries, you may be able to use territorial limitations in your license to the joint venture to a certain extent to control the activities of the joint venture. This subject, I'm sure will be discussed this afternoon in detail. The Department of Justice seems to feel that if you have patent protection, there may be more basis for licensing in certain countries and not in others. If your protection is primarily trade secrets or know-how, they appear to feel that the product made by this know-how should be available to be sold in any country. Again this changes from time to time and you may be able to use your patent assets in such a way as to control where the product is sold.

From a trademark viewpoint, you have to be a little careful because if you have a license to the joint venture, you must have provision for control of the quality, and you must actually exercise this control. Each country has different laws but in many countries if you don't control the quality, your trademark will be lost and your proprietary asset disappears. One big advantage of a trademark is that, properly handled, a trademark can last forever. They can be renewed if used properly. A patent expires after a certain number of years and after its expiration the technology covered by the patent is available. A well-known example of smart use of trademarks is the "Sanforized" trademark where Cluett Peabody gets substantial royalties from its trademark licensing program long after their patents on this technology have expired. Their technology is well known, but the trademark has become very well known and very valuable. The trademark, the licenses under it and the royalty income continue on and on. They have their mark registered in nearly all of the countries of the world.

Know-how, while it is very useful and often vital, in the initial establishment of the joint venture, does have a limited life, and if your

license arrangements relate primarily to know-how it may be difficult to have royalty last for any substantial time. There are some cases, particularly in the chemical industry, where you cannot tell from the product or from looking at plants how the product is made, and this situation may last for many years. Other technology, of course, may not have that advantage. In your arrangements relating to know-how it is very important to include confidentiality clauses so that the other partner must keep the information confidential. If the information becomes available to all, its value is destroyed.

As many of you know, there are many problems in getting technology overseas. As Felix says, the best way is not only to use people, but also have drawings, technical manuals et cetera. And, as many of you also know, there are a number of United States governmental agencies which get involved in this type of thing. For example, the Department of Commerce has export regulations. (Shows booklet) This is just a summary but the regulations themselves are quite voluminous. They are not unduly difficult but you have to consider them and make sure you have the appropriate license for your technology which is going to the particular country involved.

The State Department has a munitions list which again you have to keep in mind, and they have publications on that. Certainly you assume that bombs and that sort of thing are covered by this munitions list but you will probably be surprised that there are a number of other items which may very well require the appropriate clearance of the license agreement itself and of the arrangements for exporting the technology. These regulations change from time to time, not only as far as the written word is concerned, but sometimes the practices and the people who are administering the regulations. Sometimes the people get quite informal about it, and other times they want all the formalities performed.

Often you have equipment which may have a military use as well as commercial use and you do have to be quite careful to make sure that you get the appropriate clearance before exporting the technology. In your agreement you may also have to provide that the joint venture or the licensee may not export either the technology or the product made from it to certain countries. Some of these countries, such as mainland China, you might expect to be on certain lists, but you may be surprised to find other countries such as Southern Rhodesia or Switzerland, on the appropriate government list. You certainly have to keep this situation in mind.

Even the know-how which is contained in a patent application cannot

be sent overseas unless you have a license from the Patent Office or unless six months have passed since the patent application was filed. If you do this and are not able to get a retroactive license which may be available, the United States patent may become invalid.

Often you will be sending further information to the joint venture. This further information may be in the form of improvements of the original technology. Again you should make sure that you have the appropriate clearances for the later information as well as the original information.

One thing that might be quite important in the joint venture is the payment of the costs involved in the trademarks and, more particularly, the patents. As many of you know, in the more sophisticated areas of technology there are comparatively few countries where you ask for your patent protection. On the other hand, if you have technology which might be involved in cigarette manufacture, there are an amazing number of countries where cigarettes are made. If you were going to file a patent application in 40 countries, the initial filing costs would probably run you on the order of \$20,000. And, as you know, it is rare that you have one patent that is going to cover your technology adequately. You may have a number of patents covering different aspects. So if you have ten patents, the cost will be \$200,000. After awhile these costs become unbearable, and you have to be selective. It may be appropriate to have the joint venture or the licensee pay these costs. You also have to make arrangements on decisions on where your patents or trademarks will be filed so that you are not required to file them everywhere.

Another technique that can be used, if you have a joint venture arrangement arise after your initial patent filing, is what they call patents of confirmation which are available in many Latin American countries to confirm the patents which you have in the other countries. Patents of importation are useful in Belgium and Spain. These are similar types of proprietary assets. There really are quite a few things you can do in some countries to increase the value of your proprietary assets even after the date has passed that you normally would be concerned with.

The biggest problem from the patent attorney's viewpoint is where to file the patent applications and how to handle them in each country with its different laws. Although many corporate patent attorneys were pleased to see such things as the Patent Cooperation Treaty coming along, it is going to be an awfully long while before you can really have an effective way of getting a so-called world patent. Thus your joint



venture has to be quite cognizant of the different patent laws and different trademark laws. It makes a very complex operation, but properly handled, your proprietary assets can be very valuable to the joint venture. I think that is all the comments I have in general. If I can answer any questions, I'll try, and I'm sure some of the other people here can also answer a number of the questions.

**MODERATOR WEISER:** Homer, you really touched here for the first time on clearances and permission on exportation of technology. I have a question here relating to exports to countries which are on our blacklist. Both from your point of view and the point of view of management of the joint venture, which I would like to direct to Mr. Klass, how do you prevent the joint venture, if at all, from handling this exportation of technology particularly if there are no patents or patent protection in the country where the joint venture wants to export it.

**MR. BLAIR:** We usually use a clause where the licensee or the joint venture agrees not to export this particular technology to this list of countries. You refer specifically to the State Department or the Department of Commerce regulations. And we do place a burden upon ourselves to notify the other party of changes in these regulations, the addition of any countries, the removal of certain countries.

We had one situation where we licensed a German company under our technology for which we did need a government license. However, in order for them to show this equipment at a show in Switzerland, which seemed to be a reasonably innocuous country, they had to get special permission from the U.S. Government and they had to agree, and we had to get a signed statement from them stating this, that in order for them to show this equipment at this show, which was available to the public, they would not leave it in Switzerland, they would not sell it to anybody in Switzerland and they would bring it back to Germany. We did it. I wasn't in agreement with all the philosophy behind the arrangement because this same equipment could be bought in the United States. It's available to all but it comes within one of the official categories. However, we went along and played the game, and the other party with some muttering I suspect, signed the document.

It is just something you have to live with, to keep in mind and of course it does change from time to time. The U.S. Government is looking at it from their point of view as a whole world-wide operation.

I might not agree with some particular aspect of it but I do have to live with it, and I'm able to convince the other parties that they have to live with it too in order to have access to our technology.

**MODERATOR WEISER:** Do you find that they have been observing it?

**MR. BLAIR:** As far as I can tell. They sign statements saying that they will and as far as I know they have. I hope they have.

**MODERATOR WEISER:** How would you reprimand a joint venture for violations, Felix? You mentioned reprimanding and rewarding.

**MR. KLASS:** What you have to do depends on the nature of the technology because the regulations are not the same for all types of technology. With most of the technology that we work, it is not visible in the final product, and we impose general obligation of secrecy on the joint venture in the license we give them. If we have a new method of making plastic, we're concerned about it being disclosed to anyone. Then with respect to the export of the final product, we put a general paragraph in our license agreement, saying that you can't do anything in violation of the laws and regulations of the United States, and we notify the licensee from time to time what those laws and regulations are. At the moment you can export all these products even to Mainland China. At least with the ones I'm familiar with we have no restriction on the export of the final product, only on the technology. And we are as concerned about restricting the export of the technology as the government is because that's our stock-in-trade.

**DIRECTOR HARRIS:** Assuming, particularly in Japan, that the Japanese government is trying, through MITI, to retain control in Japanese hands, and consequently looks askance at giving 50 percent or more interest to foreigners—equity interest in the corporation. You establish your joint venture, and assuming that the major reason for the joint venture arrangement is to obtain or retain some kind of security control for the technological property you're introducing in this venture, how do you get the control that you are seeking? Do you have any difficulty with the Japanese in that they look behind the curtain? In other words, is your objective of obtaining more control acceptable in the guise of the joint venture? Do you have too much of a control problem under the joint venture? Can you not obtain control in various ways, by contract, et cetera?

**MR. KLASS:** I don't have the control question as the big thing in mind. We go in and we are trying to set up a successful commercial operation and the things you have to do to achieve that usually are reasonably well definable. If we have a joint venture partner, we will listen to them and they will listen to us, and we'll try to work out what

the best thing is to do. Now as far as control at the board of directors level, everyone of our companies is a public company—the articles and charter or the equivalent in Japan, have been filed with the government. We don't try to do anything underhanded or behind the scenes. It is not necessary. You cannot get involved in the day-to-day approval. We don't try to get involved because that is the quickest way to destroy a company—to keep the operating people from running it as effectively as they can. We don't have that problem with control. From our viewpoint it is a very theoretical problem in any country. The Japanese, the French, the British, the Germans, all of them are motivated by the same objective—how do we run a company successfully to make the maximum profit out of it. As long as you are operating with that objective you usually find what you want to do is not terribly different. If it is different, you discuss it until you reach some resolution of the matter or some compromise to let the company go ahead and continue to operate successfully.

DIRECTOR HARRIS: I wonder if anybody has had a different kind of experience—practically speaking. Either they haven't, or they don't want to say. I've heard stories that were a little bit different.

MR. LAUVAUZELLE: One thing I could mention—the *Fruehauf* case. It was a French company joint venture. The management of the company was entrusted with the board of directors. The president and executive officer were Frenchmen. Fruehauf S. A. was manufacturing trucks under a license which was granted by the American partner. The French management decided they would sell these trucks to a country belonging to the Soviet Bloc, which decision in turn raised objections from the American stockholders. It came to a deadlock. The board of directors and the French partner's position was that to sell trucks to such countries was in the interest of the French company and they were entitled to make the decision. It later came to court and an administrator was appointed by the court to be in charge of the management. The American interest was later bought out under his sponsorship. That is one of the horror stories. Perhaps that is the one you were thinking about. As a matter of fact, to the extent that there is no publicity on it, it is true there are very few at present and only one that has been recorded in the last ten years.

MR. DERINGER: Well, I have no experience myself because I am not inside the company but from the cases where we have been consulted about setting up a joint venture, I know that certain American companies regard it as very important to have a majority interest either as a controlling power or if not, some kind of veto or some kind of construc-

tion on the board so even as a minority shareholder they could control it. So this is what they intend at least when they start the joint venture. I don't know how this works out.

**MODERATOR WEISER:** Does anyone here have any experience in a situation where the control has shifted and could you give us reasons why it has shifted from a minority to equal, majority, or vice versa—or where two parties have changed to three. And could you give us the reasons for that change?

**TAGGART WHIPPLE:** Well, I've had an experience where control has shifted, yes. The reasons were purely and simply that the center of gravity of the contribution of various parties shifted. And so they got together and over a very extended period of time they managed to reshape the transaction which was set up in quite a different context over a generation ago. My thought is, with respect to Mr. Klass' comment that he hasn't run into this problem, I think there were two reasons for it—one, most of the business people I know choose their partners with very, very great discretion when they go abroad. They don't want to get into the kind of position or situation that leads to a fight to control. There is nothing more exasperating. Secondly, I think that in any business relationship, whether it is a joint venture or otherwise, there has to be a fundamental bedrock of good faith among the partners, or it just ain't going to work.

**DIRECTOR HARRIS:** This point you make is a good one, but I was trying to take it one step further. Where the country itself has some sort of prohibition against outside control. Moreover, when you choose the partner, in certain instances, you aren't entirely sure despite reasonable precautions how it is going to work out. Is the joint venture a way of protecting yourself. Let us take the case where your potential partner is anxious to cooperate with you. He wants to give you equal control, but his government says no. Is this instrument a method of getting around the legal prohibitions of the country? Could you give us your views on that?

**MR. WHIPPLE:** I don't know, I haven't run into that particular situation where you are trying to do something in substance that in form is prohibited by the particular statute, regulations, or customs of the host country.

**DIRECTOR HARRIS:** Felix' reference to Japan brought this to mind.

**MR. WHIPPLE:** Well, my experience in Japan has been that the clients I have advised had a very satisfactory commercial result, once they go over MITI—and your 20 months is a modest estimate in my experience.

MR. KLASS: It's better now.

MR. WHIPPLE: Well, O. K. This was a few years ago. May I ask one question suggested by Mr. Blair's comment about the high cost of getting patent protection in a lot of foreign countries. If it is true, and I'm not a patent lawyer, that many foreign countries provide for compulsory licensing after a certain period where you don't exploit the patent, my question is if you want to get patent protection from a given number of foreign countries, and you can't afford to start the exploitation going under the patent short of the statutory period when you run into danger of compulsory licensing, are there any techniques, any practical ways of extending or drawing the teeth of the compulsory licensing requirement.

MR. BLAIR: That's a good question. There are a number of countries that do have the compulsory licensing provision. Originally I think they were started by some of the countries that previously actually revoked the patent automatically. Now most of them have compulsory licensing. But I think, practically speaking, they aren't of as much concern as you might think. I think it rarely happens that you actually have the compulsory license that goes through the government. Now, it may be partly because somebody comes in and, because of the threat of the compulsory license, is able to work out another license with you.

I did have a couple of comments on one thing here. Here is a publication dated 1964—it's a little out of date—but it says that the United Kingdom over a five-year period had seven applications for a compulsory license based on non-use of the patent. One of these was granted and the others were either withdrawn or abandoned. In Denmark they had seven applications for a five-year period. Three were granted. The numbers go on like that. They are very small numbers. Of course if it happens at the wrong time to you you're in trouble. But I think the best thing you can do is to try to file it there and get it issued and hope that you will be able to work it appropriately in that country. It is a risk but it isn't as large as it might be. These things do come up sometimes but I think it's mostly a possibility of what could happen to you rather than something that really does.

PROFESSOR OPPENHEIM: On these working requirements, isn't it true that where there are provisions of that sort you are also permitted to show justification for the non-use? If the period for the working requirement is two years to three years, might you get an extension if you can show that the product isn't ready for the market, that you have to do some more R&D? Is that true?

MR. BLAIR: It depends on the particular country. Yes, in some cases

you certainly can do that. In some cases you can have a license arrangement with one of your licensees which could help. Some may have the provisions where you can allegedly do what they call nominal working which is to put an advertisement in the paper that you are willing to license anybody. I don't know whether it's effective or not, but it is done in some places.

**PROFESSOR OPPENHEIM:** Another thought comes to mind. Have you been talking about two-party joint ventures or spreading it to three parties?

**MR. BLAIR:** Most of the time I have been on the two-party ventures.

**PROFESSOR OPPENHEIM:** Two-party. Well, if that's the case, I would like to know are there situations where the parties, each one owning separately its proprietary information or patents, would license third parties in countries where there isn't any desire to extend—in product or market extensions.

**MR. BLAIR:** I would think that you could.

**PROFESSOR OPPENHEIM:** Do you have experience with that?

**MR. BLAIR:** I've been involved in one situation where we had some technology and patents and we felt that ours was the major part of the technology. Another company had some patents which were rather a thorn in our side and we did not need their technology. We made arrangements with them to get a license under their patents with a right to sublicense our other partner. That worked out fairly well in one respect because this other company, which happened to be a foreign company, had some patents in countries we didn't have so it gave us a better position in one respect to license the joint venture. We had our own technology, our own patents. We did not need the technology from the other company that owned the patents—all we got was the naked patent license which was all we needed. That worked fairly well as the royalty rates that we had to pay on these other patents were quite small because they realized their technology was a small part of the overall picture. The royalty and the share of the profits we were getting from the other one were very adequate to cover that.

**PROFESSOR OPPENHEIM:** I assume in a two-party situation that typically there would be cross-licensing between the two parties. Is that common?

**MR. BLAIR:** Yes. Often what we try to do is grant the license to the joint venture or the licensee, as the case may be, and because of the U.S. antitrust laws and other reasons, all we attempt to get back is a nonexclusive license. We may try to make arrangements where we have the right to grant rights under this nonexclusive license to our other li-

censees if they again will make the same contribution back but on a nonexclusive basis. We haven't tried at all to get title to inventions belonging to the other party.

MR. DERINGER: Do you have any experience with joint research—common research.

MR. BLAIR: I haven't myself except in some cases where we have been involved in one part of the research because our technology was more research type and the other party had more development type. But I haven't been involved where we have actually shared a field and both contributed research on that.

MODERATOR WEISER: Mr. O'Brien don't you have a place in Brussels where Union Carbide does research?

THOMAS I. O'BRIEN: We recently closed it down.

MODERATOR WEISER: Is this an unsuccessful story?

MR. O'BRIEN: It was not successful.

MODERATOR WEISER: Can you pinpoint the reasons why this is so?

MR. O'BRIEN: I don't think there are any special reasons. No more than any research laboratory we have in the United States. The venture just didn't turn out successful.

MODERATOR WEISER: Do you find that if you are involved in joint research with another company, the problems are much greater than if you were involved in doing your research at home alone, perhaps because of the way of approaching the research problems, or management problems?

MR. O'BRIEN: No, I don't think there is any special difficulty. We have had examples of joint ventures which have turned out quite well. I don't see that there was any particular difficulty because of the relationship between the parties. It's more usually in the success of the research program.

MODERATOR WEISER: I want everybody's mind tuned to think also the other way, where there is a joint venture in the United States involving the licensing of technology from abroad and not be just a one-track mind the other way around. Maybe we can identify some of the problems that may be peculiar to the situation of a joint venture in the United States. Does anyone have any experience in that direction?

MR. FINNEGAN: This is not a direct answer to your question, but it's related to your question. I wanted to ask Homer another question. Assume these facts: You have industrial property rights abroad, say in France for example. You have a French patent and maybe a trademark there. You are also going to supply know-how to the joint venture. If you have a French patent, undoubtedly you also have a U.S. counter-

part, and it's probably valuable, if it's valuable enough to put into the joint venture. What do you do about licensing the joint venture company under your U.S. patent rights? Do you have any set policy on this?

MR. BLAIR: We don't have a set policy. It just depends. Often we tend to license them in France and in that kind of situation we might license them in the Common Market as well. We have had occasions where we licensed somebody who manufactures in one country and gave them the right to sell, under our patent rights only, in other countries and in some cases we have included the United States, more likely we probably have not. But in those cases the particular company wasn't interested in the United States. They had enough to do in Europe.

MR. FINNEGAN: Would you ever consciously fail to give them a U.S. license, with the idea that you don't want the product coming back into the U.S.?

MR. BLAIR: Yes. Of course, here, as you know, is an active area for the U.S. Department of Justice.

MR. FINNEGAN: I realize I'm starting to slide into the antitrust problem.

MODERATOR WEISER: Still on this point, Homer, do you assign your trademarks to the joint venture or the patent? Do you distinguish between the trademark or the patent?

MR. BLAIR: We try not to assign trademarks, partly because of the concern that if the arrangement does not work out it's more difficult to get the trademarks back, if you have to get a reassignment back. We would prefer to license and have some clauses in the license to handle the situation. In case there is a bankruptcy or other failure the license will be terminated and the trademark will remain our property.

MR. O'BRIEN: Do you give exclusive licenses under your patent rights and technology in the territory of the joint venture?

MR. BLAIR: We certainly may many times. Sometimes we have semi-exclusive licenses under which we will not license anyone else but we retain the right ourselves to operate under the technology. Also often in our case, the other partner is not concerned about us going in there and beating them out of profits.

PROFESSOR OPPENHEIM: On that very point. I take it there would be a tendency to be very chary about sublicensing—giving sublicense rights. For example, giving your exclusive licensee the right to sublicense. Wouldn't that tend to get things out of control for the partners?

MR. BLAIR: We normally don't include sublicense rights but we do on occasion as long as they are licenses within a certain territory. For example, in the Common Market, it may be useful for the exclusive licensee to have a sublicensee in another country.



PROFESSOR OPPENHEIM: Within the Common Market?

MR. BLAIR: Within the Market. Sometimes we do have a clause where there is an approval by us. We don't usually do this but once in a while we do, but in each case we say the approval will not be unreasonably withheld. Whatever that means.

MR. WHIPPLE: Could you give me some feel as to how you experts in this field deal with royalties on just know-how, unpatented know-how? Are you running scared because of Judge Motley's decision in the *Painton* case and *Lear* against *Adkins*? Are you still charging for them?

MR. BLAIR: I'm still charging for them and ignoring those decisions. I hope that when they get to the right court at the right level, they will see the light.

PROFESSOR OPPENHEIM: Well, it's awaiting decision in the Second Circuit as you know.

MR. BLAIR: Right. As far as I'm concerned I'm still operating with know-how as a valuable asset and I will certainly charge royalties for it.

MR. WHIPPLE: Do you think this is generally true among your colleagues?

MR. BLAIR: I think so. We're keeping our weather eye out but I'm certainly not going to give my know-how to somebody for nothing.

MODERATOR WEISER: Mr. Cooke wants to comment on that.

HORACE B. COOKE: Is there a growing tendency, at least in some countries, for the government itself to insist that it shall have a financial stake in the venture along with perhaps the U.S. company and the domestic-foreign private company?

MR. BLAIR: I'm not familiar with that situation. I know that there are a lot of occasions where you can set up a company where there is another partner in that country or possibly the public is the other partner. In the latter case you have certain control advantages because the other 50 percent may be split up in a large number of individuals. Or you could have it where the venture includes you, the other partner, and maybe a third of the stock is sold to the public in that particular country. I'm not familiar myself with the government taking a piece of the act themselves.

MR. COOKE: I am under the impression that something very close to that may be true at least in Spain. Spain has very stringent views on foreign-held or partly held joint ventures. They are very anxious in certain instances to bring the technology into Spain, but they also have some rather peculiar handles to put onto it.

MR. BLAIR: I'm not aware of that. I know you read about these joint ventures in some Eastern European country, and there of course you're dealing with the government. I'm fortunate in that I, the Commission-

er of Patents and some other people, including a man working for Felix, are going to the Soviet Union in early June as part of the U.S. delegation on Patent Management and Patent Licensing, and maybe we will learn more about the joint venture possibilities with the Russians.

MODERATOR WEISER: Mr. Ney.

ANDREW L. NEY: In what countries are license agreements, and royalty rates subject to review by the government, and is a distinction made between a straight license to a company in that country and a license to a joint venture?

MR. BLAIR: Well, there are a lot of countries, many of which I'm not familiar with. Certainly Japan is one. The license, whether it is to a joint venture or a straight license, would require the same approval. I know, for example, in Yugoslavia, you have to get government approval, and one thing they look at is to see whether the value you have assigned to your proprietary assets or your technology in establishing a joint venture is appropriate from the government's viewpoint. In other words if they don't think it is enough, they don't give you approval. You can't go in and say I want 50 percent of this as the value of my proprietary assets or my technology if they say it's only worth 20 percent. There are many countries that do require this approval. You have to look at each one.

MR. NEY: Would you say that of most of the countries in which a typical U.S. company would deal?

MR. BLAIR: No, I wouldn't say most. In fact, it's a minority. In a lot of countries in Europe you don't have to get the approval of the government for the royalty rates.

MODERATOR WEISER: Well, maybe we could list a few. Japan—we talked about Yugoslavia—France indirectly has regulations, if not direct. Mr. Lauvauzelle may want to comment on that. Anybody else want to name some of the countries—South Africa.

MR. HILINSKI: Well, a good many of the South American countries will do this in various ways by currency controls, disallowance of payment for tax purposes—

MR. LAUVAUZELLE: I'd like to comment further on the point made by Mr. Hilinski on the disallowance for tax purposes. Aside from the regulations on the licensing arrangements between the two parties, when the company exists and has been approved, then there is a tax problem which exists in all countries, where tax law, which may be either domestic or provided by a treaty, directs that no undue payment should be made to the licensor. Of course, certain countries are more

the targets of scrutiny by the tax authorities. I understand that if a German or a French company receives some technology from a Swiss company, perhaps the German authorities as well as the French will look very carefully into the Swiss licensor company to make sure it is not the way to siphon off profits. But even between countries where the special tax haven conditions do not exist, there are still some conditions.

**DIRECTOR HARRIS:** May I interject Mr. Ney's additional question: Is there a distinction in treatment between a license to a joint venture and one to another company in the foreign country?

**MR. LAUVAUZELLE:** No, the joint venture being a corporate entity has a nationality. It is clearly treated as a national. The problem is emphasized because the licensor of the joint venture is a partner. This problem lies in the distribution of hidden dividends through royalties, thus avoiding corporate tax on the joint venture.

**MR. DERINGER:** But in this respect there is a distinction between joint venture and mere licensing agreements, because if there is a license agreement between two very independent companies, the problem of hidden internal transfer of profit cannot arise. So here joint ventures are better off than just license agreements.

**MR. BLAIR:** They will look more closely at it.

**MR. DERINGER:** Yes. They will closely examine it.

**MR. HILINSKI:** I was going to make some such comment, Mr. Deringer, because the reverse is true when you are looking at the amount that a United States corporation is charging a licensee. If it is a wholly owned licensee and the rate is relatively low there is a suggestion in the U.S. that there is in fact a hidden distribution going in the reverse direction, whereas if you are dealing with a joint organization overseas where the interests you might say are at arm's length, there is less of an ability for the United States Government to raise this hidden distribution in reverse.

I might say one other thing—going back to the question that Mr. Whipple spoke about briefly—the control question. I had a reaction at that point that if the local laws in effect either require control by local nationals or at most, an equal position of control, the effort to bypass the local laws through contractual arrangement does leave you somewhat vulnerable in case the local party then comes into disagreement with you.

**MR. WHIPPLE:** I agree. I don't know of any case from my experience where this has been tried, I'm happy to say. It might be risky.

**P. J. FEDERICO:** I'd like to ask a question perhaps on a slightly differ-

ent tack. Does anybody here have any experience of dealings of this or analogous kind with Russia? Probably not joint ventures but how are such dealings handled, if there are any?

MR. KLASS: We've had a number of license arrangements with the Soviet Union and negotiations run differently. In many instances they take a much longer period of time and there is some tendency to have new faces coming up as you continue your negotiations. In principle I don't find it terribly different from negotiating with anyone else and our actual performance experience under the agreement we entered into—and there are not many of them—there are just a few, has been very good.

I have checked around with many companies that have done a great deal of licensing of technology to the Soviet Union and the licensing usually means licensing and getting the plant built and on stream. Uniformly the experience is that the payments are good, the people are no more unreasonable than in any other part of the world, and when you get something running, they are very pleased and appreciative. I have only heard of one case where somebody went into the Soviet Union and put up a plant that just didn't run and it is still sitting there as far as I know with no payment and no operating process.

The one thing the Soviets put in all their agreements, in fact all the Eastern European countries put in a clause to the effect that if a plant is basically a failure, they can elect to terminate the contract, ask you to remove the equipment, and restore the site. And you don't get any payment. They absolutely insist on putting this into every agreement. When you argue with them that it is an unreasonable provision, they don't dispute the fact that it's unreasonable. They simply say, and as far as I know it's true, that this clause has never been invoked. So you say well, if it hasn't been invoked why do you want it? You can't make any progress and eventually you end up as far as I know taking it with no real resultant problem.

MR. GREEN: Are your negotiations with the Soviets with the actual plant managers or with an intermediary organization?

MR. KLASS: I can't speak from broad experience. Our negotiations were with Licensintorg which is the licensing organization, supplemented by somebody from the State Ministry for that industry and supplemented by somebody who was from the Ministry in the province—this was down in Armenia. We had some people from the Ministry that were in charge of the plant, so there was participation by people looking toward the actual operation, participation by the Ministry and participation by the licensing organization.

**PROFESSOR OPPENHEIM:** Did I hear you mention AMTORG?

**MR. KLASS:** Licensintorg.

**PROFESSOR OPPENHEIM:** Oh, I was wondering if the venture involves import-export trade. Is AMTORG still in existence? I haven't followed that for a long time.

**MR. KLASS:** They are still in existence. They are a good place to start, but you have to find the right person in the Soviet Union and that's difficult at times. There are all sorts of ways we go about finding the right people to deal with, but once you do, you start making progress.

**PROFESSOR OPPENHEIM:** More than know-how, know whom.

**MR. HILINSKI:** Is it ordinarily that the inquiry comes from Russia rather than you seeking them out?

**MR. KLASS:** Normally, that has been our experience. We've tried the other way in one or two cases, but without success so far. It's only been three years though; we're still working.

**MR. HILINSKI:** The reason I asked that question is with the type of controlled economy they have, I understand it is ordinarily a necessity to have some action taken there in the first instance before they can get interested in any project.

**MR. KLASS:** Like anything else they are a group of human beings, and therefore if you go there and persuade them that something is good, they will then turn around and get it put in some plant. So you can work both ways.

**MR. SPERRING:** I have heard that many companies use third parties in negotiating with East European countries and Russia, people who are specialists in this area. Have you had any experience this way or do you do your negotiations directly?

**MR. KLASS:** It works both ways. We have some people who are on a retainer and who are experienced in doing business in the Soviet Union and we have found them very helpful in some areas. In other areas we have found it possible to work directly. Again, it's different and yet there are very close points of similarity.

If you know people, even though they may not be the right people—if you know them and they know you, there's a relationship established, and if you need to find some other place to go, they will find it for you. They don't sit there looking glum waiting for someone to hand down an instruction on every sentence. They are trying to get a job done and are reasonably cooperative.

**MR. SPERRING:** Could you be just a bit more specific on the areas in which specialists are helpful?

MR. KLASS: I think it's mostly a case of knowing people. If you want to go to work and sell a product through one of the import ministries—they have divided their imports in the areas of the ministries to different types of products. And if you can find a specialist who knows the director of that particular import ministry, it is very worthwhile having him around, because he can walk in and say "Hi" and get you started. If on the other hand you establish relations with Licensintorg as we have, we can go in and get started at Licensintorg. Where we'll end up I can't forecast in every case.

MR. SPERRING: And you did this by an initial contact directly with Licensintorg, or did you use a third party to start it?

MR. KLASS: It comes in a circle. It's like dealing with an extremely large company. After you get to know some people you can do business with them.

MR. SPERRING: It's the initial contact.

MR. KLASS: The initial contact is difficult, but as in a large company, the Soviet Union is interested in developing relations with large companies over all parts of the world. In Europe for example, they have general treaties with countries like England, France and Italy, and under those treaties for technological exchange they have agreements with individual companies providing for a broad basis for collaboration between the two in the nature of a technical exchange. Now we don't have anything comparable in the United States under which to operate so we have to develop our own contacts.

MR. SPERRING: May I ask one other question which is directly related to this? I understand the Russians have many rubles but few dollars. This is only from general reading on the subject in periodicals. Is there a problem, or have you in your specific experience had difficulty in the payments for the royalties due under the license, or translating their currency, and is there a mechanism that you have employed here?

MR. KLASS: We have run into no difficulty and all our payments are in dollars. We have had no difficulty in payment from the USSR. We have more difficulty with some of the other Eastern European countries where they have wanted us to take a proportion of our payment in barter.

MR. SPERRING: Have you had barter arrangements?

MR. KLASS: We tried, but couldn't get rid of the product, so we said "No thank you." You can get a barter arrangement. There are many people in Western Europe who will handle barter for a price. When we saw the overall net to us after the difference in price, the commission to the agent and so forth, it turned out to be too low, and as a result we

declined to go ahead. They wanted to buy material in part through barter payment. We couldn't justify it. We declined and they bought it for dollars.

MODERATOR WEISER: Would you say with respect to Russia the payments are generally lump sum payments rather than long drawn-out royalty payments.

MR. KLASS: I have checked and have been unable to find anyone who has a running royalty arrangement with the Soviet Union. It's always been lump sum.

MODERATOR WEISER: I think this is somewhat of a response to Mr. Whipple's question about know-how. I detect a tendency to favor lump sum payments at the beginning, and upon further transfer of identifiable technology, then further payment. And this would not only apply to Russia but other straightforward know-how agreements where there is no peg like a trademark or patent to hang it on.

DIRECTOR HARRIS: Is there any difference in the way they treat a joint venture in that regard as opposed to an ordinary licensing arrangement?

MODERATOR WEISER: Does somebody want to answer that?

MR. BLAIR: Well, in the license you certainly do get the initial payment for the know-how. In the joint venture this may be a large part of your contribution to the joint venture. If you have a substantial amount of know-how and it is covered by a patent, it is a very valuable way to start out.

DIRECTOR HARRIS: If it were a joint venture would you still treat it the same way? You just suggested lump sum payments. Everytime you transfer another piece, you get your money, but are you liable to lose in such a case if you didn't?

MODERATOR WEISER: With the only exception that if you do have the joint venture making the contribution, which is then rated as flow back, then you may deduct that from any further payment.

MR. NEY: Mr. Klass, in your talk you commented about a foreign joint venture partner getting his costs out of his contribution to the venture but that he should not make a profit at the expense of the joint venture. How do you distinguish a U.S. partner collecting royalty income under a patent or know-how license where he is getting a profit off the top, from the attitude that you expressed about the foreign partner not getting any profit directly off his contribution?

MR. KLASS: I think that is one of the reasons why I expressed considerable uncertainty as to whether my answer was the better one. I must say that we have joint ventures which have substantial research pro-

grams. You see it is our feeling that in an industrial country you should have research activity in every enterprise to attract and hold competent, technical people because they are the ones who make the entire functioning of the organization so much better and more effective. That's why I fully agree with you. There's a serious question in my mind why, if we supply technology and get paid, someone who contributes the marketing shouldn't likewise get paid for contributing his position in the market.

MR. NEY: The alternative might be that when you form the partnership, the U.S. company comes in with its technology and its patent position, and the foreign partner comes in with his market skills, and you agree on what your contributions are. And the only pay back to each party is simply a sharing of the profits of the joint venture. I realize I'm giving away money from my company's standpoint by not getting a license fee or something like that. All of these undoubtedly can be worked out in the negotiation.

MR. KLASS: I think you have a very viable argument, and exactly where you would end up does merit a great deal of discussion. If there is no continued research by the joint venture, eventually the marketing function is as helpful to the other partner as he was helpful to the joint venture at the outset. Let me put it this way. If you start out with a proprietary unique package of technology and patents, you have something which is unavailable elsewhere. Marketing skills are probably available in every country from a half a dozen different organizations. This may be a bit of what the market will bear philosophically rather than a good logical philosophical analysis of what is completely correct. You should normally get paid for the technology and the patent even though you don't pay for the marketing skills.

MR. SPERRING: Another question relating to Russian and East European business (I have many questions because I am going to be fortunate enough to meet the Russian Patent Commissioner who is traveling in the U.S. on the other half of the exchange which I think you mentioned you are going to take part in Homer, tomorrow. I have a number of questions for him. I think we are going to learn more than we will teach him.) Do you have any experience, Mr. Klass, in having filed for and obtained a patent in either Russia or in an East European country?

MR. KLASS: I don't have personal experience but my company does apply for patents there.

MR. SPERRING: And have they obtained patents?

MR. KLASS: I believe so.



MR. SPERRING: Our company, about the middle of last year after a lot of thought and study in one particular process, did apply in Russia and a couple of East European countries. Of course, it's too early to judge—but the translation costs, the filing costs, the prosecution costs are extremely high, and I'm wondering if a patent will issue. And one of the decisions that I am pondering now is should any further attempts be made for patents, how long will it be before the patent will issue, and if it does, the possible value of licensing in Russia. That's why I was asking the question.

MR. BLAIR: We've filed some patent applications, but for those reasons there haven't been too many. And as yet we haven't got them issued but I'm not concerned because the filing has taken place only in the last two or three years. I was in a meeting last week in the State Department with these Soviet representatives you are meeting tomorrow and they discussed the problems of dealing with the Russian Government in a similar manner to the U.S. Government as far as inventions go. They indicated they will issue Soviet patents and, in the appropriate situation, they are very interested in licensing to the Soviet Union under those patents, including technology as well. There was one comment that they have the inventors' certificates as well as patents in Russia. The inventors' certificate is what the Russian inventor, through his enterprise, normally goes after. One thing they give the inventor under the inventors' certificate is money. Another thing they give are better apartments. The inventors are entitled to a little higher status. They did point out that these benefits are not limited to Russians. Foreigners can apply for the inventors' certificate so if you have need for a larger apartment in Moscow this might be of interest to you. (Laughter)

MODERATOR WEISER: I take it that that is a joint venture. (Laughter)

MR. SPERRING: Did you learn anything about their investigation system? The patents I have read have been selected ones that I have obtained from Russian inventors. I'm not a lawyer, but I wasn't very impressed about the technology once I got the patent after it had been advertised.

MR. BLAIR: They apparently have, in their factories, what they call a patent service group which is similar to a United States company's patent department. This group takes care of preparing documents which are sent into the central government patent examining operation and, as usual, they go back and forth just like in the United States. And the problems of the Soviet inventor are remarkably similar to the problems the employed United States inventor has.

The way these people were talking they did have one point which they brought out with a little bit of glee on their part—that as far as they are concerned the individual who is employed by a Soviet enterprise, in a manner similar to a corporation in the United States, has more direct incentive because he does get monetary reward and apartments and status whereas in this country, depending on the corporation you work for, there may or may not be monetary rewards. Here you often take your rewards hopefully in promotions or increases in salaries. They felt there was more incentive for their inventors under the inventors' certificate arrangement than we have for our inventors who are employed by corporations.

Part of the reason for the US/USSR exchange is their express desire to increase the licensing both of their technology into this country and also of our technology into their country. They talk like they are very interested in working out arrangements with American companies.

PROFESSOR OPPENHEIM: What is the status of the patent applications? Do they preserve confidentiality? Can you depend on that, prior to issuance, or do you feel that's quite a risk?

MR. BLAIR: I'm not aware that the ones we have filed there have been published there, but I wouldn't bet one way or the other. That's one thing I want to do when I go there is find out more about how they do handle the information, both on issued patents as well as on applications. Of course, practically speaking in our case, when we do file it in Russia, we are also filing in a number of other countries. And it would be available in these other countries in a very short period of time, so I'm not really concerned about that point.

MR. WHIPPLE: A point of information. Is there any data as to how many U. S. applications have issued as patents in Russia?

MODERATOR WEISER: Mr. Federico.

MR. FEDERICO: Well, I can answer a few of the questions that have been asked. If you have *Industrial Property* here for a year ago December, we'll get the exact figure, which is very small. (In 1969 there were 82 patents issued to American residents, out of a total of 715 patents, all to foreigners; the number of inventors' certificates was 25,911 of which 52 went to foreigners, one to an American.) To answer two questions that do not seem to have been answered completely—in examining Russian applications they make an investigation of the prior art. They have U.S. patents and patents of a dozen or more other countries classified into their system. They use the German classification type of system. They have the staff and they make a search, and they make rejections for anticipation and for what we would call obviousness.

I have heard from several people who have applied in Russia that they get kind of weird treatment now and then, and can't quite figure out what they mean. But from the standpoint of searching, some people have said that their search is comparable with other searching countries. No searching country is perfect. The applications are supposed to be confidential.

As part of the examination of inventors' certificates, since the government is taking over the invention, the application may be sent to an appropriate place to report on the utility or potential use of the invention; the government assumes some obligation to encourage its use. If they find it isn't apt to be used, they will refuse it for that reason.

According to the law, they are supposed to use the same criteria for patents. There is some ambiguity here but if they do the same with patents they would reach a stage in the examination where it is sent to somebody else, which usually is the appropriate authority that has knowledge of the subject matter, to report on utility. So to that extent there might be, and I'm only raising this as a possibility, a giving of the information to people actually concerned.

MR. SPERRING: May I comment on that? Certainly our thoughts were that the U.S. patents were similar, and because of this system they are probably reading other patents. I think a more pertinent question that arises in my mind then is how will we ever know how much of our technology which is published in U.S. patents, they might appropriate in some way.

MR. FEDERICO: They have been accumulating copies of these patents for probably ten or a dozen years from a number of countries. The patents are all public documents. They have been classifying them into their system, abstracting some of it, and diffusing the information. There's no doubt about it that they look at these things for their technical information.

MR. SPERRING: It's a problem that I don't want to hang just on Russia. Any other country that is difficult for people to get into, to contact, to assess their use of technology would be similar. But in this instance, a highly technically based organization for patent development, with lack of communication, is concerned with it somewhat because of the fact that they are obtaining U.S. patents, French patents, Belgium patents and because of the lack of any kind of a treaty or any kind of an association. And therefore I would think, Homer, that your group could possibly do something to open communication, to ease this kind of worry.

MR. BLAIR: I think it is going to be hard to run around in the Soviet Union and see if they are infringing some patent.

MR. SPERRING: Yes. But it's this initial communication that counts.

MR. BLAIR: Part of what we are trying to do in this is to come back with a report of some sort, which may be either positive or negative, on the value of getting patents and the possibility of granting licenses under a patent which is distinct from coming in and building a plant.

MR. SPERRING: Does anyone else know about other East European countries in the way that you just talked about Russia as far as the patent system?

MR. FEDERICO: Well, some of them; I would say that Rumania and Bulgaria have practically the same system of inventors' certificates and patents. But the others may swing more towards patents. In Poland a patent is granted but the inventor may also receive an inventors' certificate in addition; the significance of the latter is not clear. In Czechoslovakia patents are granted but an applicant or patentee may offer the patent to the State. East Germany has two kinds of patents: With one kind anybody can obtain a license and the other kind has regular patent rights. But on your question of copying information, a lot of people here have had the wrong idea for quite a long time. Published patent specifications of other countries are nothing but pieces of paper—pieces of technical literature. Anybody can read them and do what they please with them in another country. We do the same thing with patents of other countries, no doubt. One company told me an interesting experience they had: They built big machinery and had a very nice customer in Sweden to whom they supplied equipment from time to time. And finally it got a letter saying that they were stopping. A U.S. patent had come out. There was no patent in other countries and they found that they could get the equipment made cheaper in Germany. They started buying from Germany. That was perfectly alright legally. There was no German or Swedish patent.

MR. GREEN: Amplifying Pat's statement, some years back I spent a week in Moscow in their big information unit where they are collecting information from 95 countries in 65 languages and systematically diffusing it to every technical center. And this is national policy. Now at that time they were giving a low order of priority to patents in comparison to the literature.

MODERATOR WEISER: John, does this contribute to any interest in the United States technology and the formation of joint ventures, this dissemination of technical information in Russia?

MR. GREEN: It gives them an awareness.

MODERATOR WEISER: So that we may have obtained some benefit from that. I'm trying to connect this discussion to our topic, joint ventures.

MR. FINNEGAN: I have a question on joint ventures, Gerry, directed both to Homer and Felix. When you are contributing industrial property rights, and I mean to include all the rights—patents, trademarks, know-how and maybe even copyrights—and you are the U. S. company going into a joint venture, I'm wondering what kind of legal structure you use to set this up? It seems to me one thing you could do would be to write sort of a standard license agreement transferring the technology, and the consideration for that could be a 50 percent stock interest, or 40 percent, or whatever it happens to be. Does that automatically put you into a joint venture—that type of arrangement, or do you go deeper than that? Do you arrange for seats on the board of directors, officers in the joint venture corporation, and so forth. I'm just wondering how your two different companies might set this up. It would be interesting to hear.

MR. BLAIR: I think we work pretty much on setting up the joint venture itself with the details of the board and whatever. And our contribution in all or part, depending on what the situation is, are our proprietary assets. And in addition we have another document—the license agreement between us and the joint venture itself. But we haven't used the license itself to set up a corporate entity. We always have two documents.

MR. FINNEGAN: Does the license agreement call for royalty payments?

MR. BLAIR: Usually, yes.

MR. FINNEGAN: Paid by the joint venture?

MR. BLAIR: Paid by the joint venture itself to us. We are paying half of it ourselves, kind of. We have that and then we share in the profits as well.

MR. FINNEGAN: That's the normal way you set it up?

MR. BLAIR: That's what we do. Felix, do you have any comments on that?

MR. KLASS: Homer, you know how we do it.

MR. BLAIR: I used to work for Felix, but I don't know what he has been doing for the past few years.

MR. KLASS: We normally enter into an agreement with our joint venture partner which provides for setting up a joint venture company which has attached to it a charter and bylaws for the joint venture company. In the agreement with our joint venture partner we provide

such things as first right of refusal on the sale of shares, and other relationships, if any, that we have to maintain over the existence of a joint venture. We then have a license agreement—one or more license agreements—between ourselves and the joint venture. If our partner is going to do the marketing we have the marketing agreement, and so on and so forth. So we end up with the main agreement, a package of any place from two to ten exhibits, and after everything is worked out you get together in a room, do all the signing and you are in business.

MR. FINNEGAN: You would work out the license agreement at the same time that you are working out the basic joint venture agreement?

MR. KLASS: Yes. Everything is all worked out in one package.

MR. BLAIR: We do the same. We had one situation where the joint venture was with a foreign company but it was to be operated in the United States after a certain period of time and we had to set as exhibits in the main agreement four different license agreements covering different possibilities. So we had all of the agreements all there. It was all worked out and they were all signed. They were different possibilities on how we were going to have to do this and also if it terminated, we had arrangements so that the party could have a license under the other's technology. We had all of the agreements all negotiated and as Felix says you sit around in a room and everybody signs all kinds of pieces of paper. But it is all done at that time.

MODERATOR WEISER: I'm glad you asked that question. The relationship that I have seen in my experience, the relationship between the license agreement and the articles of incorporation and arrangement of the various relative shares, is very important because sometimes it has been possible in some situations to put within the powers of the particular corporation what it can do—some things which if they were in the license agreement may have been subject to greater vulnerability, at least on antitrust grounds. Particularly, if you could segregate some of the activities or areas of marketing or distribution to a particular board within the corporation, and hence maintain the type of effective control which is expressed in the articles of incorporation, these decisions may be more proper there than if they were put into license agreements.

DIRECTOR HARRIS: Gerry, would you get dividends from the basic joint venture arrangement and royalties from your licensing agreement?

MODERATOR WEISER: Yes, there could be dividends from the share (or in exchange therefor) from the contract. I'm saying that in some agreements it is possible to provide for some allocation of responsibilities—marketing, research, or activities of the corporation. It is better

organization to place these aspects in the basic agreement establishing the company, as some of you have called it here, rather than in the license agreement. But your royalty flow or your sale for know-how, lump payments, all these would be in the subsidiary, if you wish to call it subsidiary, agreement. The main agreement doesn't propose to regulate the royalty payment but it may assess the value of certain transfer of technology.

DIRECTOR HARRIS: Would you get both dividends and royalties or would your return be limited to dividends?

MODERATOR WEISER: Yes, both.

PROFESSOR OPPENHEIM: I see a rather startling dilemma that might exist if you have separate licensing agreements which in this country at least are not recordable. The patent bar views with alarm proposals to have patent license agreements recorded with the FTC or Justice. But if you have your partner abroad and under the local law abroad it must be recorded, then of course you are caught in between, aren't you, Mr. Blair? And of course the Department of Justice Antitrust Division would have access to the recorded agreements. So you have to be pretty careful about the kind of restrictions you put in your license agreements, I take it, in those situations.

MODERATOR WEISER: Mr. Ney.

MR. NEY: Would anybody comment specifically on citing products or product lines in these agreements versus generic descriptions for the manufacturing and sales activity of the joint venture.

MR. LAUVAUZELLE: The underlying problem when one comes to drafting the main agreement which incorporates by-laws of the joint venture and the licensing arrangement is the split-up of the market between the activities of the partners and of the a joint venture, which creates an antitrust problem. However, their split-up is the underlying concern of the parties because it expresses the precise definition of the operation of the joint venture, the way it will be operated, the control by the partners, and its aims. It describes precisely what the exact type of activity of the joint venture will be, thus stating the segmentation of the activity of the partners. So it's a very delicate point of drafting. The problem which you mentioned of the definition of the product should certainly be considered and perhaps avoided.

DIRECTOR HARRIS: Gerry, may I ask a question?

MODERATOR WEISER: Certainly.

DIRECTOR HARRIS: Are you saying that the basic joint venture contract is the instrument that these companies actually use to control

arrangements in markets and is generally more vulnerable than the licensing arrangement?

MODERATOR WEISER: Well, this is illustrated.

MR. LAUVAUZELLE: It is implied.

DIRECTOR HARRIS: Now we are getting into the heart of the matter, it's a pity we are so close to luncheon.

MODERATOR WEISER: With respect to the basic agreement itself it seems that it has particular relevance to joint ventures and subsidiaries too because, as has been illustrated by some antitrust decisions in the EEC (Common Market)—the Kodak ruling amongst others, this is the agreement which the antitrust authorities look at: what does the joint venture do, what is it authorized to do. What is set forth in that agreement is extremely important.

MR. WHIPPLE: I may be missing something here but it seems to me no matter where you put these desirable provisions, an appropriately drafted discovery instrument is going to get them. I think a lot of us have been through this. Now I've seen these things in heads of agreements. I've seen them in subsidiary licensing agreements. It does seem to me that maybe the client is lapsing into a state of euphoria if he thinks by sticking it in one particular piece of paper it's going to be secure against a carefully drawn discovery demand. This has been my experience, at least.

MR. KLASS: I wonder if I can comment? In a license agreement you have to define what the license agreement is talking about. If you are making a license agreement on some product, that is what you have to say. Whether the license agreement is to a foreign joint venture or domestic license or what have you, that's part of what the agreement must contain. I see nothing wrong with putting a license agreement of that sort into a joint venture because that's the business you're putting it into, where you are giving them technology and patent rights. Whether you can refrain from giving them licenses under your patents in other countries is a subject now being talked about by the Justice Department. I don't think there are any cases which require you to do so. And if the law develops in that way, you have to do it.

With respect to the other agreement, I fully agree with you, Mr. Whipple, you can't, by putting it in another document, achieve something which is unlawful. My suggestion is simply that you have a company and you have a board of directors and you better give the company the power to act as a company and the board of directors the right to use their best judgment to run the company to achieve success. It gets very, very treacherous if you think you can put into a document



on incorporation, the Articles of Incorporation or what have you, restrictions that would be violative of the antitrust law if you put them in the license agreement. Dick Stern writes a beautiful discovery document.

MR. NEY: I had a different point in mind when I asked the question. What I have in mind is, if you describe the product line with which the joint venture company is going to be involved in a very specific way, and something outside the scope of that definition comes up in the future, you might avoid a possible hassle between the partners as to whether it is within or outside the joint venture activity.

MR. KLASS: As part of the license agreement or as part of the Articles of Incorporation?

MR. NEY: I'm not sure you have to make a distinction.

MR. KLASS: Well, you do because in the license agreement I think we are giving technology in what we know. And if you want a broader field I might want a different sort of payment.

MR. NEY: In your license agreement there might be what you know and what you might acquire in the future relating to what you now know.

MR. KLASS: If you want that it's going to take a different price.

MR. NEY: I agree. What I'm trying to do is get at what might be a preferred mode, if there is such a thing, to avoid future hassles between the partners in determining whether something the technology contributor comes up with is in or out versus the kind of problem that might come up if you define it in a very generic manner. Is it preferred to say the products as identified by the "exhibits attached hereto" or do you say I'm going into a marriage and we're just going to have to work these problems out to avoid a divorce.

MR. KLASS: I put it a different way. If I'm going into a company as a joint venture partner, I want to do everything I can, assuming I can get reasonable compensation for it, to make the joint venture successful. That's my purpose in life. I'm on their side. I'm not fighting them. And once you do that, no matter where you draw the dividing line, you can always have a factual situation come up which is square in the middle, and you can't decide which way to go. I think if you look at it from the viewpoint of let's make this a successful operation and make our money that way, you shouldn't have too much trouble.

PROFESSOR OPPENHEIM: I take it that what Mr. Ney is talking about is a third party where you have a triangle and the third party is usually the government.

MR. NEY: No, what I'm talking about is primarily between the two

partners. I think that the problem I'm talking about is somewhat obviated if you don't have continuing royalty payments on technology, but rather, both parties are trying to make the joint venture go as well as possible. Then they are sharing only in the profits of the joint venture rather than having the problem, when part of the profit is siphoned off at the top, of determining whether something is within or outside the license agreement.

**MODERATOR WEISER:** We have had a new member join. Admiral Colclough has joined us. Lou would you do the necessary introductions, please?

**DIRECTOR HARRIS:** The Admiral has joined us for the purpose of presenting the Founders Day Award for Distinguished Government Service.

Admiral Colclough is the Director Emeritus of The PTC Research Institute and Chairman of the Institute's Advisory Council. He was formerly Dean of the Law School, Dean of Faculties, and Acting President of The George Washington University. The Admiral will act as host for the award presentation.

#### **O. S. COLCLOUGH**

Thank you, Lou. Ladies and Gentlemen. It is a privilege and also a pleasure to present the 1971 Founders Day Award for Distinguished Government Service. The recipient of this Award has recently retired as Examiner-in-Chief of the U. S. Patent Office, after 47 years of continued service. His career in the Patent Office included chairmanship of a committee which prepared the Rules of Practice of the U.S. Patent Office in Trademark Cases in preparation for the coming into force of the new Trademark Act of 1947; and chairmanship of a committee in 1948 to revise the Rules of Practice of the U.S. Patent Office in Patent Cases. He has been called upon to prepare patent legislation and appear before committees of Congress dealing with patents and trademarks. He served as technical advisor to the chairman of the Patent, Trademark, and Copyright Subcommittee of the Judiciary Committee of the House of Representatives in the preparation and passage of what we all recall, the Patent Act of 1952.

Mr. Federico has also worked at the Department of State in an advisory capacity in connection with treaties and other international matters in the field of patent and trademark law. In 1958 he was a member of the U.S. delegation at the famous conference, we all know about, in Lisbon which was gathered to revise the Convention for the protection of Industrial Property in a multilateral treaty. He has attended various international meetings on behalf of the Patent Office or the Department of State.

Mr. Federico is an author of note—from 1935 to 1941 he was the editor of the *Journal of the Patent Office Society*. His writings, particularly the Commentary on the 1952 Patent Act, appears in the *U. S. Code Annotated*, Title 35, and have frequently been cited by the courts. He has also contributed patent articles to the *Encyclopaedia Britannica* and has written on the inventions of Oliver Evans, the invention of the zipper, and on Eli Whitney's patent. He also has contributed several articles to professional mathematical journals.

Mr. Federico is now retired, but in name only, because he is a consultant to a prominent law firm, Cushman, Darby and Cushman of Washington. He is also a colleague of mine and a Professorial Lecturer in Law of The George Washington University from which he received a Master of Arts in Mathematics. He also has a Doctor of Jurisprudence degree from Washington College of Law of the American University.

Ladies and Gentlemen, this is a great privilege. May I quote from the certificate: "The PTC Research Institute of The George Washington University, The Founders Day Award for Distinguished Government Service, Pasquale J. Federico, in recognition of his outstanding contributions in the industrial-intellectual property field while in government service. Washington, District of Columbia, March 31, 1971." Lloyd H. Elliott, President of The George Washington University; L. James Harris, Director of The PTC Research Institute; and yours truly, Chairman of the Advisory Council. It is with warm sentiment that I present this to Pat Federico. (Applause)

MR. FEDERICO: All I can say is thank you and I appreciate this honor. On an occasion like this after all those things have been said it's pretty hard to try to make a speech, and I don't believe I could attempt one.

ADMIRAL COLCLOUGH: Thank you,

DIRECTOR HARRIS: Thank you, Admiral. Congratulations, Pat. This tribute is certainly well deserved. We will now adjourn temporarily to the Adams Rib on 21st and Pennsylvania. We lunch at 1:15 sharp and

we will return here between 2 and 2:15 and recommence the proceedings. Mr. Chairman, we stand temporarily adjourned.

### **Afternoon Session**

**DIRECTOR HARRIS:** Gentlemen, we will now resume the Clinic. Once again I must ask you to speak loudly and clearly and to identify yourselves. We don't want to interfere with your spontaneity but at the same time we want to be able to make as accurate a transcription from the tape as we can. Mr. Weiser.

**MODERATOR WEISER:** We want to welcome Mr. Timberg. We assume that everybody else will be here. In order to integrate the remarks a little further we thought that Sig would talk followed by Mr. Hilinski and that we would reserve our questions until both presentations have been made. Then we can go back to a general discussion of all these problems and solutions which have been raised, which are developing very nicely. I don't think Mr. Timberg needs any introduction. We have not introduced any other persons. Their qualifications are evident if not before their talk, then afterwards. Mr. Lauvauzelle is particularly well versed in taxation, EEC and French corporation laws, and Mr. Deringer is particularly well versed in EEC and German laws. So this roundtable is also representative of both sides of the Common Market. You will note that we have strategically placed them at both ends of the table. Bring up your questions relating to EEC law right after Mr. Hilinski has talked so we can get some answers.

**PROFESSOR OPPENHEIM:** I just want to say that I realize everyone here is well known and so is Betty Bock but I thought you gentlemen would want to know that Betty is the Director of Antitrust Research of the Conference Board. Betty puts on a fine annual antitrust symposium once a year in New York. Betty is one of this country's leading economists in the antitrust field. She is a genuine antitrust economist.

**MODERATOR WEISER:** I apologize. I knew that you could make this introduction much better than I could and that's why I left it for you. Sig would you like to go ahead?

SIGMUND TIMBERG

I am sorry I had to miss the morning deliberations of the group, which I understand was most forbearing, and had reserved the antitrust discussion for this afternoon. Whether this is something I will continue to be grateful for, the next hour or two will tell.

My assignment is to give an introduction to the development of the law of joint ventures. In doing this, I shall adopt the historical approach. In our preoccupation with the present status of joint ventures, we tend to forget that the joint venture has had a relatively long antitrust history. This history may be divided into three eras or periods.

There was a preliminary period, from 1939 to 1945, which may be called the "prehistoric gestation" period, when the Justice Department was preparing a large number of international cartel complaints. World War II effectively frustrated the trial of these cases. Hence, the facts concerning these cartels were set forth in lengthy legislative hearings held by Senators Kilgore, Bone and Truman.

With the end of the war, some of these cases began to see the light of day. I call this the "Sherman Act era"—roughly speaking from 1945 to 1952. During this period, joint ventures abroad with foreign firms were somewhat more dangerous antitrust-wise than joint ventures entered into in the United States; everyone knows there is something inherently evil about colluding with foreign competitors, that does not attach to U.S. competitors conspiring with each other.

During the Sherman Act period, joint ventures were considered legally more dangerous than mergers, and minority stock acquisitions were considered more risky antitrust-wise than outright acquisitions of 100 percent or the major part of the stock of a company. This era was also one of relative simplicity. There was only one national antitrust law to apply, which was the Sherman Act. Antitrust in other countries was either non-existent or non-operative as far as U. S. companies were concerned.

Between 1945 and 1952, it was established that joint ventures were not per se illegal, but they were held illegal in several types of situations. First, they were illegal if they were used as a method of allocating or dividing world territories and markets. Thus, the world aluminum cartel in the *Alcoa* case was implemented by the Alliance, a Swiss corporation owned by the aluminum companies, that allocated quotas and fixed prices. In the *ICI-DuPont* case, Judge Ryan held illegal and

dissolved selling subsidiaries in Canada, Argentina and Brazil that were owned 50-50 by ICI and DuPont. In the *Flat Glass* case, an interesting case that was settled by consent, there was a Brazilian manufacturing subsidiary jointly owned by Pittsburgh Plate Glass and Brazilian interests.

During the same Sherman Act period, joint venture arrangements were also held illegal if they had the effect of restricting exports from the United States. The most interesting case in this respect is the *Minnesota Mining* case, decided by Judge Wyzanski, involving jointly owned subsidiaries for the manufacture of abrasives established by U.S. firms in Holland and some other European countries. It was a not surprising consequence of setting up these manufacturing subsidiaries abroad that exports of abrasives from United States declined—the exports were offset by the new production in the Common Market. The court held that the defendants had violated the law in establishing joint ventures that had this effect.

Another kind of joint venture that received critical attention at that time was the Webb-Pomerene Export Association, which is a joint venture in the historical, common law sense of the term. The Webb-Pomerene Act of 1918 had immunized from antitrust prosecution associations set up for the purpose of engaging in export trade with foreign countries; such associations were authorized, as an incident of the joint venture, to allocate quotas and fix prices on export sales. However, in 1949, Judge Kaufman, in the *Alkali* case, gave these Webb-Pomerene Associations a setback from which they never recovered. He held that these American export cartels (the terminology is provocative but not unfair) could not participate in international cartels—could not form arrangements with the businesses of other countries to divide world markets. There are many other implications of the *Alkali* case into which I have no time to enter. I note only that, at the present time, the shoe is on the other foot and that Webb-Pomerene Associations, to the extent that they fix or influence prices in Sweden or in Germany, may conceivably violate the antitrust laws of Sweden, Western Germany or the Common Market.

A third kind of purpose or effect that might result in having a joint venture declared illegal is that of restricting imports into the United States. Cases were brought in the Sherman Act era against joint selling agencies—common distributorships on the part of the American importers of foreign products—which had the effect of fixing prices and allocating markets within the United States. The best known of these cases was the *General Dyestuffs* case, decided by Judge Rifkind.

There also arose during this period special problems with respect to joint ventures in the mining and extractive industries, which were mainly located in the developing countries. The most widely publicized of these were production-sharing and joint pipeline arrangements among the major international oil companies. It became recognized that, in the case of extractive industries doing business in Africa and the Far East and South America, there existed special political considerations, such as the instability of the local regime and the fact that areas such as Saudi Arabia and Kuwait were run on rather primitive, feudal lines. There also existed special economic considerations, such as the risk that political upheaval might make the investment go sour, and the tremendous size of the investment. Building a large-scale pipeline is no mean commitment of financial resources. Accordingly, for both political and economic reasons, this kind of joint venture was considered within the rule of reason and was not attacked in litigation.

May I remind you that joint ventures were in fact involved in other cases that one does not ordinarily think of as joint venture cases. Thus, the world-wide allocation of territories in the *Timken* case was sought, unsuccessfully, to be justified on the basis that it was reasonably ancillary to a joint venture. Also in the *General Electric Lamp* case, along with the international cartel there existed specific joint ventures linking General Electric with the leading lamp companies of different countries of the world. (This particular cartel, well named the Phoebus cartel, has been described in cases brought in the United Kingdom, Canada and Sweden, as well as the United States). The *National Lead* case involved joint ventures with competitors, which the court ordered terminated. These joint ventures were not of the classical type, because the U. S. parent had only a minority stock ownership and the foreign parent usually retained management control of the enterprise. Nevertheless, this kind of jointly owned subsidiary cannot be ignored, because it shares, perhaps in aggravated form, the antitrust problems of joint ventures.

So much for the initial Sherman Act period, when U. S. foreign business had only the simplistic language of the Sherman Act with which to contend. From about 1945 to 1963 there was a second period (you will note a certain temporal overlapping with the first era) that I call the "era of cultural diffusion." This was a time when massive foreign investments were made by U. S. companies. According to some 1965 figures supplied by then F.T.C. Chairman Rand Dixon, in the Common Market alone U. S. firms had formed 568 joint ventures and made 530 acquisitions. The 50 largest U. S. firms had formed 82 joint

ventures and made 93 acquisitions. This was also a period when the State Department's foreign economic policy continued to favor the liberalization of foreign trade and promoted the adoption of antitrust laws abroad. It is this diffusion of American competitive mores—both from the standpoint of business philosophy and government policy—that I refer to as cultural diffusion.

This cultural diffusion had its origin in Germany and Japan in the military occupation de-cartelization and de-concentration laws. The European Coal and Steel Community was founded in 1953 and the European Economic Community was established in 1957, both of them governed by treaty provisions directed against restrictive business practices. The German Law against Restraints of Competition was finally passed in 1957. The third major and most effective revision of the British antitrust law took place in 1956. France, the Scandinavian countries and the Netherlands adopted new legislation designed to curb restrictive business practices.

Despite this spate of antitrust laws, there was a lack of interest in proceeding against mergers, monopolies and concentrations. Article 65 and 66 of the European Coal and Steel Community Treaty required official approval for mergers and acquisitions, and the German anti-trust law imposed reporting requirements on mergers involving more than 20 percent of an industry, but these had no real significance. Article 86 of the Rome Common Market Treaty contains a provision with respect to abuse of dominant power, but this has only recently been for the first time sought to be applied to various acquisitions made by Continental Can.

The massive acquisitions and joint ventures by U. S. firms abroad had political implications and touched off public protest. Through acquisitions, a single U. S. firm, IBM, acquired control of 85 percent of the West German computer market, 87 percent of the French market and 60 percent of the U.K. market. Understandably, there was quite a burst of indignation in the British press—a cultural backlash if you will—when there were reports that the Department of Justice was investigating the acquisition by Sotheby of Parke-Bernet, the leading U. S. art auction house.

During the era of cultural diffusion the Common Market authorities had occasion to realign some selling agencies or syndicates. But to my knowledge, as of the present, there have not been any guidelines in the area of joint ventures generally, and one must therefore speculate from general principles. My good friend Arved Deringer can give you sounder surmises than I about how the Common Market antitrust provisions will be applied to joint ventures.



Finally came what I call the "Clayton Act age," which I date from 1964 and which is still continuing. This era had its roots in the Celler-Kefauver Act of 1950. This Act was a slow starter, but it did produce two novel developments. One of these was that Section 7 of the Clayton Act was applied to joint ventures. In 1964, the *Penn-Olin* case held that a joint venture with no prior operation "in commerce," formed by parent corporations not in the "line of commerce" of the joint venture, could nevertheless violate Section 7 of the Clayton Act if it had the probable effect of substantially lessening competition. About the same time as *Penn-Olin* was decided, a joint venture for the production of isocyanates (preparatory materials for foams) involving Monsanto and Bayer—the so-called Mobay joint venture—was dissolved pursuant to a consent judgment. This case involved a German firm coming into the United States as co-venturer with an American firm. When the joint venture was dissolved, Bayer bought out Monsanto's interest. Somewhat later, when Phillips Petroleum was attacked by the Federal Trade Commission because of its relationships with National Distillers in the petrochemical field, the case was settled by a consent order terminating not only domestic but also two foreign joint ventures involving National Distillers.

The other novel development in the Clayton Act age, which found its earliest expression in the *El Paso* case decided by the Supreme Court in 1964, was that Section 7 of the Clayton Act applied to potential competitors. In the *El Paso* case, involving an acquisition in the natural gas industry, Northwest was not doing business in the California territory, which was why it sought to acquire El Paso. It had neither financial support there, nor gas supply customers, nor regulatory agency approval to do business.

The practical nub of the potential competition doctrine is that any firm which has a large-scale technological potential and strong financial resources, and has a group of eager scientists anxious to develop new areas for expansion, may very well be tagged as potential competitor in those new areas. The theory is that such a firm might enter the new area unilaterally, either by a process of interest expansion or through a "toe-hold" acquisition of a relatively minor firm in the field. Where an acquisition or joint merger cuts off the possibility of entry by such a potential competitor, Section 7 may be violated.

Since the case law is so recent—1964 is only seven years ago—the concept of potential competition is still a difficult one to master. An interesting relevant case was the contemplated acquisition, by Standard Oil of New Jersey, of Potash Corporation of America, which was blocked by the District Court of New Jersey in 1966. Standard Oil of

New Jersey was not an actual producer of potash in the United States, but it had many foreign fertilizer plants, its affiliates had evidenced interest in acquiring potash deposits in the United States and in many foreign countries, and its engineers had recommended exploring for potash and phosphates abroad. Accordingly, said the court, it had vast resources, a highly competent management, great technical skills and a lively unilateral interest in entering into the potash field. Also relevant to whether an acquisition or joint venture passes muster under Section 7 of the Clayton Act, the court pointed out that there were strong barriers to new entry into the potash field, rendering still more important the preservation of potential competition.

Since acquisitions and joint ventures raise common problems under Section 7 of the Clayton Act, I will briefly refer to a few foreign acquisitions that have hit the courts. Schlitz, the famous Milwaukee-based brewer, was found guilty of violating Section 7 of the Clayton Act because it acquired 39 percent of the stock of Labatt, which was the third largest Canadian brewer. Labatt held 63½ percent of the stock of General Brewing, second largest brewer in the California and Western Pacific market and the fourteenth largest in the U.S. as a whole. If one looks closely at the court's findings of fact, there were some small imports by Labatt into the United States, but Labatt (except for its holding in General Brewing) would have to be regarded on the whole as a potential competitor. Incidentally, there were allegations of potential competition in the *Mobay* case, but there was also definite proof of actual competition.

One other important case is still in the complaint and pre-trial discovery stage. This is the *Gillette-Braun* case, where Gillette, the largest U. S. producer of safety razors and blades, acquired Braun, the third largest German producer of electric razors. Braun was not an actual competitor in the U. S. market, from which it was foreclosed by a 1954 exclusive licensing and distribution agreement, with Ronson preventing it from marketing electric razors in the U. S. until 1976.

There was involved in this case another area of potential competition; by and large the people in the "wet" shaving field (e.g., Gillette) are not in the "dry" shaving field (e.g., Braun), and vice versa. If these two fields constitute part of a larger razor market, another element of potential competition was allegedly eliminated. Also, Braun had a joint venture with Ronson—a research and development company involving improvements on the Braun-type electric razor. Hence, the Justice Department further alleged that, by Gillette's acquiring Braun's rights and obligations in this venture, it actually eliminated both actual

and potential competition between Gillette and Braun. This despite the fact that Ronson had only 5 percent of the U.S. market in electric razors.

If there are only a few cases attacking foreign acquisitions and joint ventures, it is not because the legislative committees on Capitol Hill have not been interested. Senator Hart's Antitrust and Monopoly Subcommittee in particular has been prodding the Antitrust Division to bring more cases in this area. The main reason given by the Division for not bringing more cases against U. S. acquisitions or joint ventures abroad is the difficulty of establishing the requisite adverse effect on U. S. commerce. One can well see that, if effect on U. S. commerce means effect on U. S. imports and exports, this creates a substantial burden of proof for the government.

There are also jurisdictional problems involved in applying Section 7 of the Clayton Act. Recently the Justice Department entered a decree involving a merger of CIBA and GEIGY, two Swiss corporations, but this was because their U. S. distribution subsidiaries were direct competitors on the American domestic scene.

A final word on the business motivations underlying joint ventures these days. These, of course, include the desire to employ capital resources abroad that U.S. companies do not want to be forced to repatriate, or earnings abroad that they do not want to have subject to U. S. taxation, or the fact that surplus funds in the United States find more productive investment opportunities abroad. But in addition to these factors, the wave of foreign acquisitions and mergers has a profound technological base. More often than not, the U.S. contribution has not only been that of financial capital, but the making available of vital and cost-saving patented and unpatented technology. Another major contribution, extolled by Servan-Schreiber in his book *The American Challenge*, is American management experience. This last factor has brought with it a desire for American control of joint ventures that run smack into certain European sensitivities and raises the political problems to which I have already referred.

Since the purpose of my talk was to start the discussion going, I hope I have given you some materials that will provoke such a discussion.

MODERATOR WEISER: Thank you Sig. We started out this morning by talking about management experience when Mr. Klass gave his presentation, and your final words here tie in beautifully because you end up

on the same note. It provides an excellent backdrop for the question which I know will be forthcoming. The same question relates the movement of capital, the change in the organization of joint ventures, and the flow of know-how; this is going to raise so many tax implications that we thought that in order to have a general discussion and not to interrupt it, we would move right into your comments, Mr. Hilinski, on tax implications. Then we will open up the floor. With that good introduction—why don't you go ahead?

**CHESTER C. HILINSKI**

I think it is most appropriate that the topic of taxation be the last topic under discussion. As we heard in earlier discussions, the most important first step is to make sure that you have the right party in your joint venture because without having made that very thorough investigation and being assured that you do have the right party, the rest of the road can be very, very rocky indeed. Now, in the negotiations with that joint venturer I'm afraid I do have to tell you that tax laws and considerations do require some molding of the transactions that might be involved. I think it is better, therefore, that the negotiations at the outset have some of these in mind rather than having the negotiations go forward entirely on the business considerations and then presenting the judgments on those business problems to see if there are any tax problems. Unless the negotiating parties are quite knowledgeable about taxes in both of the countries, the transaction very often may have to be restructured and might make the continuation of the joint venture a little more difficult than it would have been if these things had all been worked out in the first instance with these considerations in mind.

We had several questions this morning as to whether there were joint ventures where more than two parties were involved, and I think at this point I can safely say that you always have joint ventures with more than two parties because the governments of both joint ventures are very much a party to the profits, and in the way they influence the negotiations by the various laws that they have. You can, of course, have more than two parties to a joint venture although this is more common

in a mineral project than a commercial project.

When we talk about a United States business corporation involved in foreign operations and the acquisition by that corporation of an interest in a joint venture, you really have two primary United States tax law concepts that you should bear in mind. The first is, and this is a general concept throughout the tax law applying to both domestic transactions and foreign transactions, that gain or loss is not necessarily recognized on the transfer of property. Property is the important word here if that property is transferred to a corporation in exchange for the latter's stock where the corporation receiving the property is controlled by those who are transferring the property.

An example of this is if one transfers machinery, the other transfers say an industrial asset such as a patent or trademark, and they wind up in control of the receiver of those two items of property, gain or loss is not recognized. There is a second concept that is very important in your foreign field. It does not apply in the domestic field. In the foreign field where you have an incorporation or a liquidation or a reorganization—whether that reorganization is a combination such as a merger or a division such as a spin-off of part of the assets of a corporation—and that incorporation, liquidation or reorganization involved a foreign corporation, you must secure a ruling in advance from our Internal Revenue Service, that the exchange of property does not have as one of its principal purposes the avoidance of federal income tax. This is a ruling that has to be received before you transfer any property. If for some reason you have to transfer property without securing such an advance ruling, the result is that if there is any difference between the tax cost basis of this property and its fair market value in the sense that the market value is higher than your tax cost basis, that gain is recognized as a taxable gain and the transaction is a taxable transaction. On the other hand, if for some reason you transfer property which has a lower market value than the tax base, you do not get a loss whether you get an advance ruling or not, so this is just a one-way street as far as the Federal Government is concerned.

I might point out very briefly that this section is an old section of the law. It goes back to 1932. You can always recognize an old section of the Internal Revenue Code because it is relatively short. This one is just one paragraph, one sentence really about seven or eight lines long. It was a fairly dormant section until this wave of interest in international business started and our Federal Government became aware of some of the problems that might be developing as far as United States taxation and possible avoidance of United States taxation was concerned. This

section suddenly became quite active in the early 60's just as did the entire Revenue Service in this area as witness the passage and the implementation of the Revenue Act of 1962. It has had an expanded use ever since then and the interesting part is that this old section which really didn't have that much of an impact in years before, is being used in ingenious ways and being expanded almost day by day you might say. The most recent example is that in 1970 the Service has suggested that where you have a wholly owned Mexican subsidiary which you can include in a consolidated return for United States purposes, you have to have a ruling under this Section before you do so or you have a possible taxable transaction.

What sort of properties do you have to worry about? If you transfer cash you have no problem because there is no difference in the basis of cash so you do not need any advance ruling if all you are transferring is cash to this foreign corporation. If you have property other than cash there are fairly elaborate guidelines that have been issued by Internal Revenue Service in the last several years and the general proposition is that if property is transferred to the foreign corporation, it has to be used in the active conduct of a trade or business in the foreign country. You can ordinarily get a ruling that this does not have avoidance of federal income taxes as a principal purpose. However, there are certain limitations in certain areas where the result is negative and that covers items such as inventory items, accounts receivable, and property which we know the foreign corporation intends to sell promptly. If you have transfers of that type of property you are required to include their value in taxable income on the transfer. If you have a mixture of machinery and equipment where you can get a ruling that there is no tax consequence and a transfer of inventory at the same time, you can get a ruling that the machinery is perfectly alright but you do have to pick up the income from the inventory transfer.

I think you also have to bear one other fact in mind. When you transfer an entire business, for example, you would think that you really don't have any gain from the tax standpoint because you have some assets which have a gain and some assets which have a loss and they just about balance out. You would think that when you transfer that whole package of assets, there shouldn't be any gain for U. S. purposes. That just isn't so because the government says you do have to recognize the gain portion and you do not get the benefit of the losses that might be involved. So again it's a one-way street. I think we ought not to take any time talking about licensing as such because from a tax standpoint the results are clear that if you license a foreign corporation

and get royalties back you have taxable income in the U. S. You have a deduction in the foreign country unless you exceeded their limitations on amounts, and I think that is pretty much the end of it for tax purposes, with the foreign tax credits possibly helping you with your overall tax liabilities.

What we are primarily interested in is the transfer of know-how or technical property, because in many ways this has been the problem area where you have joint ventures being set up and the two parties transferring different types of assets with the U. S. partner transferring the technology or the know-how to the foreign operation. I might say that the Internal Revenue Service does not like the word know-how. It is much too broad for the Service and they have now coined a word "information" which they ascribe to know-how. I don't know that that advances things any further because they still have to fit in what is information.

What is property from the standpoint of that first concept we talked about? If you have patents or trademarks, that's clearly property. If you have services that are involved or promises of services, that's clearly not. In between you have the areas of secret processes, formulas, technical data, and generally the rule is that if you have a secret process or formula or any other secret information as to a device or process which is in the general nature of a patentable invention without regard to whether there has been a patent issued or not, or an application for a patent, you should be able to get a ruling that this is a property transfer. Therefore if you get your ruling in advance of the transfer of property, you can transfer that property to a foreign corporation and form a joint venture and get stock in return without having an immediate tax consequence on the disparity between the tax basis of your property and the present fair market value. We have had the benefit of clarifying rulings and procedures by the Internal Revenue Service in this area. I might say too very quickly that if the information is recorded on paper, that does not necessarily indicate the information is property in any final sense of the word.

What the Revenue Service is looking for primarily when it considers your application for ruling is whether the transferee country affords substantial legal protection against the unauthorized disclosure and use of that process, formula or other secret information that is involved. This is really not a very easy question to address yourself to. In the U. S. where we think there is substantial protection, you nevertheless very often find cases where processes move from one company to another through employee transfers and it is sometimes very difficult to

protect against that movement. To be able to say to our Internal Revenue Service that a particular country in Europe or South America does afford substantial legal protection is sometimes very difficult to do. If you transfer all of your substantial rights in a particular industrial asset, a particular process or secret formula, and the transfer pertains to all of the territory of one or more foreign countries, you can have a transfer of a property right that qualifies for a tax-free exchange. In the words of the Service, what you have to do is to have an unqualified transfer in perpetuity of the exclusive right to use a secret process or other similar secret information which qualifies as property within all the territory of a country, or the unqualified transfer in perpetuity of the exclusive right to make, use, and sell an unpatented or secret product within all the territory of the country. That's treated as a transfer of all the substantial rights and property in that particular country or territory.

There are various problems that can come up and I don't know that ingenuity has exhausted all the problems by a long shot. Recently we had a situation where the rules and procedures had not been worked out whereby you could get a ruling in advance that what you were transferring was property, and I'll come to that later because that has only come about as a development in the recent past. Many companies had to go in and ask for a ruling to the effect that the particular foreign corporation, the joint venture that was involved, was not formed for the principle purpose of avoiding federal income taxes and leave to later determination whether what was transferred in the way of the secret process or formula was property within the terms of the United States tax law. I think the experience Felix mentioned at lunch today—his company had the experience of having had to do this because there was an inability to get the second portion of the ruling that property was involved—that these transactions have now been coming to the level where the auditing agents are examining them and the exaction of tax has not been very great at least in his experience. It hasn't been very great in the cases we have had in the office either.

Suppose you do have such a transfer and the United States company retains the right to sell the product for some reason or another which the patent or process produces, in the foreign country, or just doesn't expressly prohibit by the transfer agreement or isn't expressly prohibited by the transfer agreement from selling the product in the country. In one situation the Internal Revenue Service tried to argue that all the substantial rights had not been transferred, that there had been a hold-back. They gave up eventually but this is the kind of case you can get into. Again, suppose your U. S. company grants a non-exclusive



license so that it deliberately avoids the problem of transferring substantially all the rights. One of the men in the I.R.S. National Office that is in the International Ruling Section suggested that even there the Internal Revenue Service might find that the license is in fact one in perpetuity and that although it is labeled non-exclusive, no one else has the right, and therefore the Service may argue that the transfer of property did take place. So since an advance ruling wasn't secured because no one thought it was necessary in the first place, you've got a taxable transaction. I think that is pretty far-fetched but you can see how the Service is fiddling around with the concepts we have here. They won't, I know, rule on an agreement providing for future know-how. What they are talking about is know-how that is in being today; they will rule on a transfer of that but not as far as the future is concerned.

The Revenue Procedure that has made it all possible to get rulings in advance on transfers of know-how was one that came out in 1969. You have to make certain representations in your application to the Internal Revenue Service before a ruling will issue. They will accept for example that the information being transferred in exchange for stock is property within the meaning of our tax laws and as such is afforded substantial legal protection against unauthorized disclosure in the foreign country and that whatever ancillary services you might have in connection with that transfer, you exact a separate fee for that. They will take all that into account. But in making that representation you have to describe this information. You have to say that the information is secret in the sense that it is known only to the corporate owner and the confidential employees who use it in the conduct of the activities of the business; the adequate safeguards are taken within the U. S. by the owner against unauthorized disclosure; and that the information, while it may not necessarily be patentable, is original, unique and novel. These representations and statements must be based on certain criteria that the Internal Revenue Service has set forth. One is that the information is not revealed by patents nor the subject of patent applications, nor disclosed by the product with respect to which it is used or to which it is related, and that the information does not represent your knowledge or efficiency resulting from experience. It is not that kind of know-how that is involved. This information is not merely rights to tangible evidences of information such as blueprints and so forth. You have to really have something that is unique that is being transferred. Also, the information cannot have been developed for that particular transferee.

In that situation the Service takes a position that you are in effect

selling a service that you have rendered to that particular transferee rather than the property or an asset you have within your organization. It can't be in the form of assistance in the construction of a plant building or advice on a building layout. It is not that type of know-how, nor the training of employees, which is essentially educational in nature. They also want a representation that where you have new developments, you will be asking for compensation on an adequate basis with respect to those. With all those limitations which make your application for a ruling a little more complicated than one might think off-hand, you get to wonder whether these advance rulings are being issued.

I might go back just a little and say that when this wave of interest in international transactions first came about and the Service became interested in the concept of know-how, they put such a terrible roadblock in the rulings' operation of the Service that it was impossible to get a ruling in advance. Rulings just were not issued. Worse than that, when they initially did this they did it without any advance publication, and it meant that businessmen who had negotiated transactions and then asked their tax advisors or tax counsel to go to Washington and seek a ruling that this particular proposed transfer was possible on a tax-free basis under U. S. tax law, they were met with this concept which was identified in the Service as Attachment A having so many different facets you had to cover that people just backed away from it. It just wasn't possible to get a ruling at that time. I guess what the Service was doing really was buying time until it examined the various facets of transfer of know-how and finally came out with this Revenue Procedure in 1969.

Now rulings can be had. The time frame is roughly the same time frame that you have for any advance ruling where you have a foreign transaction involved. It is roughly about three months if you are relatively fortunate. Suppose you have a transaction which you negotiated and the time frame is such that you can't wait three months for a ruling. I guess there is a possibility that you might arrange an interim licensing set-up with the proposal that you will then transfer the know-how or the information, as the Service likes to call it, at a later date after an advanced ruling is secured. This is not as good as getting the advance ruling at the outset because the Service may force you to try to continue that licensing arrangement rather than to have a tax-free transfer of know-how because it still has a feeling that as far as the United States is concerned, the United States is better off if it gets licensing income directly from technology than if companies are

allowed to transfer that technology free of U. S. tax to a foreign organization.

I think it would not be well to stop with just the income tax aspects of the transfer itself and whether you can get a ruling on a transfer because there are various other parts of the tax law that have an impact. For one, where you have an organization set up overseas, you have to remember that you do have to file information returns with the Internal Revenue Service and disclose the transaction. You have to bear in mind the interest equalization tax, although that's not much of a problem since it applies only if you have less than 10 percent of an interest over there. If you have more than 10 percent you can forget the interest equalization tax law. But if you forget that you are right into the balance of payments problems of foreign direct investments office regulations, you have to square yourself there and make sure you are not over the limits.

The subpart F areas of the Internal Revenue Code and the so-called hidden profits distribution provisions which in our country are known as Section 482 have to be very much borne in mind because this is one area where the government might attempt to reallocate profits between affiliated or related corporations. I think they have a much more difficult time as we mentioned this morning where you've got a joint venture set-up than where you have a 100 percent owned subsidiary because by definition you have someone who is set up on an arm's length basis in the foreign country. I might mention that Dick Sperring's organization has won a very substantial case involving this particular Section and it is a landmark case in the Tax Court of the United States. We all very much hope it will stay that way if it is appealed. You also have to consider the tax treaties which the United States has with various countries. We have 30 such treaties in the income tax area and they have a very direct bearing on transfer of property, licensing arrangements, royalty payments, withholding and so forth.

You also have to be very much aware of what foreign law considerations there might be. We have found in several instances that it is a pretty good idea for the United States corporation or interest to have its own foreign counsel when it is getting into such transactions so it better understands from its own point of view what the foreign law complications might be. In Japan where you have a transfer of know-how you may find yourself being taxed on the basis of a lump sum royalty even though what you are getting is for U. S. purposes a transfer of stock. You of course have to have your validation by the Japanese agency of the technology licensing. Belgium may require an appraisal of the

property where you have a transfer of property for stock and that could involve considerable delays which would make the time frame all the more difficult. I'm sorry that Mr. Lauvauzelle seems to have left because France as a sophisticated and developed nation sometimes takes a very dim view of transfer of know-how if there is any possibility that the know-how is already available in some organization in France.

South and Central American countries as I mentioned earlier have remittance restrictions, monetary restrictions. They can very effectively limit what you can take out of their country after you have put your technology down there. And of course every country has its own tax structure. Sometimes, as we know, people start out with a 100 percent owned subsidiary and wind up with a joint venture because of the impact of local laws, such as in Mexico, and more recently in Peru, where you now have to set aside part of the corporate profits of your operation down there in a fund to permit the worker community to buy a substantial interest in that corporation. Suppose that happens, for example you may have had a licensing arrangement in addition to the transfer of know-how which calls for certain royalties in order to get some money out of the country, but you have kept that rather low because you wanted to build up the operation in South America at the lower level of taxation down there and now you find that involuntarily you have a partner in that operation. If you try to change those rates of returns you may very well have some serious U. S. tax consequences before it is all over. These things go back and forth between the countries at a great rate. I've covered it very quickly, Gerry, but I think we can develop anything further if there are questions in anyone's mind.

**MODERATOR WEISER:** Thank you, Chet. I think just to get the questions started, one question which was asked was how do you evaluate know-how regarding tax? Does that fit into one of your categories?

**MR. HILINSKI:** No, it really doesn't, Gerry, because I think valuation is strictly a business consideration. It is not a tax consideration. I think where you have rates of returns in the sense of royalties you can have a feeling as to what rates are acceptable in various countries because of prior experience, but where you have a transfer of a secret process or a formula then the one best able to value it is the person who owns it and the person who wants to buy it. You have a real give and take on that one before you come up with the valuation figure. I think from the

standpoint of United States authorities where you have a joint venture and you have someone with a very real interest in the foreign corporation that is involved in the valuation process, the United States government has really very little reason to question the valuation unless for some reason that valuation is deflated in order to permit some other distribution of profits in some other area. You might get into that strange situation, but that is most unlikely I would think.

MR. TIMBERG: I would like to ask a question just to put this matter in focus, and it is related to the element of valuation. Suppose you have an exclusive license of know-how for a royalty consideration based on the amount of sales. Suppose you have that license not only for France, but for eight other countries. Does the French license qualify for capital gains treatment as an exclusive grant with no further control vested in the grantor? Is it considered a complete transfer of the know-how?

MR. HILINSKI: It can qualify as a complete transfer of know-how, as the Service looks at it as a transfer of substantially all the rights in a particular property item. Whether it qualifies for a capital gain or not depends on the amount of control you might have. If you have this kind of a transfer to a wholly owned subsidiary it no longer qualifies as a capital gain. That is expressly stated and covered by the law to result in ordinary income. Now, if you have such a transfer and you own 50 percent or less of the foreign corporation, and the payments in effect are the purchase price spread out over the term of the particular patent and based on productivity, you can get into the capital gains situation there.

MR. TIMBERG: Getting back now to the cost basis—how can the value of something abroad be fixed which has been used only in the United States? How can value in terms of use in a foreign country be arrived at? Is it thought that all of the income a licensor obtains from all of his foreign licenses is an accretion to what we know it was worth in the U. S.?

MR. HILINSKI: Well, you are talking about different concepts I think, Sig. If you are talking about tax basis, ordinarily you have very little in the way of basis for this type of property because it is research expenditures that you have expensed over the years, so it isn't as if you went and bought something and have it here. Your cost to begin with is zero. Whatever you get is either income or capital gains and it is measured by that zero.

MR. TIMBERG: Than whatever you get on an exclusive totals out as capital gains.

**MODERATOR WEISER:** Mr. Whipple.

**MR. WHIPPLE:** My question is to Sig Timberg. Sig you pointed out very properly I think from '64 on we were in the Clayton Act area center stage. Have you ever tried to set up a joint venture so as to bring it within the investment exemption of Section 7 which provides—there are those of you who may not know this—that it doesn't apply to property which is used solely for investment. I wonder if in your experience you have ever tried to set up a foreign venture to come within that exemption?

**MR. TIMBERG:** No, I haven't because the joint ventures I have counselled for have involved manufacturing entities. I think it is uncharted ground how much the Clayton Act exemption for investment enables the parties to do. I have a strong feeling the government antitrust agencies will interpret any joint venture from the competitive rather than the investment angle. Therefore I have not recommended this approach to justify the joint ventures with which I have been connected, although I recognize the utility of such a justification should the joint venture be attacked in court. Second, from the standpoint of at least U. S. joint venturers, the one thing they stipulate for is management control over the enterprise, which is the antithesis of a passive investment interest. In fact, most U. S. firms have insisted upon an outright acquisition that gives them complete control over the enterprise. Even in the case of joint ventures, they stipulate for equal control—a stalemate situation. For these reasons, I have found it difficult to suggest much use of the investment paragraph of Section 7 of the Clayton Act.

**DIRECTOR HARRIS:** Isn't this different from your experience, Felix? In response to the question I asked this morning, the control element didn't seem important in your experience and the statement here by Sig is that control is quite important in these arrangements.

**MR. KLASS:** Well, I was distinguishing then between majority ownership of the equity and a position where in the last analysis you have an equal voice on the board of directors. So you don't have control but you have a voice. Control, as I indicated this morning, of the day-to-day running of the business I think has to reside in the people who are on the scene and doing the work on a day-to-day basis.

**PROFESSOR OPPENHEIM:** May I say that the real authority in the practice of American business is Dr. Bock here. I have read a publication of the National Industrial Conference Board that specifically talks about the extent to which American industry would want to control issues, the extent to which it recognizes the political reasons that it must at least share, and wouldn't you say that the majority of American

industry want to control at least the manufacturing, the financial operation of the foreign subsidiary?

BETTY BOCK: Well, that wasn't a statistical study but the findings there were clear, yes.

DIRECTOR HARRIS: Let us define control—what exactly do you mean by control? Is there a difference in what Felix is talking about and what you are talking about Sig?

MR. TIMBERG: I don't think so. From the standpoint of answering Tag Whipple's question I don't think it important to distinguish between different types of control. "Control" could of course mean that you have a majority vote of the board of directors; therefore, if there is a course of action that the majority wants to put through, it can legally override the minority stockholders. But, as the experience in the *Fruehauf* case in France indicates, minority directors also have a substantial amount of control. I don't know if you discussed that case this morning.

MODERATOR WEISER: Very briefly.

MR. TIMBERG: That case involved an American parent which transmitted a U. S. Government directive to its French subsidiary to stop a sale of equipment that the latter had made to Communist China. The French minority directors had enough "control" to resign from the company and get the French government to appoint an administrator for the enterprise. In corporation law a very small stock interest can be controlling. If you define control realistically as opposed to investment, rest assured that the governmental and private treble damage plaintiff will describe any kind of substantial influence as constituting control. Anyone here with experience in securities or corporate litigation will know exactly what I mean.

PROFESSOR OPPENHEIM: Sig, I think we can benefit greatly by your reactions to two points: First, I believe you rightly said that the opinion of Justice Clark in *Penn-Olin* sets forth in very elaborate fashion the criteria for Rule of Reason applications. In fact I think he outdid Justice Brandeis' enumerations in the *Board of Trade* case. So first I would like to know what you think about the advisability of considering those guidelines as just as applicable to the foreign commerce as to the domestic commerce joint venture: I'm inclined to think it is a proper approach to apply seriously the Rule of Reason enumeration of factors in *Penn-Olin* to foreign commerce as well as domestic. Do you agree with that, Sig?

MR. TIMBERG: I would say that the substantive criteria are the same. What is different is the degree of impact on U.S. commerce. And what I

believe is also different is a political factor that gets entwined into the Rule of Reason. Thus, when a foreign company forms a joint venture or makes an acquisition in the United States, it obtains what I might call a diplomatic plus—I doubt whether U.S. companies would be allowed to obtain an equally advantageous market position. This is because one of the public interest or Rule of Reason facts of life is that foreign competition on the U.S. scene is desirable and steps should be taken to encourage it.

**PROFESSOR OPPENHEIM:** The other connecting point that I'd like to get your comments on is this. Recently Dick Stern, Chief of the Patent Unit of the Antitrust Division, delivered a paper on international patent license limitations. I think he emphasizes a Rule of Reason approach to international patent license limitations but as I read the article—have you had an opportunity to read that?

**MR. TIMBERG:** I think so—he has written quite a few articles.

**PROFESSOR OPPENHEIM:** Well, anyway I can state the problem as I see it. I think that some members of the patent bar are somewhat disturbed by the article because they think that what he is talking about are antitrust considerations which should be sharply distinguished from considerations that apply under the public policy of the patent laws in this country and in the countries where corresponding patent rights are obtained. Do you find that to be so? It is important, isn't it to distinguish what we consider as antitrust criteria under a Rule of Reason in an antitrust context from patent license limitations within legitimate rights of exclusion of a patent owner, within the scope of the claims of the invention covered by the patent grant, and, of course, with proper attention to what the foreign law permits under the corresponding foreign patents that are obtained by the American company. I think that that is an important matter to have in mind.

**MR. TIMBERG:** Well, in the first place if we are talking Clayton Act the acquisition of patents is the acquisition of an asset and hence subject to Section 7 of that Act. If you are talking about misuse doctrine and are saying that the doctrine of patent misuse is not the same as the antitrust abuse of patents, I agree. The courts are becoming increasingly clear that there is a distinction, both evidence-wise and relief-wise, between patent misuse, on the one hand, and antitrust violation based on patent abuse, on the other hand.

To take another aspect of the problem, I would hardly expect a representative of the Antitrust Division, in enforcing the Sherman Act, to acknowledge any Rule of Reason other than the Sherman Act Rule of Reason. To the extent that the members of the patent bar are arguing for a special status for patents, they can do so, I believe, in the



area of patent misuse. But, if they want to prevail in the antitrust area, they are going to have to go to Congress. This is the reason, of course, why the patent bar supports the Scott Amendments.

I may also say that having read several speeches by Dick Stern and by other members of the Antitrust Division, I sense that, even within the Antitrust Division, there are somewhat different concepts of the Rule of Reason, and that, when it comes to specific cases, neither Assistant Attorney General McLaren nor his chief deputies share all of Dick Stern's views.

Finally, may I suggest that even the patent bar may be confused and slightly schizophrenic about the Rule of Reason. It has been reported that, over a period of years, 24 out of the 25 judicial innovative decisions charging the boundaries between patent rights and antitrust policy emerged from private patent proceedings and treble damage claims. When members of the patent bar file antitrust defenses and counterclaims in patent infringement proceedings, they necessarily adopt the antitrust Rule of Reason. So I would not build too much on the view that the patent bar follows a different Rule of Reason than the antitrust bar. If you are advocating a Sherman or Clayton Act claim, you do better to follow the Rule of Reason appropriate to those laws. If you are pressing or defending a patent misuse claim, you'd better look to the Patent Code to see what Rule of Reason it supports.

PROFESSOR OPPENHEIM: Well, I agree with you Sig thoroughly on that.

MR. TIMBERG: *Lear v. Adkins* does not impress me as a Rule of Reason decision, and yet the opinion was written by Judge Harlan in a private patent litigation.

PROFESSOR OPPENHEIM: I agree with you if you are talking about an antitrust Rule of Reason. The Department of Justice and a private party would then have to prove the plus elements of antitrust violation beyond the particular patent license limitation in question. For example, if the patentee is outside the bounds of his patent grant by requiring a tying clause which seeks to control unpatented subject matter, or other patented subject matter not within the scope of the claims of the patented invention, that is patent misuse and may also be an antitrust violation if the extra-patent restraint amounts to a violation of the Sherman Act or Section 3 of the Clayton Act. Likewise, after a first authorized sale by a licensee, the patentee cannot control the resale price or the persons to whom the article is resold. Combination or conspiracy would also be an extra-patent restraint subject to antitrust suits.

The 1926 *General Electric* decision of the Supreme Court is often

misunderstood. It sustained a first-sale price limitation in General Electric's license to Westinghouse to make and sell the patented GE lamps. It did not involve resale price control. Furthermore, the 1926 *GE* opinion formulated a standard governing the reward to which the patentee is entitled, namely, that he may exact any royalty for a license or condition the license by any performance within the reward to which the patentee is entitled by the grant to secure. The Court used "reasonably within the reward" language which I believe was only intended to exclude from the reward as "unreasonable" tying clauses, resale price control and restrictions on purchasers as I indicated earlier. Hence, a patentee is entitled to gain reward from the exclusivity inherent in his patent grant but he is not entitled to make a profit by the extra-patent controls stated earlier.

That is why I find it confusing to talk about a patent law Rule of Reason, since the patentee, who imposed a patent license limitation within the exclusive rights of his grant, does not have to justify the limitation by a Rule of Reason test. A Rule of Reason approach in antitrust law (except for the well settled illegal *per se* offenses) is an entirely different matter. As I said, there must be proof of plus antitrust elements beyond the lawful patent license limitation as such. Take the example of an exclusive patent license. No court has required the patentee to justify that by showing it is a reasonable provision. If the exclusive license is coupled with other conduct of an antitrust violation nature, then there would be a basis for charging patent misuse or antitrust violation. It seems to me we would be better off if we referred to the pecuniary reward standard of the 1926 *General Electric* case in those terms instead of confusing that standard with a Rule of Reason applicable only in antitrust violation cases, provided the burden of proving the plus antitrust elements is sustained.

MR. TIMBERG: That was exactly my point.

MODERATOR WEISER: I don't want to interrupt you—well, I do want to interrupt you because I thought I heard some question relating to misuse just that moment you started to talk about the Rule of Reason, Oppie, and how it applies. I thought there was a question here relating to misuse. Did I hear you correctly?

MR. DERINGER: Well, I wanted to ask a very general question in this discussion. My impression is no matter how you call this Rule of Reason, whether patent or antitrust rule of reason, my impression is that here in the United States as well as in Europe, the conflict between the general goals of the patent policy and the antitrust policy—the famous patent-antitrust dilemma as it is called in your trade cases—is

solved more and more in the direction of antitrust policy. This is my impression.

MR. TIMBERG: I share Oppie's feeling that it is ridiculous to speak of a patent Rule of Reason. I would say that the *General Electric* case, with its allowance of price-fixing and its emphasis on reward to the patentee, was the expression in 1926 of what the antitrust Rule of Reason then was in the area of patent licenses. I think that most of the experts nowadays will agree that price-fixing under a patent license is no longer within the antitrust Rule of Reason. Hence, I regard the criterion of reward to the patentee simply as one of the factors to be taken into account in the Rule of Reason, rather than what it was in 1926—an overriding consideration. Among the rewards a patentee still retains is the right to royalties, provided they are not burdensomely discriminatory. Certain other things which at one time were thought to be within the patentee's proper reward are no longer so considered. Thus, in 1912, the Supreme Court decided that a tie-in of unpatented materials was within the patentee's legitimate reward. Certainly this is no longer the rule from the standpoint either of antitrust or patent policy; in fact, most members of the patent bar would say that such a tie-in never was within the proper reward of the patentee, and that the Supreme Court decision of 1912 was a mistake. But I believe one has to agree with Mr. Deringer that so far all the victories have been on the side of antitrust.

PROFESSOR OPPENHEIM: May I qualify that statement? If one is talking about what happened in the patent-antitrust spectrum during the 1940's when Thurman Arnold brought a series of patent-antitrust cases which I think really benefited the patent system, then one is referring to antitrust abuse of patent rights. I think the patent bar should pay respects to Arnold for having rooted out genuine cartel abuses. In other words, as he said at the time, antitrust law is an anticartel law. Those are antitrust cases on which I think no knowledgeable patent attorney should disagree. Antitrust supremacy results only in the sense that when the antitrust issues are properly raised and proved, antitrust does prevail. But when you look at the corpus of the law of patent license limitations—and I'm talking about Supreme Court and lower federal court cases, then I would suggest that we have to qualify what was said by the generalization that the picture looks pretty good for the patentee. In other words, the Supreme Court has sustained an assignment grant-back in the *Transparent-Wrap* case, and field-of-use limitations in *General Talking Pictures*.

Recently I Shepardized these cases through 1971. All of the cases

since *Transparent-Wrap* (with perhaps one exception) have applied the *Transparent-Wrap* full force, whether there was an assignment grant-back, an exclusive license grant-back or a non-exclusive license grant-back. All of the cases since *General Talking Pictures* also reaffirm the right of the patentee to carve out a field of use. And some of the statements in them are really gems compared to what you hear today. For example, there are statements in the court opinions that, of course, the nature of the patent grant is exclusivity and the patentee has the right to exclude all competition when he acts unilaterally, and he can unilaterally also refuse to license. So it seems to me where the confusion begins is in failing sharply to distinguish what we consider to be rights of exclusion inherent in the patent grant and conduct outside the grant.

In 1957 a House Subcommittee released a report on Antitrust Problems in the Exploitation of Patents. You read that and it is entirely different from what you hear today from the top officials in the Antitrust Division who are trying either to overrule or cut down drastically the *Transparent-Wrap* decision or the *General Talking Pictures* decision on field-of-use restrictions. In other words, it shows that the climate of thinking in the Antitrust Division has changed radically regarding patent license limitations. In previous years, the Antitrust Division did not question patent license limitations ancillary to the rights of exclusion inherent in the patent grant where there was no element of conspiracy, or any other plus antitrust violation.

MODERATOR WEISER: Chet, you had a question?

MR. HILINSKI: Gerry, yes, there was a question here this morning relating to a comment that was made that the development in the Common Market in this area seemed to be moving forward at a pace which may cause more serious problems in the antitrust concept in Europe than will be true as far as the United States is concerned. I don't think it was answered; I think it was saved for this afternoon.

MR. TIMBERG: I think that is a bit of an overstatement, but I think there is someone who is much more down on the scene—

MODERATOR WEISER: We will give Mr. Deringer a chance to answer too because he was asked to hold off.

MR. TIMBERG: Well, perhaps he would like to make the first statement.

MR. DERINGER: I would not agree with this statement in general. Generally it is true that the antitrust authorities in Berne and Brussels try hard to keep up with your development and send people over to learn, and they learn quickly. But in general I would not agree that the situation either in the EEC or in Germany is more difficult than here.

However, there may be special situations where the law of either one country or of the EEC might be stricter than your laws. I mention for instance a law of resale price maintenance which is of course stricter in France. It is not prohibited in Germany, it is still legal but it will be dying in the near future because you cannot protect a German resale price maintenance against the import from other countries according to the EEC. Or it may be that in the field of the patent licensing the beginning policy of the EEC and the European Court may be stricter than here, but this is just at the beginning, so I wouldn't give a statement on that now.

**MODERATOR WEISER:** You may want to comment on the trademark aspect?

**MR. DERINGER:** This is not in answer to this question, but I can make a general remark.

**MR. WHIPPLE:** Before Mr. Deringer swings over to trademarks, would you amplify your comment if I heard you correctly that the Christmas '62 policy statement is over?

**MR. DERINGER:** May I include this in my general remark about patents and trademarks. I would say that with regard to patents, trademarks, and copyrights there are two developments in the Common Market. They both affect joint ventures. One development is a consequence of the fact that you still have national patents, national trademarks, and national copyrights. And so until today it was by far the prevailing theory that you could by means of one patent or one trademark in one country restrict or prohibit the import from the other country although it was in the Common Market. These are different national patents. This is one answer to your question.

This Christmas policy statement said your idea of everything that is within the scope of the patent is legal. The scope of a French patent is, of course, to prohibit the import of anything that had been produced under the German or Italian patent. However, this is in my opinion still true as far as patents are concerned. I think this has even been backed up by the European Court in the *Parke, Davis* case although it is challenged by the EEC Commission, and some of the officials interpret this case as something other than I do. But it is probably no more true after the *Sirena* case with regard to trademarks. There we had the situation where an American company 30 years ago had trademark Prep in all European countries and assigned it or licensed it to others. This trademark in Italy belonged to Sirena, in Germany to somebody else, in France to somebody and so on. Then the trademark was registered in Italy on its own name because the American company had lost

its rights by not paying the fee. In '67 and '68 imports from Germany under the same trademark by the German producer who was either licensee, or maybe an owner too, I don't know, came to Italy where suit was brought by Sirena and the case went to Luxembourg. The court in Luxembourg said the mere fact that by parallel trademarks within the Common Market, the import from one country to another country may be prohibited is a restriction of competition that affects interstate commerce.

Therefore these situations probably will be legal only if—and that's a very ambiguous wording—the parties take into consideration the general goals of the Common Market protected by Article 86. The EEC Commission interprets this decision—just to give you an example—if one company has trademarks all over the Common Market and sells its subsidiary in Italy to somebody else, including the trademark, then you have to oblige the buyer not to use it to prohibit the imports from Germany, coming from your other subsidiary, meaning now after the sale from an absolutely independent owner. I confess the interpretation of this decision is still under discussion. It is not even published yet, and I studied only the French translation. When I go back I will study all the other ones to compare them. But I would say this is a general development. From the political point of view it's O. K. that property rights should not be used to divide the Common Market into two different territories. This is a development politically O.K., but legally, in my opinion, a development that should be done by the legislature, by the parliaments, by the Council of Ministers which is already prepared in the patent convention and the trademark convention. But here the European Court seems to promote political integration by jurisprudence, as an American professor called it.

MR. TIMBERG: I want to record that in certain areas the Europeans have a stronger enforcement of antitrust than we do. Both France and Sweden have strong laws against resale price maintenance, from which administrative exceptions are rarely granted. Another area where European antitrust policy has always been stronger than the U.S. law is that of patent non-use. Under the U.S. law, the cases indicate that except in monopoly or public interest situations, it is a patentee's right to sit on his patent. But in all other industrial (and many non-industrial) countries, there are statutes providing for the compulsory use or working of unworked patents.

MODERATOR WEISER: There is a third aspect: the concept of notification under EEC antitrust rules which is something in a sense stricter—in terms of private liabilities that flow from failure to comply with these non-mandatory notification provisions.

MR. TIMBERG: May I say that you can never tell when a foreign jurisdiction's concept of public interest may be asserted against a trade restriction. For example, years ago a decision by the French Conseil d'Etat prohibited field-of-use restrictions in a patent license relating to magnesium, a product which had a high military potential at the time. Field-of-use restrictions are one area where the Department of Justice is one jump ahead of the decided cases, and is trying to change established legal doctrine. Also, the Department is still looking for the case which will put the final quietus on the 1926 *General Electric* holding permitting a licensor to fix its licensee's sales prices. The Department's program or pending complaints are not the law, but they are significant for those of us who are trying to avoid trouble for our clients. In fulfilling our function, we appraise not only the correctness of the Department's program, but whether the Department's views will prevail. Hence, we must advise our clients not only about the legal precedents and their right to litigate controversial issues, but the risks they run in litigating such issues. That is where the practical problems of the antitrust adviser lie, not in any theoretical scheduling of antitrust or patent Rules of Reason. We have to take a far look ahead, and evaluate our chances of convincing a Supreme Court (which has not shown itself as being overly pro-patent) that the Justice Department is wrong.

Getting back to the European scene—you may recall that the *Schwinn* decision—which held that a manufacturer could not tell its distributors and dealers the territory in which or the customers to whom they could resell—took U.S. industry by surprise. Yet the same decision was reached a year earlier by the European Court of Justice in the *Consten-Grundig* case. In this case, the Court of Justice adopted a per se approach, in the face of the fact that its Advocate General, relying on U.S. precedents, had argued against this approach and told the Court of Justice to follow the Rule of Reason.

I think that the lessons to be drawn from the *Sirena* case are exactly what Mr. Deringer has said they were. With respect to *Parke, Davis*, no one can say with assurance what its implications are for the future. I feel particularly ill at ease when I report a view that may not correspond to that held by Mr. Deringer. One important factor in the *Parke, Davis* case is that the drug, which was imported from Italy into Holland, was not patented in Italy because Italian patent law does not allow product patents on drugs. Hence, Holland was the first country in which the drug was sold where it could be patented. There have been those who have questioned what would have happened had the drug been imported from Germany, where it would have been patented.

Here one would be faced with the question whether restrictions can be imposed on the resale of a patented product. This has long been answered in the negative in the United States.

As to *Sirena*, I recognize the validity of the argument that Article 36 of the Rome Treaty indicates an intention to preserve intellectual property rights. Also the European Court may have been legislating, but it is the kind of judicial legislation to which we are accustomed in the United States, as witness *Lear v. Adkins* and *Painton v. Bourns*.

MODERATOR WEISER: The discussion today would be incomplete if we did not mention the *Continental Can* case which is a merger case and of course involves joint ventures.

MR. DERINGER: I would like to make a more general statement about this development in Germany as well as in the Common Market. Until now for joint ventures and any cases of mergers and acquisitions in Europe, all we had under Articles 85, 86 was the problem of avoiding restrictive agreements under 85. So under some joint venture where it was necessary to have full control—not in the broad sense you were determining—but real control, it was a normal device to have a majority interest. This line is now attacked by the fact that the German law will be amended in the next months introducing a provision saying that any merger creating or increasing a monopoly position, a dominant position, will be illegal. In the *Continental Can* case the Commission has tried to interpret Article 86—which only prohibits the misuse of the dominant position—to interpret it in a new concept of monopolizing by saying that Continental Can already had a dominant position after acquiring a German company—60 to 70 percent of the Common Market—and by acquiring another one in Holland, it misused this dominant position. Although it was absolutely without discussion, just the simple fact of buying this company is regarded as a misuse. Here again I am of the opinion that if you interpret Article 86 verbally, logically the Commission should lose the case. However, I am afraid that if the Commission comes to a decision the Court again will probably back it up out of this idea—what promotes a Common Market—thereby making new law. This shows how the whole legal system of Europe is changing.

MR. HILINSKI: I might make some comment with this cross-fertilization of ideas between countries which also has considerable impact in the tax area. In the area of so-called hidden profit distributions, not only are the sophisticated countries of Europe quite well developed—Germany is a prime example of the revenue gatherers of the country in Europe doing very much the same thing that the U.S.



revenue gatherers do when they start allocating profits between related companies. Now because the U. S. has seen fit to send its tax experts to various countries in South and Central America, these countries are coming up with these very same ideas which are causing problems down there for subsidiaries of United States corporations. On the other side of the coin I think one of the developments in the United States in the not too distant future is going to be a very long and hard look at the turnover tax position. This is the one type of tax that has not been used at a national level in the U. S. and may very well be used in the next five years or so.

MR. KLASS: I wonder if I could ask one question on this tax law. When I hear the word perpetuity I get a little bit disturbed that I am trying to legislate not only for my successors but their successors. When you deal with a concept that property is information and the requirement that it be given in perpetuity, how do you interpret that? Does that mean that the giver can never use it in the territory where he has given it?

MR. HILINSKI: Not necessarily in the sense of whether you can make a sale. But if you want to have what qualifies as the tax-free transfer of property for tax purposes when you are setting up a joint venture and you want to transfer some type of technology there, some secret process, some formula, you have to give all of the rights in that property to that particular organization in the foreign country to the effect that you are giving it away in perpetuity. They have the sole right in that country.

MR. KLASS: Does that mean in effect that you can never come into that country and use that formula or that information yourself?

MR. HILINSKI: Well, I think if you reserve that right yourself to use it there you have not made a transfer of property which qualifies for U. S. tax purposes. You may want to do that for other business reasons but that will defeat the concept.

MR. KLASS: In effect, if you get the tax ruling you are barring your successors and their successors and so on from ever using that formula in that country.

MR. HILINSKI: Unless you buy it back.

MR. TIMBERG: I want to point out that there may be countervailing antitrust considerations. Several times in my practice I have been in receipt of advice from my client that the tax situation is such that he should transfer an exclusive right in his technology and divest himself of all control. I have had to advise the client that there could be antitrust hazards in such a course of action.

MODERATOR WEISER: This is a conflict, Sig, that the tax and antitrust

people have not been able to reconcile yet. Considerations for one seem to work exactly opposite to the considerations of others. I have a note here from Pat Federico that reminds me of a point we discussed a minute ago, and I would appreciate it if you would touch upon the licensing aspects of the planned European Common Market patent. If you would touch on that point I think we would be very interested.

MR. FEDERICO: Well, some of you may know more about it than I do, but I will say a few words about the patent plans. The situation at present is exactly as you stated. Each country has its own laws and some of the member countries are rather sensitive about that. A French official made a speech once where he declared "Must we substitute bailiffs for customs men"? In France bailiffs are used in the first step of enforcing patents. So they started about ten years ago with the idea of a single patent for the Community and a draft was published. The plan was that there would be a single patent for the Community of six countries. They were concerned with two problems: One problem was whether to permit Americans to obtain the Common Market patent. The second was this one we are concerned with now. In that draft the solution was that the patentee could give territorially restricted licenses but that anything made by a licensee could move freely throughout the Community without regard to any conditions in the license. The first draft was put on the shelf mainly through the objections of France and strange as it may seem it was the French government which revived the plan along some new lines just a few years ago. Their drafting committee started work again on a new draft.

PROFESSOR OPPENHEIM: Beginning with Pompidou?

MR. FEDERICO: No, even before. The preliminary new draft was published a couple of years ago. The new plan is divided into two parts—one part establishes a common patent office which will grant patents for all the European countries that adhere. The patent will be a single document but will constitute a separate patent for each country. Then there will be a second treaty among the six only and as to them, the document will be a single patent for the entire six countries. This published draft was incomplete and the drafting committee continued working on more problems and on revisions. The revised draft is finished, I understand, and apparently was scheduled to be published or released to the public this month. I haven't heard whether it was and what they are proposing now I do not know.

The draft of two years ago had a provision in it which would exclude U.S. nationals from getting a Common Market patent. I do not know whether it is still in but it should not be. The excuse given is pretty

weak and insubstantial. If they kept the U.S. out they would have to retain their national laws because they are obligated to give patents to U.S. citizens; they would have to keep their national laws for the benefit of Americans. If they had kept the U.S. out of the Common Market patent, there would be individual patents. That would preserve the situation that Mr. Deringer spoke about for the benefit of Americans. Some of the countries may be definitely planning to drop their national laws. One of the representatives from Holland here last June specifically indicated that if the Common Market patent were in operation, they would propose to cancel their local patent laws and rely entirely on the Common Market patent. That is about where the thing stands. They are moving. They had meetings all last year revising their draft, and the word we got was it is going to be published very soon. You know more about it, Mr. Deringer, so I wish you would correct me.

MR. DERINGER: I do not know the developments within the last year because I am not in this Commission but maybe I can give you some background information about the development of the draft of February last year. By the way, there will be an article by me in the next antitrust bulletin about this draft.

I was Chairman of the legal committee of the Parliament at that time and when the discussion was lagging I tried to get the discussion moving again by some report in our committee. As rapporteur I appointed my friend Mr. Armengaud. He is a famous French patent lawyer. And while he was very reluctant to push the report forward, in November '68, he then suddenly changed his position because of the development of the PCT Treaty that caused French industry to have the feeling that if there will be an international PCT arrangement with an American, a Russian, and maybe even the German patent office monopolizing the whole thing, then we prefer to have a European patent where we at least are stronger in the international area. This was the psychological background of the changing of the French position. If you would like to have some more information about these different clauses—as far as accessibility is concerned this clause about the American patent law is a compromise between the French position refusing any access, and the position of the other five countries. Maybe it has changed.

MR. FEDERICO: It has been changed; we have been told that.

MR. DERINGER: O.K.? I didn't know that. With regard to the economic clause I would say the solution is absolutely logical. Seeing there is just one Community patent, every sale under this Community patent exhausts the whole patent for the whole Common Market. However, the

fact that the national patents are still or will still exist besides the European patent is not only due to the American situation, but there is a general tendency to say there may be smaller enterprises that have sufficient protection with a patent in Luxembourg. Why not? Then under these national patents the same problem will exist in the future. In the treaty they are resolved because there it is expressly forbidden for affiliated companies even with national patents to divide the market, which means that big enterprises may do it.

MR. FEDERICO: I will say that the Dutch are definitely thinking of dropping their own patent regardless, for other reasons.

LANTY SMITH: I was interested in Mr. Timberg's reference to the toe-hold acquisition doctrine of the *Bendix-Fram* case in the joint venture context. I wondered if he had any direct authority for application to joint ventures?

MR. TIMBERG: No, I have no direct authority. As you know, the toe-hold theory was developed by Commissioner Elman in the *Bendix-Fram* case and has been supported in principle by the head of the Antitrust Division. The theory is somewhat more appropriate to acquisitions and mergers than it is to joint ventures. The argument usually put up for a U. S joint venture involving a foreign parent is that the foreign parent could not enter the U.S. market by internal expansion. If the joint venture involves a U. S. parent and takes place abroad, the U.S. parent customarily argues that it is necessary to enable it to enter the foreign market. The toe-hold theory enlarges this justification for an acquisition or joint venture by allowing a large potential competitor, whether located in the U. S. or abroad, to make the acquisition or consummate the joint venture provided it does not choose too big an American company.

MR. SMITH: May I take that one step further? Is it your feeling that the major European companies could not come into the U.S. in joint ventures with a leading or dominant firm in a particular market simply on the basis of the doctrine of potential competition?

MR. TIMBERG: Well, I think the experience of British Petroleum in its acquisition of Sohio is some indication of the fact that there is a limit to what the foreign acquiring firm will be permitted to take over. If there is any particular market in which the Antitrust Division or the courts think the competition between the acquiring and acquired firms is sufficiently strong, the foreign acquirer may have to relinquish all or part of that market. Maybe Tag Whipple has something more on that.

MR. WHIPPLE: No, not at all. I just wanted to ask you if acquisition involving the foreign firm ran the other way? Let me amplify my

question without getting into too many details. We have been talking about joint ventures a good deal as a way of getting Americans interested in foreign markets, where there is some slight restraint on export trade. Would you share the view that this is of minimal concern to the Antitrust Division as compared with a restraint on imports?

MR. TIMBERG: I think the Antitrust Division does not carry the torch for a favorable balance of payments (laughter). They will, in my view, follow the conventional dictum in the *Minnesota Mining* case and determine whether there is an effect or intention to restrict American exports that makes the transaction illegal. They are not concerned with the level of imports into the United States, but only whether those imports have been restrained. I also believe that the Antitrust Division is going to assume that U.S. companies that are strong enough to enter foreign markets are strong enough to protect their domestic market. It is my feeling that the Division will not weigh both sides of the balance of payments ledger, but will focus on the losses in exports and not the gains in imports.

MODERATOR WEISER: I have been informed that the bell has tolled. It is a shame! We would like to go on but yet there is a time where even good things have to end. Lou stated at the beginning that one of the aims of this Clinic was to develop new thoughts, new ideas, and new approaches. I'm sure it was stimulating. I cannot attempt to summarize now what Felix Klass has spoken of, what Homer Blair has shown us, what Sig Timberg has predicted and how Chet Hilinski has shown us how to save money. Mr. Klass touched on the organization, the veto power, and the managerial problems. Homer Blair carefully brought out the trademark, patent, and clearance question. Sig Timberg talked on antitrust and Chet on the tax aspects. But the consensus was that we have a joint venture that we do want to be successful. The discussion emphasized that we have a technical, unique product which we want the joint venture to exploit. For details you will see it all in print.

DIRECTOR HARRIS: On behalf of The PTC Research Institute let me thank the speakers for their contributions and all the Clinic participants for their rich and informative input. As Gerry mentioned, the proceedings will be published. However, you will all have an opportunity to edit your remarks prior thereto. Until then, they are confidential. Thank you again. The Clinic stands adjourned.

# Priority Assertion and Early Disclosure Through Author Abstracts

IRVING H. SIEGEL\*

## IDEA IN BRIEF

THIS PAPER, WHICH EMERGES FROM A CONTINUING STUDY of individual creativity sponsored by The PTC Research Institute, calls attention to a new potential for author abstracts in contemporary scientific communication. We say "new" because we have in mind the kinds of abstracts that already provide scholars, librarians, editors, referees, indexers, patent counsel, and clearance officers of companies and government agencies with compact reports on on-going or completed research. Such abstracts already are familiar, for example, as summary head-notes to papers published in "primary" journals, which for three centuries have served as standard media for the registration, professional dissemination, and storage (both quick-access and archival) of scientific findings. They also are the ingredients of booklets intended to give members of professional societies an advance idea of the contents of papers to be presented at meetings. If, however, the notion of abstracts is construed more liberally (and precedent for so doing does exist), then the additional roles here proposed are seen to be not new at all. Indeed, they are seen to be traditional ones that even antedate the primary journal

---

\* Dr. Siegel, an economic and business consultant, has been associated with The PTC Research Institute's research program from its inception.

itself—as well as formal abstracting and indexing services, which originated in the early nineteenth century.<sup>1</sup>

#### LOW-COST BENEFIT FOR JOURNALS

Just what added functions do we envisage as plausible for author abstracts, modern-style? Beyond condensing information for the convenience of various users, such abstracts could serve as vehicles for timely *initial* reportage of research results in primary journals. They could thereby also satisfy the persisting felt need of scientists to claim and record priority—a need comparable to the inventor's for patent protection, as we shall stress later.<sup>2</sup>

Specifically, abstracts of the sort already appearing together with full papers should be made eligible for separate evaluation and for comparatively early presentation as brief documents of disclosure in a new journal section. The publishability of an abstract by itself in this section should not necessarily depend on a forecast of the eventual disposition of the complete paper. Ideally, if a full paper is not rejected out of hand, if it passes gross editorial screening upon receipt so that it proceeds to the refereeing stage, the accompanying abstract should be printed by itself, as a disclosure document, in the very next journal issue. A much stricter alternative rule would defer decision on publishability of the abstract until a referee report on the complete paper is returned to the editor. Such a rule, of course, would diminish timeliness in favor of quality in selection. (Incidentally, it is recognized with equanimity that an abstract might be printed twice in the same journal, once by itself and in a later issue as a headnote.)

Establishment of an abstract section for facilitating priority quests and expediting disclosure ought to strengthen the primary journal as an institution—to restore some of its faded lustre, and to do so at relatively low cost. The accumulation of huge backlogs of accepted

---

<sup>1</sup> On this paragraph, see *Scientific and Technical Communication* (Washington: National Academy of Sciences, 1969), especially Chapters 4-6; and L. S. Feuer, *The Scientific Intellectual: The Psychological and Sociological Origins of Modern Science* (New York: 1963, Basic Books), pp. 66-67. According to the latter, the *Journal des Sçavans* (Paris) and *Philosophical Transactions of the Royal Society* (London) were established in 1665, and *Acta Eruditorum* (Berlin) in 1682.

<sup>2</sup> The view taken in this paper differs to some extent from that expressed in the informative works of the eminent sociologist, R. K. Merton—e.g., "Behavior Patterns of Scientists," *American Scholar* (Spring 1969), pp. 197-225; and "Priorities in Scientific Discovery: A Chapter in the Sociology of Science," in Bernard Barber and Walter Hirsch, eds., *The Sociology of Science* (Glencoe: 1962, Free Press), pp. 447-485.

papers and of papers still in process has encouraged wide resort to informal "preprints" and "letters to the editor"; both may escape indexing, and the former may also pose special dangers of information pollution in addition to explosion. Furthermore, "letter journals" have sprung up as rival media promising much quicker manuscript turnover than the regular primary journal and a better chance to beat the competition. The standard journals offer little comfort by noting in each issue the accepted manuscripts that await printing and by noting the dates of submission and revision for each published paper. Finally, the refereeing process is itself subject to the same human frailties that afflict all scientific enterprise, which James Watson's *The Double Helix* (1968) has so strikingly if unintentionally exposed to public view. When the track is already crowded and muddy and the economic sky overcast, the race for fame and new grants is to the left; and the representative of the wrong stable may find himself at a considerable disadvantage compared to a member or favorite of an "invisible college."<sup>3</sup>

Once adopted, any scheme for early publication of author abstracts as initial and independent reports in primary journals would surely undergo subsequent evolution. In particular, we might expect the abstracts to become somewhat longer and to be subjected to increasingly rigorous standards regarding form, content, language, and indexability for easy retrieval. The experience that contributions to letter journals are very often not followed by full writeups elsewhere is frequently interpreted pejoratively, as evidence of a somewhat unwholesome thirst for priority recognition; but it may also suggest the happy possibility that scientists will yet learn to prepare concise "complete" papers. Editors of primary journals should encourage any such trend, even if its present indications are doubtful.<sup>4</sup>

#### A HARDY TRADITION

As the opening paragraph of this paper observed, a backward glance over history readily reveals that variants of today's author abstracts

---

<sup>3</sup> On this paragraph, see Merton's first paper cited in note 2; the several articles on the primary journal in *Journal of Chemical Documentation* (February 1970), pp. 26-46; two issues of *American Psychologist* (November 1966 and April 1971), devoted to scientific communications; and *Scientific and Technical Communication*, already cited.

<sup>4</sup> On this paragraph, see first Merton paper cited in note 2; Arthur Herschman, "The Primary Journal: Past, Present, and Future," *Journal of Chemical Documentation* (February, 1970), pp. 37-42; and J. H. Kuney, "New Developments in Primary Journal Publication," *ibid.*, pp. 42-46. It appears that only about half of the items published in *Physics Review Letters*, a well-regarded letter journal, ever mature into full-fledged journal articles.



have long supported the "novel" proposed functions of promoting priority bids and hastening disclosure. In particular, before formal journals existed, or before they could convincingly demonstrate that speedy publication was the best safeguard against the "philosophical robber" (as Robert Boyle, the famous Restoration chemist, called the plagiarist), cryptic author abstracts already abounded. Scientists sought, through terse and obscure disclosure, to "bargain" for the private benefit of recognition in return for the public benefit of new accessible knowledge. They also sought additional time, by the stratagem of revelation with concealment, for bolstering their expertise against the prowess of rivals they were about to inform. Of course, even today, a mathematician may try to sustain an advantage over gifted readers by "elegance" in derivation and presentation; a physicist or chemist need not tell the limit he has already reached in whatever paper he is writing; and a scientist who is thought to have more to say may be invited to consult, lecture, or prepare additional papers.

The enigmatic author abstract of the past, like the published abstract of a paper to be given at an annual scientific meeting nowadays, was not necessarily a summary of an existing, more complete manuscript. Rather, it stated the essence of a discovery or body of work that was a fit subject for extensive treatment if the situation required or if the scientist had the leisure. Accordingly, the simple definition of an abstract as "a condensation that presents succinctly the objectives, scope, and findings of a document," which appears in an authoritative book published in 1971, requires broadening.<sup>5</sup> As noted above, even today, the gist of a paper yet to be written is presented in print prior to a meeting. But earlier precedents can be cited too. Thus, in the introduction and in the concluding chapter of *The Origin of Species* (1859), which Darwin finally wrote when in danger of losing his priority status to a young competitor who had arrived at the same results with much less time and effort, the "father of evolution" referred to the book as only an "abstract" of "work" almost finished but requiring additional years to complete.

In any catalog of author abstracts notable for brevity and impenetrability, we should have to include the Latin motto scrambled into an anagram. One example is the famous Hooke's Law for Springs: *Ut tensio, sic vis* (roughly translated as "force is proportional to the elongation"). In his third Cutlerian Lecture (1676), this discovery by Hooke was included in a postscript listing "a decimate of the centesme of the inventions I intend to publish." Described simply as the "true

---

<sup>5</sup> R. E. Maizell, J. F. Smith, and T. E. R. Singer, *Abstracting Scientific and Technical Literature* (New York: Wiley-Interscience, 1971), p. 1.

theory of elasticity or springiness," this result is then stated as a cipher: *ceiinossttuu*.<sup>6</sup>

Our other examples concern the planet Saturn, which was an object of great curiosity in the early days of the telescope. In 1610, Galileo proudly announced an incorrect finding in a Hooke-like string of 37 rearranged letters. The original abstract said: *Altissimum planetam tergeminum observavi* ("I have observed the farthest planet to be a triplet"). Kepler failed to crack the code. Years later, in 1656, Huyghens found the right answer to the riddle of Saturn but gave the world a new riddle as his abstract in an interim publication. Unsurprisingly, he himself had to provide the restatement of his anagram into Latin in his final report three years later: *Annulo cingitur, tenui, plano, nusquam cohaerente, ad eclipticam inclinato* ("It is circled by a thin ring, plane, without adherence, inclined to the ecliptic").<sup>7</sup>

These early instances are not cited for mere journalistic interest. They demonstrate in pristine clarity (for all their obscurity) the concern of scientists for due recognition, and, in this connection, the dialectic interplay of impulses to reveal and to conceal.

#### RELEVANCE TO PATENTS

Although the preceding discussion has focused principally on journal science, it has some pertinence for patents, the handmaidens of technology. The joint interest of scientists and society in priority recognition and early disclosure is matched by an equivalent joint interest of inventors and society. Of course, the recognition of the inventor's priority carries with it a right to exclude, and this right often has an economic value. The prospect of economic exploitation, however, tends to be overemphasized, to the comparative neglect of (1) the similarity of the drives of the scientist and the inventor and (2) the symmetry of their positions *vis-à-vis* society. The echoed protestations of economic innocence of famous dead scientists (e.g., such nineteenth-century worthies as Joseph Henry and Henry Rowland) and the authoritative statements of prominent scholars (like the sociologist, Merton) about the "communism of intellectual property" as basic to the "ethos" of science<sup>8</sup> should not drown out what we are also told by the ambiguous

---

<sup>6</sup> Margaret Espinasse, *Robert Hooke* (Berkeley: University of California Press, 1962), p. 78.

<sup>7</sup> R. Taton, *Reason and Chance in Scientific Discovery* (New York: Science Editions, 1962), pp. 156-157.

<sup>8</sup> Merton, in *The Sociology of Science* (see note 2), p. 464.

abstracts of Galileo, Huyghens, and Hooke and by the activity patterns of contributors to contemporary letter journals.

The inherent brevity of the abstract as a genre of communication tends to confer a social respectability upon incomplete disclosure that ought also to apply to the whole patent document that is finally published. This document, after all, tells what is legally required. Besides, it cannot be complete in any very strict sense. Indeed, any description of a technology, even if a whole book is devoted to the task, is bound to remain, like Darwin's volume on evolution, only an abstract. A book-length version of a patent disclosure is sure to slight some know-how, trade secrets, and other details, even non-proprietary ones, that an interested reader would consider pertinent to successful practice.

In conclusion, we note another interface of the main topic of this paper and the patent system. An eventually significant role for author abstracts in the patent field may develop as a result of the establishment of "defensive publications" as a category of documents in 1968. The new arrangement permits discontinuance of a patent application before completion of examination by the Patent Office in favor of publication of an abstract in the *Official Gazette*, whereupon the file relating to the application becomes open to public inspection. The number of defensive publications is still small, perhaps because of the newness of the arrangement as well as the administrative, rather than statutory, basis.<sup>9</sup>

---

<sup>9</sup> E. A. Hurd, "Patent Literature: Current Problems and Future Trends," *Journal of Chemical Documentation* (August 1970), p. 169; and D. B. Baker, F. A. Tate, and R. J. Rowlett, Jr., "Changing Patterns in the International Communication of Chemical Research and Technology", *ibid.* (May 1971), p. 98.

# Emerging Restrictions on Transfer of Technology

JOHN C. GREEN\*

## INTRODUCTION

DESPITE THE ACTIVITIES OF THE UNITED NATIONS, other international agencies, national governments, foundations, et cetera, the bulk of the transfer of technological information takes place through private channels. When we look at transfers to the developing countries we find this to be especially true. However, here the mechanism is usually initiated by a firm in a developed country which controls technology that it believes can be put to use profitably in a developing country. Often such a firm seeks to identify a local capability to produce or, if such capability is non-existent, to create one. This process would be reasonably simple if the interests of the foreign firm and its potential affiliate or licensee were decisive.

However, governments in developing countries are concerned with penetration of their domestic industry by foreign sources for a number of reasons. One, which is often quoted, is to avoid exploitation of national resources which may benefit the foreign firm but which does not contribute measurably to the local economy. Unfortunately there

---

\* Project Leader, International Trade and Development Studies, The PTC Research Institute; Scientific Communications and Research Consultant, Washington, D.C.

are examples of such exploitative operations from the past which remain fresh in the minds of policy officials in many developing countries. As the private sector in the developed nations becomes more experienced in overseas ventures, this example is becoming rare. Nevertheless, there are a number of other reasons justifying the concern of governments when a foreign firm seeks to establish a manufacturing or business operation within their boundaries.

What is needed is a balanced view which takes into account the needs of the developing country and those of the investor from abroad. The U.S. Council of the International Chamber of Commerce, Inc., has expressed this admirably.

The government of the host country must be assured that the foreign investment is consistent with its economic and social plans and priorities, that locally available resources play an appropriate role and earn a fair return and that the long-range net effect of the investment is beneficial to the country's economic and social development. The investor, on the other hand, must be confident that the government of the host country will give fair consideration to his legitimate interests and responsibilities, will afford reasonable protection to the resources which he is willing to provide and will permit him to earn an adequate return on his investment commensurate with the risks involved and having regard to his alternative investment opportunities elsewhere.<sup>1</sup>

#### THE PROBLEMS OF A PLANNING OFFICIAL

Perhaps it would be useful to attempt to place oneself in the position of a key official in a developing country with a responsibility for achieving certain economic and social objectives in a limited time frame. He is aware of the fact that his country has substantial unemployment, small capital resources, few technically trained persons in the labor force, limited markets and little purchasing power. Also he appreciates the fact that the economic and social infrastructure of his country is inadequate.

Thus he is faced with the task of advancing on the public and private fronts simultaneously, yet having few resources at his command which can be applied to the tasks. He can get some help from international banking facilities and from other governments, such as our own, on "infrastructure" projects directed to better education, transportation,

---

<sup>1</sup> Statement of the Commission on International Investments and Economic Development. United States Council of the International Chamber of Commerce, Inc., p. 3. (New York: June 10, 1971.)

utilities, medical care, public housing, et cetera. However, he will have to complement these by local government resources since such activities are, by their nature, not those for which private enterprise can assume the role of creation, financing and operation.

One might expect such a policy official to welcome any source of additional capital since the needs of his country far exceed the resources. And in fact foreign capital is welcome *if* the objective of the foreign firm is consistent with the country's national plan. That "if" is extremely important and leads to government examination of proposed arrangements and to government regulations concerning the planned activities.

#### AN EXAMPLE OF A REGIONAL POLICY

Recently five Latin American countries (the Andean Group) announced an agreement which proposes common treatment for foreign capital, trademarks, patents, licensing agreements and royalties. This agreement became effective on July 1, 1971. Let us look at the general principles found therein:

- (a) Economic growth and social progress are the responsibility of Latin America, on whose own efforts primarily depends the achievement of their national and regional objectives.
- (b) The nations have the full and sovereign right to dispose freely of their natural resources.
- (c) In the economic development of the sub-region, priority should be given to national enterprises and capital of these countries.
- (d) Foreign capital investment and the transfer of foreign technology are necessary for the development of these countries and should be assured of stability to the extent that they really constitute a positive contribution.
- (e) Rules regarding the treatment of foreign investment must be quite clear in formulating the rights and obligations of foreign investors and the guarantees which foreign investment shall receive.<sup>2</sup>

These principles, properly applied, seem logical and reasonable. The matter, which will be addressed in this paper, is whether there are

---

<sup>2</sup> *Id.*, p. 1.

signs that these and like principles may be applied within individual countries in ways which will stultify the foreign investment that is so badly needed.

One example is found within the Andean pact countries just mentioned. In addition to the general principles noted, there are a body of articles whose purpose is to define their implementation. Three of these articles (28, 30 and 35) merit special mention. The first two say that within three years from the coming into force of this portion of the agreement a foreign-owned enterprise existing in a member country, which hopes to enjoy the advantages of customs liberalization, must conclude an agreement under which a minimum of 51 percent of its shares are transferred to local ownership. If the enterprise is located in Colombia, Chile or Peru the maximum time for such divestiture is 15 years; if the firm is situated in Bolivia or Ecuador it is 20 years.

The third article (35) provides that the government or state enterprise must be given the right of first refusal. On first examination these requirements may not appear to be unduly onerous. But let us ask ourselves whether they will contribute to the economic growth of the countries concerned. And that in essence is the objective of all of the signatory countries.

#### IMPACT ON FOREIGN INVESTMENT AND TECHNOLOGY TRANSFER

One can state immediately that joint ventures as such are not a discouraging deterrent. As a matter of fact, most foreign companies find such ventures attractive. The direct involvement of a capable local firm with its special knowledge of local markets makes the new venture more certain of success.

Today the foreign enterprise is prepared to work in a variety of alternative arrangements depending upon the economic environment. These may embrace (a) fully owned subsidiaries, (b) partially owned subsidiaries, (c) 50-50 partnerships and (d) licensing arrangements with local enterprises.

Similarly, the transfer of technology will follow a pattern dictated by local resources and economics. Often, in the early stages, the parent company will supply the necessary production equipment. Then, as the market grows, there is a conscious movement toward providing the technical information and training necessary to increase production and productivity within the local firm. The goal is an integrated factory

including, where scientific competence is available, a technical unit to undertake adaptation to local conditions.

This does not mean that the overseas company will welcome the divestment schedule described. It is one thing to seek out local capital and competence and to join with them in a partnership arrangement. It is quite another to have partial ownership by local interests required whether said interests have any contribution to offer to the venture. When this is coupled with the requirement that the government be given the right of first refusal one can see that many foreign firms will say—"Why bother? Let us seek other avenues for expansion of our activities."

In this connection one feels that policy officials in developing countries may be misinterpreting the attitudes of responsible management in industrialized countries such as the U.S. If the managers were anxiously vying with one another to start up manufacturing or commercial enterprises in countries with the limited economic potential of the developing nations, new restrictions and prohibitions would be of less effect. But the facts are that such ventures are experimental and risky accompanied by special difficulties in management, training, production and sales. In addition, in our country questions are being raised about the wisdom of overseas operations while unemployment persists at home. Cumulatively these are deterrents in the existing climate, adding others cannot be expected to enlarge the current volume of technological transfer.

There is another difficulty which the developing countries may not be aware of. This might be thought of as a drying up of the flow of technology. This will be a natural result of management decisions in the course of business. If the situation is one in which control is to be diminished and ultimately lost, the firm cannot be expected to be as willing to contribute its new technical advances or its best management practices. This of course will be especially true as the time for divestment approaches. The result will be that the local enterprise will be less capable and will make a smaller contribution to economic growth than would otherwise be the case.

There may be a distinction between new and existing investments. If there is, it would appear to be a negative one. Heretofore the potential investor might welcome the opportunity for a stable investment with long term growth possibilities. Faced with a divestment according to the formula imposed, he can be expected to shift his sights to high profit, quick return ventures. These, and the withdrawal of capital, are less desirable from the point of view of fostering the nation's economy.



AN EVOLVING ATTITUDE?

If the Andean pact agreement were unique one might consider it to be less serious. However, it is the writer's opinion that the agreement is consistent with attitudes, philosophies and practices evolving in many developing nations. In this connection let me recount a recent experience at the United Nations.

Last spring, the U.N.'s Under-Secretary-General for Economic and Social Affairs invited The PTC Research Institute to participate in a meeting at the U.N. Headquarters on a subject which has been a concern to the Institute for many years. The Secretary-General advised that he was convening "an interregional meeting of experts to evaluate . . . the effectiveness and cost of arrangements for the transfer of technology between enterprises (public and private)."

Most apparent to me during my attendance at the meeting was a distinction in representation. Most participants from developing countries were people who influenced policies in those countries. The few representatives from industrialized countries appeared to have been chosen for their technical expertise. A spectrum of officials from such developing countries as Mexico, Chile, Israel, Nigeria, Tanzania, Lebanon, and India spoke. The free world industrialized countries had persons from Canada, France, Sweden, Japan, and the U.S. The Eastern European countries were represented by Czechoslovakia and the USSR. While each delegate was said to be there as an "expert" and not as a representative of his country, this distinction was of little substance since each spoke from his experience, and his ideas reflected that experience.

It is difficult to define the flavor of the sessions, but my impression, shared by other U.S. citizens who were there, is that many of the developing countries have an unrealistic view of the mechanisms of technology transfer. In particular, the subject of forced divestment was offered as desirable and the attitude of some seemed to be that the industrialized countries had a duty to share their technological achievements with the less developed and that present reliance on commercial arrangements was too expensive and disadvantageous.

One way of looking at these attitudes is that the persons were expressing personal views and that this would not affect the "real world" of technology transfer. There may be some support for this view; however, when a number of separate persons offer similar positions, they tend to reinforce one another. Further, when their views are recorded, the printed word lends them substance and authority. As a

result, a body of principles is evolving in such groups as the U.N. and the Andean pact adherents which will inhibit the flow of technology, the flow of which is already inadequate.

#### NEED FOR BETTER PREPARATION

Why is this coming about? One can offer many reasons, but one which appears most significant to me is that the United States doesn't seem to prepare properly for these meetings. Our invitation to the U.N. meeting in June was not accompanied by relevant studies, nor was there any indication of the attendees. On the assumption that the U.S. element to the U.N. was taking care of an official delegation, we didn't consider the meeting a priority item. However, when I arrived I found that I was the leading delegate from the U.S. and that there were no official representatives from the area of expertise—the private sector. Fortunately a few persons from U.S. industry had learned of the meeting and obtained permission to attend as observers. In this capacity they were limited in their ability to participate. However, I can say without false modesty that the most cogent and practical comments came from them, especially Charles S. Dennison of International Minerals and Chemical Corporation. He, and Paul Brent, of the Council of the Americas, were especially helpful.

Brought together informally as we were, I believe we succeeded in avoiding the formal acceptances of some of the unrealistic proposals advanced. However, this is a negative accomplishment. If the U.S. Government had a policy of insuring proper and early accreditation of industrial experts to such meetings I'm convinced that new and constructive incentives would be forged in such bodies. The representatives from the developing countries are intelligent and sincere; they earnestly strive to advance their respective economies. What has been lacking from their deliberations is the direct participation of those very industrialists who generate and control the technology they so ardently desire.

## EDUCATIONAL ACTIVITIES

---

*We are including the first paper in the Educational Activities Section of IDEA to illustrate the problems and experience of developing countries in applying the results of government laboratory research to their emerging industries.*

*The second paper in this Section is intended to provide our readers with another aspect of the problem concerning international research and development programs. This second paper takes up the problem of sharing the high costs of developing sophisticated military equipment with countries that support little or no research and development for defense purposes.*

### Special Problems of Innovation and Technology Transfer

JOHN P. SHELTON\*

#### SUMMARY

A HIGH PROPORTION OF THE TOTAL RESEARCH and development effort in Australia is carried out in government research organizations, the largest of which is the Commonwealth Scientific and Industrial Research Organization (CSIRO).

The work of CSIRO falls broadly into two classes: (1) Research on topics of broad national importance that would be outside the di-

---

\*Secretary, Industrial and Physical Sciences, Commonwealth Scientific and Industrial Research Organization, Dickson, Australia.

*EDITOR'S NOTE: The Indonesian Academy of Sciences (Lembaga Ilmu Pengetahuan Indonesia) invited the U.S. National Academy of Sciences last year to assist them in developing policies and programs designed to contribute to Indonesia's economic growth and stability.*

rect interests of the laboratories controlled by private industry; and (2) research and development on topics intended to be of direct benefit to industry by leading to new or improved technology.

Experience in CSIRO has shown that publication of information is not sufficient to ensure that new technology is used by industry. While publications and information services for industry are an important activity, CSIRO must also actively promote the adoption of new technology. Patents are widely used by CSIRO in a variety of ways to assist in the application of research results in industry. It is not always feasible to complete the development stage in a government laboratory, and exclusive patent agreements are used when necessary, under which CSIRO and a selected company jointly works on the development and engineering of new technology that has been initiated in CSIRO research.

The capacity of Australian industry to handle development work has been greatly increased by the success of the Australian Industrial Research and Development Grants Board, which fosters expanded industrial R&D through financial rebates.

Perhaps the most difficult problems in the whole research-develop-

---

*Subjects for early attention included forest products, metals, and chemicals and the need for supporting institutions concerned with patents and standards. The U.S. team was led by Dr. Harold Wilcke and the Indonesian counterparts by Dr. Sumantri. Dr. Arismunandar and Mr. John Green, who is Project Leader, International Trade and Development Studies of The PTC Research Institute, conducted the sessions directed to patents.*

*The entire activity benefited much from the presence and participation of experts from Japan, Singapore, England and Australia. In particular, the patents group was fortunate in having the advice and assistance of the author of this paper, Dr. John P. Shelton.*

*Since a high proportion of all research performed in Indonesia today, and in the foreseeable future, is under government auspices, there was a lively interest in the problems inherent in transferring the results of research performed in government laboratories to Indonesia's emerging industries. This is a problem faced by governments in many countries, including the U.S., with varying success. Australia has evolved patterns and programs which have enjoyed excellent results. For that reason, Dr. Shelton's observations, as expressed in the above paper, were especially interesting. In view of the broad spectrum of interest, it was felt useful to give his narrative wider circulation in IDEA.*

ment-engineering area concern the selection of those research projects that will lead to innovation. In CSIRO a balance is maintained between short-term work with specific industrial objectives, and more basic work in subjects relevant to the interests of industry, but having no specific industrial objectives. While the short-term work has a high proportion of successes, and the economic returns are predictable, these are relatively modest. The major industrial successes of CSIRO, both in primary and secondary industries, came from research without specific objectives, at least in the early stages of each project. In this more basic work in CSIRO the judgment and intuition of the working scientists are given greater weight than estimates of the probable economic value of the results, because of the difficulty in predicting what will be discovered in original research.

---

---

## INTRODUCTION

THIS SUBJECT COVERS A WIDE FIELD of activity and rather than attempting to touch on all aspects of the whole subject, I would like to concentrate on those aspects of innovation which I have met in my own work. This is concerned with the problems involved in undertaking, in a government laboratory, research and development for the benefit of industry and in encouraging and fostering the application of the results of this research in industry.

I will, therefore, refer only briefly to a major source of new technology, namely, that which is available from the industries of highly industrialized countries. Such overseas sources of new technology have made a major contribution to the industrial and economic development of Australia over the past 25 years. However, the problems in the use of such technology are different from those that are met in attempting to pioneer new technology based on original research. In particular, when dealing with imported technology we know that it works in practice—there is none of the uncertainty that is always present along the path from research to development to innovation when a new product or process is being brought into industrial use for the first time. Free from this uncertainty, the problems in the application of imported, fully proven technology are chiefly those of adaptation to local conditions—to changes in raw materials, to different cost structures, and so on.

Much of the actual work of diffusion of this technology throughout

the world is carried out by the large international companies, either through their own subsidiaries or through licensing of local firms in other countries. One important set of problems relating to such diffused technology concerns the terms under which the technology is made available to industries in other countries. Tax concessions, land grants, special power costs, guarantees about remission of profits, and so on, all come into the picture. Such problems are important but there are others better qualified to discuss them than I am.

However, let me emphasize that the value and importance of imported technology should never be underestimated. Certainly, it would make life easier if the industries of every country could be self-sufficient and base their economic and industrial development on the results of local research. Experience shows that this is not practical and, indeed, studies made of the sources of new technology in some of the largest companies in the U.S.A. have shown that a substantial proportion of new processes and products have been initiated by research outside the firm that is the successful innovator. The problems of importation of new technology, however, are not chiefly technical problems; they are economic and political.

Turning now to the problems that must be faced in bringing into industrial use results of research from government laboratories, may I say first of all that different patterns of government involvement in industrial research have been developed in different countries to meet different needs. For example, in the United States of America, government funds for research are predominantly spent in industry laboratories, through research contracts. In Australia, the opposite pattern prevails and the main part, although not the whole, of government research money is spent in government research laboratories, the chief one being that for which I work, the Australian Commonwealth Scientific and Industrial Research Organization. No matter what the actual pattern of expenditure is the principle is the same: namely, that problems of national interest and economic development require research on some topics that industry is not willing to work on, or require more research in total volume than industry can afford, or is willing to afford, to work on.

In many cases, and the experience of CSIRO bears this out, innovation has stemmed from research that began in a government laboratory before the relevant industry existed. For example, Australia has large resources of ilmenite and rutile, and even 20 or 30 years before there was any reasonable market for these materials, CSIRO, or as it was then, the Council for Scientific and Industrial Research, had under-

taken research on the methods of mining and separating the various components of these materials. The thought behind this was that here we have a national asset in which our country is fairly well favored. We therefore have a greater incentive than many other countries to understand more about this national resource and to seek to find ways of exploiting it and using it in industry. Another example was work on the chemistry of Australian uranium deposits that began well before we knew of the important role uranium would play in nuclear energy generation.

### THE WORK OF CSIRO

The Commonwealth Scientific and Industrial Research Organization is, by Australian standards, a large body. Its budget in the current year is \$A62 million. The staff exceeds 6,000, of whom approximately 2,000 are qualified scientists and engineers. It operates laboratories in every State of Australia and its interests range from the solution of day-to-day problems of some industries (especially those mainly composed of small operating units) up to research of a highly speculative nature at the forefront of scientific progress, such as in radioastronomy, animal genetics, plant physiology, and so on. In addition to the substantial research effort of CSIRO, various State departments and instrumentalities operate research laboratories. There are universities in each State with substantial research programs and many of the major industries of Australia now operate large and active research laboratories.

The purpose for which the Commonwealth Scientific and Industrial Research Organization was established is defined in the Science and Industry Research Act of the Commonwealth Parliament. There are a number of subsidiary functions, such as the awarding of research fellowships, support of industrial research associations, et cetera, but the chief function is "the initiation and carrying out of scientific researches and investigations in connection with, or for the promotion of primary or secondary industries in the Commonwealth. . . ."

This definition contains by implication two characteristics that can be expected of CSIRO research, namely, that it will be relevant, in the short or long term, to the needs of primary or secondary industry, and that the results will be applied to the benefit of Australian industry. Each of these factors has a bearing on the Organization's role in innovation.

## PATENTING AND APPLICATION OF RESEARCH RESULTS

In interpreting the relevance of research projects to the development of Australian industry, the Executive (the governing body of CSIRO) has not given special priority to projects with short-term applied objectives. Experience has repeatedly shown that the benefits obtained from such ad hoc investigations are generally marginal and limited in scope by the narrowness of the preconceived objectives. It happens fairly frequently that projects started with a short-term objective make little progress, due to a lack of essential basic information. The need for this information often forces an ad hoc investigation into work on a more fundamental level, at times with results of far greater practical value than would have been likely from the original ad hoc approach. Indeed, the most spectacular and far-reaching benefits from CSIRO research have been obtained from fundamental research projects undertaken, in the first place, for their scientific importance, although on subjects relevant to the interests of Australian industry. Similarly, the most successful CSIRO patents have come from basic research projects in which the patentable results also represented important scientific advances.

*Different Orientation of University and Industrial Research*

If considered as individual projects, much of CSIRO research would not seem out of place in the universities, and it is sometimes questioned whether it belongs in CSIRO. However, the place of fundamental research in the universities depends on recognition of different factors from those that have led to the scale of fundamental research in CSIRO. In the universities, research is an essential adjunct to effective teaching and to the maintenance of standards of scholarship. For these purposes university research must be free to follow its own course, uninfluenced by political or economic considerations. In CSIRO, fundamental research is the basis on which an organized and sustained attack is being directed towards the solution of problems of national importance.

Within industry the relevance of a firm's research program to its future needs might be evaluated by the output of patentable inventions. This criterion does not apply to CSIRO research. In fact, a contrary view must often be taken, for a great number of problems exist for which a solution would be of great national benefit, although not



necessarily yield a direct return to the successful research laboratory. For example, research on a legume for use in Northern Australia, on the characterization of Australian mineral resources, on weather and drought forecasting, and many similar projects, are of high priority in the national interest. From the very nature of these problems, it would not be reasonable to expect them to be the subject of a substantial research effort by industry, since the benefits would largely flow to the country as a whole, rather than to the individual person or organization that finds the successful solution. The activities of a national research agency must therefore be weighted towards examination of those national problems for which industry can offer only a low priority.

### *CSIRO Research for Benefit of Australian Industry*

The second characteristic of CSIRO research that is implied in the Act is that its results will be applied to the benefit of Australian industry. After CSIR (the predecessor of CSIRO) was formed, it concentrated for many years on the primary industries. Most of the problems in applying the research results in the industries concerned were handled by the extension services of the State Departments of Agriculture.

When CSIR research was extended to areas of interest to Australian secondary industry, it was expected that publication of the results of the research in the scientific press would be sufficient to ensure that industry would put these results to practical use. Experience over a number of years, however, showed that mere publication of research results frequently did not lead to their expected application in industry. It is now recognized that the functions of CSIRO include taking active steps to promote the application of its research results in industry so that the community will receive the maximum benefit. Several of the techniques being used to encourage the industrial adoption of CSIRO research results are based on the patenting of its inventions, and a comprehensive policy on patenting of CSIRO inventions now exists. This policy may be summarized in the general statement that patents will be sought on inventions from CSIRO research when this seems desirable in the public interest. There are five main categories in which the public interest is usually involved:

- (1) *When there is a danger that others may obtain patents based on the results of a research of CSIRO.* Having undertaken a

research project with the object of assisting Australian industry, it is part of the responsibility of CSIRO to see that the results of this work are available for use by industry. On occasions the most effective protection against patenting by others is for the Organization to apply for patent coverage on its inventions, and then make them freely available to industry. Others are free to improve on this technology, and even to obtain patents on their improvements, but the contribution of CSIRO can be protected in this way.

- (2) *When it is desirable for CSIRO to control the quality and technical efficiency of production.* A good example of the need for such control arose with the SI-RO-SET process for permanent pleating and creasing of pure wool garments. The pleating industry in Australia contains a large number of very small firms, as well as a small number of large firms. The larger firms presented little difficulty in achieving the technical standards required, but because of the very large proportion of the total number of garments that were pleated in the small firms, special attention had to be given to control of quality in those firms. For this reason the SI-RO-SET patents were licensed to users for a small annual fee and it was made a condition of licensing that appropriate quality standards were maintained and that CSIRO had rights of inspection and supervision. There have been many other cases in which, especially in the early stages of industrial use, an innovation could have failed as a result of careless application had it not been for appropriate supervision by CSIRO.
- (3) *When it is likely that an invention will not be developed and exploited commercially unless covered by a patent.* In this situation patenting can make a positive contribution to the industrial application of research results. There are many examples given in the literature on industrial innovation in which new technology has been offered freely to all comers, but no firm has been willing to go to the expense of pioneering the new technology, knowing that its competitors will be able to share in the benefits from this pioneering work. Such examples of unused technology can be traced to the fact that expenditure was needed on the development and engineering stage and that no firm was willing to invest its money unless given an opportunity to recoup development costs before other firms were able to share in the benefits. CSIRO now is-

sues 10 or so exclusive licenses each year in order to create an incentive for a firm, or a small number of firms, to undertake the industrial development and application of research results. Some licenses are exclusive for the life of the patents concerned, others are exclusive only for an initial period of two or three years. Each case is dealt with individually and the conditions, so far as we are able, are tailor-made to meet each situation.

- (4) *Where an invention may assist in maintaining or extending the use of Australian products overseas.* A large program of research on woolen textiles is conducted in Australia and it is in the interests of Australia to see that the results of this research are made available to the users of wool throughout the world. In many cases the industrial application of Australian research results can be assisted in overseas countries through the use of patents.
- (5) *Where substantial royalties may be earned, especially from industry overseas.* In general, royalties are earned from CSIRO patents whenever possible. However, the first responsibility of CSIRO is to assist in the development of Australian industry by encouraging the adoption of new or improved technology that has arisen from its research. Attempts to maximize royalty income would often delay industrial application of new and more efficient technology, and hence in the long run be against the public interest. In Australia, CSIRO aims to bring about the widest possible use of its inventions. Ideally, therefore, nonexclusive licensing of patents is the first choice and, to encourage early adoption of new technology, nominal royalties of up to \$A30 annually are generally considered appropriate. When an exclusive license is granted, and one manufacturer is receiving benefits that are not available to his competitors, a commercial royalty is charged.

#### *Foreign Licensing of Patents As Income*

A different set of conditions applies in licensing overseas. In general, the aim is to earn the maximum income possible through royalties, since CSIRO has no responsibility to foreign industry as it has to industry operating in Australia. A substantial, although widely variable, income is obtained from CSIRO foreign patents. An exception is made

when licensing overseas patents from the wool research program that are intended to be used as promotional aids for wool. In these cases attempts to charge high royalties might conflict with the main objective, and lower royalties, or even no royalties, are charged.

In any case, the earning of royalties from overseas licenses must be considered as a side issue in CSIRO. It is only on very rare occasions that the royalties earned from overseas licensing cover the costs of the relevant research. The major benefits from a technological advance go not to the licensor but to the manufacturer, who can use an invention as the starting point for a permanent share of a manufacturing area, whereas the licensor of a patent is, in effect, selling a capital asset and on expiry of the patent obtains no further return.

For Australia to receive the maximum benefit from CSIRO research, its results must be applied to Australian industry. A wide range of benefits results from the application of local research. These include improvements in efficiency of production, a stronger position in competitive export markets, increased employment, larger-scale production, lower manufacturing costs, reduction of imports, and so on. By comparison, the returns obtained from overseas patent licensing are generally of a much lower order.

#### *Development Aids to Australian Manufacturing Industry*

To further assist in bringing CSIRO research results into industrial use, CSIRO has established what we call a development pool. This enables us to provide substantial amounts of money and staff at relatively short notice to undertake development work when a project reaches the development stage. Inevitably, in the financing of a large organization such as CSIRO, the main part of budget planning has to be done nearly a year ahead. The need for development assistance usually arises unpredictably and the development pool has given us in the past few years a flexibility that has been of widespread assistance in bringing research results more rapidly to the stage at which industry can assess the economic value of a potential innovation and take over the final stages of development and engineering.

One of the most serious obstacles that CSIRO has faced in dealing with Australia's manufacturing industries, especially 10 or 20 years ago, has been the lack of experience in industry in handling development work. The introduction into Australia of fully developed technology from overseas has led successfully to the rapid establishment

of modern and efficient manufacturing industry. Important though this source of innovation has been, it does have some limitations, especially as it often does not provide a good basis for building up exports of manufactured goods. In order to export successfully, a country must have something distinctive to offer, such as a new product, or a known product made by a new, improved, or cheaper method. Copied technology will always lag behind best industrial practice and cannot be expected to be the main basis for a manufacturing industry hoping to capture a substantial share of total world trade in manufactured goods.

Until Australian industry undertakes a significant proportion of its own development work, it will not be able to make fully effective use of CSIRO research. At present, foreign industry is the first to apply some CSIRO research results which, were it not for the problems of local development, might have been applied to greater benefit in Australia. The appropriate use of CSIRO patents can assist the adoption of research results, but the application of this research depends in the long run on the ability of the firms concerned to take over development from the stage beyond which it can no further go in the nonmanufacturing environment of a government laboratory.

However, this situation is rapidly changing as a result of the establishment by the Commonwealth Government of financial incentives for expansion of research and development work in private industry. The government has formed the Australian Industrial Research and Development Grants Board which refunds to industry a proportion of the costs of additional research expenditure. In the current financial year payments by this Board to industry will approach \$A12 million.

#### CONCLUSION

Finally, I wish to refer briefly to what I regard as the most difficult problem in the hard path from research to innovation. This is the selection of research projects and management of the research program. The first product of research is not new technology but new information. Some of this information may be useful in the industrial context immediately. Some of it may be one part of what will eventually be new technology made up of many such components. The interesting and valuable study of the I.I.T. Research Institute,<sup>1</sup> under contract

---

<sup>1</sup>*Technology in Retrospect and Critical Events in Science*. Report of Illinois Institute of Technology Research Institute, under contract NSF-C535 to National Science Foundation (December 1968).

to the United States National Science Foundation, shows that in all the examples of major new technology covered in the study, the starting point had been non-mission research. That is, research that had been undertaken primarily to obtain new scientific knowledge, without a specific industrial application in view. While economic analyses are essential in setting priorities between projects in the development and engineering stages, economics has only a minor role in the selection of the longer term research projects from which the major advances are derived.

An example in support of this view is Brown's retrospective study of the atomic absorption project in CSIRO.<sup>2</sup> Brown's analysis shows that a reasonably accurate prediction of the economic importance of atomic absorption could not have been made until at least 10 years after the research had begun, and, indeed, until the project has been several years in the development stage. In doing research aimed at industrial innovation we must take into account that the major advances will usually have their starting point in good basic research, undertaken in an area of relevance to the needs of industry, but without the ultimate application being defined. As the Illinois study shows, the closer the project approaches the innovation stage, the more clearly and narrowly can the aims of the R&D be defined, but correspondingly, as this definition becomes narrower, so does the chance lessen of a new major step forward coming from the work.

There is, as you know, a mass of literature on research planning, but much of it seems to ignore the unpredictable nature of the major technological advance. The paper that I admire in particular for its description of the element of surprise in the path from research to innovation is that of Professor Townes,<sup>3</sup> and I would like to conclude by quoting from his paper.

Mankind consistently errs in the direction of lack of foresight and imagination. We continually underestimate the power of science and technology in the long term. Eminently knowledgeable planners and scientists, in attempting responsibility to make realistic appraisals of research, and facing what is at the time uncertain or unknown, all too frequently fall short in foresight and imagination. The element of surprise is a consistent ingredient in technological development, and one we have great difficulty in dealing with on any normal planning basis.

---

<sup>2</sup>A. W. Brown, "The Economic Benefits to Australia from Atomic Absorption Spectroscopy," *The Economic Record*, Vol. 45 (June 1969), p. 158.

<sup>3</sup>C. H. Townes, "Quantum Electronics, and Surprise in Development of Technology," *Science*, Vol. 159 (February 16, 1968), p. 699.

# Recoupment of Defense R&D Costs in NATO Countries

WILLIAM G. GAPCYNKI\*

## SUMMARY

LEADING NATO NATIONS ARE TURNING to various methods of sharing, with other countries having similar military requirements, the high costs of developing sophisticated military equipment. International cooperative research, development and coproduction programs; foreign military sales programs; the adaptation of military items to civilian use, and the application of levies on sales made to both foreign and domestic customers are among the methods currently being used. Several leading NATO countries, particularly France, the Federal Republic of Germany, the United Kingdom and the United States have adopted procedures for the recoupment of R&D costs by applying a levy, in the nature of a royalty, on sales of hardware or industrial property generated under their research and development projects. The

---

\*Deputy Chief, Patents Division, Office of The Judge Advocate General, Department of the Army; U.S. Representative to the NATO Working Group on Industrial Property; U.S. Member of the Technical Property Committees established in accordance with the Patent Interchange Agreements entered into between the United States and most of the NATO countries.

The opinions expressed herein are those of the author and do not necessarily express the policies of the Department of the Army.

levy may be applied as a percentage of production costs of hardware sold by contractors either to domestic or foreign purchasers or as a percentage of license fees paid for rights to industrial property necessary to produce such hardware. In some instances a government will negotiate directly with another government or international organization to reimburse the originating government a proportionate share of its R&D costs. Efforts to recoup R&D costs have met with varying degrees of success. With a few notable exceptions, however, recovery usually appears to be relatively minor in proportion to their total R&D expenditures.

---

#### INTRODUCTION

AS THE COSTS OF RESEARCH AND DEVELOPMENT SKYROCKET, more countries are turning their attention to means for recouping at least a portion of their expenditures for the development of major military equipment. One means of achieving this end is through the direct sale by the developing government of a technical data package and reproduction rights to a foreign purchaser with potentially large requirements. Perhaps a more common method of recoupment employed by several of the larger NATO countries is the imposition of a levy by the developing government on all sales made by its contractors to third parties of items developed under government contract. Such levies are usually applied to both domestic and foreign customers and apply equally to the manufacture and sale of the end product by the developing contractor, to the sale of technical data, and to the licensing of others to produce and sell. Occasionally, this indirect method of recoupment through the contractor may be short-circuited by direct negotiations between the developing government and a foreign purchaser or licensee. Under such an arrangement the levy is paid directly to the developing government in lieu of payment through the contractor. The amount of the levy paid is usually determined by apportioning the common costs of a specific article to the total number of articles expected to be produced by both parties.

The United Kingdom, the Federal Republic of Germany, and France have long maintained such a policy of recoupment by levy. The United States in recent years has also initiated a policy of recoupment which is still in a state of development. The extent of recovery of costs varies widely among the nations having such a policy. For example, the U.S. Department of Defense attempts only to recover a fair pro



rata share of its investment in the equipment sold, measured by its nonrecurring costs associated with the research, development and production of that equipment. Under French practice, recovery is limited, as a general rule, to 80 percent of the R&D contract costs regardless of the extent of governmental use in proportion to total sales. The Federal Republic of Germany seeks to recover its contract costs plus interest on its investment. The United Kingdom places no limitation on the total amount recovered and, ideally, could realize an amount sufficient to help defray the costs of other and less financially successful research work. Most of the other NATO member countries perform, contract, or otherwise support little or no research and development for defense purposes and accordingly have found no need to establish policy along these lines. Included in this group are Belgium, Denmark, Iceland, Luxembourg, Greece, Portugal and Turkey.

#### RECOUPMENT BY THE FEDERAL REPUBLIC OF GERMANY

The Federal Republic of Germany has a long established practice of requiring its contractors to reimburse the government for development contract costs borne by the government, plus a 6½ percent surcharge, to the extent that the contractor either grants a license to or delivers the development item (or a modification) to third parties for non-governmental use. Under the German procedure, the contractor pays to the German Government either 5 percent of the unit sales price of the developed item or parts thereof or 50 percent of the net license fees where the contractor licenses a third party for delivery to others than the German Government. The amount to be reimbursed includes only those sums received by the contractor (including his subcontractors) under the contract; it does not include the cost of test samples and special tooling delivered to the government, costs incurred by the government such as field tests, et cetera, nor costs under other contracts. The obligation to make reimbursements expires five years after the date of signature of the final report unless otherwise provided in the contract. This final report is a document made jointly and signed by both parties to the R&D contract, indicating that the contractor has accomplished his work. The contractor must automatically report his sales and make payments accordingly. If the contractor can prove inability to compete because of the reimbursement requirements, the German Government will negotiate a reduction in the terms of reimbursement.

German procurement personnel report that the financial results of these provisions have not yet been very substantial. "The total amount recovered by this policy comes to 0.1–0.2 percent of the annual expenditure of the development budget. To date the German Government has never gotten back the entire amount which could be recovered under a specific contract." Insofar as the five-year period is concerned, the experience of the German Government has shown it to be desirable to avoid extended periods of recoupment where possible. In practice, the period of recoupment is adopted by the contracting authorities in accordance with the value of the contract. Thus contracts of minor importance (up to about 10,000 DM) generally provide for a recoupment period of less than five years, whereas contracts of more than 50 million DM provide a period between five and ten years, and contracts on the development of major equipment a period of at least ten years. When development programs are based on more than one R&D contract, care is taken to ensure a uniform period in all contracts including follow-on contracts where separate final reports are requested.

#### RECOUPMENT BY THE UNITED KINGDOM

The United Kingdom also has a well established system for reimbursement of R&D costs. Under Form 6/15A of the series of special contract clauses relating to patents and designs used by the Ministry of Technology, "The Contractor shall not sell otherwise than for the purposes of the Government any articles to the said Design or grant any license to manufacture articles to the said Design without first agreeing with the Authority the sum or sums (if any) which should reasonably be paid to the Authority by the Contractor in respect of such sale or grant having regard inter alia to the amounts paid or payable to the Contractor by the Authority under this contract."

The sum agreed is stated to be a contribution towards amortization of design costs expended by the United Kingdom. The actual amount of contribution depends on the circumstances of the case and particularly on the amount of money for the development provided by the government. A usual figure where the whole of the money for the development has been provided by the government is  $7\frac{1}{2}$  percent of the selling price where the contractor manufactures or  $33\frac{1}{3}$  percent of the money received by the contractor from licensees. These "design recovery levies" do not cease when the amount contributed by the contractor exceeds the development expense of the Ministry of Technology.

The reason for this is that the MOT takes the view that successful commercial exploitation of a design should offset amounts spent on that design and on all R&D sponsored by the government. Business conditions change, and it is rare that a design can be successfully exploited commercially over a long period of years, so that these levies generally cease after a few years. Industry and government are both satisfied that this provision is fair and works reasonably well in practice.

The United Kingdom appears to take a very broad interpretation of the word "design" and their contractors pay the levy on the entire amount of their sales contract without restricting the applicability of the levy only to those elements developed under the original R&D contract. Thus, the levy is applied to the final sales price of the item and may cover major parts or components not originally developed under its government R&D contract. Also the levy may be collected more than once under a sales agreement. As an example, manufacturer A has a non-UK Government sales contract for an aircraft comprising an engine supplied by manufacturer B, a navigation system supplied by manufacturer C and a weapons system supplied by manufacturer D, all developed under a UK Government contract; the UK would then receive levies from the sale of each of the components to A, and would receive another levy on the sale of the entire aircraft by A.

An article in the *London Times*<sup>1</sup> is indicative of the success of the UK efforts to recoup its costs, at least in the field of aircraft engines. After noting that the manufacturer had to pay levies to the British Government for commercial sales of military engines and their civil derivatives, the article noted that in order to overcome commercial disadvantages in meeting foreign competition, the UK Government participated on a selective basis in the launching costs of civil engines. The government contributed a fixed amount leaving the company to bear any excess costs over original estimates. According to the news item, the UK Government had furnished about one-third of the cost of the launching program for five aircraft engines. The UK Government was stated to have "recovered more than its original investment" in one engine and was expected to recover its total investment in the other four engines.

#### RECOUPMENT BY FRANCE

The French Government has an analogous procedure with regard

---

<sup>1</sup>The *London Times*, 23 June 1970, p. 1.

to the utilization of the results of government-sponsored work for commercial purposes. Under its normal domestic contracting procedures the French Government requires that its contractors pay certain fees to the government for the commercial exploitation of the results of the work performed under its contracts. Thus, Article 89 of the General Administrative Provisions Applicable to Industrial Contracts (Title (VI) Decree No. 67-999 of 3 November 1967) provides that unless a contract specifically provides to the contrary, a contractor must pay specified fees to the government for the sale and for the granting of licenses for reproduction to third parties, either in France or abroad, of materials, elements or parts resulting from the work conducted under the contract.

In the case of sales by the contractor of materials, elements or parts resulting from the contract, the fees paid by the contractor to the French Government are based on the sale price of the item FOB and exclusive of taxes. Unless otherwise provided by the contract, the fee in such cases is 2 percent. In the case of the contractor granting rights to reproduce such items to third parties, the fees are based on the amounts recorded in the accounting records of the contractor either as lump-sum payments or percentages of the cost of the materials manufactured. Unless otherwise provided in the contract, the fee in such cases is 30 percent. In either case the total fees to be collected by the French Government are limited as a general rule to 80 percent of the total amount of the contract. In practice, specific contractual clauses might provide for a percentage higher or lower than the 80 percent fixed in general standard administrative clauses.

Under the terms of the contract, the French contractor is obligated to forward automatically each quarter to the authority charged with supervision of the contract a statement of collections giving rise to fees and made in the course of that quarter. Payment of the fees is made by the contractor on receipt of an order to pay issued through the administrating authority. The contractor is further obligated to provide qualified government representatives with the means for verifying the accuracy of the statements furnished. Provision is made for government approval of a reduction or elimination of the fees upon presentation of adequate justification.

In practice, the levy paid by French contractors ranges from 0.5 percent and most frequently falls within the 2-3 percent range. The levy is set by contract administration personnel with the object of recovering as much of the R&D investment as is economically feasible based on a reasonable estimate of the total market that can be reasonably pre-

dicted without at the same time applying such a large levy as to make it economically unattractive for the contractor to enter the commercial market. If the contractor makes no objection, the percentage levy stated in the contract is applied across the board to contractors' sales of the developed item to others than the French government. The contractor may, however, request postponement, reduction or waiver of the levy partially, wholly, temporarily or permanently upon good and sufficient showing that the levy will place him in an economically burdensome position. Thus the levy may, and frequently is, waived for the initial stages of production until the contractor has been able to recover initial production expenses and establish a market. Also, at anytime thereafter the contractor, upon adequate showing, may request and receive a waiver or reduction of the levy either permanently or for a specific period of time. Since the levy is a contractual matter there is no appeal from the decisions of the contract administrator.

Although no precise figures are available, French procurement personnel indicate that on the whole, the percentage of recovery of R&D costs by the government has been quite low, even though in the case of a few items, complete or nearly complete recovery of R&D costs have been achieved.

On occasion some NATO governments have employed a more direct approach in the recoupment of research and development costs. Where the foreign purchaser has potentially large requirements and desires to procure from other sources, the developing government will negotiate with the foreign purchaser for the direct payment of a levy to the government, rather than through the contractor, the amount of such a levy being determined by the requirements of the foreign purchaser in proportion to estimated total production of the item by all parties concerned. Agreements of this type have recently been negotiated by France and the Federal Republic of Germany. Since normally neither the French nor the German<sup>2</sup> governments acquire royalty-free sub-licensing rights to technical data developed under their R&D contracts,

---

<sup>2</sup>"General Terms and Conditions for Development Contracts with Industrial Firms" (ABEI)—Article 14, "Transfer of User Rights to Foreign Countries." Under normal German development contract procedures, the German Government acquires the right to transfer to other NATO countries and organizations the user rights for defense purposes only. In defining these rights, no distinction is made between foreground and background data and inventions and the rights would only be available on the same terms, including royalty payments, as are available to the German Government. This provision would only be applied for the benefit of another NATO government or organization on a reciprocal basis, and since no other NATO government has a similar provision, it has never been used.

this type of direct government-to-government arrangement is usually limited to the direct payment of the levy to the government and, in effect, constitutes the permission of the developing government for the sale of end items or technical data and reproduction rights by the developing contractor.

#### RECOUPMENT BY THE U.S. DEPARTMENT OF DEFENSE

As has already been mentioned, the U.S. Department of Defense has, in recent years, initiated a policy of recouping a share of its investment in nonrecurring costs associated with major defense equipment. "Major Defense Equipment" is defined as those weapons or weapons systems which required, or will require, a research, development, test and evaluation expenditure estimated in excess of \$25 million or total production expenditure estimated in excess of \$100 million.

"Nonrecurring costs" are defined as costs incurred or to be incurred for the benefit of the entire production run, including initial, past, current and future runs, and which are allocable to all units, rather than to those units, if any, produced at the time the cost is booked. Nonrecurring costs include such costs as research, development, test, evaluation, preproduction, facilities, special tooling, special test equipment, production engineering, product improvement, destructive testing, and pilot model production, testing and evaluation.

Department of Defense Directive No. 2140.2, March 15, 1967, entitled "Recovery of Nonrecurring Costs Applicable to Foreign Sales," as implemented by the Armed Services Procurement Regulation,<sup>3</sup> establishes the principles which govern the sale of major defense equipment to buyers outside the U.S. Government whether (1) from U.S. Department of Defense inventories, (2) directly from a U.S. producer, or (3) indirectly from a U.S. producer through the U.S. Department of Defense. The policy also includes the sale of technical data and the licensing of third parties to manufacture the equipment. The policy is mandatory whenever major defense equipment is sold to a foreign purchaser and may be applied to domestic commercial buyers at the discretion of the Secretary of the Department concerned.

The objective of the policy is to recover from non-U.S. Government purchasers a fair pro rata share of the U.S. Government's investment in the equipment sold, measured by the nonrecurring costs associated

---

<sup>3</sup>ASPR 4-110; 7-104.64.

with the research, development, and production of that equipment. The objective is not to recover the total amount of that investment from a single foreign purchaser in connection with a single sales transaction, nor to obtain a profit, that is, any amount over and above the aforementioned fair pro rata share.

For each sale or license agreement, the amount to be reimbursed to the U.S. Department of Defense (DOD) for the nonrecurring costs is determined by dividing the total DOD nonrecurring costs, incurred and projected to be incurred, by the total production quantity of the item, past and projected, including the production quantity for the DOD, and multiplying the results by the quantity involved in each such sale or license agreement. The phrase "foreign sale or license agreement" includes all sales to or license agreements with foreign buyers, including foreign governments and international organizations, whether made through the U.S. Government or directly by U.S. domestic firms.

In accordance with this policy, all DOD contracts for major defense equipment contain one or both of the clauses of the Armed Services Procurement Regulation, ASPR 7-104.6 requiring the U.S. producer to incorporate a specified charge in its sales price of major defense equipment and collect that charge from non-U.S. Government buyers for reimbursement to the DOD on equipment sold or for licenses entered into by the contractor. An analogous policy has been established with regard to the sale to foreign governments of technical data packages by the DOD.

#### RECOUPMENT BY OTHER COUNTRIES

In Canada, consideration is being given to the application of a levy in a manner similar to but more flexible than the procedures employed by other countries but no definite policy has been adopted. The remaining NATO countries, Italy, The Netherlands and Norway appear to have no formal announced policy with regard to recoupment, however they all appear willing to apply such a practice in international cooperative R&D agreements or on a case-by-case basis as a reciprocal measure in sales to foreign governments.

#### RECOUPMENT UNDER INTERNATIONAL COOPERATIVE R&D AGREEMENTS

The application of the concept of recoupment of research and development costs to international cooperative research, development and

production programs is receiving increasing attention by countries entering into such agreements. Provisions to that effect have been incorporated in a few international agreements covering the sale of the results of such programs. Few, if any, of the programs which incorporate provisions for recoupment have as yet proceeded to the point where it is possible to evaluate the effectiveness of the clause. All NATO countries appear to recognize the increasing need for a program of recoupment under international programs and approve, at least in principle, the use of such levies provided they are restricted to sales to nonparticipating countries. Since France, Germany, the United Kingdom and the United States already have established domestic practices in this area, no great difficulties should be encountered in extending these practices in international programs. There appears to be uniform agreement that the imposition of such an agreed levy must be uniformly applied by all participating countries to be effective and to avoid placing any one country in a greater or less favorable competitive position with regard to sales; also the net return from such levies must be distributed among the participating countries in the same proportion as their contribution to the cooperative research and development program. Since France, Germany, the United Kingdom and the United States have standard domestic contract provisions for recouping part of their research costs, precautions should be taken under an international agreement to ensure that these domestic practices are not used to exact a levy on sales to other cooperating governments.

None of the countries reporting appear to have a rigid policy requiring the application of a levy on items developed under international agreements. All countries have a flexible attitude as to the amount of such levy and the extent to which recoupment should be achieved. In general, provisions for levies are appropriate only in programs where production of a specific end item is contemplated as part of the program. They would normally not be appropriate in data exchange or pure research type programs. Also, in view of the experience of Germany and the United Kingdom, it would appear to be desirable to establish a cutoff date for the recoupment.

It is recognized that under certain types of international programs it may be necessary or desirable to incorporate in the end item, a component or part which was developed by one participating government prior to or outside the program. The question as to whether the developing country should be able to apply a levy on sales of that component or part to other participating countries has seldom, if ever,



arisen. In any event it should, of necessity, be negotiated on a case-by-case basis at the time a determination is made as to whether that component or part will be incorporated in the end product of the program. Another means of resolving inequities in national contributions to the cooperative program, particularly when one of the participating countries has previously incurred R&D expenses which are of benefit to the common program, might be found in the increase of that country's share of the levies paid by nonparticipating countries or individuals.

## STUDENT PAPERS

---

By making available student papers, students will receive an incentive and our readers will appreciate the evidence of scholarly development in the fields of interest. These papers are carefully reviewed by the Editorial Committee and other specialists, and helpful suggestions are made to the students as part of the educational function of *IDEA*. The Research Institute invites educational and research institutions to submit informative student manuscripts on the patent, trademark, copyright, and related systems.

### Computer Program Protection in Three British Commonwealth Countries: What Can U. S. Learn?\*

LAURENCE R. LETSON

AS A PRELIMINARY TO the investigation of the patent protection available on computer programs in each of the three most highly industrialized British Commonwealth nations, a definition must be set forth in order to fully handle the subject matter of this disclosure.

A computer program is defined and used in this paper in the context

---

\* This paper was submitted in partial fulfillment of the requirements for a course in Legal Writing at The National Law Center of The George Washington University.

The author is an employee of International Business Machines Corporation, and the statements, opinion or conclusion, herein, are those of the author and not necessarily those of International Business Machines Corporation.

of that which defines an intellectual concept embodying a conclusion based on a precise or mathematical premise and line of reasoning. When a narrower sense of program is meant direct reference to that instance will be made.

To discuss in detail the protection available for a very specific set of detailed step-by-step instructions is relatively simplistic, since avoidance of such detailed steps is readily available by reprogramming or rewriting and therefore protection afforded by any means to only that specific set of instructions is comparable to copyright protection and not of significant value as a patent.

One significant question raised by the search for an answer to the question, "Are computer programs patentable in the United States?" is the question "What have the three most highly industrialized countries of the British Commonwealth done with respect to patent protection for computer programs?" Is there a trend? If there is a trend, are their decisions useful in addressing the question in the United States, notwithstanding the differences in the several statutes governing patentability.

#### UNITED KINGDOM

In the United Kingdom, Section 101 of the Patent Act of 1949, defines what is a patentable invention. Section 101 of the Patent Act is reproduced in the margin in part.<sup>1</sup>

Section 101 of the Patent Act of 1949 defines those categories allowed within the exception of Section 6 of the Statute of Monopolies for:

Letters Patent and grants of privilege for the term of 14 years or under hereafter to be made, of the sole working or making of any manner of new manufacture within this realm, to the true and first inventor and inventors of such manufactures which others at the time of making such Letters Patents and grants shall not use, so as also they be not contrary to the law or mischievous to the state. . . .<sup>2</sup>

These two statutory provisions provide the authority under which patents are issued in the United Kingdom and also limit that for which

---

<sup>1</sup> 101.—In the act, except where the context otherwise requires, the following expressions have the meanings hereby respectively assigned to them, that is to say— . . . "invention" means any manner of new manufacture the subject of letters patent and grant of privilege within section six of the Statute of Monopolies and any new method or process of testing applicable to the improvement or control of manufacture, and includes an alleged invention; . . ."

<sup>2</sup> The Act of the twenty first year of the reign of King James, the First, chapter three, intituled "An Act concerning monopolies and dispensations with penal laws and the forfeiture thereof."

a patent may be issued. The invention of Section 101 is any manner of new manufacture or new method or process of testing applicable to the improvement or control of manufacture. To secure a patent for a computer program it must be "fitted" into one of these two categories of invention.

Since it appears that the processing of data and therefore the definition of the process involved does not readily fall within "... method or process of testing . . ." the effort of the Patent Appeal Tribunal of the United Kingdom has been to find a position under "... manner of new manufacture." This is brought clearly to the fore by the decision in *Slee and Harris' Applications* (1966) R.P.C. 194. In this case the Superintending Examiner held that the invention, relating to a method of operating a computer which performed iterations characterized particularly by the process where one iteration was initiated before the previous iteration was completed, was patentable provided that the form of the claim was acceptable. The form which was acceptable to the United Kingdom Patent Office was one directed to a computer when programmed in accordance with the program technique disclosed to be *Slee and Harris'* invention. The United Kingdom Patent Office further gave guarded approval to a claim which was directed to the means carrying the program (paper sheet or magnetic tape) and which was used to control the operation of the computer, so long as the process performed was novel, useful and inventive.

Not long after the decision in *Slee and Harris' Application* which was directed toward the means carrying the program, two more recent cases were decided by the Patent Appeals Tribunal. They are *Gevers Application* (1969) F.S.R. 480 and *Badger Company, Inc.'s Application* (1969) F.S.R. 474.

In *Gevers Application* the Patent Appeal Tribunal held that the claim was for a piece of machinery which was constrained to function in a certain way and produce a certain result by reason of perforated cards being placed in it. The substance of the claim was directed toward the formation of a file for wordmarks where certain letter combinations and certain letters were replaced by other letter combinations and letters in accordance with predefined conditions. This allowed a search of the wordmarks to be made rapidly in such a way that all possible spellings of the wordmarks and pronunciations of the wordmarks would be found on a search for a particular word.

The Patent Appeal Tribunal framed the issue in such a manner that the question was raised whether a claim to an apparatus constrained to operate in a particular manner was in fact a "manner of manufacture."

By characterizing the claim as directed to a manner of manufacture the claimed invention is then an invention for which patent may be issued under Section 6 of the Statute of Monopolies. Further it may be acceptable under Section 101 of the Patent Act as a manner of manufacture. It is stated in *Gevers Application* supra:

In the light of these cases [*Badgers' Application* infra, et al] it seems to be quite impossible to say that the proposed claim here or a claim along these lines to data processing apparatus which is, by reason of the presence in it of certain perforated cards giving operating instructions, constrain to function in a particular way and produce a particular result, is not a manner of manufacture. . . . Whether it is new and whether it is obvious are, of course, entirely different questions which will no doubt have to be decided at some time, but the only matter before the Appeal Tribunal today is, is . . . it . . . not a manner of manufacture under Section 101.<sup>3</sup>

By addressing only the question of whether the claim as drafted to a data processing apparatus is a manner of manufacture, and finding that it is, and completely overlooking where the invention lies, the Patent Appeal Tribunal has given sanction to the claiming of a process primarily embodying mental steps or intellectual in nature by couching the claim in hardware terms.

The second case recently decided in the United Kingdom is that of *Badger Company, Inc.'s Application*, supra. In *Badger's Application* the claim appealed was directed to a method of mechanically designing and forming a visible drawing illustrating piping systems interconnecting different operating units where the basic data on the operating units and their positions were provided to the computer along with other constraints on the positioning of the interconnecting piping. The sequential designating of a route for a particular pipe acted as a constraint on all subsequent located pipes.

The specification of the *Badger Application* specifically acknowledges that the mechanism required, i.e., computer and data converter or plotter, were known prior art devices and thus *only the manner of operating the computer* was disclosed as novel. The claim directed to the method as described above was rejected as unpatentable but suggestions as to possible claim form which would be acceptable were made by the judge. Two such suggestions were:

- (a) A process for conditioning the operation of a computer and an associated plotter of known types to produce the layout of a composite system . . . , and
- (b) A computer of known type arranged to produce a sheet suit-

---

<sup>3</sup> 1969, F.S.R., 480, 486.

able for conversion into a visible plan on submission to a plotter of known type, the arrangement being such that data procured, etc., etc., and suitably tabulated and coded is introduced into the mechanism together with (constraining factors) . . . and operated upon in such a manner as to locate . . . interconnections in sequence and impose each such interconnection as an additional constraining factor and the location of each successive interconnection, collecting the computer data, etc., etc.<sup>4</sup>

Upon remand to the Patent Office for further proceedings, the application was eventually allowed with claims of the general form set forth in subparagraphs *a* and *b* above.<sup>5</sup>

A close analysis of the decision in this case shows that, in the United Kingdom, one form of the claim is clearly not allowable and another form of the claim is allowable where the inventive step or invention lies only in the non-hardware or intellectual portion of the claim and where the claim must be directed to hardware to satisfy the requirements of Section 101 of the Patent Act and Section 6 of the Statute of Monopolies.

The Report of the Committee to Examine the Patent System and Patent Law (herein referred to as the Banks Report) concludes, with respect to the present position of patentability of computer programs that it is uncertain whether valid patents can be obtained for computer programs as no case has thus far gone before the High Court with respect to this issue. The present practice of the Patent Office is to refuse the grant of patents for computer programs expressed as such. The Patent Office raises no objection to novel methods of programming a computer to operate in a specified way or for computers so programmed. Further no objection is raised to tape or other similar mediums having recorded on its programs to control a computer or to operate a computer in a desired specified way. The position of the Patent Office is further clarified and the reasoning behind the Gevers and Badger cases is explained further by the statement from the Patent Office that:

It is to be noted that the Patent Office will refuse to proceed with an application only when it is clear that on no reasonable view could the invention be said to be within the definition [in the Patent Act which states that patents may be granted only for inventions which are either manners of new manufacture or methods of testing applicable to the control of manufacture]. . . .<sup>6</sup>

---

<sup>4</sup> 1969, F.S.R., 474, 477.

<sup>5</sup> *Ibid.*, 477.

<sup>6</sup> The Report of the Committee to Examine the Patent System and Patent Law, para. 473.

The above quoted paragraph follows the decision in *R. v. P.A.T. ex parte Swift and Company* (1962) R.P.C. 37. In *Swift's Application*, the court took the position that the question of patentability rested not with the Patent Office but was a matter to be decided by the High Court. The High Court was of the opinion that "[the Comptroller and the Tribunal's] function is only to refuse to allow applications to proceed which on no reasonable view could be said to be within the gambit of the Act."<sup>7</sup>

The Banks Report states that it is open to doubt whether or not there can be a distinction between a program invention claimed in a roundabout manner and a claim for the program itself.<sup>8</sup>

The Banks Report further recommends that computer programs not be afforded patent protection in any form.<sup>9</sup>

### *United Kingdom Summary*

It appears from the foregoing cases and the Banks Report that if a claim to a programming invention is drafted in such a manner that it is in hardware form, embodying in it a prior art computer programmed in accordance with the invention, then this claim will satisfy the *form* requirements of the United Kingdom Patent Office. It appears the reason that the Patent Office requires a format relating to hardware is based upon their inability to place a programming invention within any of the categories specified by Section 6 of the Statute of Monopolies or Section 101 of the Patent Act, which defines inventions which are patentable. The Patent Appeal Tribunal has adopted form requirement in an effort to resolve a question which has only been partially addressed. The entire question of patentability of computer programs will not be answered in Great Britain until such time as a consideration by the High Court of the question of patentability of computer programs and the question has been considered whether the claiming of an old prior art mechanism operating in a new manner under the control of a computer program lends sufficient novelty to the claim to be patentable. An alternative to the above is legislative grant or denial of patentability to programs. The judge in *Badger's Application* specifically side-stepped the question of novelty residing only in the operation of the apparatus being claimed as an apparatus. In view of this doubt, it

---

<sup>7</sup> *Ibid.*, para. 217.

<sup>8</sup> *Ibid.*, para. 417.

<sup>9</sup> *Ibid.*, para. 487.

is a rather tenuous position for one to take if he asserts that valid patents are obtainable in the United Kingdom on computer programming inventions. At best, one may safely say that program patents have been issued in Great Britain but their validity remains to be determined before the High Court. I believe that the High Court, when a proper case comes before it for hearing, will find that where the novelty lies in the programming technique that a claim to an old machine which operates in a specific manner will not have patentable novelty lent to it by the novel programming technique and will be invalid. It is entirely possible that the phrase "new manufacture" may well be interpreted by the High Court to include such inventions as programming inventions but at least for the present it is the opinion of the lower tribunals that that phrase does not encompass programming inventions and therefore the programming inventions are not patentable when claimed as a program per se.

#### CANADA

There having been no programming cases or program oriented cases that have been decided, the Patent Office of Canada has promulgated guidelines governing the consideration of subject matter to determine whether it is nonstatutory or not. Section 2 (d) of the Canadian Patent Act provides that patents may be issued for inventions which are in the classes of "art, process, machine, manufacture and composition of matter." At first glance it would appear that computer programs neatly fall within the process which is considered statutory subject matter in Canada.

Within the guidelines there are two specific categories relating to computer programs which are listed as unpatentable. These two categories are . . . :

- (f) a method, process or scheme principally intellectual in character, or a product or result of such method, process or scheme, is unpatentable, and . . .
- (i) a program, algorithm, or set of instructions should cover the operation or use of a computer or any other device, rules for games and the like or a method of its establishment, is unpatentable.<sup>10</sup>

Under examples of unpatentable subject matter, computer programs and software are specifically excluded from patentability and under

---

<sup>10</sup> Canadian Patent Office Notice, Non Statutory Subject Matter, Section 2 (d).



examples of patentable subject matter computer hardware is specifically enumerated. In the Preamble to the Office Notice, above, it is stated that the substance of the claimed subject matter should be looked to rather than the form to determine whether statutory subject matter is present or not. This appears to be a distinct departure from the position taken by the Patent Appeals Tribunal for the United Kingdom.

The case which is probably most in point in Canada is *Lawson v. Commissioner*, 62 C.P.R. 101, (1970).

*Lawson v. Commissioner* dealt with the method of subdividing land, wherein, the plots were in the shape of alternately reversed champagne glasses, thereby staggering the large portion of the plot and placing the maximum square footage into one portion of the plot and still leaving access to the property from both a street and alley. The Examiner and the Exchequer Court of Canada held that the subject matter was not statutory under Section 2 (d) of the Canadian Patent Act because an art or process, to be patentable must be some manual, chemical or physical effect to transform or reduce something to a different state of thing. In this case there was no such act or effect which transformed the land into anything but the same land. The court felt that the subject matter outlined and claimed was that which fell within the skill of a surveyor, conveyancer and land developer and since they were within the professional skills they were not patentable. Further, the court held that the subject matter was not an art or manufacture within the meaning of the words in Section 2 (d) of the Canadian Patent Act and what was being claimed more approximated a plan or scheme. A plan or scheme is not patentable in Canada and is not readily open to argument. The Exchequer Court felt that the United States statute on patents being *in pari materia*, so far as statutory subject matter is concerned, is more controlling than Section 101 of the Patent Act of 1949 in the United Kingdom due to the difference in defined patentable inventions.

Gordon F. Henderson, Queens Counsel, in a speech distinguishes between a program process and a program technique. "The program process is defined as including (1) a plan or algorithm setting out the problem in logic form, (2) a sequence of instructions which reduces the problem to a sequence of simple tasks that are within the capability of a particular computer and (3) the placing of the program language steps on a suitable medium to actuate the machine. The second two steps of the program process are known in the prior art and as such could not lend any patentability to the program process. Any novelty supporting the patentability of the program process would then, of necessity, fall within Step 1 and as Step 1 is a purely mental act would fall outside the

present bounds of Canadian Law as far as patentability is concerned."<sup>11</sup>

Similarly, a definition of program technique was a concept relating to a program which will enable the computer to operate in a particular unexpected manner in the solution of a program or processing data. The speaker felt that a program technique defined in the form of a claim relating to the control of a computer apparatus in an unexpected way could give rise to a valid patent in Canada. The basis of the invention and the patentability was the unexpected operation of the apparatus under the control of the program.<sup>12</sup>

One problem in this distinction appears to be that in order for the apparatus to solve the problem in accordance with the constraints and conditions set up by the program the apparatus must operate in a manner which is *not* unexpected and therefore there is *no* unexpected operation to support invention or patentability.

The speaker further states that the law will not protect a process or method which is entirely mental or intellectual steps but will grant protection to the process which is a combination of physical and mental steps so long as the novelty does not reside in the mental steps.<sup>13</sup>

The reason that a patent may be granted for a method which embodies physical steps and mental steps where the novelty lies in the physical steps is that there is an act upon something physical resulting in an end product which is different or changed from that which was originally acted upon. This distinction between mental steps or an intellectual process not being granted protection and the physical process being granted protection is that a process must have a substrate or substance to act upon and a program process or algorithm has no such substrate or substance. It is felt that a solution to this seemingly improper interpretation may be to consider data as a substance and data as a vendable product thereby giving something to be acted upon to the computer and receiving from the computer something which has been "manufactured or processed and therefore is vendable and is a marketable commodity."<sup>14</sup> If such a characterization is given to data it is entirely possible that the Canadian Patent Act would encompass the patenting of computer programs and even algorithm processes would be patentable. So long as the data is considered only as an arrangement of printed matter and not a raw material or product then the algorithm

---

<sup>11</sup> "The Patentability of Computers, Computer Systems and Programs" by Gordon F. Henderson, Q.C., Speech delivered at the Conference on Computers in the Law, Queens University in Kingston, Ontario, June 3, 1968.

<sup>12</sup> *Ibid.*

<sup>13</sup> *Ibid.*

<sup>14</sup> *Ibid.*

processes and computer programs would not be patentable under Canadian Patent Law.

Some patents have been issued on a case-by-case basis as to both systems and processes relating to computers.<sup>15</sup>

Mr. Henderson specifically feels that, notwithstanding the position of the Patent Office of Canada, computer programs should be patentable. His primary position appears to be that data is a raw material and the processed data is a product and that as such they should fall within the present patent statute and should be patentable as any other process of manufacture.

### *Canadian Summary*

Canada does not appear to be progressing toward the patentability of programs but rather regressing away from such a position. There is no firm decision on the point other than the Patent Office guidelines which, of course, are subject to change and revision in view of the developing case law. However, there are no patent cases in point with respect to computer programs and only conjecture based on similar and arguably analogous cases may be the basis for a conclusion. The action of Great Britain has had little or no effect on Canada as they tend to interpret United States cases with equal or more authority than the British cases. It therefore appears that programs and program processes in Canada are not at present patentable either per se or in apparatus oriented form.

### AUSTRALIA

The position of Australia with respect to the patentability of computer programs is probably the clearest and is delineated in three cases decided on appeal from the Examiner.

The first, *N. V. Philips' Gloeilampenfabrieken*, 36 Official Journal of Patents, Trademarks and Designs 2392, (1966) dealt with the designation of data locations in a storage according to a set of rules. The claim is reproduced in the margin.<sup>16</sup> The Hearing Examiner held that

---

<sup>15</sup> *Ibid.*

<sup>16</sup> "An electronic computer comprising in combination a directly accessible storage, an indirectly accessible storage, and a control circuit permitting block transfers of information from the indirectly accessible storage to the directly accessible storage, in which consecutively numbered locations of the indirectly accessible storage are arranged in spaced disposition in said directly accessible storage."

under the holding of *British United Shoe Machinery Company, Ltd. v. Standard Rotary Machine Company, Ltd.* (1918), 35 R.P.C. 33, a scheme was not patentable. The programming of a computer is in the nature of the scheme for the use of the computer and so long as the claim is in the form of an old apparatus to be operated in a particular way, the novelty being the mode of operation or in the constraint placed upon the apparatus for its operation, the substance of the claim was a scheme of operation and under the *United Shoe* decision was not patentable.<sup>17</sup> The spacing of the data in storage was not of a physical character and furthermore was known in the prior art and thus was not novel.

The Australian Hearing Examiner indicated that he was well aware of the Divisional Court's decision in *Swift's Application* (1962) R.P.C. 37, but that a decision by the British Patent Office, although it should be considered as carrying great weight, could not be controlling unless exactly the same issues and objections had been considered in the British Patent Office.

In the present case the counterpart British application had been accepted with a claim identical to the one reproduced in the margin, *supra*, and was ultimately rejected in Australia.

The Australian Hearing Examiner appears to have observed the substance of the claim and applied rules of novelty to the claim to defeat it rather than trying to rely on a statutory subject matter rejection. His decision is buttressed by the finding that a computer program is a scheme of operation of the program and is not patentable under the *United Shoe* decision.

The second case bearing on the issue is the *Application of Texas Instruments, Inc.*, 38 Official Journal 2846. The *Texas Instrument* case dealt with a method of processing seismic traces to determine subterranean features. The claim in issue is reproduced in the margin.<sup>18</sup> The seismic traces were reduced to data and the data manipulated by

---

<sup>17</sup> 36 Official Journal 2392, 2393.

<sup>18</sup> "A method of processing seismic traces obtained by geophysical exploration to indicate the presence, inside a predetermined time delay range, of signals in each trace having a time delay with respect to signals in another trace, wherein each trace is a function of its spatial origin in relation to the spatial origin of each other trace, comprising the steps of: (a) weighting each trace in relation to each other as a function of their respective spatial origins, (b) time shifting each trace in relation to each other as functions of their respective spatial origins and the predetermined time delay range, (c) and compositing all the weighted and time shifted traces to produce a composite output indicative of the presence, inside the predetermined time delay range of signals in each trace having a time delay with respect to signals in another trace."

mathematical operations and the end result was then interpreted to determine subterranean features. The issue in the *Texas Instruments* case was neatly stated as "The claim is directed to a method of processing information to obtain more information, and the question is whether such a method may be deemed to be a patentable invention."<sup>19</sup> The Hearing Examiner looked to the substance of the claim and determined that the applicant was attempting to get Letters Patent to a method of making sense out of seismic information and was essentially trying to get protection for a method of solving a mathematical problem. If a new machine was invented to solve the mathematical problem it would clearly be patentable, however, the method of solving the problem is not patentable whether done by a live mathematician or a mechanical computer.<sup>20</sup> The claims to the method of processing the seismic traces were denied patentability.

The third case bearing on the issue is that of the *Application by the British Petroleum Company, Ltd.*, 38 Official Journal 1020. This application is the Australian counterpart of the *Slee and Harris' Application* in the United Kingdom, *supra*. As discussed before, the invention dealt with partially simultaneous iterations to speed the solution of a matrix problem. In the specification there were no electrical or mechanical details disclosed with respect to the apparatus and it was stated that it could be performed on known computers.

The Hearing Examiner stated that in addition to falling outside the provisions of the Statute of Monopolies, Section 6, patent grants could not be made for inventions which would be mischievous to the state. To spend a million dollars on a computer and then be deprived of its efficient use because the program which would be most efficient was patented and therefore he would be prohibited from using it, surely would be mischievous.<sup>21</sup>

A claim to a computer being so arranged so that it automatically performs a specified function is ambiguous since it does not tell how the arrangement is carried out nor how the portions of the computer interact to function as the claim would require. Further, such a claim would not be allowable in this case because the application does not disclose any electrical or mechanical details but only the mathematical procedure to be carried out. Thus the argument that this computer when operating in accordance with the disclosed invention is a new and different computer from any other previously known computer is not a

---

<sup>19</sup> 36 Official Journal 2846, 2848.

<sup>20</sup> *Ibid.*, 2849.

<sup>21</sup> 38 Official Journal 1020, 1021.

sound contention since there is no showing in the disclosure that this was in fact a new computer.<sup>22</sup>

The Examiner addressed several of the different claim forms which had been presented to the British Patent Office but were not presented to the Hearing Examiner in Australia. It was concluded that an effort to claim the tape, be it magnetic, paper or some other type, with data arranged on it, such as holes in the tape, the holes corresponding to words and information, the words not making the tape patentable, was ineffective to secure a patent. For support, the Examiner cited an earlier case dealing with the patentability of playing cards where the characters on the playing cards were different from those known in the prior art but that the structural form of the cards themselves were essentially identical to the prior art cards. The question was whether the changes in the characters was sufficient to justify the issuing of a patent. The Hearing Examiner deferred to the judge which heard that case insofar as inventiveness and the fact that the card deck was a manner of manufacture, then addressed the point of novelty and conceded that where the novelty lie solely in the change of characters this would not give rise to patentability. *Cobianchi's Application* (1953), 70 R.P.C. 199.

The Examiner then found that *Cobianchi's Application* was controlling with respect to the *British Petroleum Application* and disallowed the claims.

### *Australian Summary*

In Australia, there does not appear to be a way under the present Patent Act to secure a patent on a computer program. The process steps themselves when disclosed and claimed as a series of instructions for controlling a computer are not acceptable as they form a scheme of operation and are not patentable under the decision of the *British United Shoe* case. Where the invention is claimed as an apparatus operating in a particular manner or an apparatus arranged in a particular manner to perform a specified function and no new and inventive apparatus is disclosed the application is denied on the basis that all the novelty lies in the mental or intellectual steps required for operation and control of the computer. When an attempt is made to claim the invention in the form of a control means, i.e., tape, cards, etc., the

---

<sup>22</sup> *Ibid.*, 1022.

configurations of the data and instructions on the tape, although differing from all prior art forms of data and instruction configurations, are not allowable as printed matter is not allowable, and the data arrangement on the control means is considered analogous to printed matter.

Although Australia does not appear to place all the emphasis upon the lack of statutory subject matter, the considerations of statutory subject matter and novelty are combined to defeat patent applications embodying a programming invention. The Australian Patent Office appears to look not at the form of the claim, as is the case in the United Kingdom, but rather to the substance of the claim and does not choose to ignore the specification and what the applicants have disclosed as their invention.

IS THERE A TREND IN THE THREE MOST HEAVILY  
INDUSTRIALIZED NATIONS OF THE BRITISH COMMONWEALTH  
TOWARD THE PATENTABILITY OF COMPUTER PROGRAMS?

The United Kingdom to date has issued patents on what are, essentially, purely programming inventions but have restricted the claims to the form of an apparatus or structure which operates under the constraints of the programming invention or structure that contains the programming invention carried thereon and, steadfastly refuses to issue patents which claim the program as a program per se. Doubt has been expressed as to the validity of these patents in view of the fact that no decision has been rendered by the High Court on whether program inventions meet the statutory requirements so far as subject matter is concerned.

The Canadian position appears to be that of administrative decision that programming inventions are not patentable in any form regardless of the manner in which the invention is claimed. Again it is difficult to determine the viability of the Patent Office guidelines in view of the fact that no case in point has been heard by the courts and the only controlling decisions at present in Canada are cases which bear some possible analogy to the problems in computer programming and the Patent Office guidelines. It would be relatively safe to say that for at least the present no valid patents may be secured on a programming invention in Canada under the present patent law until such time as data is held to constitute a raw material or product within the meaning of the Patent Act.

Australia has combined the statutory requirements as to subject

matter and a consideration of novelty to deny patent applications on programming inventions and their position appears to be the most thoroughly considered position of any of the three countries considered herein.

Precedents in Australia are much more commonly followed by the United Kingdom and Canada than are the United Kingdom decisions followed by Australia, since the statutory subject matter requirements of the United Kingdom are differently stated than those in Canada and Australia. Further, there is great reluctance on the part of Australia to follow United Kingdom decisions and Canada specifically defers to the United States statute and United States cases in view of the two statutes being *in pari materia*. It remains to be seen whether the Canadian Patent Office and Canadian courts will follow the move by the CCPA in the United States in granting patents to programming inventions in view of their holdings that a process requires something to be acted upon to yield something different and considering that data is not a raw material or product.

One can readily see from the foregoing that there is a present trend, albeit not well defined. The trend is away from the granting of patents for programming type inventions in the three most highly industrialized countries in the British Commonwealth. The only exception to this trend is the Great Britain position of granting patents for hardware claims, and even there, there is doubt expressed as to the validity of such patents.

CAN THE UNITED STATES PROFIT AND LEARN FROM THE  
TREND AND DECISIONS IN THE UNITED KINGDOM, CANADA, AND  
AUSTRALIA WITH RESPECT TO COMPUTER PROGRAMMING?

In view of the differences in the statutory requirements between the United Kingdom and the United States and also the divergent positions taken by Australia and Canada with respect to the United States' position, it is difficult to see that the Court of Customs and Patent Appeals will secure any substantial guidance from considering the decisions of any of the three countries discussed. Further, it appears that the three countries are all substantially behind the United States in considering the issue and that a more complete consideration, albeit not necessarily more rational consideration, of the issue has been conducted in the United States Patent Office, and Court of Customs and Patent Appeals. It therefore appears that the United States may be



leading rather than trailing the other three countries in addressing the issue. Further, it appears from the decisions of the United States Court of Customs and Patent Appeals that little, if any, deference is shown to foreign decisions in the field of patents and therefore the changes of any substantial assistance to the CCPA coming from the decisions of British Commonwealth nations is negligible.

Notwithstanding the lack of identity of the statutes of the several countries, the apparent disregard of foreign decisions by the Court of Customs and Patent Appeals, and an apparent lead, the United States Courts have an excellent opportunity to profit from the decisions of these three countries.

The United States Courts, District and Supreme, have not yet had the opportunity to address the issue of computer program patentability. When the District Courts do consider the question, their result may be entirely opposite to that position taken by the CCPA. The District Courts historically have taken a harder line on borderline questions than has the CCPA, when they considered the same or similar questions. Therefore, it is entirely within the realm of possibility and probability that some, if not most, of the District Courts' computer programming cases will be decided based on the nonpatentability of computer programs. If this is the case, attempts will be made to secure Supreme Court decisions on the issue in view of the conflicting decisions between circuits and the CCPA. At the time the District Courts are considering the question, there will be a complete reappraisal of the question of program patentability and a close consideration of the basis upon which the CCPA rested their results. At this point the decisions, judgments and reasoning in other highly industrialized nations of the world should be considered and used as a basis for the decision in either a District or an Appeal Court in the United States.

Close attention should be paid to the decisions in the United Kingdom and Australia. These decisions provide a basis and reasoning which, although they have not been appealed to the High Courts in each country, are at present the controlling law in each country. These decisions need not be blindly followed as precedent, but they should serve as a summarization of arguments and considerations.

The decisions in some of the United States' cases seem to come to the same results as the British cases although the reasoning is not the same or even analogous.<sup>23</sup>

It appears that if the question of patentability of computer programs

---

<sup>23</sup> *In re Bernhart et al.*, 163 U.S.P.Q. 611, U. S. Patent 3,519,997.

is to be answered in the negative by District Courts or Appeals Courts, the reasoning and logic of the Australian decisions will probably be more closely followed than any other decisions decided at this time. The concept of claiming a programming invention as structure where little or no hardware is disclosed and merely claiming a prior art device arranged to operate in a particular and novel manner will be probably rejected as not patentable under 35 U.S.C. 101 and 102, where the novelty of the claim lies solely in the manner of operation or more specifically in the control of the apparatus by computer program.

Further, a consideration of the Australian rulings with respect to schemes of operation of the computer may be extended to a claim directed to the method of operating a computer in the United States. In view of nonpatentability of schemes under the Australian law and the holdings in the United States with respect to methods of doing business, it appears the two are analogous.

When considering whether the program expressed as a program per se would be patentable, the considerations return not only to the United States decisions denying patentability to literary works and intellectual processes but also to consideration of the Australian decisions with respect to the patentability of intellectual matter and mathematics. These decisions provide an additional basis, if the courts so desire to use it to deny patent protection to computer programming inventions.

Although the statutes of the respective countries and the United States are not in exact accord, the overall basis for the granting of patents and the material which have been held to be patentable in the past is very, very close throughout the four countries.

The United Kingdom is in a position where it can go either way. It can reaffirm the present position that form of the claim is determinative and thus programmed inventions are patentable if claimed in a satisfactory form, or it may easily decide that form is not determinative and that substance controls, and reverse the present holdings resulting in the nonpatentability of programs in the United Kingdom.

Canada, due to the wording of its statute usually defers to United States decisions if there are some on the point but has chosen not to follow the United States decisions on this point.

Australia so far has taken a relatively hard nosed approach to computer program patents and where there is a reason which can be used for not following a decision in another country they choose to reject the other country's decision and decide the case anew in Australia. However, if the United States Supreme Court were to decide that computer

programs are not patentable, the Australian High Court may use the reasoning of the United States Supreme Court to buttress the present Australian position. The Australian courts would probably distinguish any United States cases leading to the conclusion that patents are allowable on computer programs in view of the differences in the statute and their interpretation of patentable subject matter.

In summary, the judiciary and patent bar of the United States cannot blindly ignore the positions of other highly industrialized countries when considering the question of patentability of computer programs. The issue, although some feel the battle is over in the United States, is in no sense settled or dead and will, in all probability, be revived in the near future for a complete reappraisal. The United States patent bar and judiciary would be remiss not to draw upon the reasoning, considerations, and decisions of other countries addressing the same question in attempting to find the correct answer to the patentability of computer programs. The United States can and must learn and gain from the considerations and bases of these decisions in these other countries notwithstanding the fact that the United States Court of Customs and Patent Appeals has continually reviewed the question of program patentability.

The Court of Customs and Patent Appeals has been an activist court and in favoring applicants for patents has changed and extended the law. The CCPA may have overextended the law and if so it will require a retrenching. District Courts, not being as activist and faced with infringement situations and the facts and equities presented by the alleged infringer, will have to address the broader public policy issues presented by program patentability, and may arrive at a position contrary to that taken by the CCPA. In arriving at any such position, the District Court should benefit from the rationale and holdings of the courts of these three countries.

In all the countries discussed the question of program patentability has not been decided by the highest court of the country, so the position of any of these countries is subject to change.

## SELECTED TRANSLATIONS

---

From time to time, in this section, we make available to our readers translations of original, distinctive or outstanding articles, reports or notes relating to The PTC Research Institute's fields of interest.

# Scientific and Technical Development, the Monopolies, and the Patent System\*

YU. A. SERGEYEV and N. YU. STRUGATSKAYA

### INTRODUCTION

IN THE HANDS OF THE LARGEST AMERICAN MONOPOLIES the patent system has become an important tool in the competitive struggle and economic division of the world capitalist market and spheres of influence. This is why the study of the patent system is taking on important significance for its own sake in the complex of the problems of contemporary capitalism. An analysis of the structure, dynamics, and

---

\*Reprinted from the Russian monthly research journal, *SShA: Ekonomika, Politika, Ideologiya* (Moscow: Institute of U.S. Studies, USSR Academy of Sciences; April 1971). Translated from the Russian by Joint Publications Research Service, U.S. Department of Commerce.

scale of the issuance of patents in the United States makes it possible to determine the most recent trends in the development of its productive forces, the pathways of evolution of scientific and technical developments, and of their introduction into production, as well as to predict in advance the direction of the expansion of exports by American monopolies in the struggle for sales markets.

#### HOW IS A PATENT OBTAINED?

The 1952 patent law, which was the result of the development of previous patent laws and the 1955 patent regulations,<sup>1</sup> is now in effect in the United States. Throughout the country's entire history, patent law has always been regulated by Congress. This fact indicates the great importance which is given to the patent in the United States.

Under the law, a patent may be obtained by "anyone who invents or discovers a new and useful method of manufacturing a product, a machine, an article, or a combination of substances, or any new and useful improvement of them" (Paragraph 101 of the United States patent law). The law also envisages the issuance of patents on the external shape of an industrial article, and these are called design patents.

As distinguished from the patent laws of most capitalist countries, one peculiar feature of the United States patent law is that patents can be issued for any new substances, including those obtained chemically, as well as on new varieties of plants produced through cultivation. This provision of the legislation does not extend to plants that reproduce by means of tubers or plants that exist in a wild state. A patent on a plant may be obtained by any inventor, and a foreign national may obtain it under the same conditions as a United States citizen.

The law states that a proposal may be acknowledged as an invention if it possesses two essential characteristics: novelty and usefulness. But the latter criterion is not restricted to the limits of commercial feasibility alone. Newness can be determined not by the date when the application was submitted, but by the time when the invention was actually created. It is not considered new and the patent is not issued if information on it has been published in the United States or abroad, or if its discovery has been used or sold in the United States for more

---

<sup>1</sup>The patent regulations consist of a collection of normative and other materials that regulate in detail the procedure for examination of applications.

than one year before the day when the application for the patent was submitted.

The validity of the patent is 17 years from the date of issuance. In the United States there is no annual payment established to maintain a patent in force so that most patents remain in effect throughout this entire period. The description of the invention must contain data on the design, the way it is done or used, et cetera. It must begin with the name of the invention and end with the patent formula, which defines the nature of the article being patented and specifies the limits of the patent's legal force.

The priority of an application submitted is ordinarily established according to the date of its arrival at the U.S. Patent Office,<sup>2</sup> which means the day when the Patent Office receives a complete application that is correctly filled out, and in the case of an incomplete application, the day of arrival of the missing material.

If the commission of experts refuses to issue a patent to the applicant, he has the right to appeal this ruling first with the Commissioner of the Patent Office and then to the Appeals Board of the Patent Office. An inventor who is not satisfied with the decision of the Appeals Board may turn either to the U.S. Court of Customs and Patent Appeals, or he may file suit against the Commissioner of the Patent Office with the United States District Court of the District of Columbia.

Patents in the United States are classified according to a specific national system which at the present time has 311 classes and more than 57,000 subclasses. In connection with the rapid development of science and engineering, the Patent Office very frequently abolishes the old classes and introduces new classes. In such cases all existing patents are appropriately reclassified.

In 1970 the annual budget of the Patent Office was \$46 million. Half of the expenditures are covered with the funds appropriated by the federal government, and the rest comes from patent fees and proceeds from the sale of patent materials, i.e., copies and microfilms of the description of patents, yearbooks containing information on patents is-

---

<sup>2</sup>The U.S. Patent Office is a government establishment under the Department of Commerce. It is headed by the patent Commissioner, who is appointed by the United States President with consent of the Senate. The division of the commissioner for patents includes the Commissioner of the Patent Office himself and his four deputies, who head the divisions of planning and programming, scientific development and analysis, the division of expert evaluation of trademarks, the division of patent services, the committee on priority conflicts and appeals, the group for expert evaluation and documentation in the field of chemistry, electrical engineering, and mechanical engineering, the international division for patents and trademarks, etc.

sued, et cetera. The cost of applying for a patent in the United States is therefore rather high, amounting to between \$150 and \$250. Inventors may personally fill out and submit their applications, but because of the specific manner in which business is handled in the Patent Office, as a rule they turn to patent attorneys or agents, whose services cost \$150-200. In recent years there have been changes in the organization of the U.S. Patent Office to improve the service to American firms and monopolies. The U.S. Patent Office now consists of 17 main subdivisions.<sup>3</sup>

Nevertheless, the influx of applications and their increasing value, on the one hand, and the increase in the volume of the published technical literature on the other, are greatly impeding the work of the Patent Office. Expansion of the office's staff is going very slowly. This is bringing about an increase in the number of applications that have not been examined (200,000), longer periods for their consideration (three years on the average), and a decline in the quality of expert evaluation. United States patent experts are energetically seeking a way out of the situation that has taken shape. The change in the procedure for examination of applications, which was introduced as of 1 July 1964, did not have an important influence on the work of the Patent Office. This indicates that at the present time no reforms of the national Patent Office are able to fully solve the problem of expert evaluation of patents.

In the United States, therefore, we observe an effort to economize on manpower and funds for expert evaluation, especially by organizing international cooperation in this area. Special attention is now being paid by American patent experts to possibilities associated with conclusion in June 1970 of the international Patent Cooperation Treaty. The basic purpose of the Patent Cooperation Treaty is to simplify procedure and expert evaluation of applications to protect one and the same invention in several countries and to reduce administrative expenditures of national patent offices.

#### WHO OWNS PATENTS?

By and large the owners of patents in the United States are not the inventors, but monopoly capital. Under present conditions it is primarily the corporations that are able to conduct large-scale research and to take advantage of its results. For example, whereas in 1901 in-

---

<sup>3</sup>*Official Gazette of the U.S. Patent Office*, Vol. 855, No. 2 (1968), p. 2.

dependent inventors obtained 82 percent of all patents, in 1967 their share was only 23.4 percent. At the same time, corporations obtained 74 percent of all patents on inventions, while government establishments obtained 2.6 percent.

The obtaining of patents and especially the commercial exploitation of them do not take place without fierce conflicts between firms. They strive by every means to hinder the issuance of patents to competitors, and they go so far as to actually violate the patent rights of rivals and patent legislation. For example, the small American company Photo Magnetic System filed a suit against IBM, American Telephone and Telegraph, Chesapeake and Potomac Telephone, and Western Electric, accusing them of illegal use of the principle of a telephone with press-button dialing on which it owned a patent. The invention of Photo Magnetic System had also been patented in France, Italy, the Republic of South Africa, and Rhodesia, and applications for patents were under consideration in another 26 countries, including England. None of the respondents wanted to pay the license fee. At the present time the suit is limited to the territory of the State of Maryland, but if the company that is the plaintiff wins the case, it is not excluded that it will file suit against the respondents over the entire territory of the United States.

The use of technical improvements makes it possible to extract additional profit. The monopolies have therefore begun to pay increasing attention to the introduction of scientific achievements into production and to modernization of production. In the present-day competitive struggle, "the old forms of crude dumping are yielding before new means of conquering a market, means which are based on science."<sup>4</sup>

United States technical superiority over the other capitalist countries, along with other factors, results from the incomparably greater expenditures for scientific research and from the introduction of new production methods. The United States spends two and-a-half to three-fold more for scientific research and development than all the Western European countries. Moreover, 85 percent of the research work in industry is concentrated in the laboratories of the important concerns that have 5,000 employees or more.<sup>5</sup>

Whereas previously technical progress was determined to a considerable degree by the creative activity of individual inventors, and expenditures to conduct specific research were relatively small, at the present time the solution of fundamental technical problems results as

---

<sup>4</sup>*Science in Industry. The Influence of Government Policy* (London: 1962), p. 15.

<sup>5</sup>*East Economist*, No. 2 (1966), p. 64.



a rule from the activity of a large staff of researchers and involves large capital investments, which frequently exceed the possibilities not only of individual inventors, but even of the small or medium-size firm.

The share of expenditures for scientific research of the largest United States firms is frequently only 5 to 10 percent of their turnover. According to the estimates of economists, total expenditures in the United States for scientific research and the introduction of their result into production will amount to \$40 billion in 1975, i.e., they will double as compared to the 1964 level.<sup>6</sup>

The United States is the home of many industrial discoveries, inventions, and improvements. For example, in the chemical industry there are such very important types of synthetic fibers as nylon and orlon; in medicine, there are preparations for treatment of rare forms of blood cancer; a new type of vaccine has been obtained against poliomyelitis and measles; there are drugs against tuberculosis, and strains of penicillin previously unknown have been discovered; in machine-building very important types of equipment necessary to automation of basic preparatory and manufacturing processes have been created. The firm General Dynamics Corporation, together with the Edison Institute, developed a zinc-air battery whose use in the future may make it possible to replace the internal combustion engine of the automobile with an electric motor; the use of the laser in a number of branches is a very important achievement; in powder metallurgy new methods of producing steel and alloys have been invented; and in the textile industry new looms have been designed whose operating principles are used by industry all over the world.

The bulk of federal funds allocated by the government for science are assigned to scientific research in the field of industry, particularly to research associated with military orders, nuclear power engineering, space, and chemistry. Appropriations for these purposes exceed more than 20-fold expenditures for research in the field of public health, education, and so on. It is precisely in these fields that most of the patents on inventions have accumulated.

By investing large sums in research, the State itself has become a patent-holder. At the present time more than 20 government organizations and enterprises possess patents. American government organizations received their first 32 patents in 1932, they received more than 11,000 between 1941 and 1960, and between 1956 and 1967 their number increased to 15,600.<sup>7</sup> Under current legislation, federal authorities

---

<sup>6</sup>*Patronat Français*, No. 256 (1965), p. 9.

<sup>7</sup>*Statistical Abstract of the U.S.* (Washington: 1968), p. 536.

retain inventions for themselves only if contracts to conduct the research are concluded with the Atomic Energy Commission or NASA. All other patents become the property of the corporations, which must, however, grant their use by the State without payment if they are needed. General Electric, for example, has obtained 471 patents in this way, at the taxpayers' expense.

The control of the monopolies over scientific research and, consequently, over patents on new technical discoveries, inventions, and improvements restricts the use of inventions by other companies. Production of one of the most important types of plastics—polyethylene—has been closed for many years to other American companies as a result of the patent monopoly of the DuPont firm. On the other hand, DuPont for a long time had no right to produce nitrogen fertilizers, even though it had a strong raw material base and much experience in the production of nitrogen compounds for explosives, since the patent belonged to the firm Allied Chemical. Only after the DuPont firm developed and patented its own process of urea synthesis did it undertake the production of nitrogen fertilizers.

#### THE BRANCH BREAKDOWN OF THE PATENTS ISSUED

Statistics show that about one-third of the patents have been obtained on inventions in the chemical industry, one-fourth in electrical engineering and radioelectronics, and one-fourth in general and transportation machine-building. These branches together account for more than 70 percent of all patents. A considerable portion of the patents have to do with the food industry, the metallurgical industry, the textile industry, and construction.

At the present time the U.S. Patent Office annually receives about 100,000 applications and every week issues 1,300 patents. The total number of inventions under consideration in the middle of May 1969 was 186,360; at the same time there were 3,380 applications for design patents.<sup>8</sup>

The United States occupies first place in the world with respect to the number of patents issued on inventions. In the 1950-1968 period the Patent Office issued more than 800,000 patents, considerably more than in any other advanced capitalist country, while the number of patents issued is increasing every year. Data on the number of applications submitted and patents issued in the United States are given in Table 1.

---

<sup>8</sup>*Official Gazette of the U.S. Patent Office*, Vol. 863, No. 1 (1969).

TABLE 1

Increase in the Number of Patents Issued in the United States

	1950	1960	1968
Applications	67,369	79,721	93,471
Patents	43,129	47,286	59,102
Number of the above issued to foreign nationals	4,408	7,712	13,320

The number of patents obtained by United States firms over a seven-year period beginning in 1960 increased 8 percent. It is illustrative that the influx of applications from foreign firms increased 44 percent over the same period. The activity of foreign companies in patenting their inventions in the United States is explained by the high level of development of engineering and the availability of a large domestic market in that country. Moreover, they are striving to guarantee patent protection of their industrial exports to the United States; because of the high tariff barriers and transportation costs, the firms of the capitalist countries are expanding their trade licenses in the United States, which are not subject to duty. Even though the share of foreign applicants is increasing steadily, foreigners own fewer patents there than in any other capitalist country.

In 1968 patents obtained by applicants from other countries accounted for 22.5 percent of the total number issued. Citizens of West Germany obtained 25.8 percent of them, Great Britain accounted for 18.6, Japan 10.8, France 10.8, Canada 6.7, Switzerland 6.6, Sweden 4.3, Italy 3.6, and Holland 3.6 percent. On the average, according to 1968 data, 50.7 percent of applications submitted by foreigners are granted. In spite of the formal equality of local and foreign applicants, cases are known in which the latter have been subjected to discrimination, particularly if the Patent Office has under consideration applications for similar inventions made by American inventors or organizations.

THE PATENT AND ECONOMIC EXPANSION

The practice of capitalist firms shows that they obtain foreign patents in cases where they are interested either in protecting their exports, in closing a sales market to a competitor or in carrying on license transactions. An analysis of the breakdown of the foreign patents obtained by a firm therefore can serve as a key to a study of its commercial activity.

American companies are increasing the number of their foreign

patents faster than the number of their domestic patents. The patents obtained abroad are used by the United States monopolies primarily to protect industrial exports. One can clearly see how the geographic distribution of industrial exports coincides with the orientation of foreign patents obtained by United States firms. In 1968 American firms applied for about 125,000 patents on inventions in other capitalist countries, 70 percent more than in 1961. In Great Britain, West Germany, France, Canada, and Japan the United States occupies first place among the foreign applicants with respect to the number of applications submitted and patents obtained.

Even though the patent monopoly is not perpetual on foreign markets, it still makes it possible for the patent-holder to obtain higher profits immediately in many countries. This is why, for example, about 1,000 patents of the American Polaroid Company protect its sales every year in 28 countries where it sells approximately 800,000 cameras for instantaneous photo development and 3 million rolls of film for them. The Westinghouse firm has patents to protect its exports amounting to \$200 million per year, et cetera.

An analysis of patent statistics shows that operations concerning foreign patents are undertaken above all by firms with a large volume of foreign economic operations, and the dynamics of the number of patents they obtain depends directly on the dynamics of their export of goods, capital, and technical achievements.

TABLE 2

## Patent Operations of United States Firms Abroad in 1968\*

Country	No. of Applications	No. of Patents
Australia	5,886	2,471
Austria	1,092	1,089
Belgium	4,640	4,617
Great Britain	13,961	12,588
Denmark	1,196	381
India	1,144	1,238
Canada	19,138	17,583
Netherlands	4,919	725
Norway	944	414
West Germany	12,083	3,804
France	11,392	10,794
Switzerland	2,978	3,126
Sweden	3,985	2,279
Japan	11,916	4,903
Other countries	26,706	12,097
Total	121,980	78,109

\**Industrial Property*, No. 12 (December 1969). (Geneva: BIRPI.)

Most of the American patents obtained abroad have to do with the chemical industry, transportation machine-building (mainly the building of motor vehicles and tractors), electrical engineering, electronics, and the atomic industry.

#### THE PATENT DEPARTMENTS OF THE FIRM

As is evident from what we have said above, American firms are paying much attention to patent work. They therefore attribute extremely great importance to their patent department in their organizational structure. The patent division performs functions which have essential significance to successful production and sale of the commodities produced. We might single out the following functions:

- (1) Regular information supply to the engineering services and subdivisions as well as production enterprises concerning technical innovations and the new patents of competitors in the relevant field;
- (2) Guaranteeing the patent protection of the results of the firm's scientific research and technical development in its own country and abroad;
- (3) In the necessary cases, preparation of contracts for the sale or purchase of patents and licenses in transactions with other firms, government organizations, and individual inventors; the drawing up of contracts to exchange licenses (in certain firms this function is performed by special license divisions);
- (4) Guaranteeing the patent clearance of their products and prevention of cases of violation by research, production, and commercial services of the patent rights belonging to other domestic and foreign companies;
- (5) Handling the judicial and other processes concerning the firm's patent affairs;
- (6) Maintaining contacts with inventors and setting the amount of their remuneration.

In each individual case the amount of work of the patent department, the functions it performs, and finally its place in the organizational structure of enterprises are determined by the character of production and by the share of research work in the firm's activity. Small companies which do not conduct specialized research and development usually take advantage of the services of patent attorneys from outside when they need them.

Corporations which have patent departments define the place of the

patent division in their administrative scheme as a function of their own configuration, the traditions that have taken shape, and so forth. As a rule the division is subordinate either directly to the board, to one of the directors or to some other executive. In cases where the company has several plants, factories, and research centers, the patent experts assigned to them are not administratively subordinate to the management of those enterprises, but are under the jurisdiction of the firm's central patent division. The work of patent groups is coordinated by the company's chief patent advisor; he provides general supervision, sees that the same work is not done by more than one group, calls conferences of the individual groups, et cetera.

An influential organization of American business circles, the National Industrial Conference Board, conducted a special study on the organization of the patent services of American firms. The survey covered 93 companies. In 38 the patent departments were organizationally subordinate to the central legal service, in 24 to the central engineering service, and in 31 directly subordinate to one of the firm's executives.<sup>9</sup>

In view of the shortcomings associated with the subordination of the patent service to the legal or engineering departments, many American firms consider the most acceptable organizational form to be the creation of an independent patent division which is under the jurisdiction of one of the members of the firm's top management—the president, the general director, the assistant president, the vice president, or secretary of the board. Of the 31 American companies surveyed which had independent patent divisions, 21 also have independent legal divisions, while 10 companies have only patent divisions (these firms turn to specialized law offices on general legal matters that arise).<sup>10</sup>

The following requirements pertaining to his business qualifications are usually imposed on the patent attorney who is the supervisor of a group: Higher education (a B.A. degree) in the relevant branch of science and engineering; legal education; membership in a Bar association; registration as a patent attorney in the U.S. Patent Office, at least 10 years' practical experience in the firm's patent division or in a specialized law firm; a knowledge of all aspects of patent affairs; the capacity to professionally evaluate the results of specific research, the ability to determine the value of patents, et cetera.

---

<sup>9</sup>*Patent Counsel in Industry*, a research report from the Conference Board (New York: 1964), pp. 4, 6, 7.

<sup>10</sup>*Patent Counsel in Industry*, p. 7.

In large firms for every patent engineer there are between one and three technical workers who do not have a higher education. In this connection we should emphasize that the managers of corporations attribute great importance to staffing the patent services with a sufficient number of technical workers so that the patent engineers are completely relieved from doing work which does not require high qualifications and specialized knowledge.

Together with the firm's commercial services, the patent division determines the feasibility of patenting an invention abroad and the group of countries in which this is economically justified. Large expenditures are involved in obtaining patents abroad, and it is therefore very important to determine the value of an invention in good time and in a competent manner, and then on that basis to budget expenditures for obtaining patents.

The decision on patenting a specific invention is in practice a concrete embodiment of the commercial and technical policy of the company. The problem of obtaining patents therefore goes beyond the limits of the activity of the specialized subdivisions of the firms. Since these matters are directly bound up with the prospects for selling products, many American corporations are setting up special patent committees. Their members include representatives of research divisions, production subdivisions, commercial divisions, and other interested services.

Depending on the nature of the firm's production and research activity, the share of patented inventions varies greatly. Certain American companies patent between 65 and 85 percent of their inventions, while others conduct a more thorough screening, and the share of inventions on which patents are issued runs from 15 to 25 percent. To be specific, this circumstance has a considerable influence both on the membership of the patent committees and also on the feasibility of setting them up. Of the 54 American companies surveyed which have their own patent divisions, in 32 responsibility for deciding on submittal of applications for patents is borne by patent committees, in 18 by patent divisions, and in four by the management of the research subdivisions.<sup>11</sup>

Medium-sized and small firms, as well as large companies whose activity is not related or is little related to research work consider it more advantageous from the economic standpoint to take advantage of the services of law firms or associations working in the field of patent law. In the United States approximately two-thirds of the industrial com-

---

<sup>11</sup>*Patent Counsel in Industry*, p. 91.

panies use the services of these firms. Many cases are known in which the experience of an attorney has proven to be decisive for the destiny of patents that were the most important from the technical and commercial standpoint. For example, it was only because of competent legal aid that the following obtained their patents: Alexander Bell on the telephone, Glen Curtis on the airplane, Lee de Forest on the triode, the International Standard Electric firm on the radar device, the American Cyanamid Company on melamine, among others.

The massive redistribution of patents and the results of research have brought about the emergence and development of the institution of patent agents (brokers). Two types of operations are typical of them: serving as middlemen between the patent-holder and an industrialist and the handling of a patent on behalf of the holder. Through the agent the industrialist establishes contact with the holder of the patent, and if an agreement is reached for sale of the patent or license, the agent receives a commission, usually 8-15 percent of the amount involved in the license agreement. In cases where the patent firm serving as a broker handles a patent on behalf of the holder, its commission is considerably higher and reaches 50 percent in especially complicated cases.

Among the most important brokerage firms concerned with middleman operations in the United States, the best known are Products Development Corporation, Patent Research Corporation, Porter International Company, Ad Arima Incorporated, Boston Products Development Corporation, and Resources and Facilities.

Certain brokerage firms specialize in international operations. They include, for example, the firm Porter International, which was organized in 1954 and operates in 30 countries. The company Pegasus International, which was established in 1950 and has a similar configuration has opened offices in London, Frankfurt-am-Main, Paris, Tokyo, Copenhagen, and Melbourne. Administrations for the exploitation of patents and the results of research at universities, colleges, and research establishments usually recorded as non-profit corporations are a specific form of patent brokerage organization. These include Ohio State University Research Foundation, University of Connecticut Research Foundation, Rutgers Research and Endowment Foundation. In addition to operations with their own patents, in recent years these organizations have been buying and selling the patents and research results of others on an increasing scale.

An analysis of the patent activity of American monopolies vividly



shows that in determining their technical policy, which is reflected in the structure and geographic orientation of patent activity, they are guided not by the interests of scientific and technical progress and raising the standard of living of the workers on this basis, but above all by the aspiration to derive maximum profit through commercial utilization of the results of the intellectual work of scientists, engineers, and workers.

## NOTES

---

---

### Fifteenth Annual Conference Program Announced

The Institute's Fifteenth Annual Conference on "Enterprise Under Stress: Changing Premises and New Responses" to be held on October 20, 1971 at the Shoreham Hotel in Washington, D.C., will examine the responsibilities and opportunities of government and private enterprise to meet the evolving demands of society in the Seventies.

The Conference program consists of three parts: A. New Context for Research; B. New Circumstances for Industrial Property; and C. New Setting for Antitrust and Unfair Competition. Dr. Robert W. Cairns, Deputy Assistant Secretary of Commerce for Science and Technology, U.S. Department of Commerce, will chair the morning sessions and Mr. John C. Bodner, Jr., of Howrey, Simon, Baker and Murchison, the afternoon sessions. The Kettering Award Address will be delivered at luncheon by 1970 recipient, Dr. Walter J. Derenberg.

Key presentations will be made by Dr. Henry David, Executive Secretary, Division of Behavioral Sciences, National Academy of Sciences; Mr. P. P. Huffard, Jr., Director of Environmental Affairs, Union Carbide Corporation; Pro-

fessor Corwin D. Edwards, formerly Head of Bureau of Economics, Federal Trade Commission; Mr. S. Delvalle Goldsmith of Langner, Parry, Card and Langner, New York; Mr. Allen C. Holmes of Jones, Day, Cockley and Reavis, Cleveland, Ohio; and Mr. Robert Pitofsky, Director of the Bureau of Consumer Protection, Federal Trade Commission.

The Conference will consider risks attendant on the introduction of new products and the social requirements for enhancing the quality of life and the material welfare and leisure of our people. Attention will be directed to national and international problems due to technological hazards such as pollution of the environment, and to consumer protection. Emphasis will be placed on the role and potential of R&D, industrial property and competition in meeting these current and emerging challenges. Notice will be taken of the new constraints on R&D and on industrial property.

Publication of the Conference will be limited to the principal papers. The full proceedings will *not* be published. The Conference fee, including luncheon, is \$65.

## PTC Clinic Scheduled on "Avoiding Fraud on the Patent Office"

The next PTC Research Institute Clinic is scheduled for November 18, 1971 and will be on "Avoiding Fraud on the Patent Office." Among the invitees having a special interest in the topic are patent attorneys, research directors, inventors, antitrust specialists, and business and government executives.

Since the Supreme Court decision of *Walker Process Equipment, Inc. v. Food Machinery and Chemical Corporation*, 383 U.S. 172 (1965), increasing attention is being given to the subject of "Fraud on the Patent Office." This attention stems, in large part, from the frequency, since the *Walker* decision, with which the

claim of "Fraud on the Patent Office" is being alleged in patent cases and the concomitant possibility of the courts invalidating the patent or barring recovery. Moreover, there is the chance of a heavy antitrust damage award and of ethical implications for the professional man from a charge of irresponsible conduct.

To date most of the writing and discussion has centered on the doctrinal aspects of the subject. To provide guidance of a more practical nature, the Institute is scheduling this Clinic to explore specific solutions to the various problems of "Fraud on the Patent Office."

## Nominations for 1971 Inventor of the Year Award Invited

Nominations for the 1971 Inventor of the Year Award are invited by The PTC Research Institute. Closing date for nominations is November 15, 1971. Members of the Research Institute and all other interested persons are asked to submit the names of candidates for consideration by the Awards Board. Submissions should include information to clearly identify the candidate and contain sufficient evidence of his *character* and *contributions* to enable the Board to make an evaluation.

The Inventor of the Year Award honors a journeyman or professional inventor who has made a significant patented invention or inventions even though he may not have had wide public service. Presented annually, the Award provides a university forum for recognition of the accomplishments of creative people.

The award program is not necessarily intended to honor the great invention. It affords an opportunity to recognize a relatively unknown dedicated inventor who overcomes

obstacles and expands his resources to produce an invention or inventions. The Award is not limited to an inventor's contribution in any one year but will be given for any or all of his achievements to date. Chester F. Carlson was named Inventor of the Year for 1964 (Xerog-

raphy); Samuel Ruben for 1965 (batteries); Gordon K. Teal for 1966 (silicon transistor); Robert Adler for 1967 (electronics); Jay W. Forrester for 1968 (computer memory); Stanley D. Stookey for 1969 (glass); and Billy M. Horton for 1970 (fluidics).

### New Books Reviewed

Schiff, Eric, *Industrialization without National Patents; The Netherlands, 1869-1912; Switzerland, 1850-1907* (Princeton University Press: 1971).

The author's intention is to provide insights with respect to the function of patent systems as stimuli to invention, innovation and industrial development. Two countries, The Netherlands and Switzerland, which some time back did not have patent systems, are considered. Schiff finds that in these countries industrial growth and inventive activity continued during the patentless periods, more positively in Switzerland than in Holland. He observes that one of the elements of this growth was the benefit derived from foreign inventions which were adopted, sometimes without purchase of the technology from its discoverers and developers. The fact that during this time, Swiss and Dutch nationals actively sought patents outside

their borders is noted and there is passing reference to the value of such protection as an incentive to domestic innovation.

Schiff's conclusions are admittedly tentative, but he does indicate that, as he sees it, a country can enjoy *economic* progress if it can withstand *political* pressures exerted by other countries to conform to the rules and requirements of The International Union for the Protection of Industrial Property. Such findings are, in this reviewer's opinion, unrealistic and inaccurate. They ignore the Twentieth Century with particular emphasis on (a) the contribution of industrial research to economic growth and (b) the significance of technology to international trade. Today the continuing introduction of new products and processes is recognized to be a significant feature of an expanding economy. At the same time large expenditures are required to support the research,

development, new plants and marketing costs, on all but minor improvements. Further, the introduction of a new idea is accompanied by a high degree of risk. Without protection, company managers cannot justify diverting resources to the new and experimental.

Complementary to this employment of research for economic purposes is the transfer of the technology between countries. Licensing or sale of the patents and related know-how are convenient and widely used transfer mechanisms. One need not be an international economist or historian to perceive that in 1971 the interlaced interests of companies and countries are far different from those conditions obtaining in the time period examined in this book (Netherlands 1867-1912; Switzerland before 1907.)

Commercially there are worldwide networks embracing multinational firms, affiliates and subsidiaries, all of which transfer inventions and technology across borders. On the governmental level the need to foster foreign trade has led to a family of international organizations, treaties and trade agreements. A system for protection of industrial property rights is embedded in both the commercial and governmental activities. The fact that, in a time when the communication and interchange of ideas were far

less, two small countries, with limited domestic markets, both oriented toward international commerce, went without patent systems and did not decline may be historically valuable. However, it would be dangerous to conclude that such a situation would be reproducible today. It would be unfortunate if policy makers in developing countries found, in this book, justification for neglecting their patent systems as they seek to strengthen their industries and to export their products.

J.C.G.

Machinery and Allied Products Institute and Council for Technological Advancement, *Rules of Law on Technical Data* (Washington, D.C.: Machinery and Allied Products Institute, 1971.)

We bring to the attention of our readers a new book, *Rules of Law on Technical Data*, published under the auspices of the Machinery and Allied Products Institute. This work is an updating of the technical data portion of a previous MAPI publication on *Comptroller General Decisions on Technical Data and Related Patent Problems*. The MAPI flyer announcing the book states that the purpose of this study is threefold: "First, it reviews the history and implications of the technical data problem and the development of Section IX, Part 2, of the Armed

Services Procurement Regulation (ASPR) which sets forth the policy and procedures of the Department of Defense in acquiring technical data and rights. Second, and of key significance, the study summarizes the general rules of law established from Comptroller General decisions in the area of technical data and rights therein. Third, the study contains

briefs of 37 leading Comptroller General decisions on technical data."

In view of the importance of trade secrets and know-how to companies and the changing policy of government with respect to such data, this systematic work should prove a convenience for busy practitioners and serve as a guide for less experienced people.

## **Government Patent Policy Revisited: Reflections Occasioned by President's 1971 Memorandum\***

Martin G. Raskin

The subject of what the government's policy should be with respect to patents evolving from federally financed R&D, both from inhouse agency research and from outside contractor sources, is one that has engendered much controversy. More specifically, whether the government should retain the title to such patents while making the right to practice the inventions disclosed therein freely available to anyone who so desires in the form of a royalty-free license (the so-called title-policy) or whether the contractor (or for that matter, the government employee-inventor) should retain title to the patents, only providing to the government an ir-

revocable royalty-free license thereto, (the so-called license-policy) is a question with which commentators have debated for a considerable period of time. The factors to be considered relative to the determination of which policy would be followed has similarly been extensively considered.

On August 23, 1971 President Nixon issued a Memorandum for Heads of Executive Departments and Agencies containing various revisions and modifications of an earlier 1963 Memorandum from President Kennedy aimed at providing guidance to the agencies in the determination of the disposition of rights to inventions made

---

*Editor's Note: The issuance of the President's Memorandum of August 23, 1971 on Government Patent Policy while we were going to press prompted the preparation of this Note for the benefit of IDEA readers.*

under government-sponsored grants and contracts. The various reports in newspapers and other media sources concerning this latest Memorandum seemingly presented it as less in the nature of a step in policy evolution and, instead, as more in the realm of a striking patent policy shift on the part of the Nixon Administration.

The federal patent policy (if indeed one can talk of a single policy) since the second World War has been more in the nature of a continuum with only relatively infrequent changes being made and even then, such changes being essentially in degree rather than in kind. The Memorandum of 1971 represents another step in a continuing effort to more clearly define what the federal patent policy should be.

As mentioned above, many commentators have written regarding the nature of the formulation of a government policy. A number of studies and investigations have been made as to what should be the proper criteria to consider in the formulation of a consistent policy. In addition, various evaluations of the success of government patent policy in light of stated objectives have been attempted. The PTC Research Institute of The George Washington University has been much concerned with these subjects, reporting from time to time in its Journal, *IDEA*, the opinions and investigations of both its staff

researchers and outside authorities relating to this complex subject. It is the purpose of this presentation to briefly note the work of some of these authors.

In an early expression of discontent with the existing government patent policy,<sup>1</sup> Dr. Howard I. Forman cited the failure of non-exclusive licenses, which the government offered to patents which it held title, to “. . . induce the investment of the many thousands of dollars which are often required to foster embryonic developments having numerous ‘bugs’ to be cleared up before an efficient commercial operation can be evolved. Why should anyone take the chance that, after he works the patented inventions into a commercial success, another government licensee will come along and readily compete with him without anything approaching the additional investment required of the first licensee?”<sup>2</sup>

In addition to using their patents in a defensive manner, presumably to protect the government against infringement suits, Dr. Forman states a second responsibility which he supposes the legislative and executive branches saw in administering patents arising out of federally financed research as being that equitably, all people should be equally entitled to this government property which has been developed through public funding. However, two contingencies prevent policy formulations from being governed

by these equitable bases. First, the inventions which arise out of government contracts cannot be clearly defined as having been made entirely at the government's expense and a balancing of contributions certainly would not be feasible. Secondly, Dr. Forman urges that ". . . the prime concern of the government should be the implementation of a policy which tends to make every patented invention contribute as much as possible of its potential utility to the country's welfare. Encouragement should be given to the investment of capital, labor, and materials to convert each such invention into a useful article of manufacture, composition of matter, or manufacturing process."<sup>3</sup>

Thus, although he concedes that it is a noble thought that the government should not unjustly enrich the contractor by giving to him that which has been publicly financed, Dr. Forman indicated that the government owes an even greater obligation to its citizens, namely, to see that the patented inventions which it may cause to come into being are stimulated into adoption and application, and this can only be accomplished through giving to the contractor a measure of exclusivity in the invention. "The balance would clearly indicate that allowing for exclusive exploitation of the inventions advances the public welfare far beyond any other consideration."<sup>4</sup> Dr. Forman proposes a policy whereby exclusive title

should automatically be vested in the contractor, presumably for all patents resulting from government sponsored R&D contracts, subject only to a reversionary right in the government upon failure of the contractor to work the invention.

In summary, a public interest is defined relative to government patent policy, which places the commercialization of patents resulting from federally sponsored R&D ahead of all other considerations, and it is the author's opinion that only by giving the contractor title to such patents can such an objective be attained.

The following year, the Institute published the results of a comprehensive study<sup>5</sup> whose purpose was to examine the effects of the patent policies of the federal agencies in awarding contracts for R&D and to appraise them in the light of the public interest. After citing a lack of uniformity among the several agencies as to patent policy, the report enumerated the leading issues relative to the choice between adopting a license or title policy. First, the missions of the agencies were deemed important in that when an R&D contract has the objective of procurement of improved equipment for use by the agency itself, the license policy is generally considered appropriate. However, when a contract is for the advancement of a particular technology, the title policy is usually followed. Secondly, the major financial con-



tributor to the invention was held to be a factor with the title policy advocates citing the "big give-away" as an element tending in their favor. Getting the best contractor for the job should be considered also with the license policy advocates seeing this policy as inducing the best contractors to bid for a job. Thirdly, which policy would best promote the useful arts? Here, those in favor of the license policy cited a need for exclusivity to provide an incentive for the development of inventions while those favoring a title policy insist that this is best accomplished by making the invention freely available to all.

The method the report utilized in analyzing the existing policy was to define what the public interest is relative to that policy, conduct a study of a license policy agency (DOD) and a title policy agency (AEC) and evaluate in each instance the extent to which the public purpose as defined was served. The public interest was defined in terms of improvement of technology (new products and processes, improvements in existing ones and reductions in costs of production); economy and efficiency in procurement (federal funds for contract R&D should be well spent; does retention of patent rights affect the quality of contractors); the avoidance of concentration in industry and of preferred positions for individual corporations (it was noted

that efforts to attain the goals of national security and of improved technology may run counter to the maintenance of competition); and the accomplishments of the missions of the agencies.

The license policy study consisted of taking a sample of patented inventions and sending questionnaires to the contractors owning them. It was found that although both large and small companies owned the sampled patents, the larger ones predominated. Of the 143 patents on which replies were received, the number of those put to actual commercial use was 19, or 13 percent as compared to a utilization rate of between 55 and 65 percent for privately developed patents. The usual reasons given for absence of commercial use were that the product was for government use only; there was insufficient market demand; the product was outside the normal market line; and that the company was at an insufficient competitive advantage. It was also found that patent rights in contracts were important to a majority of contractors.

The survey regarding AEC policies was directed to nuclear related industries likely to engage in R&D contracts with the AEC. When asked, would and could the industry do more in the atomic energy field if it had more patent rights, 14 respondents answered Yes while 4 answered No. Fifteen respondents indicated that the title policy of

AEC impaired their incentives to develop while only 3 replied negatively. Is AEC's title policy satisfactory in hastening the development of a commercially competitive nuclear industry? Thirteen said no, 3 answered yes. It was found the commercial utilization of AEC owned patents amounted to only 15 percent.

The findings of the report noted that in the period 1946-1959, the Federal Government spent \$37 billion on R&D out of a total of \$70 billion. Only 6 percent of the patents issued in that time originated in federal R&D. Accordingly, the report concluded that the importance of the issue of patent rights in R&D contracts has been much exaggerated. In its evaluation of the license policy in operation, it was found that the license policy is appropriate where government agencies pay for R&D so as to get better equipment, where they must deal with a broad range of technologies, and where they do not otherwise have control over industries. Further, it was deemed that the value of the patent rights retained by the contractors under the license policy is nebulous and probably quite small. Thus, there is scarcely any basis for the charge that the license policy results in a give-away. The report recommended that since this policy has been in stable operation for a long time, and since the bulk of contract R&D is geared to it, radical change

would be disruptive.

With regard to the title policy, it was found that this policy has been used when government agencies have sought to foster the technologies of particular industries. Patents owned by the government can be and are used by industry under certain conditions. These conditions are the ease of putting the inventions to use, the absence of further costs of development, and the existence of a competitive industry. But where inventions need much additional development at high cost, where risk is high and future profitability uncertain, chances are that the invention will not be used. The report concluded that no strong case can be made for a uniform patent policy due to the differences among the R&D missions of the federal agencies and from the different positions of business firms in their dependence, or lack of it, upon government R&D contracts. Further, that undue concentration would result from the license policy is a possibility so negligible that it may be disregarded.

One year later, new facts became available on the effectiveness of the government patent policy in the form of data accumulated by the Subcommittee on Patents, Trademarks and Copyrights of the Committee on the Judiciary of the United States Senate. The data was reported<sup>6</sup> by Dr. Donald S. Watson in a manner so as "to cast light on the major issues attending the op-

eration of the license policy of the DOD." The Subcommittee sent questionnaires to 120 business firms, 100 of which were the leading defense prime contractors. The companies reporting to the Subcommittee indicated that in the period 1949-1959 about 12 percent of all patents issued to them were products of federally financed R&D (compared to 6 percent found in the 1960 report).<sup>7</sup> Conforming to the results obtained in the 1960 report, it was found that the dollars of federally financed R&D yielded a much smaller number of patented inventions than did dollars of privately financed R&D.

Further, the "mildly astonishing" calculation of the earlier report that only 13 percent of the federally financed contractor-owned inventions had been put to commercial use was reinforced based on the Subcommittee's finding that less than 7 percent had been so used. Thus, the Subcommittee's report furnished new factual information which gave additional weight to the conclusion reached in the 1960 report that the value of the patent rights in federally financed R&D contracts is quite small.

The Institute then turned its attention from the investigation of the effectiveness of the license policy to a study of the title policy in the form of a survey and lengthy report by Dr. Mary A. Holman.<sup>8</sup> It is interesting to note that in this and the preceding article, the de-

termination of whether or not a particular policy is deemed to be functioning well seems to depend in large part on the effectiveness of that policy to achieve commercialization of patents emanating from federally sponsored research. The objective of the study was to determine the nature and extent of the commercial utilization of government-owned patented inventions and the causes for nonutilization with a view toward testing to see if the advocates of a title policy are correct.

Dr. Holman begins by noting that government-owned patents comprise only 2 percent of all the unexpired U.S. patents. Therefore, she concludes, any favorable effect of innovation on economic growth or unfavorable effects on competition will be far less than is claimed by the defenders of the license policy and of the title policy. After a discussion of how an economist might view government-owned patents wherein it is noted among other things, that the same patent protection (presumably exclusivity) is necessary as an incentive for commercial utilization of these patents as it is for patents in the private sector, Dr. Holman notes the traditional arguments against a title policy and against a license policy, i.e. a title policy allegedly retards commercial utilization and further retards efficiency in procurement in that some firms will not contract unless they are assured

of principle patent rights whereas a license policy does not adequately assure the avoidance of infringement suits, nor prevent concentration of business but rather results in a large scale economic give-away.

The survey consisted of questionnaires sent to both inventors of government-owned patents and licensees thereof and were mainly concerned with the extent of and reasons for utilization or lack thereof. It was asserted that the extent of commercial use depended on two things, viz., the nature of the products or processes covered by the patents and the amount of further development necessary before commercialization would be possible. With respect to the first reason it was noted that about one-third of all government-owned patents relate to radiant energy, inorganic chemical procedures, electrical and wave energy chemistry, ammunition and explosive devices and ordnance—certainly not fields which are readily amenable to commercial adaptability. Regarding the second reason, it was stated that about one-half of all government-owned patented inventions require further development for commercial use.

Information supplied by inventors showed the rate of commercial use of government-owned inventions to be between 10 and 15 percent. It was noted that none of the commercially used inventions fell within the five classes mentioned

hereinabove. Of the 23 inventions reported utilized, only one required extensive development before commercialization was feasible. The inventors gave three reasons for non-use: (1) the subject matter held little commercial potential; (2) the invention was for government use only; and (3) there was insufficient market demand.

Information supplied by licensees indicated that neglecting the possibility of use without a license, the rate of use for all government-owned patents was slightly less than 3 percent. About 20 percent of the licensed sampled patented inventions were reported to have been used commercially. The reasons for nonuse cited by the licensees were: (1) too much sales or development effort is required; (2) the product is outside the usual market line for the firm; (3) comparable or better substitutes are readily available; (4) the product is for government use only; and (5) the market position of the final product is in doubt because the government holds title to the patent.

In regard to the method of administering its patent portfolio, Dr. Holman noted that the usual policy of granting nonexclusive, royalty-free licenses often does not accomplish a successful transmission of technology covered by the patent and, at present, there was no central agency assigned the task to promote the dissemination of such technology. The study then cites five

traditional proposals for changes in the administration of government-owned patents, namely: (1) charging a royalty for use; (2) a provision for exclusive licensing; (3) a provision for the sale of patented inventions; (4) arrangements for cross-licensing with private industry; and (5) the creation of a central administrative agency.

Returning to government patent policy and its effect on the commercialization of inventions, the inventor of each sampled patent was asked whether or not he, or his employer, would have commercialized the invention if title to the patent or an exclusive license had been obtained. The inventors of 10 percent of the sampled inventions answered in the affirmative. About 48 percent of the inventors didn't believe that government ownership of patents encouraged commercialization of the inventions.

Summarizing, Dr. Holman found that the rate of commercial use of government-owned patented inventions was low—between 10 and 15 percent. The low utilization rate stemmed not from the fact that the inventions were available to anyone so desiring but rather from more advantageous alternative investment opportunities. It was concluded that providing for a form of exclusivity would probably increase the rate of utilization. However, the possibility of raising the rate of commercial use by providing for exclusivity was deemed to

be not large. However, it was also found that because government-owned inventions hold slight commercial potential, and because the commercial value of these inventions is small, the possibilities for monopolistic abuse were slight. Generally, the title policy of the government and the coincident dedication to the public of inventions affected thereby, does have a slightly adverse effect on commercialization.

Almost immediately subsequent to the appearance of Dr. Holman's study, the Kennedy Memorandum, mentioned above, was issued. Attached thereto was a set of basic considerations for the formation of a consistent government patent policy. There it was stated that the inventions resulting from work performed under government contracts constitute a valuable national resource and that the use of these inventions should, among other things, meet the needs of the government, recognize the equities of the contractor, and serve the public interest. Presumably, the public interest required that efforts be made to encourage the expeditious development and civilian use of these inventions. It is noteworthy that these considerations had all been recognized in the articles discussed previously.

The worth of the "national resource" to the public in light of the findings in these articles and the ones to follow is the substantial

question. Dr. Barkev S. Sanders, soon after the Holman study, published an article<sup>9</sup> in which he proposed to examine the inventive productivity of federal versus industrial R&D expenditures in terms of useful patented inventions. In the judgment of Dr. Sanders, the primary consideration for a government patent policy should be the responsibility of the government to foster the fullest exploitation of all inventions for the public benefit. Asserting that the Kennedy Memorandum accepts this as the preeminent consideration, the first matter to consider, Dr. Sanders says, is the comparative significance of government R&D expenditures in promoting inventiveness in general and the commercial exploitation of the resulting invention.

After making some adjustments in the figures used in the 1960 report,<sup>10</sup> he asserts that for the period 1946-1959, corporations whose outlays for R&D were about 40 percent accounted for 284,400 patents and government, with 53 percent of R&D expenditures, accounted for 2,000. This yields a ratio of 12:1 between corporate R&D expenditure per patent as compared to government expenditures for R&D per patent. Furthermore, Dr. Sanders points out that merely a measure of the number of patents provides no direct evidence of economically significant inventions. He relies on the Institute's earlier Patent Utilization Study as evidencing that 50-

60 percent of patented inventions issued to individuals and corporations find their way into commercial use while the Institute's 1960 report indicates that only 13 percent of contractor-owned patented inventions resulting from government-sponsored R&D are utilized. Taking these figures into consideration, an equivalence ratio of 55:1 results; i.e., 50 to 60 federally contributed R&D dollars are as productive in terms of commercially useful patents as one R&D dollar spent by the average private corporation (this estimate is conservative according to the author).

The article goes on to point out that the 13 percent utilization rate was for inventions for which the contractor was allowed to hold the title. With respect to the utilization rate of government-owned patents, Dr. Sanders cites the Holman report<sup>11</sup> and, while questioning the validity of her interpretation of the inventor response vis-à-vis the licensee response, accepts her finding of a rate of utilization of about 2.5 percent based on licensee response.

With regard to the reasons for the lack of utilization, the author independently comes to a conclusion similar to Dr. Holman's, that the utilization rate for patents in classes which predominate in the federal portfolio is lower than those not so classified.

A second article by Dr. Sanders continued to explore the value of the national resource. By investigat-

ing and discovering the propensity of such government R&D to produce patents, the relative value thereof could be better defined and, accordingly, policies dealing with the administration of the resource could be made more realistic. In this two-part report,<sup>12</sup> Dr. Sanders analyzes the patent production of 78 companies who returned a questionnaire sent to them by the U.S. Senate Subcommittee on Patents, Trademarks, and Copyrights which requested information regarding the amount of government R&D received by these companies for fiscal years 1949-1959 relative to the R&D expenditures of company monies, and the number of patent applications and patents granted as a result of each. Referring to his earlier work<sup>13</sup> along the same lines where in a ratio of 12:1 was obtained between government and corporate expenditure per patent, the author found useful the statistics published by the Subcommittee as yielding more definitive evidence on the comparative patent yields. Dr. Sanders cited a number of reasons why his computations may unduly favor the government which, among others to be discussed below, included his inclination that there was appreciable underreporting of the sizes of the federal grants.

With these reservations in mind, it was found that the ratio in expenditure funds relative to applications filed is 11:1 (\$1,792,000 federal R&D dollars per patent appli-

cation: \$163,000 industry R&D dollars per patent application) while the ratio relative to patents granted was 13:1 (\$3,702,000 federal R&D dollars per patent granted: \$288,000 industry R&D dollars per patent granted). To offset the bias mentioned above which perhaps led to an unduly low differential yield, some offsetting factors were cited, namely, no consideration had been given to applications and patents issued to federal agencies from these same R&D expenditures and the tacit assumption that all non-federally financed applications and patents filed by industry are produced by their R&D expenditures. Thus, the ratios might not be too far off the "true" differential.

Of course, Dr. Sanders points out, the ratios mentioned above merely represented averages of the 78 company's statistics. However, the differential in yield for the individual companies was found to vary tremendously: regarding applications, the highest ratio was 1,136:1 while the lowest was 1.5:1. With respect to patents issued, the highest differential was 1,734:1 while the lowest ratio was .4:1. In the second of the two reports, Dr. Sanders attempts to relate the diverse ratios to various characteristics of the reporting companies. A summary of his findings follows.

Firstly, there is some indication that companies which sell all or almost all of their production to the

government have a higher federal R&D expenditure per patent, i.e., show a larger ratio. Secondly, the larger the corporation was in terms of aggregate net sales, the smaller the ratio appeared to be, suggesting that, in a relative sense, large corporations seem to be more productive from their federal R&D grants than smaller corporations. His third finding was that there is no regular pattern or relationship between the amount of federal R&D grants given to various companies and the differential ratio of patent productivity of these companies. Fourthly, the most significant pattern was found between the amount of company-supplied R&D expenditure and the differential ratio. This ratio is lowest for companies with the largest company-supplied R&D funds and increases progressively and sharply with declining amounts of company-supplied R&D funds. Lastly, it was found that companies with the highest federal R&D grants in relation to company R&D outlays have the highest differential ratios.

The fourth and fifth findings tended to strengthen a conclusion reached by Dr. Sanders earlier in the report (one of the reasons given for his computations unduly favoring the government) that the 78 companies getting the lion's share of federal R&D did not represent the most skilled companies in the country, i.e. companies which would have the highest patent yield

per unit of government R&D dollars. As the author puts it, "[i]f this inference is correct, it could have very significant implications for the country regarding the economic value of federally financed R&D grants."

A similar finding was made by the Subcommittee on Research and Development of the National Defense Committee of the U.S. Chamber of Commerce whose report was condensed<sup>14</sup> and published in two parts in the same volume with Dr. Sander's report. Mr. Helge Holst, the Chairman of the Subcommittee, directed the study so as to focus on what he calls the best interests of the nation by concentrating on two major considerations, namely, (1) what policy will best enable the government to secure the most helpful assistance on primary governmental problems and (2) how can the inventions resulting from federal R&D be commercialized most efficiently? It is interesting to note that Mr. Holst states that in any consideration of this subject, it is necessary not to become lost in the relative equities of the government and the contractor, considering that the Kennedy Memorandum specifically requires this factor to be considered.

The results of a survey, conducted by questionnaires sent to contractors, large, small and intermediate, who provide over \$10 billion of procurement to the government each year, indicated that



government patent policy is a significant factor in discouraging responsible, competent, organizations with substantial backgrounds of experience and proprietary rights from bidding on work for the government. The questionnaire specifically asked, "Has [the government's] patent policy been a factor in discouraging you from bidding on work for any government agency?" The answers were Yes, 80 percent; No, 18 percent; Other, 2 percent. More surprising, however, were the responses to the question asking, "have you actually refrained from bidding on government work for any agency because of its patent policies?" Here, 56 percent answered affirmatively, 36 percent said No while Others totalled 8 percent. Mr. Holst noted that this reply, 56 percent actually not bidding on work, came as a surprise. It refutes the assumption by those who maintain that no matter what the policy, bidders will take government contracts.

Clearly then, the author concludes that the first major consideration of public interest is not being fulfilled. The reasons for this were found to be that when contractors undertake R&D for the government, they do so in the hope and expectation that the government-sponsored R&D will provide opportunity for follow-on production. For this purpose, it is to be expected that the contractor will seek to retain the patent rights to in-

ventions resulting from its work. Where such patent rights are important to the company (the questionnaire indicated that 92 percent of the respondents depended on such rights for their commercial position), it is to be expected that their unavailability will deter that company from seeking contracts with the government. The author points out that the government in placing contracts for R&D is not seeking patents. Its interest is in effective systems, services and tangible items.

The report indicates that the secondary objective of the patent policy should be securing widespread public use of resulting inventions. Mr. Holst notes that for this to occur it is necessary that (1) the new developments be communicated as promptly and effectively as possible to potential users; and (2) that there be incentive for further effort and expenditure by the private sector to achieve widespread use for nongovernmental purposes. Both of these will be facilitated by leaving the title to patents emanating from federally sponsored R&D with the contractor. Thus, both of the suggested major considerations in the formulation of a government patent policy mentioned above will best be achieved by leaving ownership of inventions and technology with those who originate them.

A subsequent study<sup>15</sup> published in *IDEA* concerning the govern-

ment patent policy and its operation under the Kennedy Memorandum is divided into three parts. The first part covers the evolution of a patent policy for inventions made under government-sponsored R&D. The second part examines the experience of NASA's operation under the policy, and the third part includes policy recommendations. In the first part, Dr. Robert Solo asserts that the Presidential Memo has two explicit purposes: (1) to achieve a sufficiently consistent federal patent policy, and (2) to promote the commercial utilization of inventions produced through government R&D contracts. However, he suggests that the criteria determinative of who gets the principle patent rights embodied in the Memo are so equivocal as to be valueless in accomplishing the first purpose. Regarding the second purpose of promoting the commercial application of the inventions, the author notes that under the Memo the grant of principle rights to the contractor is conditioned on the proven commercial application of the invention or of an effort to so develop the invention within three years. However, he feels that here too, the wording of the Directive is so equivocal as to render the provision nugatory.

In part two, Dr. Solo defines NASA inventions as comprising two sets—one being produced by private contractors and offered for nonexclusive royalty-free licensing,

the other consisting of inventions where the exclusive rights have been waived to the contractors who produced them. Diverting for a moment, Dr. Solo attempts to discover the "inventiveness" of NASA employees relative to contractor employees and by examining relevant data finds that the output of inventions per scientist and engineer is almost exactly the same for NASA employees as it is for NASA's R&D contractors. He also explores the relation of government R&D expenditures by those contractors in 1965 to the number of inventions produced thereby. The findings indicated such extreme differences and such random variations in company performance as to suggest to the author that the differences were to be accounted for by the policies of companies to positively discourage invention disclosure. Finally, he compares the relative cost per patent where company R&D money is used with the situation where government money is used and finds approximately a 5:1 ratio (cf. the Sanders' study discussed above). From this, he presumes that either inventions or inventive manpower are siphoned off of government programs or that "inventiveness" is just less where government work is involved. Further, Dr. Solo suggests that contractors do not as readily seek patent protection for inventions resulting out of a federal R&D for purely business reasons, e.g. more profitable alternative oppor-

tunities exist.

In his discussion of the rate of commercialization of NASA inventions, Dr. Solo first deals with the "waived" inventions, i.e., those inventions where the contractor takes title. He concludes that the economy at large has not benefited from such commercialization. With over \$15 billion in R&D contracts from 1959-1964, Dr. Solo found only six inventions used, none of them important. Similarly, where NASA retained title, the effort to transfer technology by offering inventions for nonexclusive royalty-free licensing has been just as sterile. The strongest impression the author received from his findings was the pervasive and sometimes absolute indifference on the part of contractors to the commercial potentialities of inventions made under government R&D contracts.

In part three, Dr. Solo makes recommendations whereby inventiveness and commercialization may be increased. He suggests making a company's past record of inventiveness and inventive contribution a basis to be considered in awarding R&D contracts with a NASA branch implementing this procedure. He further recommends a direct invention reporting system between contractor inventors and NASA. Also, strict enforcement of the so-called "march-in" rights is recommended so that any exclusivity granted to the contractor could promptly be voided at the

end of the stipulated time period unless there is clear evidence of an attempt by the contractor of some sort of commercialization.

Dr. Sanders wrote a commentary<sup>16</sup> on Dr. Solo's work and although he agreed with Dr. Solo regarding the negligible returns from the patented inventions, when it came to possible remedies, Dr. Sanders saw little merit in his recommendations. Firstly, Dr. Sanders disputes an assertion of Dr. Solo's that the Kennedy Memo has not produced any discernable difference in invention disposition citing statistics pointing to the fact that, since the Memo, there has been an upward trend for the government to retain title to the patents. With respect to Dr. Solo's quantitative analysis, Dr. Sanders points out a number of flaws, namely, the two "sets" of inventions, i.e., waived and government-owned, are biased samples especially with respect to commercialization; that the possibility that the traits of employees working with government funds differs from those working with private funds was not taken into account; and that relating disclosures of one year to R&D expenditures for that same year is questionable. In his own computations relating the numbers of disclosures in one year to R&D obligations received in the preceding year, Dr. Sanders finds, in general, higher costs per patent to the contractor than was originally thought.

Dr. Sanders takes exception to Dr. Solo's recommendations. With respect to "direct reporting," Dr. Sanders asserts that to make such reporting practical, the government would have to establish offices with different contractors with the consequent disruption of the contractors operations thereby further decreasing efficiency. As to the recommendation of using inventiveness of corporations as a basis of offering a contract, the commentator suggests that the procedure would be cumbersome and costly and of dubious effectiveness to really measure comparative inventiveness of various competing firms. Lastly, as to enforcement of march-in rights, Dr. Sanders suggests that in the face of the indifference shown by contractors, this suggestion appears pointless.

One of the purposes of the Kennedy Memorandum was to have a Patent Advisory Panel collect data relating to the operation of the patent policy. Very little data collection had been attempted prior to a study done by Drs. Watson and Holman<sup>17</sup> which collected the numbers, the sources, and the kinds of patented inventions flowing from government-sponsored research and development. The information for the article on the numbers of patents assigned to and licensed to the government was obtained from records maintained by the Assignment Branch of the U.S. Patent Office. The article goes on to disclose in

table form the numbers of patents owned by and licensed to the government in the years 1945-1962 inclusive. Also, data disclosing the patent portfolio (unexpired patents) of the government for those years is given. The data is further broken down as to the titles and licenses held by the individual agencies. The federal R&D patents are categorized into their fields of technologies both according to the Patent Office classes and by industry. Finally, data is given as to the numbers of patents obtained from contractors vis-à-vis government employees.

The same authors later reported<sup>18</sup> on the criteria used by the six largest government patent departments in screening and evaluating inventions for patent applications. It is apparent that the propensity to patent ranges from the low of the Air Force, which files applications on only 10 percent of disclosures submitted to it, to a high in Agriculture which files on 80 percent of its disclosures. It was noted that although, usually, expected profitability was not a criterion, both AEC and NASA do use "commercial potential" as a factor. Another criterion applied by all agencies was "technological importance," presumably, the expected extent of use within the department. A majority of the agencies make use of a point system in evaluating their disclosures. From the accumulated data it was found that, in general,

there has been a slight decline in the government's propensity to patent, although three agencies have had a constant or nearly constant propensity.

The authors conclude that the principle cause of the decline in propensity, where it has occurred, is to be found in the number of patent attorneys in the agencies.

An inverse relation between the propensity to patent and the rate of use of patented inventions was found. The authors terminate the report with the thought that these quantitative generalities should be given weight in any future changes in patent policy relating to government financed research and development.

#### FOOTNOTES

<sup>1</sup> Howard I. Forman, "Wanted: A Definitive Government Patent Policy," PTC J. Res. & Ed. (*IDEA*), Vol. 3, No. 4 (Winter 1959), pp. 399-415.

<sup>2</sup> *Ibid.* p. 400.

<sup>3</sup> *Ibid.* p. 410.

<sup>4</sup> *Ibid.* p. 408.

<sup>5</sup> Donald S. Watson, Harold F. Bright and Arthur E. Burns, "Federal Patent Policies in Contracts for Research and Development," PTC J. Res. & Ed. (*IDEA*), Vol. 4, No. 4 (Winter 1960), pp. 295-434.

<sup>6</sup> Donald S. Watson, "New Information on the Operation of the License Policy in Federal Contracts for Research and Development," PTC J. Res. & Ed. (*IDEA*), Vol. 5, No. 4 (Winter 1961-62), pp. 287-296.

<sup>7</sup> See note 5, *supra*.

<sup>8</sup> Mary A. Holman, "The Utilization of Government-Owned Patented Inventions," PTC J. Res. & Ed. (*IDEA*), Vol. 7, No. 2 (Summer 1963), Vol. 7, No. 3 (Fall 1963), pp. 109-161.

<sup>9</sup> Barkev S. Sanders, "What Should the Federal Government's Patent Policy Be?," *IDEA*, Vol. 8, No. 2 (Summer 1964), pp. 169-198.

<sup>10</sup> See note 5, *supra*.

<sup>11</sup> See note 8, *supra*.

<sup>12</sup> Barkev S. Sanders, "Comparative Patent Yields from Government Versus Industry Financed R&D," *IDEA*, Vol. 9, No. 1 (Spring 1965), pp. 1-23; Vol. 10, No. 1 (Spring 1966), pp. 33-60.

<sup>13</sup> See note 9, *supra*.

<sup>14</sup> Helge Holst, "Government Patent Policy—It's Impact on Contractor Cooperation with the Government and Widespread Use of Government Sponsored Technology," *IDEA*, Vol. 9, No. 1 (Spring 1965), pp. 109-130; Vol. 9, No. 2 (Summer 1965), pp. 273-296.

<sup>15</sup> Robert A. Solo, "Patent Policy for Government-Sponsored Research and Development," *IDEA*, Vol. 10, No. 2 (Summer 1966), pp. 143-212.

<sup>16</sup> Barkev S. Sanders, "Commentary on Patent Policy for Government-Sponsored Research and Development," *IDEA*, Vol. 11, No. 1 (Spring 1967), pp. 61-87.

<sup>17</sup> Donald S. Watson, Mary A. Holman, "Patents from Government-Financed Research and Development," *IDEA*, Vol. 8, No. 2 (Summer 1964), pp. 199-222.

<sup>18</sup> Donald S. Watson, Mary A. Holman, "The Federal Government's Propensity to Patent," *IDEA*, Vol. 10, No. 1 (Spring 1966), pp. 61-74.



# Observations on the Role of Trademarks in Ecology

JOSEPH M. LIGHTMAN\*

## INTRODUCTION

ENVIRONMENTAL PROTECTION IN THIS COUNTRY is complex and expensive—the basic demands are to stop polluting and to clean up what is already polluted. Government and industry sectors gearing up to meet the pollution crisis are undertaking a broad spectrum of legislative, administrative, and institutional action. The effectiveness of their programs is conditional not only upon technological achievements but also upon adequate awareness by the public of what is being accomplished and what it can do to improve the situation.

Within this context, The PTC Research Institute has undertaken a project on the role and contribution of industrial property in environmental improvement, with particular reference, in the first phase of its study, to innovations, patents and licensing. This phase of the project

---

\* Research Associate, The PTC Research Institute; International Economist, Foreign Business Practices Division, Office of International Investment, Bureau of International Commerce, U.S. Department of Commerce.

has included a Special Conference bringing together a number of experts to explore the role of our industrial property system in pollution control. The results of that meeting have been reported in a special publication titled, "Air and Water Depollution: Roles of Industrial Property, Innovation and Competition." An additional report on this study has also been published.<sup>1</sup>

The current phase of the Institute's study deals with another segment of industrial property being increasingly emphasized in public awareness aspects of pollution control, namely, trademarks.<sup>2</sup> This article is based upon a survey of government and industry practices relative to the role of trademarks in this context. The survey is also part of the Institute's on-going study of the economic aspects of trademarks in corporate management practices and consumer protection, the results of which have also been published in *IDEA*.<sup>3</sup>

#### PROGRAM MAGNITUDES

Today's society dictates problem areas for the American business community transcending the traditional profit and efficiency motives. Among those posed foremost by our growing and urbanized economy is pollution control.<sup>4</sup> The magnitude of the problem may well be understood by an examination of the scope of environmental fall-out in this country, the projected clean-up costs, and the publicity methods needed to spur appropriate action.

#### *Consumption and Expenditure Factors*

Presently, although Americans account for only about 7 percent of the world's population, they consume about half of the industrial raw

---

<sup>1</sup> John C. Green, "Innovators View Effect of Industrial Property on Depollution Technology," *IDEA*, Vol. 14, No. 4 (Winter, 1970-71), p. 471.

<sup>2</sup> Included within this context are commercial names, slogans, acronyms and other markings in which individuals or groups may have proprietary rights. These may include registered and unregistered marks and other distinctive labelings available for ecology-oriented activities.

<sup>3</sup> "Economic Aspects of Trademark Utilization"; "The Economic Role of Trademarks and Their Utilization as Business Assets"; "Economic Interests in Service Marks," *IDEA*, Vol. 11, No. 4 (Winter 1967-68) pp. 472-499; Vol. 10, No. 3 (Fall 1966), pp. 323-336; Vol. 13, No. 1 (Spring 1969), pp. 25-56. Also, Institute Clinic on "International Trademark Protection," *IDEA*, Vol. 15, No. 1. (Spring 1971), pp. 79-174.

<sup>4</sup> This is not intended to minimize other basic problem areas confronting industry, such as minority employment and urban revitalization, nor to imply that they may be less formidable than pollution control.



materials it produces. Just in the past 15 years, the number of cars on U.S. roads has doubled, electrical output in this country has tripled, and consumption of plastics production has increased tenfold. Also, in today's trillion dollar economy, new products ranging from high phosphate detergents to nonreturnable bottles are exacting a high price in air, water and land pollution for consumer convenience. In terms of uncollected or unprocessed trash, abandoned cars, littered cans and bottles, and untreated sewage dumped into waterways, the U.S. is estimated to contribute about 40 percent of the world's pollution.<sup>5</sup>

Although there is no comprehensive or officially published data on amounts spent by American industry to control pollution, there are several studies published by private research organizations providing insights on industry magnitudes.

A recent report by McGraw-Hill's Economics Department notes that U.S. firms in 26 industries surveyed will increase pollution control outlays by 46 percent over last year for a total of \$3.6 billion. The total projection for the next five years is \$18 billion. Of such industries, those under major pressures to clean up the environment and which will reportedly spend more than \$1 billion each are electric utilities (\$3.2 billion), iron and steel (\$2.64 billion), petroleum (\$2.12 billion), paper (\$1.84 billion), nonferrous metals (\$1.62 billion), gas utilities (\$1.04 billion), and chemicals (\$1 billion).<sup>6</sup>

The National Industrial Conference Board states that 248 respondent manufacturing firms reported investing \$238 million in 1968 and \$306 million in 1969 (a 27 percent increase) for pollution control. In total, it was estimated that U.S. manufacturing industries spent slightly less than \$1 billion in 1968 for this purpose.<sup>7</sup>

The Research Division of the Center for Political Research, a divi-

---

<sup>5</sup> *Business Week* (October 17, 1970), p. 88.

Also pertinent is elaborative statement by Richard D. Vaughan, Acting Commissioner for Solid Waste Management Office, Environmental Protection Agency, noting that:

"In a typical year, Americans will discard over 30 million tons of paper, 4 million tons of plastic, 48 billion cans and 26 billion bottles. Solid wastes generated from municipal and industrial sources amount to more than 360 million tons annually; this figure includes 250 million tons of household, commercial and municipal wastes, and 110 million tons resulting from industrial activities. Altogether, over 3.5 billion tons of solid wastes are generated in the U.S. every year, if wastes from agriculture and mining and fossil fuel production are included." *Waste Age* (April 1970), p. 10.

<sup>6</sup> *Business Week* (May 15, 1971), p. 46.

<sup>7</sup> See National Industrial Pollution Control Council's Report (February, 1971) p. 40, prepared for the Secretary of Commerce. No further NICB data was available at the time the NIPCC Report was published.

sion of the *National Journal*, prepared in 1970 a five-year expenditure projection (1971 through 1975) by manufacturing industries for environmental control. The projection is based on data derived from relevant federal agencies. It shows a total outlay of \$7.45 billion for this period for pollution control relative to air, water, and solid waste problems.<sup>8</sup>

It is apparent from these reports that private expenditures for pollution control will increase substantially within the foreseeable future as pressures mount to conform with local and federal laws. While much of the expenditures will be for new plant and equipment as well as restructuring efforts, more funds will also be going into research and development. McGraw-Hill notes that the R&D budgets of its respondents for pollution control will rise about 25 percent in 1971 to a total of nearly \$926 million, including some government financed programs.<sup>9</sup> Aerospace and automotive industries are reportedly the largest spenders for antipollution R&D.<sup>10</sup>

Not to be overlooked in these pollution control costs are expenditures for protecting industrial property rights. Patenting and prosecution costs will continue as important aspects of industries' R&D efforts to implement and improve their programs. The U.S. Patent Office reported that in 1970 it allowed 700 issuances of an ecological nature.<sup>11</sup>

### *Identity Considerations*

Yet, industry is faced with another important aspect of industrial property rights expenditure in pollution control—its public image. Foremost in the management planning of a growing number of U.S. manufacturing and service firms are corporate identity programs geared to environmental improvement, as well as to market expansion activities. Such companies are highly concerned about their "perception" by the public and what they can do to improve their images through proper trademark adaptations.

Earlier surveys by The PTC Research Institute have shown that, in many instances, the trademark portfolios of leading U.S. firms are being

---

<sup>8</sup> *Ibid.*, p. 41. Yearly breakdowns are 1971 (\$1.15), 1972 (\$1.55), 1973 (\$2.06), 1974 (\$1.63) and 1975 (\$1.06).

<sup>9</sup> *Business Week*, *supra* note 6.

<sup>10</sup> *Ibid.* See also U.S. Department of Commerce, "The Economy at Midyear 1971 with Industry Projections for 1972," pp. 38 and 40.

<sup>11</sup> Under the Patent Office's special priority procedures for processing patent applications related to environmental improvement, 380 antipollution inventions were expedited over 200,000 pending cases. Their processing and examination were reduced from the current 21½ year average to under 8 months.

tied to extensive educational campaigns to achieve as wide an identity as possible with involvement in today's social problems, including environmental improvement.<sup>12</sup> Ecology is a particular field in which trademarks have largely transcended their traditional roles as distinctive markings for goods and services and where their functions as advertising tools and as focal points for goodwill identification have extended beyond commercial marketing considerations. Ecology-minded companies are finding trademarks, as well as trade names and other forms of labeling, useful devices for impressing on the public images of their social consciousness. The U.S. government likewise has undertaken extensive publicity campaigns, built around trademarks and slogans, relative to environmental improvement.

This article will delve into the "corporate identity" aspects of ecology, as well as governmental public awareness programs.

#### GOVERNMENT INITIATIVES IN PUBLIC AWARENESS

The Environmental Policy Act of 1970 requires every U.S. federal agency to take into account the ecological impacts of its programs, to redesign them in the interest of environmental improvement, and to undertake appropriate publicity in this context.<sup>13</sup> Within this policy framework and the implementing actions, there permeate public awareness initiatives for institutions and programs—some built around trademarks, others utilizing symbolic identities, and still others emphasizing slogans and acronyms.

#### *Other Major Legislation*

The Refuse Act of March 3, 1899, intended to free national waterways from navigational obstacles, bars dumping of refuse into rivers or lakes without a permit from the Army Corps of Engineers. As the oldest antipollution law on the books it is now, after 70 years, being enforced to regulate discharge of pollutants into waterways from some 40,000 industrial plants in this country. Further strengthening the government's system for up-grading U.S. waterways is the 1965 Federal Water Pollution Control Act and the Clean Water Restoration Act of 1966.

---

<sup>12</sup> *IDEA*, Vol. 11, No. 4, p. 477; Vol. 13, No. 1, pp. 41-42; *op. cit.* (Note particularly the report of the utility company respondent.)

<sup>13</sup> Each agency is required to include in every recommendation or report on proposals for legislation and other major federal actions significantly affecting the environment, a detailed statement on the environmental impact of the proposed action.

Legislation designed to combat air pollution is embodied primarily in the Clean Air Amendments of 1970 Act providing for national air quality standards to be implemented and enforced by the states.

Other salient legislation includes the Environmental Quality Improvement Act, the Solid Waste Disposal Act, and the Fish and Wildlife Coordination Act. There are other major amendments to earlier legislation, such as that governing insecticide and pesticide control and forestry and agricultural activities.

### *Federal Agency Framework*

A three-member Council on Environmental Quality was established in 1970 under the Environmental Policy Act. Its basic responsibilities are to advise the President and to coordinate policy and action, and to develop legislative proposals, in the environmental field. The statute also provides that the Council consult with the Citizens Advisory Committee on Environmental Quality.<sup>14</sup>

The National Industrial Pollution Control Council (NIPCC) was created in 1970 to advise the Administration on environmental policies as they affect industry and to provide leadership for voluntary industry initiatives in pollution clean-up. NIPCC is headquartered at the U.S. Department of Commerce and furnishes its advice to the President and Council on Environmental Quality through the Secretary of Commerce.<sup>15</sup>

The major regulatory institution, which came into being in 1970, is the Environmental Protection Agency (EPA). It took over about 15 programs scattered throughout the federal government for setting and enforcing standards for air and water pollution, solid waste disposal, and pesticide and radiation control. Its functions also include research on causes, effects and control of environmental problems and assistance to state and local governments.<sup>16</sup>

---

<sup>14</sup> Originally established in 1966 as the Citizen's Advisory Committee on Recreation and Natural Beauty; reconstituted in 1969 in a broader environmental context; consists of 15 representatives.

<sup>15</sup> NIPCC's work is carried out through 30 Sub-Councils and special committees dealing with specific industry problems. Consisting of top corporate executives, they make periodic reports of recommendations and progress in achieving pollution clean-up within the industry sectors.

<sup>16</sup> Within EPA's Water Quality Office, there also functions the Student Council on Pollution and the Environment (SCOPE). SCOPE was initially organized in 1969 as a student advisory body to the Secretary of the Interior on methods and programs to deal with environmental problems. It now operates through student regional councils and undertakes programs such as public education on recycling, community action for antipollution activities, and advice on resource usage.

Another newly established key agency is the National Oceanic and Atmospheric Administration (NOAA), in the Department of Commerce, responsible for long-range research on future pollution problems, including global trends affecting the oceans and atmosphere.

Most federal agencies with operating responsibilities are involved with matters affecting environmental programs. Salient examples include the Departments of Interior and of Agriculture, in their recreation and conservation activities; of Health, Education and Welfare, in its public health activities; and of Housing and Urban Development, in its community beautification programs. These agencies have technical assistance, educational, and publication programs on environmental improvement responsibilities within their purviews.

### *Program Identity Facets*

The U.S. government's ecology campaign affecting its own real estate has, as its focal point, the JOHNNY HORIZON trademark, consisting of an especially designed logo and a symbolic forester-type individual "who represents the thoughtful user of America's publicly owned lands."<sup>17</sup>

Launched by the U.S. Department of Interior's Bureau of Land Management in 1968, the trademark, coupled with the slogan "This land is your land—keep it clean," is aimed at pollution control in about 800 million acres of land managed by federal agencies, including parks, forests and playgrounds. Available from that agency to civic and other public groups are materials such as litterbags, classroom packets, decals, posters and other exhibit material using the trademark, for clean-up project campaigns. The mark is also available for use in TV and radio public service announcements. In its publicity campaign, the Department of Interior has enlisted the services of various celebrities, most notably Burl Ives, whose name and "forester image" also appear in some of the JOHNNY HORIZON literature in the same logo.

The Department of Interior recently decided to license the JOHNNY HORIZON trademark for commercial use, with royalties to be used to expand the program. Licensing, to be handled by Columbia Special Products, will be available for coloring and comic books, greeting cards, outdoor equipment, and children's boots.

The U.S. Department of Agriculture's Forest Service, guided by the publicity experience of its SMOKEY BEAR trademark in fire preven-

---

<sup>17</sup> U.S. Department of Interior announcement JH 1120-2 (August 1969).

tion programs, recently adopted a new trademark, WOODSY OWL, for comparable publicity purposes in its antipollution campaign.<sup>18</sup> The trademark, picturing an owl clad in Robin Hood hat and green pants, with the slogan "Give a Hoot . . . Don't Pollute," will be used in extensive publicity and education campaigns for a broad range of antipollution programs to be undertaken by the agency. The Public Service Council, a tax-free, non-profit corporation, has been designated to secure private financing and other help for the campaign.<sup>19</sup> The mark will also be licensed for commercial use, with royalties to be used for operational purposes similar to the SMOKEY BEAR program. The symbol will focus attention on environmental improvement through Forest Service programs on soil protection; proper vegetation, air and water use; elimination of unnecessary noise; and control of vandalism and of destruction in public lands. As in the JOHNNY HORIZON program, WOODSY OWL material, including decals, bumper stickers, and coloring sheets for school children, will be made available.

Other agencies have adopted ecology-oriented symbols although not necessarily for specific promotional campaigns as have the above agencies. The Environmental Protection Agency, for example, now has an official seal depicting a flower with a bloom that symbolizes blue sky, green earth and blue-green water.<sup>20</sup>

The National Industrial Pollution Control Council's literature conspicuously displays its symbol—the NIPCC logo superimposed on the design of a gear wheel, research test tube, and rippled line—depicting industry in progress on research and other activities affecting clean air, land, and water.

Special legislation is reportedly under consideration in the Senate and House Public Works Committees to utilize roadside rhyme signs, similar to those identified with the trademark BURMA SHAVE, for antipollution appeals along the nation's highways.<sup>21</sup> State and local government entities are also utilizing specially designed trademarks and

---

<sup>18</sup> U.S. Department of Agriculture, Forest Service, announcement of June 2, 1971. Subject: WOODSY OWL Environmental Education Campaign.

<sup>19</sup> Business supporters for the WOODSY OWL program include, so far, American Metal Climax, Campbell Soup Co., Hughes Aircraft Co., Hunt-Wesson Foods, Los Angeles Clearing House Association, and Title Insurance and Trust Co. *Advertising Age* (September 27, 1971), p. 92.

<sup>20</sup> Established by Presidential Executive Order, October 18, 1971.

<sup>21</sup> *The Washington Post* (September 14, 1971), p. B 15. Jack Anderson ("The Washington Merry-Go-Round"), article entitled "Roadside Verse May Decry Pollution."

symbols in their antipollution programs.<sup>22</sup> Government initiatives to arouse and involve the public in environmental improvement activities have not overlooked the very useful role that can be played by trademarks and other distinctive symbols.

#### ECOLOGY SYMBOLS IN THE PRIVATE SECTOR

Identities used by private firms and by ecology groups to symbolize their environmentally oriented activities may include national "all purpose" symbols, or "special purpose" marks, such as those that denote recycling. Firms have also developed their own specialized marks for particular environmental improvement activities. Also, among many ecology action groups, the practice is to adopt a name capable of being publicized as an environmentally identifiable acronym (see Appendix).

##### *The National Ecology Symbol*

Basically, the symbol now generally accepted throughout the U.S. as the national ecology trademark consists of a circle, usually elliptical, with a horizontal line through the diameter. The symbol has evolved as ecology's "silent salesman" appearing in national publications and as pledge insignia of the many private industrial, professional and civic organizations active in environmental improvement campaigns.

R. Cobb, the cartoonist originator of the symbol, depicts it basically as a derivation of the lower case "e" for "environment" (and corollary alliteratives such as "earth," "Eden") on which is superimposed the circle or letter "o" for "organism" (and alliteratives such as "oneness" and "oasis").<sup>23</sup>

A green flag of ecology consisting of the above symbol in the upper left hand corner and 13 green and white stripes is also used and distributed by various ecology groups for national awareness purposes.

---

<sup>22</sup> For example, the Maryland-National Capital Park and Planning Commission, which prepares zoning plans and recommendations for Montgomery and Prince Georges counties, has rights to a CHARLIE ECOLOGY symbol consisting of a penguin character with the slogan "Pollution is bad for penguins and other people," to be used on litter bags and in other publicity material in its antipollution campaign.

<sup>23</sup> Cartoon appearing in *Action: April 22*, published March 19, 1970 by Environmental Action, Inc., Washington, D.C., notes that symbol was authored in a cartoon explanation by R. Cobb, October 25, 1969; also, that the cartoon was copyrighted in that year by Sawyer Press with "all rights reserved" and that "the symbol is offered in public domain."

The green stripes depict "unspoiled land" and the white stripes, "pure air."

Another adaptation of the ecology symbol is the nationally used "clean water" sign, consisting of an elliptical circle with a rippled center line; the top white half bearing the word "clean"; the bottom blue half, "water." Other, more particular, adaptations are exemplified by the coast-to-coast "Clean Air Car Race" launched by students of Massachusetts and California Institutes of Technology last spring with 33 low pollution car entries built by students at 33 colleges. The national poster distributed for this race prominently displayed the ecology symbol, on which was superimposed a cloud-like design for exhaust; with the logo "Clean Air Car Race."

### *The "Keep America Beautiful" Campaign*

Keep America Beautiful, Inc. had been in existence as an organization dedicated to promotion of environmental improvement activities long before the current antipollution program began. Formed in 1953 by leading firms and civic and trade associations as "The National Public Service Organization for the Prevention of Litter," it is now headquartered in New York City. The organization's symbol—an American flag circled by "Keep America Beautiful," and two stars—appears with its public service announcements in magazine and newspaper ads. In its current program, The Advertising Council and The International Newspaper Advertising Executives have prepared a 1971 "Help Fight Pollution Campaign" under which specialists voluntarily prepare "Keep America Beautiful" public service messages for magazines and newspapers. These messages, urging the public properly to dispose of trash and to cut down on pollution, emphasize the slogan "People start pollution. People can stop it."

Keep America Beautiful, Inc. has also cosponsored, with Tom McAn Shoe Company, CAPTAIN CLEANUP clubs to which over 30,000 youngsters now belong. The club program utilizes a CAPTAIN CLEANUP logo and symbol which appear in coloring books and advertising media encouraging readers to help "Keep America Beautiful."

### *National Special Purpose Symbols*

The usual techniques for disposing of solid wastes are landfill, incineration, and water dumping. Through industry and government initiatives, however, new techniques are being developed to reclaim



such materials from collected waste for recycling and reuse.<sup>24</sup> A number of nationally publicized trademarks and slogans have been developed to attract public attention to this activity, involving, primarily, metals, paper fibers, and glass.

The principal private association now concerned with promotion of recycling is The National Center for Resource Recovery, Inc. (formerly The National Center for Solid Waste Disposal, Inc.) headquartered in Washington, D.C. It is a non-profit corporation organized and financed by industry and labor groups engaged in production, use and sale of packaging. The Center provides many services to industry, labor and government, including a technology information center on solid waste disposal, research on economics of technology in this field, public awareness and demonstration programs, and technical assistance activities. The Center's nationally used trademark consists of a "Chinese infinity symbol" which is similar to a horizontal figure-eight with a heavy black center bar with a broken space. The Center notes that "our modern version of the Chinese infinity symbol has the open space to signify the unsolved solid waste problems—and the unlimited opportunities to be gained from solving them through recycling and resource conversion."

#### The Metals Industries

The metal can industries have greatly accelerated their container collection and recycling programs in the past few years. Particularly active in sponsoring and publicizing such programs have been the aluminum producers.

The Aluminum Association of America has up-dated its collective "mark of aluminum" trademark which now consists of a circular figure formed by two half circles each with an arrow pointing in a clock-wise direction. Within the circle are the words "Recycle aluminum" or "Recyclable aluminum" and a pyramid-shaped folded figure. The mark

---

<sup>24</sup> The Resource Recovery Act of 1970, sponsored by Senator Muskie (Maine), authorizes \$467.7 million over three years for research and demonstration grants. The Chase Manhattan Bank, N.A., New York City, notes in its bimonthly *Business in Brief* (No. 99, August 1971), that "At present, some 35% of the silver used in this country comes from secondary sources. Reclamation from waste currently accounts for nearly half the iron and steel, over 50% of the lead, 40% of the copper, and 25% of the zinc made available for new products in the United States. And about one-third of the aluminum in the world is being recycled. Nonmetallic minerals, such as mercury, are also recycled to some extent, as are other materials, such as glass, fibers and paper."

is offered by the Association to makers of all-aluminum cans and semi-rigid foil containers for use in advertising, and on packaging.

Major aluminum can producers engaged in recycling promotion have effectively utilized their own special markings and slogans. For example, Alcoa's recent program for encouraging collection of used aluminum cans in California communities for recycling was successfully sparked by a "Yes We Can" mark and slogan publicized through a series of newspaper, radio and television messages.

Among aluminum can users, Adolph Coors Co. of Golden, Colorado, a brewery firm, provides a good example of symbol utilization in collection and reuse. Early last year, it announced a "Cash for Cans" program as a means of securing used aluminum cans for recycling. Under its program, the company distributed an explanatory kit bearing the aforementioned Aluminum Association of America recycling mark and a magnet for testing aluminum. The magnet, 1" by 2" square, bears the Coors' trademark logo and a distinctive red and white design with the legend "Coors Metal Check—If It Sticks It Isn't Aluminum."

### The Paper Fiber Industries

Paper accounts for about 50 percent of all solid wastes in the U.S. In 1969, over 40 million tons of paper and paperboard were thrown "away."<sup>25</sup> Now, many paper companies are rolling out recycled paper, and users are buying it not only for newsprint and packaging materials, but also for use in tissues, stationery and company publications. Environmental organizations, such as the Sierra Club,<sup>26</sup> are conducting active campaigns encouraging paper manufacturers to utilize recycling, and paper consumers to use such recycled products.

In the identity aspects of these programs, a national trademark has been developed and made available for public use by Container Corporation of America, Chicago, Illinois, to denote and promote recycled paper. It consists of a hexagonal figure formed by a design of three separately folded stripes each with an arrow pointed in a clockwise direction. The mark may be used with appropriate legends by manufacturers and others to identify paper "Made from 100%

---

<sup>25</sup> *Environmental Action* Vol. 3, No. 2 (June 12, 1971), p. 3, published by Environmental Action, Inc., Washington, D.C.

<sup>26</sup> An environmental organization headquartered in San Francisco, California. It has 85,000 members in 30 chapters and coordinates efforts of other conservation groups, among other activities in ecology, in preserving national forests.

Recycled Paper (or Fibers)”; or “Made Primarily from Recycled Paper (or Fibers)”; or to denote “Recyclable Paper (Package or Fibers).”

Companies which have developed their own distinctive “ecology paper,” such as Simpson Lee Paper Co., San Francisco, California, and Bergstrom Paper Co., Neenah, Wisconsin, are now promoting and selling it under trademarks, such as RENOVATION Mimeo, BERGSTROM ECOLOGY PAPERS, and RECYCLE/BOND. Such papers are intended primarily for use by consumer-oriented industries for annual reports, stationery and packaging materials. Many leading firms, such as Bank of America, Coca-Cola Company, and Canada Dry, as well as a number of state and city governments, to whom these new ecology products have been identified, are using them extensively for the above purposes.

### The Glass Industries

Although discarded bottles comprise a lesser percentage, tonnage-wise, of the nation’s solid waste than metal and paper products, they are, nevertheless, within the active recycling programs being undertaken by industry with government encouragement. Waste container glass is not only being recycled into the production of more glass products but is also being used to produce a wide variety of by-products such as compost, building blocks and insulation material.

Trademark identities are not yet as prevalent as in the aforementioned recycling programs, particularly in collective mark usage. Individual glass companies, however, have adopted trademarks to identify certain recycled glass products, as, for example, Anchor Hocking Company, Lancaster, Ohio. Utilizing technology developed by the University of Missouri, under a grant from the U.S. Public Health Service, in cooperation with the Glass Container Manufacturers Institute (GCMi), the company has produced a paving material from recycled glass, asphalt, and sand which it has identified as GLASPHALT. GLASPHALT usage is being closely watched by the glass industry and the government as an important possibility for solving waste glass disposal problems.<sup>27</sup>

Increased public attention is being drawn to these and other industry recycling programs. Trademarks are proving to be valuable tools in this context, not only for directing public awareness to resource recycling but also to the industries actively concerned with it.

---

<sup>27</sup> National Industrial Pollution Control Council, *Casebook of Pollution Cleanup Actions* (February 1971), p. s-5.

*Corporate Identities for Particular Programs*

Most U.S. firms with production facilities, being ecology-oriented, are directing efforts toward controlling their own pollution. In many instances, their trademarks and other forms of corporate identity have been changed to reflect these efforts.<sup>28</sup> Ecology-type products, of course, are also appearing on the market—some under new trademarks and others under revisions of trademarks used for the “pre-ecology” versions. Rather than cover the broad magnitude of U.S. manufacturers’ identity programs, The PTC Research Institute deems it more meaningful to discuss examples of such programs in selected industries. The examples chosen are those where ecology-oriented marketing is particularly innovative.

Petroleum firms and their subsidiaries are conducting a variety of ecology programs utilizing specially developed trademarks and symbolic designs. Mobil Chemical Co., Macedon, New York, for example, maker of plastic disposal bags under the trademark HEFTY has undertaken a “Bag Your Trash” campaign in various cities. Under the program, municipal authorities are encouraged to promote utilization of plastic bags in clean-up campaigns and in normal household trash and garbage disposal. Mobil’s “municipal specialists” serve as campaign coordinators in the selected cities, assisting municipal authorities and others in publicity and waste disposal problems. Mobil makes available, in addition to the bags, buttons, stickers, decals, posters and other display material. Serving as the advertising focal point for the program and appearing on the publicity material is a symbol showing a tied bag (plastic) on which appears the logo BAG YOUR TRASH. KEEP A NEAT STREET appears under the bag design which partially obscures that of a garbage can.

Clean air programs undertaken by gasoline marketers are exemplified by American Oil Co., Chicago, Illinois. In April 1971, the company initiated its FRESH AS A DAISY program to tie in with its efforts to identify with ecology and clean air. The objective of the promotion is to merchandise lead-free gas. Dealers are provided with kits consisting of daisy packages to be distributed to motorists; and with promotional and display material. The markings used on the packages and display material, and in publicity campaigns, consist of a uniquely

---

<sup>28</sup> For example, Consolidated Edison Co. of New York, Inc., changed its basic trademark logo from CON EDISON to CON EDISON CLEAN ENERGY. Several manufacturing firms that had smokestack designs in their trademarks eliminated or changed them to obviate possible identity implications with air pollution.

designed "daisy" with the logo LEAD FREE AMOCO and FRESH AS A DAISY in the presentation.

The low-lead or no-lead gasolines designed to effect cleaner exhaust, being marketed by American Oil Company and others in the "Big Five,"<sup>29</sup> plus some regional marketers, are publicized under such respective company trademarks as 100 OCTANE AMOCO SUPER PREMIUM, SHELL OF THE FUTURE, and BIG PLUS (Humble).

Other industries are undertaking specific antipollution campaigns through centrally organized educational programs. For example, meat packing, animal and poultry processing industries have established an Animal Products Industries Pollution Control Program. An "Official Pollution Control Training Kit" made available for company purchase and use includes educational films, posters, radio and television scripts, and suggested plant news releases. Prominently offered in this kit as a "Symbol of your effort to curb pollution" is a "Plant flag for exterior display below our national colors. Forest-green field emblazoned with 'ecology' symbol tells your employees and neighbors that your plant has joined in our industry's campaign to control pollution." Companies are encouraged to "Display it proudly!"

In the electrical appliance field, Whirlpool Corporation, Benton Harbor, Michigan, began marketing a trash compactor last year, pioneering a new field of ecology-oriented activity for household goods manufacturers. The machine facilitates bagging, handling, and disposal of household trash by compressing 30 pounds of it (amount reportedly generated in a week by a family of four) to approximately one-fourth of its original size. The trademark TRASH MASHER was adopted for this product and now serves as the focal point for its advertising. A SEARS KENMORE trademarked compactor is also made by Whirlpool for Sears, Roebuck & Co., Chicago, Illinois. Emerson Electric Co., St. Louis, Missouri, is now marketing a similar product under its IN-SINK-ERATOR mark. Amana Refrigeration, Inc., Amana, Iowa, Tappan Co., Mansfield, Ohio, and General Electric Co., New York City (Hot-point Division), are also reportedly planning to enter this new ecology market, utilizing distinctive trademark identities in their sales campaigns.

The market for bottled purified water has expanded rapidly, as the general public has become increasingly concerned about municipal water system impurities. The soft-drink industry, particularly, has shown the most interest—not only because these companies already

---

<sup>29</sup> Texaco, Inc., Shell Oil Co., Humble Oil and Refining Co., and Gulf Oil Co.

purify water for their products but also because of possible threats to sales. Some now have their own logos to identify "purified water," as, for example, Canada Dry which markets the product in its usual bottle with the CANADA DRY trademark and the logo PURE DRINKING WATER. Other leading soft-drink bottlers are expected to enter this growing market utilizing their own distinctive markings to publicize a pure water product made by their distinctive processes.

Within the soft-drink industry, the Coca-Cola Company reports that the manufacturer of its metal containers will now supply it with soft-drink cans the tops of which will be embossed with the labeling "Please don't litter—dispose of properly." Special advertising has also been developed to promote the sale of returnable bottles. The symbolic thrust of the campaign is a conspicuously publicized question "Wouldn't you rather borrow our bottle than buy it?"

Another ecology-oriented market ripe for expansion is that for noise monitoring systems. Such systems usually bear special identities for advertising and public awareness purposes. For example, the system made by Northrop Aircraft Corporation, Hawthorne, California, for noise monitoring at airports is identified as ECOLOG-1. It is used to determine the exact effect of airport noise in localities and to provide data upon which effective noise abatement programs can be built.

New ecology-type products, distinctively trademarked, are showing up in "ecology displays" at department stores and major appliance outlets, as manufacturers expand production of such products. In the Washington, D.C. area, for example, a number of local stores will have displays featuring such "ecologizers" as an electric can opener, trademarked OPEN SESAME, made by Westinghouse Electric Corporation, Pittsburgh, Pennsylvania. The opener cuts the rim off cans instead of just the top, permitting re-use since the lid can be tightly fitted back. A new bottle recycling kit identified as EPHREM's OLDE TIME BOTTLE CUTTER KIT, made by Stylecraft Packaging, Charlotte, North Carolina, is also to be displayed. Ecology-oriented wastepaper baskets featuring the national paper recycling trademark and variations of the HELP FIGHT POLLUTION and SAVE THE EARTH slogans are also to be shown.

It is not possible within the scope of this article to provide details on all of The PTC Research Institute's findings relative to company identity programs in ecology. The above examples may serve to illustrate the significant role of trademarks and other forms of distinctive identities in their activities.

## CONCLUDING OBSERVATIONS

In today's ecology-oriented society, few companies with production facilities can afford to be without a corporate image related to environmental improvement. This poses the question of how best to convey such an image directly and succinctly to the public.

According to advertising researchers, today's average consumer is bombarded by anywhere from 500 to 1500 different advertising impressions per day. This includes, not only radio, television, newspapers and magazines, but also billboards, and advertising from trucks, signs, packages, store displays, handout circulars, et cetera. This constant effort by companies to publicize themselves and their goods and services necessitates, of course, communicative shortcuts, i.e., trademarks and other symbols, to enable the public clearly to discern what the company is, does, and has to offer.

Company trademark programs reflecting ecology consciousness may be projected primarily through product or service marks, with lesser emphasis on overall corporate identities. Or, such programs may be projected basically through overall house marks and corporate names, rather than brands. In this connection, companies may promote an all-purpose ecology-oriented mark to supplement, and publicize with, existing housemarks and brand names.

In the governmental context, Environmental Protection Agency Administrator, William D. Ruckelshaus has stated that:

We have been a people dedicated to change and invention and production and progress. Sometimes we have thought that virtually all change was progress and that all production was good. Millions of citizens now have arrived sharply at an awareness that much of our production and much of our consumption—in television or toasters or in automobiles or whatever—leads to pollution. This is the first time in American history that we as a nation started to re-think our old concepts on the proper development and conservation of our resources. At the turn of the century, President Theodore Roosevelt and Gifford Pinchot were ardent spokesmen for conservation and there was a strong leadership which led to major conservation measures. But only now have we developed a mass base, a growing public opinion, demanding that government and industry stop mis-using our resources. Most interesting of all, we have many citizens interested in taking actions themselves, to reduce their own contributions to pollution.<sup>30</sup>

Governmental agencies—federal, state and local—carrying forward their programs and related publicity campaigns are recognizing the import-

---

<sup>30</sup> Address on "The Structure and Program of the Environmental Protection Agency" presented at The Committee on Challenges to Modern Society, in Brussels, Belgium, which met April 19-20, 1971.

ance of trademarks and other distinctive symbols as attention-attracting mechanisms.

One national observer suggests the desirability of a strict system of product labeling comparable to, but broader than, that of a proposed Federal Trade Commission ruling which would require manufacturers to list prominently on detergent packages a warning that certain recommended use levels of the product contain quantities of phosphorous contributing to water pollution. Under the observer's suggested system, a wide variety of consumer goods would be labeled not only on performance and comfort contribution but also on what they contribute—good or bad—to the environment. Such "social cost labeling," it is contended, could contribute significantly to environmental clean-up by devising for the public "realistic signals which will alert us to unnecessary garbage, extra water and air pollutants."<sup>81</sup>

Ecology is thus creating a new dimension of trademark and labeling usage transcending commercial objectives. Many firms are utilizing new trademark logos, designs, and labels for ecology-type products, as well as to emphasize to the public their ecology-consciousness. Government use of trademarks in environmental improvement contexts has also established new magnitudes of identity for public interest purposes. The public, itself, is demanding to be better informed about pollution aspects of the products and services it uses, and the companies that offer them. Communicative shortcuts in this respect are most important.

---

<sup>81</sup> Sylvia Porter, article "Social Cost Labels Asked" in column "Your Money's Worth," *Washington Star* (October 11, 1971). Miss Porter notes that:

"This social cost labeling goes far beyond obvious pollution. For instance, if you knew more about the life expectancy of a toaster or an automobile or a stove or a TV set, might you not favor a longer-life product—even at higher cost—over the product which unexpectedly falls into hopeless disrepair? And, of course, you would be pleased by the thought that you were helping to reduce the volume of metallic trash in our land.

"Or, if you knew more about the environmental dangers of toxic drain cleaners, paint and stain removers, oven cleaners and the like, would you not take elementary precautions about adding them eventually to our ground water supplies?

"And what about basic information on the ingredients of the products in our medicine cabinets and on our dressing tables? Could any of them poison even a septic tank?

"And what about the excellent suggestion that labels on products made of materials that can be recycled carry the addresses of recycling facilities?

"Or what about a requirement that labels on paper containers, other paper products and publications tell whether or not the paper used has been recycled? The Federal government has begun requiring such information on some of the paper products it buys. Why not extend this requirement to other recyclable products?"



APPENDIX

**Examples of Ecology Acronyms Used by Environmental  
Civic, Professional and Other Organizations**

**F.O.E.**

Friends of the Earth  
New York City

**UNHITE!**

University of New Hampshire Improve the Environment  
Durham, New Hampshire

**CEASE**

Center for Ecological Action to Save the Environment  
Pearl River, New York

**C.L.E.A.N.**

Citizens League for Environmental Action Now  
West Virginia University  
Morgantown, West Virginia

**CLEAN**

Committee to Leave the Environment of America Natural  
Starkville, Mississippi

**MECCA**

Minnesota Environmental Control Citizens Association  
St. Paul, Minnesota

**CAP**

The Campaign Against Pollution  
Chicago, Illinois

**ENACT**

Environmental Action for Survival  
University of Michigan  
Ann Arbor, Michigan

**GOO**

Get Oil Out  
Santa Barbara, California

**STOP**

Society to Overcome Pollution  
Women's Action Group organized in Canada

**GASP**

Group Against Smokers Pollution  
Washington, D.C.

**GASP**

Greater Birmingham Alliance to Stop Pollution  
Birmingham, Alabama

**IMAGE**

Internal Mercury Action Group on Environment  
(Pollution Control Program)  
Kiekhofer Mercury  
Division of Brunswick Corporation, Fond du Lac, Wisconsin

# American Patent Utilization in Canada

O. J. FIRESTONE\*

## INTRODUCTION

IN THE FISCAL YEAR ENDING March 31, 1969, 27,703 patents were granted in Canada, 18,542 to American residents, or 67 percent.<sup>1</sup> In the same year, a sample survey was undertaken of patents granted in Canada in the years 1957, 1960 and 1963, to establish who did the patenting, what kind of inventions were patented, to what extent and how these patents were utilized, and how necessary the patent system was to facilitate the working of patented inventions in Canada.<sup>2</sup>

---

\* Professor of Economics, University of Ottawa.

<sup>1</sup> In the fiscal year ending March 31, 1970, the corresponding figures were 28,981, 19,173 and 66%.

<sup>2</sup> This survey was undertaken under the auspices of the Economic Council of Canada, which had requested the author to examine certain aspects of the Canadian patent system. The results of this survey are included in the author's study *Economic Implications of Patents* (Ottawa: University of Ottawa Press, 1971). Account of some of the survey results were taken in the *Report on Intellectual and Industrial Property*, Economic Council of Canada, Information Canada (January 1971), Chapter 4.

The survey consisted of 100 percent of patents granted to Canadian patent owners and 5 percent of patents granted to foreign patent owners, selected on the basis of a random sample, that is every 20th patent. On a weighted basis, the survey yielded 17,985 patented inventions of which 12,557 or 70 percent were American-owned, 25 percent owned by other nonresidents and 5 percent by Canadians. The 17,985 patents represented 30 percent of the total number of patents granted in the three survey years.<sup>3</sup>

This article summarizes some of the results as they pertain to American-owned patents granted in Canada in 1957, 1960 and 1963, in order to establish what happened to the inventions covered by these patents during a time span varying in length from 6 to 12 years after the patent grant.

#### WHO ARE THE PATENTEES

Of the total of 12,557 American-owned patents, 11,687 or 93 percent represented inventions made by corporate employees, and assigned to American companies. About 5 percent of American inventions patented in Canada were owned by independent inventors and 2 percent represented inventions made by employees of government agencies.

Two-thirds of the patented inventions owned by American corporations were in the hands of firms which operated subsidiaries in Canada and one-third of which did not have subsidiaries. Such companies were mainly interested either in utilizing the patented invention through licensing arrangements with other firms doing the manufacturing in Canada, or to protect their position by serving the Canadian market through exports from plants located in the United States. The figures were as follows: with subsidiaries 7,694; without subsidiaries 3,718; and not stated 275.<sup>4</sup>

Most patents were obtained by large U.S. corporations. To illustrate: About four-fifths of all unexpired patents owned by American patentees for which patents had been granted in Canada in 1963 were held by firms with 100 patents or more, and close to two-fifths involved firms with 1,000 patents or more.

---

<sup>3</sup> For details of the methods employed in conducting the survey and the weighting procedures used, see *Economic Implications of Patents*, Table 1, Appendix A and Appendix B. Since the sample survey represents a 30% coverage, this means that the 12,557 American-owned patents are indicative of the behavior pattern of a total of about 42,000.

<sup>4</sup> *Id.* Chapter 6.

## PATENTED INVENTIONS BY TYPE

American-owned inventions for which patents are taken out in Canada are strongly new-product oriented as the following tabulation shows.

	Number	Percent
New products	7,975	63.5
New method or process <sup>5</sup>	2,186	17.4
Both	1,154	9.2
Not stated <sup>6</sup>	1,242	9.7
Total	12,557	100.0

Of the product inventions patented, those pertaining to consumer goods are in the lead, followed by capital goods, semi-fabricated components and industrial materials (see below).

	Number	Percent
Consumer goods	2,938	23.4
Capital goods	2,326	18.5
Semi-fabricated components	2,151	17.1
Industrial materials	1,312	10.5
Other	367	2.9
Not stated <sup>7</sup>	3,463	27.6
Total	12,557	100.0

## PATENTED INVENTIONS BY INDUSTRY

Innovational activity is strongest in the science-oriented industries. They include four groups: chemical and electrical products, transportation equipment, and machinery. These four industries were responsible for about two-thirds of all patents granted and close to three-quarters of patents granted to manufacturing industries (see below). In Canada, these four industries provide employment for 24 percent of persons working in manufacturing and about 6 percent of the total employed in the country.

These four strongly technologically oriented industries record some of the highest proportions of foreign ownership, over four-fifths for the four groups combined. And further, foreign-owned and controlled

---

<sup>5</sup> Some new methods may also be new-product oriented.

<sup>6</sup> Includes "not applicable."

<sup>7</sup> Includes "not applicable" which also covers process inventions mentioned above.

	Number	Percent
Chemical products	3,061	24.4
Electrical products	2,589	20.6
Transportation equipment	1,434	11.5
Machinery industry	1,102	8.8
Other manufacturing	3,287	25.9
Non-manufacturing	577	4.6
Not stated <sup>8</sup>	507	4.2
Total	12,557	100.0

companies in these sectors and doing much better earning-wise than do Canadian firms, as the data below show. There are a number of reasons for the greater profitability of these foreign-owned companies, mainly large American corporations, operating in Canada. They include: large scale of operations, access to technological know-how from their parent companies, adequate financial resources and high credit rating, competent and mobile management, strong emphasis on innovations, et cetera.

	Foreign-Owned and Controlled Companies <sup>9</sup> as Percent of All Companies Reporting, 1968	
	Assets	Net Earnings <sup>10</sup>
Chemical products	87.5	92.4
Electrical products	66.9	86.7
Transportation equipment	87.7	88.9
Machinery industry	73.9	87.1
Sub-total	81.0	89.3
Total manufacturing	60.0	63.8

#### PATENT UTILIZATION

Of American-owned inventions patented in Canada, 51.5 percent were worked abroad but only 15.7 percent were worked in Canada. To some extent this illustrates the great reliance on imports of products covered by patented inventions into Canada from the United States.<sup>11</sup>

<sup>8</sup> Including "not applicable."

<sup>9</sup> Defined as 50% or more nonresident owned.

<sup>10</sup> Covers taxable income.

<sup>11</sup> A sample study of patents granted in the United States in 1938, 1949 and 1952 showed the following proportions as being commercially used: for assigned patents 56.5% and for unassigned patents 49.4%. See "Patterns of Commercial Exploitation of Patented Inventions by Large and Small Companies," by Barkev S. Sanders, *IDEA*, Vol. 8, No. 1 (Spring 1964), p. 51.

These percentages apply to the total period patented inventions were worked, that is, before patents were granted in Canada and after it, up to 1969.

Another question asked in the survey was the number of patented inventions actually worked in 1969, eliminating those that had ceased being worked. The results were as follows:

	Inside Canada		Outside Canada	
	Number	Percent	Number	Percent
Worked	1,504	12.0	4,529	36.1
Not worked	10,966	87.3	7,766	61.8
Not stated	87	0.7	262	2.1
Total	12,557	100.0	12,557	100.0

American-owned patented inventions worked in Canada during the whole period numbered 1,959. Deducting the 1,504 still being worked during 1969 meant that work had been discontinued on 455 inventions for which patent protection was still in force.<sup>12</sup> The latter number represented 22 percent of the total worked.

American-owned inventions patented in Canada but worked abroad during this period numbered 6,470 and those still being worked in 1969 numbered 4,529. The difference of 1,951 or 30 percent of the total comprised patented inventions on which work had been discontinued abroad. This suggests a lesser failure rate in Canada than abroad. In part the explanation would be less pressing competition in Canada than in the United States and in part the working of the time-lag factor since most patented inventions are first worked in the United States before they are utilized in Canada.

#### PATENT LICENSING

Out of a total of 12,557 patents granted to American patentees, 1,679 licenses equal to 13 percent of the total, were made to Canadian firms. Of these, 927 or 54 percent were exclusive licenses, 612 or 36 percent were nonexclusive licenses, and 140 licenses or 8 percent were in the "not stated" category.

---

<sup>12</sup> Few of these patents would have been found invalid because of court action.

Of a total of 1,679 licenses granted, 647 patented inventions or 38 percent were issued on the basis of cross-licensing, that is for the licensee in return making available to the licensor a license for another patented invention. This suggests increasingly that the quid pro quo approach does not necessarily mean more royalty payments but the ability of one firm to be in a position to exchange its technological know-how for that of another firm.

#### SIMILARITIES AND DISSIMILARITIES

The Canadian patent system has many similarities with the American system. In fact, the first Patent Act passed by the Canadian Parliament in 1869<sup>13</sup> borrowed many statutory provisions of the U.S. Act of 1836.<sup>14</sup>

Currently, Canadian patent legislation, like that of the United States bases inventorship priority rights on the date of the invention and not on the date of the filing of the invention.<sup>15</sup> Other similarities of the Canadian and U.S. patent systems include the 17-year duration of the patent grant, the absence of renewal fees to keep a patent in good standing, the right to assign patents to other parties as to the whole interest or any part thereof.

Some of the differences include the existence of more far-reaching licensing provisions in Canada than in the United States and this is particularly the case in food and drug products. The U.S. Supreme Court has set particularly high standards as a prerequisite for a patent grant, including the requirement for the invention, "to make a distinctive contribution to scientific knowledge."<sup>16</sup> American interference proceedings go somewhat further than Canadian conflict procedures in that the former require that the applicant must show that he was "diligent" in reducing his invention to practice and in filing, while the latter do not require this.

---

<sup>13</sup> 32 and 33 Vict., c. 11.

<sup>14</sup> Act of July 4, 1836, Ch. 357, 5 Stat. 117.

<sup>15</sup> The Philippines is the third country to use the first-to-invent principle while all other countries use the first-to-file system. The Canadian Government is presently considering proposals to change from the first-to-invent principle to the first-to-file system, following recommendations to this effect made by the Economic Council of Canada (see *Report on Intellectual and Industrial Property, op. cit.*, p. 88).

<sup>16</sup> *Great Atlantic & Pacific Tea Co., v. Supermarket Equipment Corp.*, 1950, 340 U.S. 147, at pp. 154-155 (concurring opinion).

In the United States, elaborate and extensive clinical testing is required before a drug patent can be issued. In Canada, the Patent Office is concerned with applicants meeting the requirements of the Patent Act, leaving it to the Food and Drug Directorate of the Department of National Health and Welfare to protect the public from the marketing of unsafe pharmaceuticals.

Further, the more vigorous administration of the antitrust provisions in the United States in the post-war period has induced many large corporations to follow cautious policies in utilizing monopolistic grants granted to them under the patent legislation. In Canada, proceedings under the Combines Act are less far-reaching than proceedings under the antitrust laws in the United States. It is therefore of interest to establish how American firms feel about the protection they can obtain under the Canadian patent system to proceed with the working of inventions as compared with the views held by Canadian and other non-Canadian patentees.

In the sample survey, patentees were asked how important they considered the Canadian patent system as a factor in deciding to work the invention covered under the patent in Canada. A greater proportion of American corporations considered that the existence of the Canadian patent system was of fair or major significance in their decision to proceed with the working of an invention in Canada than did Canadian-owned corporations, with companies owned by other non-residents taking a middle position, as the data below indicate.

	Canada	United States	Other Countries	All Countries
Little or no significance	51.4	39.6	44.4	41.8
Fair significance	29.5	48.5	44.4	45.3
Major significance	19.1	11.9	11.2	12.9
Total	100.0	100.0	100.0	100.0

Since 90 percent of Canadian patents issued are held by corporations and since 96 percent of these are foreign-owned, this means that 86½ percent of Canadian patents granted are held by corporations owned and/or controlled abroad. When it comes to utilizing inventions in Canada, the majority of these companies say that the Canadian patent



system is a fair or major factor in their decision to proceed, while the majority of Canadian patentees hold the opposite view.

#### POLICY IMPLICATIONS

Increasingly, the question is being raised in Canada whether the Canadian patent system is giving greater advantages to foreign-owned companies than to Canadian-owned companies, not because the law and the regulations do not treat all patent applicants as equals, but because of the economic advantages which foreign companies operating in Canada enjoy.<sup>17</sup>

This greater reliance of foreign corporations on patent protection in Canada to maintain their superior position seems to lend support to the argument of those who say that Canada might be better off if the protection offered by the patent system was reduced. This was also the conclusion of the Economic Council of Canada which had been charged by the Canadian Government in a Reference dated July 22, 1966 "to study and advise regarding . . . patents, trademarks, copyrights and registered industrial designs . . . with a view to bringing the policy in these matters into harmony with the overall economic policy of Canada and the needs of the consumer and other important segments of the economy."<sup>18</sup>

After assessing the evidence and in particular examining the price effects on the consumer, the Council concluded that Canadians may be "carrying too large a proportion of the costs of the system in relation to the proportion of the benefits that [they] receive."<sup>19</sup>

Among other things, the Council recommended import competition with respect to articles covered by patents granted in Canada under certain circumstances. "The patent right should be so defined that neither the holder of a Canadian patent nor any licensee thereunder should have the right to prevent the importation into Canada by any person of the patented article or an article made by the patented process, from other countries where the article or process enjoys patent protection."<sup>20</sup> Some move in this direction was made in 1969 with respect to pharmaceutical and food products, but the recommendations of the Economic Council, if implemented, go much further.

---

<sup>17</sup> *Supra* note 3, Chapter 6.

<sup>18</sup> *Report on Intellectual and Industrial Property*, *supra* note 1, p. 1.

<sup>19</sup> *Id.*, p. 81.

<sup>20</sup> *Id.*, p. 90.

Public pressure is growing in Canada to reduce some of the protection provided under the Canadian patent system and to subject foreign patentees to greater public scrutiny than has been the case in the past.<sup>21</sup> Among the various reasons advanced as contributing to it are:

- (1) 95 percent of all patents granted go to foreign patentees, including 70 percent to American firms and individual inventors;
- (2) The bulk of the patents are held by a small number of large multinational corporations, mainly American;
- (3) These companies control the bulk of the science-oriented industries operating in Canada, with these firms being the greatest beneficiaries of the Canadian patent system;
- (4) Such corporations do not do enough R&D in Canada;
- (5) Such firms, in most instances, limit Canadian production of patented articles or goods produced using patented processes to supply the Canadian market only, limiting or prohibiting access to export markets even if the Canadian firms, subsidiaries in most instances, are competitive worldwide;
- (6) The price effects of patents work to the disadvantage of the Canadian consumer without adequately compensating employment and income effects;
- (7) Defensive patenting practices followed by some foreign firms hold back technological progress in Canada; and
- (8) Patents generally strengthen the overwhelming hold which foreign-controlled corporations, mainly American, already have over Canadian secondary and resource industries.

Canada had over 350,000 patents in effect in 1970. Close to 250,000 would be held by American patentees and the bulk of these by large multinational corporations. Management of such corporations may wish to consider the growing public sentiment in Canada which expects such firms to use patents obtained in Canada not only in their own interest but also in the interest of the host country.

---

<sup>21</sup> *Act to Amend the Patent Act, the Trade Marks Act, and the Food and Drugs Act*, 17-18 Eliz. II. c. 49.

## STUDENT PAPERS

---

By making available student papers, students will receive an incentive and our readers will appreciate the evidence of scholarly development in the fields of interest. These papers are carefully reviewed by the Editorial Committee and other specialists, and helpful suggestions are made to the students as part of the educational function of *IDEA*. The Research Institute invites educational and research institutions to submit informative student manuscripts on the patent, trademark, copyright, and related systems.

### Copyright Protection for Sports Broadcasts and the Public's Right of Access\*

PAUL E. KRITZER

#### THE THESIS

THIS PAPER INVESTIGATES two contemporary thrusts in American copyright law. One is the angry demand of millions for access to see or hear sports events of paramount public interest broadcast on the commercial airwaves. The other thrust is the plea by sports promoters who sell broadcast rights to their events for protection against cable television (CATV). The first is a reaction against the severe restrictions imposed upon access to the recent Frazier-Ali heavyweight boxing

---

\* This paper, chosen to represent the Georgetown University Law Center, received the Patent Office Society Student Award for 1971. The Patent Office Society Student Award program is conducted annually under the auspices of The PTC Research Institute. This paper was submitted in partial fulfillment of the requirements of a course in copyright law.

championship. The second relates to a provision buried deep in the 1971 Copyright Revision Bill<sup>1</sup> that would grant copyright protection to the broadcasters of live sports events.

It is the thesis of this paper that a resolution of these ostensibly unrelated interests would comprise a viable *quid pro quo* that would promote the public interest and the "useful arts."<sup>2</sup> Section 111 (c) (4) (C) of the Copyright Revision Bill, granting copyright protection to broadcasts of live sports events, should be enacted by Congress. In return—the *quid pro quo*—Congress should also enact either H.R. 7127 (the "Aspin Bill") or H.R. 6992 (the "Sandman Bill")<sup>3</sup>, both of which deny to private sports promoters the right to arbitrarily limit access to a major sports event or championship (i.e., closed-circuit television screenings only) and which also require such events to offer their broadcast rights in an open market to the television networks.<sup>4</sup>

These proposals are unorthodox, but they are not radical departures from contemporary law. This paper presents arguments demonstrating how these two thrusts can be resolved and accepted without violating the Copyright Clause of the Constitution.<sup>5</sup> Specifically:

- (1) These proposals do not unconstitutionally infringe sports promoters' freedom of enterprise or freedom of contract.
- (2) Major sports events with a significant history of live television network broadcasting should be considered "public goods"; further, because of the extensive "state action" involved in the dissemination of television broadcasting, programs of live sports events have evolved such a "public character" that the public interest demands their dissemination to the greatest possible audience.

<sup>1</sup> S.644, 92nd Cong., 1st Sess., § 111 (c) (4) (C) (1971).

<sup>2</sup> *U.S. Const.*, art. I, § 8, cl. 8.

<sup>3</sup> 92nd Cong., 1st Sess. (1971).

<sup>4</sup> The fear is that popular spectator sports will be limited just to wealthy witnesses. This would be economic discrimination against millions of television viewers, whose support was instrumental in popularizing professional sports. See, Sandman, "Discrimination in Favor of Wealthy Witnesses at Major Sporting Events," 117 *Congressional Record* H1425 (daily ed. March 10, 1971); Reston, "The Greedy Sports Promoters," *New York Times* (March 10, 1971), p. 41, col. 1; Cosell, "Speaking of Sports," American Broadcasting Company (Radio Network) (March 10, 1971). In an editorial entitled "The Fight," the *New York Times* said:

In the case of the two gladiators of Monday night, the state and the society and the media not only encouraged it but glorified it and rewarded it beyond the wildest dreams of barbaric avarice. What has this to do with the "manly art of self defense"? This is a paid professional superspectacle in which the two men battering each other for the delectation of the mob, and for \$2.5 million each, are at the center of a world-wide business enterprise involving expenditures and hoped-for profits reaching into the stratosphere. *New York Times* (March 10, 1971), p. 40, col. 2.

<sup>5</sup> *U.S. Const.*, art. I, § 8, cl. 8.

- (3) Granting copyright protection to broadcasts of live sports events—whether or not recorded on tape—is a logical extension of the Copyright Clause of the Constitution and the Copyright Act of 1909 and is compelled by the exigencies of advanced technology.
- (4) The broadcast of live sports events meets constitutional requirements: classification as a “writing,” tangibility, originality and creativity.
- (5) Acceptance of these proposals would be in the public interest.

### THE CONTEXT

On March 8, 1971, Joe Frazier and Muhammad Ali engaged in a pugilistic contest of momentous public interest. Some 20,455 persons—the lucky ones—paid up to \$150 to be witness at Madison Square Garden in New York (total gate receipts: \$1.6 million).<sup>6</sup> Another 1.6 million persons, paying from \$12.50 to \$30 for a seat, saw “The Fight” at one of 365 closed circuit television facilities in the United States and abroad. Total revenues were estimated at \$16.5 million.<sup>7</sup>

Unfortunately, an estimated 118 million Americans were unable to see or listen to “The Fight.” The promoters allowed no network television coverage (either live or subsequent) and no radio coverage. The Overseas Armed Forces Radio Network was blacked out. During the contest, Associated Press and United Press International were limited by court injunction to sending only brief summaries.<sup>8</sup>

---

<sup>6</sup> *New York Times* (March 10, 1971), p. 49, col. 8.

<sup>7</sup> *New York Times* (March 10, 1971), p. 50, col. 2.

<sup>8</sup> The Frazier-Ali fight has already been tabbed a “triumph of . . . news restriction” by the influential *Columbia Journalism Review*. The fight promoters were so concerned about restricting interim reporting that they served a legal threat upon Associated Press reporters seated at ringside. The *Review* included a note by Roger Tatarian from the March 18, 1971, edition of *UPI Reporter*:

While the promoters did not succeed, they did come away with a court ruling that literally invites them to block all interim reporting from ringside if they feel it essential to safeguard their commercial rights as promoters. . . . The court said the promoters “had and still have available to them the means to prevent the complained-of use—by barring wire services either from the arena or from transmitting during the fight.” It is this observation that clouds the future of interim reporting. . . . [W]e are on notice as to where things will begin when we start discussing the ground rules for the next closed-circuit bonanza.

*Columbia Journalism Review*, Vol. 10 (May-June 1971), p. 4.

In Europe, such restrictions would be impermissible. See, Larrue, “Sports Programmes and International Television: The Legal Aspect,” *European Broadcasting Union Review*, Vol. 110B (1968) p. 52.

Since the Frazier-Ali fight, loud protests against the promoters<sup>9</sup> have stirred calls for Congressional action. Two types of bills have been introduced. The first type—the “Aspin Bill”<sup>10</sup>—would ban closed circuit telecasting of major sports events unless the television networks had first declined to purchase broadcasting rights on the grounds of insufficient public interest. The second type—the “Sandman Bill”<sup>11</sup>—would ban nationwide television and radio blackouts of major sports events. This bill would require access to major sporting events for each type of electronic medium: Television, subscription television, radio, closed circuit television, cable television and any other medium approved by the Federal Communications Commission. Under the Sandman Bill professional football’s “Super Bowl” could be carried by a closed circuit television network so long as it was also available simultaneously on free network television, radio and cable television.<sup>12</sup>

Section 111(c) (4) (C) of the Copyright Revision Bill is designed expressly to protect the broadcast rights of sports events from being

<sup>9</sup> Chief promoter is Jerry Perenchio. He hired Management Systems Television Network, Inc., whose chairman is former FCC chairman E. William Henry, to establish and operate the closed circuit network, which was the largest in history. After the fight, a spokesman for Management Systems said his corporation hoped to secure exclusive rights for telecasting the “Super Bowl” (on closed circuit), for which he estimated revenues of \$48 million. *New York Times* (March 10, 1971), p. 50, col. 2.

This same firm announced an antitrust suit against 16 National Football League teams and the three television networks on July 24, 1970, because it was allegedly denied the right to stage a closed circuit telecast of the 1970 “Super Bowl” after it had leased the Rivergate Auditorium in New Orleans. *Philadelphia Evening Bulletin* (July 25, 1970), § B, p. 12.

<sup>10</sup> H.R. 7127, H.R. 7679 and H.R. 7680, 92nd Cong., 1st Sess. (1971), are identical bills introduced by Rep. Lee Aspin (D.-Wis.). He claims 31 cosponsors. S.1435, 92nd Cong., 1st Sess. (1971), is an identical bill introduced by Sen. Adlai E. Stevenson III (D.-Ill.).

<sup>11</sup> H.R. 6992, H.R. 7962, H.R. 8060, H.R. 8061 and H.R. 8102, 92nd Cong., 1st Sess. (1971), are identical bills, three of which were introduced by Rep. Charles W. Sandman, Jr. (R.-N.J.); the second and fifth bills were introduced by Reps. Harold R. Collier (R.-Ill.) and Joseph G. Minish (D.-N.J.) respectively.

<sup>12</sup> Parenthetically, a countertrend should be noted. Rep. Morris K. Udall (D.-Ariz.) introduced a bill (H.R. 6897) on March 29, 1971, to limit the seasons during which professional sports could be broadcast. The bill would eliminate overlapping sports seasons on television, such as baseball-football or football-basketball/hockey. However, Rep. Udall’s bill would eliminate several events of our cultural heritage, such as the World’s Series, and it is applicable only to four sports. Rep. Udall remarked in introducing the bill: “Wall Street, Madison Avenue and television—with all their bucks and executive savvy—are on their way to turning professional athletics into another Edsel.” Udall, Press Release to H.R. 6897, March 29, 1971, at p. 1.

purloined and retransmitted without permission by cable television systems. The key provision of the section states:

[T]he secondary transmission to the public by a cable system of a primary transmission made by a broadcast station . . . embodying a performance or display of a work is actionable as an act of infringement . . . (C) Where the reference point of the cable system is within a United States television market, . . . and—

(i) the content of the particular transmission program consists primarily of an organized professional team sporting event occurring simultaneously with the initial fixation and primary transmission of the program.<sup>13</sup>

There are two other conditions precedent to copyright protection:

(ii) [T]he secondary transmission is made for reception wholly or partly outside the local service area of the primary transmitter; and

(iii) the secondary transmission is made for reception wholly or partly within the local service area of one or more television broadcasting stations licensed by the Federal Communications Commission, none of which has received authorization to transmit said program within such area.<sup>14</sup>

Integral to this section is the instantaneous character of copyright protection for the broadcast. Moreover, the broadcast itself is granted copyright protection even though the copying process (by electronic or magnetic video tape) is a procedure entirely separate—and rather unnecessary—to the broadcast.

The thrust of this section of the Copyright Revision Bill is intended to reverse the effect of *Fortnightly Corporation v. United Artists Television, Inc.*,<sup>15</sup> wherein the Supreme Court found the Copyright Act no impediment to cable television systems which retransmit program signals picked up from FCC-licensed television stations. The Court held the *Fortnightly* cable system to be no more than a passive viewer of the television signals it picked up and retransmitted and thereby not subject to liability under the Copyright Act.

CATV systems receive programs that have been released to the public and carry them by private channels to additional viewers. We hold that CATV operators, like viewers and unlike broadcasters, do not perform the programs they receive and carry.<sup>16</sup>

*Fortnightly* gave CATV systems free access to retransmit television programming, which inexorably would include broadcasts of live sports events.

Section 111 (c) (4) (C) is thus needed by sports promoters to protect

---

<sup>13</sup> S.644, 92nd Cong., 1st Sess., § 111 (c) (4) (C) (1971).

<sup>14</sup> *Id.*

<sup>15</sup> 392 U.S. 390 (1968).

<sup>16</sup> 392 U.S. at 400-401.

their broadcast rights from being used freely on CATV, without the permission of the owner of the rights.

## THE PUBLIC'S RIGHT OF ACCESS

### *Favored Treatment*

#### Judicial

Organized professional sports have enjoyed favored government treatment—exemption from antitrust regulations—for 50 years. Favoritism was established in 1922 by a unanimous Supreme Court in *Federal Baseball Club of Baltimore, Inc. v. National League of Professional Baseball Clubs*.<sup>17</sup> Although member clubs of the National and American Leagues provided baseball games for profit and systematically transported their players from one state to another, the Court held that this did not constitute “interstate commerce.” Ergo, no violation of antitrust statutes. By contemporary standards, the Court’s reasoning is hollow:

The business is giving exhibitions of baseball, which are purely state affairs . . . [T]he fact that in order to give the exhibitions the League must induce free persons to cross state lines and must arrange and pay for their doing so is not enough to change the character of the business . . . [T]he transport is a mere incident, not the essential thing. That to which it is incident, the exhibition, although made for money would not be called trade or commerce in the commonly accepted use of those words. As it is put by the defendants, personal effort, not related to production, is not a subject of commerce. That which in its consummation is not commerce does not become commerce among the States because the transportation that we have mentioned takes place.<sup>18</sup>

*Federal Club* was tersely affirmed by the Court in 1953.<sup>19</sup> Employing an estoppel argument, the Court reasoned that as baseball had been left to develop for 30 years on the understanding that it was exempt from antitrust legislation, to change at such a late date required an act of Congress.

*Federal Club* is an atrocious decision, a triumph of gastronomical

<sup>17</sup> 259 U.S. 200 (1922).

<sup>18</sup> 259 U.S. at 208-209.

<sup>19</sup> *Toolson v. New York Yankees*, 346 U.S. 356 (1953). (*Per curiam*, Justices Burton and Reed dissenting.)



jurisprudence. Justice Oliver Wendell Holmes later allowed that his opinion was myopic.<sup>20</sup> In its haste to preserve baseball's status quo the Court, indulging in a shell game of legal reasoning, ignored the obvious interstate features.<sup>21</sup>

In the 50 years since *Federal Club* the Supreme Court has reversed itself on the meaning of "interstate commerce."<sup>22</sup> In *Federal Club* the Court used the example that

[A] firm of lawyers sending out a member to argue a case, or the Chautauqua lecture bureau sending out lecturers, does not engage in such commerce because the lawyer or lecturer goes to another State.<sup>23</sup>

Contrast that with an example of the Court's contemporary thought. In *Daniel v. Paul*,<sup>24</sup> the Court ruled that a privately owned Arkansas recreational facility, which catered to out-of-state guests and served food, leased boats and provided a jukebox—all of which were produced in, and imported from, another state, was identified with interstate commerce (and thus liable under Civil Rights statutes). The extent to which the Court stretched the meaning of "interstate commerce" in *Daniel* clearly repeals the legal foundations of *Federal Club*.

### Legislative

Congress, like the Supreme Court, has not failed to extend favored treatment to organized professional sports. In 1961, two months after a federal court had ruled that the National Football League's plan to sell exclusive television rights of league games to the Columbia Broadcasting System violated antitrust statutes,<sup>25</sup> Congress passed remedial

---

<sup>20</sup> "The bill was brought before the decision of the *Base Ball Club Case*, and it may be that what in general is incidental, in some instances may rise to a magnitude that requires it to be considered independently." *Hart v. Keith Vaudeville Exchange*, 262 U.S. 271, 274 (1923) (Holmes, J.). *Accord*, *Toolson v. New York Yankees*, 346 U.S. 356, 360-361 (1953) (Burton, J., dissenting).

<sup>21</sup> *Federal Club* is still good law; organized baseball's exemption from antitrust legislation was recently upheld in *Flood v. Kuhn*, 316 F.Supp. 271 (S.D.N.Y. 1970), *affirmed* 443 F.2d 264 (2d Cir. 1971), *cert. granted*, 40 U.S.L.W. 3174 (October 19, 1971).

<sup>22</sup> *See*, 259 U.S. at 208.

<sup>23</sup> 259 U.S. at 209.

<sup>24</sup> 395 U.S. 298 (1969).

<sup>25</sup> *United States v. National Football League*, 196 F.Supp. 445 (E.D. Pa. 1961). *See also* *United States v. National Football League*, 116 F.Supp. 319 (E.D. Pa. 1953). Ironically, the NFL was boxed into selling broadcast rights to just one network by the threat of antitrust prosecution by the fledgling American Football League, which found that the NFL had preempted both the CBS and NBC networks.

legislation.<sup>26</sup> Noting that the “public interest in viewing professional league sports warrants some accommodation of antitrust principles,”<sup>27</sup> P.L. 87-311 was hastily enacted “to enable the member clubs of a professional football, baseball, basketball, or hockey league, to pool their separate rights in the sponsored telecasting of their games and to permit the league to sell the resulting package of pooled rights to a purchaser, such as a television network, without violating the antitrust laws.”<sup>28</sup> Other provisions of the statute required television “blackouts” where a broadcast would compete with a live home game of a league member or with a weekend college football game.<sup>29</sup>

### “Public Goods” and “State Action”

Books, photographs, dress designs, maps, films, musical compositions, architects’ drawings: these are types of creations that already enjoy copyright protection.<sup>30</sup> They have an attribute in common. Economists refer to them as “public goods,” i.e., a thing whose consumption by someone does not diminish the quantity available for others.<sup>31</sup> Television broadcasting—its product infinitely divisible and readily available to millions at the flick of a switch—fits this category.

The popularity and prosperity of professional sports has increased tremendously since the networks first started televising them in the mid-1950s. Audience ratings for professional football, baseball, hockey and basketball grew in leaps and bounds throughout the 1960s; in all cases except baseball the number of franchises in each sport doubled.<sup>32</sup>

<sup>26</sup> P.L. 87-311; 15 U.S.C. §§ 1291-1295 (1961), as amended 15 U.S.C. §§ 1291-1295 (1966).

<sup>27</sup> 1961 *U.S. Code Cong. and Adm. News* 3042, 3044.

<sup>28</sup> *Id.*, 3042. See 15 U.S.C. § 1291 (1961).

<sup>29</sup> 15 U.S.C. §§ 1292 and 1293 (1961, as amended 1966). Section 1292 was upheld in *Blaich v. National Football League*, 212 F.Supp. 319 (S.D.N.Y. 1962).

<sup>30</sup> See, Senate Committee on the Judiciary, Copyright Law Revision, Study No: 3, The Meaning of “Writings” in the Copyright Clause of the Constitution, 86th Cong., 1st Sess., 61-108 (1961).

<sup>31</sup> Samuelson, “The Pure Theory of Public Expenditure,” *Review of Economics & Statistics*, Vol. 36 (1954), pp. 387-389; Davis & Whinston, “On the Distinction Between Public and Private Goods,” *American Economic Review*, Vol. 57 (1967), p. 360.

<sup>32</sup> Baseball expanded to 24 from 16 major league franchises.

It is indisputable that free network television was integral to the development of vast public support for these sports.<sup>33</sup>

A basic presumption underlies both the Aspin and the Sandman bills: that the public has a right of access to view major sports events and championships on free network television. Sports promoters and Madison Avenue have oversold their products and have so imbued them with a "public character" in the process that now legislation is deemed necessary to protect the interests of the sports viewing public. A type of estoppel argument is proposed: that once a significantly large public television audience is bred, weaned and conditioned to periodic doses of televised professional football, baseball, hockey or basketball, such programming should not be arbitrarily denied to its audience. The greater interests of the polity subordinate the quick-profit private enterprise schemes of the few. By using television to establish their products and develop a massive public following, the promoters are estopped from pulling the plug upon the "convenience, interest or necessity"<sup>34</sup> of its vast audience. The needs and desires of 10 million or 50 million or 118 million sports fans constitute a greater public interest force than the monetary desires of a group of promoters. The public interest dictates that major sports events be barred from closed circuit television unless compliance with the strictures of the Aspin or Sandman bills is first made.

Favored treatment for organized sports within the federal government is based on the rationale that these are sports events put on for the divertissement of the whole nation from its normal preoccupations and to provide the populace with a common interest for a few hours. But closed circuit television threatens to change this and make major sports events the pleasure of the rich, with the ordinary citizen left outside the gate or staring at a sixth re-run of "I Love Lucy." Under such circumstances, this rationale should be reexamined; it may be time to dispense with the legal fiction that professional teams that gross millions of dollars each year are not doing business in interstate commerce, and thus not liable to antitrust regulation.

What is the source of the public's alleged right of access to watch important sports events on their home television sets? It emanates from

---

<sup>33</sup> See, *Quarterback*, Vol. 48 (February 1970), pp. 48-51, 83-88. Herein the three network sports directors (Bill MacPhail of CBS, Carl Lindemann of NBC and Roone Arledge of ABC), in a joint interview, modestly acknowledge that television was instrumental in popularizing professional sports, especially football.

<sup>34</sup> 47 U.S.C. § 307 (a) (1962).

a duopoly of factors: (1) an awakening in the judiciary that the public has rights equal to the broadcaster in the communications process; (2) an involvement by the government in the regulation and evolution of broadcasting so extensive that principles of "state action"<sup>35</sup> can be—and must be—invoked to protect the public interest.

The judicial awakening germinated with *Office of Communication of the United Church of Christ v. Federal Communications Commission*.<sup>36</sup> In an opinion that bristled at the FCC, then-Judge Warren Burger wrote:

After nearly five decades of operation the broadcast industry does not seem to have grasped the simple fact that a broadcast license is a public trust subject to termination for breach of duty.<sup>37</sup>

*United Church* recognized that broadcast programming should fulfill the needs of the community, and that the public—on a level at par with broadcasters—has rights in the operation of the communications process. These principles were broadly supported by the Supreme Court in *Red Lion Broadcasting Co. v. Federal Communications Commission*.<sup>38</sup>

The close regulation of broadcasting by the FCC, the exemption from antitrust legislation by special dispensation of Congress, and the outlandishly favored treatment granted to professional sports by federal courts together comprise a deep involvement by the government into the business of broadcasting professional sports events. Unquestionably, government regulation and statutory restrictions upon such broadcasts is justified by the "state action" doctrine.

The concept of a public right of access to particular major sports events on television can be implemented under the "public function" doctrine of "state action," adopted by the Supreme Court in *Evans v. Newton*.<sup>39</sup> If the Court can hold that parks in private hands cannot escape the stigma of an abiding "public character," then it is logical to conclude that programming of intense interest and wide audience has a "public character."<sup>40</sup>

---

<sup>35</sup> *Ex parte Virginia*, 100 U.S. 339 (1880); *Shelley v. Kraemer*, 334 U.S. 1 (1948); *Gomillion v. Lightfoot*, 364 U.S. 339 (1960); *Burton v. Wilmington Parking Authority*, 365 U.S. 715 (1961); *Amalgamated Food Employees Union v. Logan Valley Plaza, Inc.*, 391 U.S. 308 (1968).

<sup>36</sup> 123 U.S. App. D.C. 328, 359 F.2d 994 (1966).

<sup>37</sup> 359 F.2d at 1003.

<sup>38</sup> 395 U.S. 367 (1969).

<sup>39</sup> 382 U.S. 296 (1966).

<sup>40</sup> This would not place the FCC in a position where it would regulate programming; rather, it would merely insure that the interests of the public were not subordinated by greedy promoters.

*Freedom of Enterprise Subordinated*

Denying private sports promoters the right to restrict access to an event of great public interest, for the purpose of inflating ticket prices and employing closed circuit television, is not an unconstitutional impingement upon their freedom of enterprise and contract. When a subordinating public interest is invoked, such entrepreneurs may be denied the unlimited exploitation of economic opportunities and can be limited to making a profit that is modest or reasonable.

The actual taking of private property without compensation has been held to be constitutional, under the police power of the state, when it is necessary to protect the public health, safety, morality or general welfare.<sup>41</sup> Such "taking" must be done for a "public purpose" and it must be reasonable. The Supreme Court is inclined to find a use or purpose to be "public" if its advantages flow to a significant segment of the populace.<sup>42</sup> The finding of a rational basis for the legislation is an easy legal hurdle:

[D]ue process . . . demands only that the law shall not be unreasonable, arbitrary or capricious, and that the means selected shall have a real and substantial relation to the object sought to be obtained.<sup>43</sup>

Thus, freedom of economic enterprise can be subjected to governmental regulation by both federal and state governments when the regulation is reasonable and has a reasonable tendency to protect the public health, safety, morality or general welfare.

Although the Fifth Amendment demands "just compensation"<sup>44</sup> be paid by the government when it appropriates a person's property, it is noteworthy that the

Supreme Court has never ordered compensation paid to a citizen subjected to regulatory controls by either the federal or state governments on the theory that the regulation "had gone so far as to become a taking."<sup>45</sup>

Thus it is more likely that the regulation of broadcasting proposed in the Aspin and Sandman bills will not be so egregious as to require any compensation.

Passage of either of these bills would place the needs of society above the sanctity of the private contract—for which there is precedent. In

<sup>41</sup> *Miller v. Schone*, 276 U.S. 272 (1928). However, under the Fifth Amendment, it is rare to allow a public "taking" without "just compensation."

<sup>42</sup> *Berman v. Parker*, 348 U.S. 262 (1954).

<sup>43</sup> *Nebbia v. New York*, 291 U.S. 502 (1934).

<sup>44</sup> *U.S. Const. amend. V*, cl. 3.

<sup>45</sup> Antieau, *Modern Constitutional Law*, Vol. 1 (Supp. 1970), p. 214.

*Home Building and Loan Association v. Blaisdell*,<sup>46</sup> the Supreme Court upheld a state law barring the foreclosure of farm mortgages so long as a token fee was paid by the tenants because of the exigent economic conditions. The Court thus opened the Constitution to an interpretation that freedom of contract could be abridged in the public interest in order to alleviate *economic* discrimination. In the area of sports events, the Ali-Frazier fight was the ultimate in "economic discrimination." In view of the extent of "state action" involved, such economic discrimination is unconstitutional under the Equal Protection Clause of the 14th Amendment and the Due Process Clause of the Fifth Amendment.

#### COPYRIGHT PROTECTION FOR LIVE SPORTS BROADCASTS

##### *Moral-Economic Rights and Public Policy*

Assume for the moment that organized baseball's argument that absolute control over the dissemination of its product by broadcasts is necessary to preserve the financial integrity of the leagues' structure, especially from free-loading, pirating CATV systems. The next issue becomes whether a live broadcast of a sporting event, aside from whether or not it is being recorded simultaneously, is a copyrightable work.<sup>47</sup> There are good arguments to support copyright protection for live broadcasts of sports events: It is morally justified,<sup>48</sup> it is economically justified, and it should be adopted as a public policy.

The moral and economic justifications are based upon the premise that a creator is entitled to the fruits of his labor. Copyright establishes and recognizes the creator's property interest in the product of his labors and protects them from inequitable misappropriation.<sup>49</sup> The threat to professional sports that is most immediate is violation of the intent of the "blackout" laws<sup>50</sup> by CATV systems, which can retransmit the broadcast of a sports event into a market area where it might detract

<sup>46</sup> 290 U.S. 398 (1934). See Antiéau, §§ 3.16-3.18.

<sup>47</sup> 17 U.S.C. § 207 (1909); Nimmer, "Does Copyright Abridge the First Amendment Guarantees of Free Speech and Press?," *U.C.L.A. Law Review*, Vol. 17 (1970), p. 1180; Regulations of the Copyright Office, §§ 202.4-202.16.

In Europe, copyright would not be granted on the absence of "creative intellectual effort." Larrue, *supra* note 8; Giannini, "The Protection of Sporting Events," 58B *European Broadcasting Union Review* (1959), p. 27.

<sup>48</sup> Senate Committee on the Judiciary, Copyright Law Revision, Study No. 4, *The Moral Right of the Author*, 86th Cong., 1st Sess., 109-142 (1961).

<sup>49</sup> See, *International News Service v. Associated Press*, 248 U.S. 215 (1918).

<sup>50</sup> 15 U.S.C. §§ 1292, 1293 (1966).

from gate attendance.<sup>51</sup> With copyright protection, sports promoters could recover actual damages for decreased game attendance due to the infringement.<sup>52</sup> In addition, the copyright infringer can be enjoined from continuing his conduct. However, without copyright protection, the sports promoters and television networks carrying sports broadcasts can be victimized by a lack of remedies. Television station owners, the Ninth Circuit Court has held, may recover from competing CATV systems for retransmitting programs which were being broadcast simultaneously by the station only in an action based on copyright infringement.<sup>53</sup> Moreover, under the *Sears-Compco* doctrine, courts are loathe to grant "backdoor" protection on the grounds of "unfair competition" after statutory copyright protection has expressly been denied.<sup>54</sup>

There lurks a danger with copyright protection—that it may be used to suppress rather than to exploit access to ideas and developments. By pyramiding ownership of many individual copyrights in a particular area, a single person can establish an "enterprise monopoly." This runs contrary to the thrust of the First Amendment. With the establishment of an "enterprise monopoly," its owner would have procured not only the capacity to regulate the timing and pricing of public access to its inventory, but also an ability to control, in rough proportion to the size of his copyright aggregation, the selection of works made available to the public.<sup>55</sup> For this reason the public must have a statutory right of access, as detailed by either the Aspin or the Sandman bill.

Under principles of public policy, a copyright is granted when it will benefit the public interest. The function of copyright is to encourage the creation of works for public dissemination, especially where the absence of a copyright scheme of rewards and restraints would cause an inexorable matriculation of the article into the exclusive reserve of the wealthy or the politically motivated.<sup>56</sup>

A tort concept—a weighing of the opposed interests—should be

<sup>51</sup> An example: Courier Cable Co., a CATV subsidiary of the Buffalo Courier-Express, has imported the broadcast of home games of the Buffalo Bills from the NBC affiliate station in Erie, Pa., 90 miles southwest. Because of Buffalo's early winter weather and Memorial Stadium's lack of parking, high prices and location in a high-crime area, many Bills fans prefer to watch their heroes on home CATV. So 20,000 empty seats during a regular season game has not been an unusual sight during the past three seasons.

<sup>52</sup> International News Service, *supra* note 49.

<sup>53</sup> Cable Vision, Inc. v. KUTV, Inc., 335 F.2d 348 (9th Cir. 1964).

<sup>54</sup> Sears, Roebuck & Co. v. Stiffel Co., 376 U.S. 225 (1964); Compco Corp. v. Day-Brite Lighting, Inc., 376 U.S. 234 (1964).

<sup>55</sup> Goldstein, "Copyright and the First Amendment," *Columbia Law Review*, Vol. 70, (1970), pp. 983, 986.

<sup>56</sup> *Id.* at p. 995.

employed to determine the copyrightability of sports broadcasts. If continued broadcasts supporting unauthorized CATV retransmissions into "blackout" areas imposed economic loss upon certain promoters, then the interests of those victimized sports promoters and the large public audience will dictate that copyright protection be granted. However, if copyright protection should become obstructive to the public interest, it must be removed.<sup>57</sup> Remember that the paramount purpose of the Copyright Clause of the Constitution is "To promote the progress of science and useful arts."<sup>58</sup>

### *Constitutional Requirements*

The Constitution provides that:

The Congress shall have Power . . . (8) 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.<sup>59</sup>

A literal reading of this clause would invalidate most copyright legislation passed by Congress since 1790 and the extension of copyright protection to motion pictures and video tapes, as well as advertising, photographs, paintings, maps, cartoons, and three-dimensional objects. But courts have interpreted the Copyright Clause far beyond its original meaning. To be copyrightable under the Copyright Clause and the Copyright Act of 1909,<sup>60</sup> a work must (a) be in the form of a "writing," and (b) be a product of original, creative authorship.<sup>61</sup>

"Writings" have been defined by the Supreme Court in terms of principles and standards, not whether the form is tangible.<sup>62</sup> It is sufficient if the means through which the idea is expressed can be identified.<sup>63</sup> In *Metro-Goldwyn-Mayer Distributing Corp. v. Bijou Theatre Co.*,<sup>64</sup> a lower federal court held that motion pictures

<sup>57</sup> *Baker v. Selden*, 101 U.S. 99 (1879).

<sup>58</sup> *U.S. Const.*, art. I, § 8 (emphasis added). For discussion of this clause and its interpretation by the courts, see, Senate Committee on the Judiciary, *supra* note 30, at pp. 87-89.

<sup>59</sup> *U.S. Const.*, art. I, § 8, cl. 8.

<sup>60</sup> 17 U.S.C. § 1 *et seq.*

<sup>61</sup> Register of Copyrights, Copyright Law Revision: Report on the General Revision of the United States Copyright Law, 87th Cong., 1st Sess., 9 (1961).

<sup>62</sup> Senate Committee on the Judiciary, *supra* note 30, at p. 84.

<sup>63</sup> *White-Smith Music Publishing Co. v. Apollo Co.*, 209 U.S. 1 (1908). See, Nawalanic, "Common Law Copyright and Conversation," *Cleveland State Law Review*, Vol. 20 (1971), pp. 188, 189-190.

<sup>64</sup> 3 F.Supp. 66 (D.-Mass. 1933).



qualified for copyright protection under the heading of "writings." If motion pictures qualify as "writings," then it is safe to conclude that the same treatment should be extended to electronic and magnetic video tapes.<sup>65</sup>

Can broadcasts of live sports events, whether or not they are recorded, be copyrighted? An affirmative answer finds impetus in a recent New York decision—*Hemingway v. Random House, Inc.*<sup>66</sup> Oral conversations can be subjects of common law copyright, the New York Court of Appeals held in a pioneering opinion. Outstanding in the court's opinion is its conclusion that the traditional requirement for common law copyright protection of an "embodiment in a tangible form" is oversimplified and outmoded. Instead, the court adopted "the principle that it is not the tangible embodiment of the author's work but the creation of the work itself which is protected."<sup>67</sup> It approvingly quoted Nimmer's treatise<sup>68</sup> that

[T]he underlying rationale for common law copyright (i.e., the recognition that a property status should attach to the fruits of intellectual labor) is applicable regardless of whether such labor assumes tangible form.<sup>69</sup>

The Assistant Register of Copyrights noted the importance of the case:

Although cautiously expressed, this judicial recognition that tangible embodiment is probably not a fundamental requirement of common law copyright protection represents the most significant legal point in the decision.<sup>70</sup>

The court said that to reserve one's common law copyright in an oral conversation, the speaker would be required to "indicate that he intended to mark off the utterance in question from the ordinary stream of speech, that he meant to adopt it as a unique statement and that he wished to exercise control over its publication."<sup>71</sup> Such indication is possible in speech:

It might, for example, be found in prefatory words or inferred from the circumstances in which the dialogue takes place. . . . Another way of formulating such a rule might be to say that, although, in

---

<sup>65</sup> The Copyright Office of the Library of Congress already registers electronic and magnetic video tape productions under motion picture categories, 17 U.S.C. §§ 5 (1) and 5 (m).

<sup>66</sup> 23 N.Y.2d 341, 296 N.Y.S.2d 771, 244 N.E.2d 250 (1968).

<sup>67</sup> 23 N.Y.2d at 346, 244 N.E.2d at 254.

<sup>68</sup> *Nimmer on Copyright*, § 11.1, 40 (1964).

<sup>69</sup> 23 N.Y.2d at 346, 244 N.E.2d at 254.

<sup>70</sup> Ringer, *Judicial Developments in United States Copyright Law 1968-69*, pp. 25, 27.

<sup>71</sup> 23 N.Y.2d at 349, 244 N.E.2d at 256.

the case of most intellectual products, the courts are reluctant to find that an author has "published," so as to lose his common-law copyright . . . , in the case of conversational speech—because of its unique nature—there should be a presumption that the speaker has not reserved any common-law rights unless the contrary strongly appears.<sup>72</sup>

Thus, copyrightability of broadcasts of live sports events depends not on the form or the tangibility of the "writing." Rather it focuses upon whether the broadcast is (a) original and (b) creative. To be original, it is only necessary for the author to produce a work by his own intellectual efforts, as distinguished from copying a pre-existing work.<sup>73</sup> The author need only show that a given expression originated with him; it is not necessary that the expression or subject matter be novel.<sup>74</sup> The crux of copyrightability therefore devolves upon the issue of creativity: Does the work represent an appreciable amount of creative authorship?<sup>75</sup>

A recent federal case, *Time Inc. v. Bernard Geis Associates*,<sup>76</sup> held that an element of creativity exists per se in any motion picture of an event, so that a motion picture is copyrightable regardless of its aesthetic value or the artistic effort required to make it. Film of a news event—in the particular form recorded by the "author"—is copyrightable.<sup>77</sup> In *Bernard Geis*, Judge Wyatt held that amateur "home movies" have many elements of creativity sufficient to render the film copyrightable. He cited Judge Learned Hand to the effect that "no photograph, however simple, can be unaffected by the personal influence of the author, and no two will be absolutely alike."<sup>78</sup> Judge Wyatt then cited specific elements of creativity in an amateur's films of President Kennedy's assassination:

Among other things, Zapruder selected the kind of camera (movies, not snapshots), the kind of film (color), the kind of lens (telephoto), the area in which the pictures were to be taken, the time

---

<sup>72</sup> 23 N.Y.2d at 349, 244 N.E.2d at 256.

<sup>73</sup> International News Service, *supra* note 49.

<sup>74</sup> *Burrow-Giles Lithographic Co. v. Sarony*, 111 U.S. 53 (1884). Interestingly, copyright protection is denied to some "art" for lack of originality. "Pop" artist Andy Warhol is cited as an example. *Boston College Industrial and Commercial Law Review*, Vol. 10 (1969), p. 993.

<sup>75</sup> *Mazer v. Stein*, 347 U.S. 201 (1954).

<sup>76</sup> 293 F.Supp. 130, 159 U.S.P.Q. 663 (S.D.N.Y. 1968).

<sup>77</sup> *Id.* at p. 143. However, no copyright claim can be made in the "news element of the event."

<sup>78</sup> *Jewelers Circular Publishing Co. v. Keystone Publishing Co.*, 274 Fed. 932, 934 (S.D.N.Y. 1921), *affirmed* 281 Fed. 83 (2d Cir. 1922). Judge Hand was quoting from *Bleistein v. Donaldson Lithographing Co.*, 188 U.S. 239 (1903).

they were to be taken, and (after testing several sites) the spot on which the camera would be operated.<sup>79</sup>

It is incontrovertible that if the elements of creativity are found in the production of motion pictures by an amateur, then such elements can only be magnified in the case of a professional cameraman or television cameraman. Producing a live broadcast of a sports event demands special creative talents: Establishing camera angles and sites, lighting effects, sound requirements, directing the efforts of a large team of technicians and announcers, instant video tape "replays" and so forth. Mr. Zapruder's "creativity" shrinks in comparison.

Also significant in *Bernard Geis* is the Court's rejection of the "oligopoly" argument—that since a film of a news event can be made "in only a limited number of ways," to grant copyright protection "would result in the appropriation of the subject matter. . . by a limited number of copyright proprietors."<sup>80</sup>

Judge Wyatt answered:

Life (magazine) claims no copyrights in the events at Dallas. They can be freely set forth in speech, in books, in pictures, in music, and in every other form of expression. All that Life claims is a copyright in the particular form of expression of the Zapruder film. If this is "oligopoly," it is specifically conferred by the Copyright Act and for any relief address must be to the Congress and not to this court.<sup>81</sup>

### *The Video Tape Problem*

There is one additional problem—a technical snarl—to resolve before copyright protection can be granted to broadcasts of live sports events. The issue: can material recorded on an electronic or magnetic video tape be copyrighted? The problem arises<sup>82</sup> because, unlike conventional motion picture film, the images on video tape are not visually perceptible to the naked eye. Only by playing the video tape through an electronic playback machine can the tape's content be translated.<sup>83</sup> This distinction, based on the form of technology, "may prove of

---

<sup>79</sup> 293 F.Supp. at p. 143.

<sup>80</sup> See, *Morrissey v. Procter & Gamble Co.*, 379 F.2d 675 (1st Cir. 1967), wherein the court declined to extend copyright protection to the rules of a sales promotion contest because the number of ways the rules could be expressed was very limited and the grant of a copyright would have appropriated an idea.

<sup>81</sup> 293 F.Supp. at pp. 143-144.

<sup>82</sup> *Nimmer on Copyright*, § 25.3, 113-118 (1964).

<sup>83</sup> The translation is a two-step process. First the tape's contents are activated into electronic impulses. Then the impulses are converted into visually perceptible pictures.

profound importance when the courts come to rule upon the copyrightability of magnetic tape."<sup>84</sup> Nimmer cites the requirement of *White-Smith Music Publishing Co. v. Apollo Co.*<sup>85</sup> that to be a copyrightable "copy" the material must have a written or printed record in intelligible form. In other words, it must be visually perceptible. Nimmer distinguishes the case of video tape from the strictures of *White-Smith* which disallowed copyright protection for phonograph records,<sup>86</sup> by noting that the reproduction by the tape gives a visually perceptible image "which appeals to the eye."<sup>87</sup>

Video tape is one of many examples of technology outstripping the breadth of the Copyright Act. Still there are strong arguments favoring copyright protection for the contents of video tapes. The Supreme Court holds an expansive, flexible view of the Constitution's Copyright Clause and Congress' power to enumerate what shall be bestowed with copyright protection.<sup>88</sup> The fact that Congress expressly made motion pictures<sup>89</sup> copyrightable,<sup>90</sup> that a lower federal court held a motion picture photoplay film to be a copyrightable "writing,"<sup>91</sup> and that the Copyright Office already considers video tapes to be copyrightable lends inertia.<sup>92</sup> If the courts consider the final product or effect as the crucial criteria, instead of whether the raw copy is "visually perceptible," then the contents of video tapes will be granted copyrightability.

#### CONCLUSION

In light of the *Hemingway* and *Bernard Geis* decisions, the extension of the present law to include the provisions of Section 111 (c) (4) (C) of S. 644 is minimal in terms of legal quanta. A key provision of this section grants copyright protection to the broadcast of an "organized professional team sporting event occurring simultaneously with the initial fixation and primary transmission of the program."<sup>93</sup> Such

---

<sup>84</sup> Nimmer, *supra*, at p. 114.

<sup>85</sup> 209 U.S. 1 (1908).

<sup>86</sup> 209 U.S. at p. 17.

<sup>87</sup> Nimmer, *supra*, at p. 114.

<sup>88</sup> *Burrow-Giles Lithograph Co. v. Sarony*, 111 U.S. 53 (1884).

<sup>89</sup> Or more correctly: "motion picture photoplays and motion pictures other than photoplays."

<sup>90</sup> Copyright Act of 1912, 37 Stat. 488, c.356 (1912).

<sup>91</sup> *Metro-Goldwyn-Mayer Distributing Corp. v. Bijou Theatre Co.*, 3 F.Supp. 66 (D.-Mass. 1933).

<sup>92</sup> *Bulletin of the Copyright Society*, Vol. 8 (1961), p. 205. See, *supra* note 65. Nimmer, *supra*, at p. 114.

<sup>93</sup> S.644, § 111 (c) (4) (C) (i), 92d Cong., 1st Sess. (1971).

instantaneous fixation solves a major problem: satisfaction of the copyright registration requirements.<sup>94</sup> In the case of live television broadcasts, such copyright protection must be granted instantaneously and automatically, otherwise CATV systems will be free to retransmit these broadcasts. But the grant for copyright protection must be balanced in the public interest by the simultaneous passage of either the Aspin or Sandman bills<sup>95</sup>—the *quid pro quo*—to guarantee a measure of insurance to the American televiewing public (especially those economically disadvantaged) that they will not be denied participation in the national sports culture.

While seemingly unorthodox and unpopular, the proposals of this paper bear thoughtful consideration. Progress appears to be in the offing. On August 5, 1971, the Federal Communications Commission released its plans for CATV regulation.<sup>96</sup> This policy statement, in the form of a letter to Congress, recognized that "Sports events stand on a separate footing from other programming presented on commercial television,"<sup>97</sup> based on the expression of Congress in Public Law 87-331.

The Commission has taken some limited steps toward regulating CATV and sports broadcasts. It has adopted a rule that prevents cable systems from showing sports events for a separate per program or per channel charge unless these events have not been televised live on a regular basis on broadcast television at no direct charge to viewers during the two years preceding the proposed subscription showing.<sup>98</sup> The Commission has also initiated a rulemaking proceeding proposing a ban on the showing of sports events on CATV systems on a subscription basis if the events were televised in the community of the system during any one year in the five years preceding the proposed subscription showing.<sup>99</sup> These steps, however, do not go very far.

A prime concern presently for the Commission is CATV's potential adverse impact on sports broadcasting, and especially the possibility that CATV may siphon such broadcasts off the airwaves. The Commission recognizes its limitations to act:

---

<sup>94</sup> 17 U.S.C. §§ 10, 11 (1909). In S.644, the provisions are §§ 401-412.

<sup>95</sup> *Supra* notes 10 and 11.

<sup>96</sup> "Commission Proposals for Regulation of Cable Television," 31 F.C.C.2d 115; 22 R.R.2d 1755 (1971).

<sup>97</sup> 31 F.C.C.2d at 124; 22 R.R.2d at 1768.

<sup>98</sup> 47 C.F.R. § 74.1121.

<sup>99</sup> F.C.C. Docket 18893, "In the Matter of Amendment of Sections 73.643 (b) (2) and 74.1121 of the Commission's Rules and Regulations Pertaining to the Showing of Sports Events on over-the-air Subscription Television or by Cablecasting." (Notice of Proposed Rule Making, June 24, 1970.)

We would . . . welcome Congressional guidance in this area of national concern. It may be that the scope of the issue is so complex—involving not only communications policy, but also antitrust and other considerations—that legislation may be the ultimate answer if, in fact, sports siphoning were found to be an imminent danger, contrary to the public interest.<sup>100</sup>

Congressional leadership in resolving this complex copyright definitional problem is required. The Copyright Clause of the Constitution<sup>101</sup>—as it is expansively interpreted by Congress and the Supreme Court<sup>102</sup>—presents no significant restrictions upon granting copyright protection to the broadcasts of live sports events, regardless of whether or not they are recorded on video tape.<sup>103</sup> As Judge Learned Hand said, it is not true that the Constitution

embalms inflexibly the habits of 1789. . . . [I]ts grants of powers to Congress comprise, not only what was then known, but what the ingenuity of men should devise thereafter. . . . [T]he new subject-matter must have some relation to the grant; but we interpret it by the general practices of civilized peoples in similar fields, for it is not a strait-jacket, but a charter for a living people.<sup>104</sup>

---

<sup>100</sup> 31 F.C.C.2d at 125; 22 R.R.2d at 1769-1770.

<sup>101</sup> *Supra* note 2.

<sup>102</sup> Senate Committee on the Judiciary, *supra* note 30, at pp. 86-91.

<sup>103</sup> Once copyright protection is granted to sports broadcasts that happen to be video taped, it becomes illogical not to grant copyright protection to *all* sports broadcasts, including those that are not video taped. Whether or not a broadcast is being taped has no bearing on the originality and creativity of the product. Moreover, in light of the growing popularity of video tape cassettes and home video recording devices, it seems certain that even untaped sports broadcasts require copyright protection.

<sup>104</sup> *Reiss v. National Quotation Bureau, Inc.*, 276 Fed. 717, 719 (S.D.N.Y. 1921).

# What's New With Novelty\*

Section 102 of S. 643

LEWIS ANTEN

## INTRODUCTION

LEGISLATION CAN TAKE A BIRD'S EYE VIEW of a total problem, break with the past and avoid the wasteful cost in time and money of the piecemeal litigations of the common law which may result in a crazy quilt of rules defying intelligence and logical application. Ideally, legislation, and particularly legislation concerned with the distribution of such a complex form of property as the patent right,<sup>1</sup> should precisely define the legal relationships between men to create order out of chaos so that inevitable conflicts may be amicably terminated.

---

\* This paper was chosen to represent The George Washington University in the 1971 Patent Office Society Student Award Competition, which is conducted annually under the aegis of The PTC Research Institute. The paper was submitted in partial fulfillment of the requirements of a course in patent law. The author is an associate with the firm of Darby & Darby, New York.

<sup>1</sup> The patent is property in its purest form. As with all property the prerequisite of the right to exclude others from the *res* is present. For a brilliant article on what is property, see Cohen, "Dialogue on Private Property," *Rutgers Law Review*, Vol. 9 (1954), p. 357.

An investigation of the novelty provisions of S.643, a bill for the general revision of the patent laws,<sup>2</sup> reveals that the desired ideal is far from attained. Proposed Section 102<sup>3</sup> obfuscates issues presently settled and introduces new issues surrounded by an aura of uncertainty. As will be evident from later discussion, many portions of Section 102 are so indefinite that any attempt to make a precise determination of its overall effect would be hazardous.

It shall be the purpose of this paper to point out possible issues that appear likely to arise due to the terminology of Section 102 of the proposal. No discussion of Sections 101<sup>4</sup> or 103<sup>5</sup> will be made except as these sections may be interrelated with Section 102. It is hoped that the Bar, Congress and the Administration, forewarned of the deficiencies of such a vital section of S. 643, as is Section 102, will act to provide a better vehicle for promoting the progress of the useful arts, as well as incidentally preventing future injustice and possible personal anguish to the inventor.

It is advisable at this time to set forth a uniform notation in order to simplify our discussion. Any reference to the proposed Section 102 of S. 643 will be preceded by a capital "P," such as P102(a). The absence of the "P" will denote the 1952 Act,<sup>6</sup> such as 102 (b).

#### NOVELTY

Every patent system conditions the grant of a patent on the invention possessing some degree of novelty. The exact degree of novelty required varies from country to country. In some countries the degree of novelty required is "absolute"—the invention cannot have been made known by prior publication or prior use anywhere in the world. Other countries require "a relative" degree of novelty—some prior disclosure or prior use of the invention is permitted, qualified as to the nature, time and place of such disclosure or use.

"Relative" novelty is generally considered to be further restrictable into two distinct classes. The first class treats only *local* use or *local* divulgation as a bar. The second class still considers only local use as a bar but treats divulgation anywhere in the world as a bar. The United

---

<sup>2</sup> S.643, 92d Cong., 1st Sess. (1971). [Hereinafter S.643.]

<sup>3</sup> See Appendix A.

<sup>4</sup> 35 U.S.C. §101 (1964).

<sup>5</sup> 35 U.S.C. §103 (1964).

<sup>6</sup> 35 U.S.C. (1964).



States presently is considered to employ the latter class but, as will be seen, P102 (d) (1) may alter this.

Of course, the above explanation of novelty is an oversimplification of a complex body of law. The laws of each country must provide exact details as to what dates, what kinds of disclosures, and what acts defeat novelty. It is to this purpose that Section 102 is directed.

### S. 643 Vs. 1952 Act

A section by section comparison of P102 with 102<sup>7</sup> will now be made, indicating briefly the current status of the law, the changes made in statutory language and the significance of these changes on the substantive law.

Generally, P102 may be considered tripartite, consisting of (1) a preamble; (2) bars to patentability applicable to special classes of applicants; and (3) prior art applicable against all applicants.

### I. THE PREAMBLE<sup>8</sup>

#### *The Invention*

The introductory language of P102 is partially definitional in nature. An applicant is entitled to a patent for "the invention defined in each claim" of his application if "the invention" meets the conditions of patentability. This is a codification of the position, long espoused by Judge Rich, that *the invention* is what the applicant *claims* it to be.

It is possible to give this definitional phraseology of the preamble greater effect than merely that indicated above. It has been suggested that there are at least four possible meanings of the word "invention" in the 1952 Act.<sup>9</sup> This is due to the fact that the word "invention" is capable of being used as both a noun and a verb. As a noun, *invention* is the *thing* invented. As a verb, it is the act of inventing. The use of

---

<sup>7</sup> 35 U.S.C. §102 (1964). See Appendix B.

<sup>8</sup> An applicant shall be entitled to a patent on the invention defined in each claim of his application upon establishing by a preponderance of proof that the invention meets the conditions for patentability. A patent may not be obtained if: . . . S.643, §102.

<sup>9</sup> See P. Janicke, "The Varied Meanings of 'Invention' in Patent Practice: Different Meanings in Different Situations," in Dunner, Gambrell and Kayton, *Patent Law Perspectives*, Appendix 1 (Mathew Bender & Co.).

the word "invention" is used, for example, in 102 (a) as both a noun and a verb. Such usage promotes confusion. P102 largely eliminates the use of invention as a verb and with one exception<sup>10</sup> uses invention only as a noun. Questions relating to the meaning of *the invention* in determining *what* has been abandoned or *what* has been patented in a foreign country may be clarified. Further discussion of the effect of this interpretation will be found below in the analysis of P102(a) and P102 (b).

### *Burden of Proof*

All too often academicians dismiss the allocation of the burden of proof as *merely* procedural, subordinate to the *substantive* provision of the law. The dichotomy drawn in law school between procedure and substance is perhaps the most unfortunate aspect of the study of law. Certainly no facet of the practice of law presents the new practitioner with a ruder awakening. All the substantive provisions of S. 643 i.e., granting damages, enjoining infringers or setting forth the categories of prior art, are of little value if the *procedural* aspects of S.643 prevent the applicant from getting the patent. This is exactly what P102 will do.

The preamble of P102 provides that a patent will be granted upon *the applicant* establishing "by a preponderance of proof" that the invention is patentable. This represents a complete shifting of the burden of proof from the Patent Office to the applicant. Section 102 simply states that "A person shall be entitled to a patent unless . . ." there is a bar. This change represents an incorporation of the position of the President's Patent Commission<sup>11</sup> which viewed the "rule of doubt," i.e., granting a patent unless the Patent Office can prove by a preponderance of proof that a bar exists, as antithetical to the statutory presumption of validity of a patent. The Commission view rested on the fact that since the reasons for issuing a patent are not made of record, a court can never be sure that any one particular patent was not issued despite doubts by the Patent Office as to the validity of that particular patent.

A "simple" expedient is employed to hopefully bolster the presumption of validity, so sorely battered by court decision. All that was

---

<sup>10</sup> See p. 000, *infra*.

<sup>11</sup> The Report of the President's Commission on the Patent System (Washington, D.C.: G.P.O. 1966), Recommendation X.

required was to eliminate the issuance of "doubtful" patents by the Patent Office. This is achieved by placing the burden of proof on the applicant. Anytime the Patent Office has any doubts as to the patentability of an invention it will not issue the patent. The courts will no longer be troubled by "doubts" as to whether the Patent Office itself had any doubts. This philosophy is equivalent to throwing out the proverbial baby with the bath. Unquestionably the presumption of validity will be strengthened. Patents will only issue on inventions that the applicants have convinced the Patent Office are patentable. But, is having a high percentage of patents held valid the final goal of a patent system or is it merely one indication or barometer of the effectiveness of a system designed to promote the progress of the useful arts? Adoption of the burden of proof of beyond a shadow of doubt would obviously cause an even higher percentage of patents to be held valid, yet no one desiring the maintenance of a viable patent system advocates adoption of such a burden.

Presently, the "rule of doubt" is only occasionally applied in determining patentability under Section 102. This arises when during the prosecution of an application there is uncertainty as to whether a reference is evidence of a Section 102 rejection. If the Patent Office is permitted to reject the application, despite doubts as to the *ground* of rejection, under Section 102 the applicant is precluded from showing commercial success, long felt need or any of the other vital indications of nonobviousness permitted in overcoming a Section 103 rejection.<sup>12</sup>

Even without the additional burden of proof imposed by P102 the applicant is faced with formidable obstacles in attempting to overcome a Section 103 rejection. Many of the most important indications of nonobviousness may not be available to the applicant for presentation to the examiner for consideration during prosecution. For example, unsuccessful attempts by others to achieve the applicant's results, as a means of demonstrating the state of the art, most likely will not be available to the applicant. In most circumstances a showing of commercial success of the invention will be impossible. What this will mean is that any invention that is *structurally* similar to the prior art will be

---

<sup>12</sup> In Kayton, *The Crisis of Law in Patents*, Pt. I, 31 (Washington, D.C.: Patent Resources Group, 1970) [hereinafter *Crisis*] it is suggested that *any three* of the following eight factors *necessarily* establishes nonobviousness: (1) Solutions to long felt need sought unsuccessfully by those of ordinary skill in the art; (2) Long felt need generally; (3) Commercial success; (4) The prior art teaches away from the claimed invention; (5) Significant licensing; (6) Conspiracy *not* to license; (7) Prompt infringement; and (8) New and unexpected results. It is also suggested that condition (1) is a *per se* statement of nonobviousness.

rejected by the Patent Office. The burden will be on the applicant to present indicia of nonobviousness sufficient to convince the Patent Office of patentability. How often will the applicant be able to meet this burden? Clearly the incredible Adam's battery, of *U.S. v. Adams* fame, would not have issued. How many other truly great discoveries, measured by any standard, would have failed to meet their burden?

What is the real harm in issuing a patent for an invention which the Patent Office, with their scientific library and trained scientific examiners, cannot prove is not patentable? As indicated above, the "rule of doubt" is applied almost exclusively where the rejection would be based on Section 103. By definition, the *identical* invention claimed by the applicant has not been found to exist. Therefore, the grant of a patent under the "rule of doubt" does not remove anything presently in the possession of the public. To the contrary, the *refusal* to issue a patent, even if under the "rule of doubt," may greatly retard the constitutional goal of promoting the progress of the useful arts. Rejection of an application may prevent disclosure of subject matter to the public which might in fact later prove to be of immense value in prompting further research and development. Obviously, it is the public that suffers the injury due to the unavailability of the disclosure.

Now let us investigate how the shift in the burden of proof may affect the practitioner in his dealings before the Patent Office. As stated above, the burden is on the applicant to convince the Patent Office that the invention claimed is patentable. This means that the applicant must prove, by a preponderance of the evidence, that no bar exists under P102 or that the invention claimed is not obvious under the criteria of P103. How does one prove, for instance, that the claimed invention has not been described in any publication, or never been in public use in the United States prior to the applicant's invention? The onus of proving a "negative," that something has *not* happened, is virtually insurmountable. One would have to account for every day since the genesis. What proof, if any, will the Patent Office find sufficient to overcome this burden? Will a patentability search be required or sufficient? What other steps might the applicant be required to take?

What kind of Office action can be expected? A typical response may soon read: "Applicant has failed to convince the examiner by a preponderance of proof of the patentability of the claimed invention over the art of record." It has not been many years from the time when the Patent Office would reject claims for "lacking invention," without

concern for the statutory basis. An era of indefinite rejections *with* statutory basis may be at hand.

## II. BARS APPLICABLE TO SPECIAL APPLICANTS

### *Abandonment*

P102 (a) —102 (c) ;

P102 (d) (5) —102 (g) .

P102 (a)<sup>13</sup> comprises essentially the same language as that of 102 (c), but has been modified to reflect the change made by P100<sup>14</sup> which defines the "applicant" as any person who owns an application for a patent. Under the present law only the inventor, with a few exceptions, may apply for the patent. The assignee of the invention may apply for the patent in his own name, but the names of the true inventor or inventors must still be identified in the application.<sup>15</sup> In view of the fact that a great proportion of all applications are the result of corporate research with virtually automatic assignment to the corporation, a great many misjoinder difficulties may be avoided. Similarly, appropriate language has been inserted into P102 (b) and P102 (d) (2).

Under present law abandonment requires a deliberate, but not necessarily expressed, surrender of any right to a patent.<sup>16</sup> The mere delay in filing an application after a reduction to practice is not abandonment.<sup>17</sup> During the time that the inventor fails to file he lays himself open to each time bar set forth in the statute.

Although there are a great many cases on what constitutes abandonment, there are very few that address the question of what it is that is abandoned.<sup>18</sup> It would be undesirable for abandonment of one embodiment of a device to be considered abandonment of all embodiments.<sup>19</sup> As indicated above, the language of the preamble of P102 might prove

---

<sup>13</sup> (a) The applicant or any of his predecessors in title has abandoned the invention; S.643, §102 (a) .

<sup>14</sup> S.643, §100.

<sup>15</sup> S.643, §115.

<sup>16</sup> *Metallizing Eng'g Co. v. Kenyon Bearing*, 153 F.2d 516, 68 U.S.P.Q. 54 (2d Cir. 1946) .

<sup>17</sup> *Wheeler v. Lenton*, 186 F.2d 738, 88 U.S.P.Q. 382 (CCPA 1951).

<sup>18</sup> See *Fed. Pac. Elec. Co. v. Wadsworth Elec. Mfg. Co.*, 221 F. Supp. 148, 138 U.S.P.Q. 301 (D.D. Pa. 1963) .

<sup>19</sup> See note 9, *supra*.

valuable in resolving this question. "The invention" in P102 appears to be shorthand notation for "the invention defined in each claim." Therefore it is the invention as defined in each claim that must be abandoned. This would mean that abandonment of the entire concept, or of the "idea," embodied in all of the claims must be found abandoned before P102 (a) would be employed as a bar.

P102 (d) (5),<sup>20</sup> presently 102 (g), is also concerned with the issue of abandonment. Under P102 (d) (5) and 102 (g) the prior invention by another is not a bar against the subsequent inventor if the prior inventor has abandoned the invention.

P102 (d) (5) adds a new last sentence to 102 (g) providing that "one year of inactivity with respect to the invention shall *prima facie* constitute abandonment." There is no question but that the meaning of "abandonment" in the first sentence of P102 (d) (5) is controlled by this provision. One year of inactivity is at the very least *prima facie* waiver of priority. Does such inactivity also govern the meaning of "abandonment" in P102 (a) ?

It is well known that patents are not generally favored by the courts,<sup>21</sup> with even the Supreme Court castigating patents as monopolies.<sup>22</sup> It is not an unlikely event that a district court judge, innocent of the subtle nuances of the patent laws, in search of a reason for holding a patent invalid, will seize upon the language of P102 (d) (5) to find that one year of inactivity with respect to the invention constitutes abandonment under P102 (a).

Even without any statutory authority some courts have found a delay in filing an application a bar.<sup>23</sup> With this new language as support, holdings of abandonment should flourish.

---

<sup>20</sup> (d) The invention is identically disclosed or described in any of the following prior art:

. . . (5) An invention made in this country by another before the 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 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 with respect to the invention shall *prima facie* constitute abandonment. S.643, §102 (d) (5).

<sup>21</sup> From February 1966 when the Trilogy was decided, up to and including the U.S.P.Q. of March 8, 1971, 30.3% of patents before the courts of appeals have been held valid. *Crisis*, Appendix A-2 updated to March 8, 1971.

<sup>22</sup> *Blonder-Tongue Labs, Inc. v. Univ. of Ill. Foundation*, 403 U.S. 313, 169 U.S.P.Q. 513 at 535 (1971).

<sup>23</sup> *Levenson v. Nordskog*, 301 F. Supp. 589, 163 U.S.P.Q. 52 (C.D. Cal. 1969) specifically held that the invention was *not* abandoned but had been forfeited due to a delay of five years before contacting his attorney.

The use of the same term in two different portions of Section P102 with different intended purposes is going to force some poor inventor into expensive litigation where even then the intended result may not be obtained. A split among the circuits is almost a certainty. If one year of inactivity is to be only a waiver of priority the statute should clearly say so.

Aside from the breadth to be given to the *prima facie* abandonment it is also unclear what is the critical span of time for the one year of inactivity. One likely interpretation would appear to be that one year of inactivity after the actual reduction to practice of the invention constitutes the abandonment. This would have the effect of preventing a party in interference from proving acts occurring more than a year prior to the filing date.

It is also possible that the one year of inactivity could refer to any period after conception but before the reduction to practice. This would represent a change of the present law which requires that diligence be proven only from the time immediately prior to the conception by the other until the reduction to practice. Adoption of this alternative is buttressed by the fact that the additional sentence was inserted following the second sentence instead of immediately following the first sentence referring to abandonment. Adoption of such an interpretation would have one year of inactivity prior to reduction of practice *prima facie* nondiligence.

It is also possible to adopt the view that the new language modifies *both* the previous sentences. This would find one year of inactivity either before or after a reduction to practice a bar. Inactivity before reduction to practice would be a waiver of priority while inactivity after the reduction to practice would be abandonment.

Yet another problem present is what is *inactivity with respect* to the inventions? Are investigations related to improving the operability of the invention or of making the invention more commercially palatable *with respect* to the invention? Is the attorney's efforts in preparing the patent application activity with respect to the invention?

As mentioned above, it appears that "invention" is used only as a noun in P102. This is evidenced by the fact that wherever invention is used as a verb in 102 the language "the invention was made" is inserted in P102. Despite the attempt to limit the use of invention to a noun, invention in P102 (d) (5) may be found to be the exception. Inactivity with respect to the *invention* (act of inventing), if invention is a verb, would limit abandonment to inactivity only when such inactivity is after conception but before reduction to practice.

Finally, the question arises as to whether the one year of inactivity must be a consecutive period of 365 days. Would intermittent periods of activity avoid the "abandonment" or does an applicant have only one year to reduce his invention to practice and file his application following a conception?

Only time and litigation will resolve all the above questions.

### *Prior Foreign Applications*

#### P102 (b) —102 (d)

P102 (b),<sup>24</sup> as did 102 (d), provides that the patenting of an invention in a foreign country on an application filed more than 12 months prior to filing in the United States is a bar. Both events must be present: the grant of the patent *and* the filing more than 12 months prior to United States filing.

P102 (b) would add an additional means for defeating the grant of a patent. Many countries are adopting deferred examination systems as a means of reducing backlogs of applications in their patent systems.<sup>25</sup> Such systems permit the applicant to wait for as many as seven years before requesting an examination for determining the patentability of the invention. The application, however, is published a fixed number of months after the application is filed, regardless of the status of the application. P102 (b) makes such official publication of the application a bar, as long as it occurs prior to the filing date in the United States.

Although it is the present practice of the countries employing the deferred examination system to wait for more than 12 months before publishing the application, there is no sanctity attached to this time.

P102 (b) makes no provision for any country that adopts a period of less than 12 months. As a result, P102 (b) may be inconsistent with P119 which grants convention countries<sup>26</sup> the benefit of their earlier foreign filing date, if filing is made within 12 months of such foreign filing.

<sup>24</sup> (b) The 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 . . . S.643, §102 (b).

<sup>25</sup> Countries employing a deferred examination system are Germany, Hungary, The Netherlands, and Japan.

<sup>26</sup> Countries *not* party to the convention include Argentina, Chile, Communist China and Taiwan.



No conflict would exist if the official publication of the application was made by a nonconvention country within the 12 months. The publication would clearly present a bar under P102 (b). It is questionable that this result is intended.

For the same reasons as were stated in the discussion of abandonment, what is barred by the foreign patenting may be governed by the preliminary language of the preamble. Once again it is the invention as defined in each claim that is barred from further patenting in the United States.

### *Derivation*

#### P102 (c) —102 (f)

It is intended by P102 (c)<sup>27</sup> and 102 (f) to ensure that the patentee must be an original inventor and not one who merely sees a device, or a disclosure of another which is not prior art, and then files an application for a patent in the United States claiming the subject matter.<sup>28</sup> Although P102 (c) no longer requires that the applicant be the inventor it still maintains the condition that the inventor must not have derived the invention. Perhaps the most obvious example of derivation involves actual theft, perhaps by a competitor or a laboratory assistant, of an invention.

Despite the desirability of preventing the granting of valid patents to those who have not invented anything, there is a real possibility that P102 (c) may not achieve this result. It is the very rare infringement suit that has a literal infringement of a claim.<sup>29</sup> By the same token it would be an extremely rare instance that one who has actually stolen a device will file an application with claims reading on the exact same device allegedly stolen.

On the above facts one would have to look to the portion of the statute setting forth the condition of obviousness for a ground of rejection. P103 provides that the test of obviousness applies the prior art *as set forth in P102*. P102(d) lists the categories of prior art, none of which is derived subject matter. Thus, it would appear that P103 cannot be used to defeat the grant of such a patent.

<sup>27</sup> (c) The inventor did not himself invent the subject matter sought to be patented, but derived it from another; or . . . S.643, §102(c).

<sup>28</sup> See Federico, "Commentary on the New Patent Act," 35 U.S.C.A. 102 (f) (1952).

<sup>29</sup> Two recent Supreme Court decisions did involve literal infringement. *U.S. v. Adams*, 383 U.S. 39, 148 U.S.P.Q. 479 (1966) and *Lear, Inc. v. Adkins*, 395 U.S. 653, 162 U.S.P.Q. 1 (1969).

It may be argued that P102 (d) is not an exhaustive list of the prior art. P103 refers to the prior art as set forth in P102 without making specific reference to P102 (d). Therefore P102 (c) could conceivably be considered as prior art.

Undisclosed subject matter is prior art under 102 only in 102 (e). A patent granted in the United States is a reference as of its filing date even though it is maintained in secrecy.<sup>30</sup> As will be discussed in detail below, P102 (d) (3) may expand the use of secret subject matter for use as a reference. Any further extension of this concept appears undesirable.

Is it really possible that any court would find such an antisocial practice as theft sanctioned by law? The answer is yes! At least one court will view the literal language of P102 (c) as congressional approval of such activity on the theory that the applicant has disclosed subject matter to the public that otherwise may have been kept concealed. This view would be strengthened if in fact the true inventor was inactive for more than a year or actually concealed the invention. However, logical extension of the theory would require the elimination of P102 (c) entirely.

Most courts do not look with favor on any patents, never mind a patent with such dubious origins as the instant one. It is to be expected that some test will be employed so as to defeat the patent. The test employed may be that the invention "lacks invention," "doesn't push back the frontiers of science," "doesn't promote the progress of the useful arts" or even perhaps is "obvious" under the standard of P103.

Mere mortals, as are inventors, are limited to elements and materials available on the planet earth (barring moon rocks). Further, inventors are charged with constructive knowledge of all the prior art applicable against their application.<sup>31</sup> Is it inconceivable that a court permitted in some instances to use a test other than P103 may combine constructive knowledge with derivation and achieve the judicial invention of "constructive derivation?" Such a result would permit bypassing P103 in those situations where the invention would be patentable under P103 but not under the courts chosen test.

There is no doubt that the test to be applied should be that of P103. If the modification made by the alleged deriver is not obvious under the test of P103 then a patent should issue. The applicant has made a nonobvious contribution to the public knowledge. Are patents to be subject to a test of "intent to invent" patentable subject matter?

---

<sup>30</sup> *Hazeltine Research, Inc. v. Brenner*, 382 U.S. 252, 147 U.S.P.Q. 429 (1965).

<sup>31</sup> *In re Winslow*, 365 F.2d 1017, 151 U.S.P.Q. 48 (1966).

The 1952 Patent Act should be a harsh lesson to the effect that the courts will try to avoid applying any test that lends itself to rational application. Application of a rational test requires the writing of rational decisions. The standard of "lacks invention" lives yet 20 years after that Monday morning in 1950 that *A & P*<sup>32</sup> was decided spawning Section 103. The statute should be sure that if any test of patentability is applied it is that test ensconced in P103.

The derived subject matter need not be prior art against all applicants, but only against the applicant actually deriving the subject matter. A suggested means of accomplishing this result is to include as prior art under P102 (d) "subject matter derived from another." Such a provision would calm the fears of those who are concerned that prior undisclosed inventions of others may be combined under P103 to defeat patentability.

### III. BARS TO ALL APPLICANTS

#### *Prior Art*

P102 (d) ; P102 (d) (1) —P102 (d) (5)

For the first time what is prior art for consideration under P103 nonobviousness is set forth in the statute. P102(d) provides that a patent may not be obtained if "the invention is identically disclosed or described in any of the following prior art: . . ." while P103 states that a patent may not be obtained even though the invention is not identically disclosed "in the prior art as set forth in 102."

As pointed out above it can be argued that P102 (d) is not an exhaustive list of the prior art. P103 incorporates at least P102 (d) but it does not preclude the argument that P102 (a) through P102 (c) *may* also be prior art. The simple expedient of changing "102" in P103 to "102 (d) " would eliminate such an issue.

A more important issue that may be presented is what is a P102 rejection in its relationship to P103? A rejection based on P102 precludes further investigation into the nonobviousness of the invention. Therefore, categorizing a rejection as based on P102 may be outcome determinative. P102 (d) may permit what are essentially P103 rejections to be categorized as P102 rejections.

At the present time many courts are determining patentability by

---

<sup>32</sup> Great A & P Tea Co. v. Supermarket Equip. Corp., 340 U.S. 147, 87 U.S.P.Q. 303 (1950).

applying the test of *Anderson's Black-Rock*.<sup>33</sup> If all the elements that comprise a combination invention are known in the prior art then in the absence of synergistic effect the invention is unpatentable. Such a test ignores the reality that in fact *all* inventions are combinations of known elements. P102 (d) could be viewed as a codification of the erroneous test.

There is no limitation in P102 (d) that the invention be identically disclosed or described in a *single piece* of prior art. As long as the invention is "described in *any* of the . . . prior art" categories a P102 rejection is proper. "Any" may be construed as singular or plural.<sup>34</sup> If a court divides the invention into elements then P102 (d) suggests applying prior art against each element separately. Such a test would not even be concerned with P103 or synergistic effect.

This problem was not present in 102 where each of the categories of prior art were singular in nature—i.e., "a patent," "a printed publication." P102 on the other hand employs plural language in setting forth the prior art, i.e., "any" "subject matter." Even if it is argued that P102 (d) (1) requires the invention to be disclosed in *one* patent or *one* publication (P102 (d) (1)) or *one* U.S. patent (P102 (d) (2)) this would not prevent the combining of "a patent" with "subject matter" or any other combination and permutation of prior art. In addition, publications or patents may be considered, for the great part, to be prior art under P102 (d) (3) as well as P102 (d) (1). Combining two patents may be achieved in this manner.

#### *Printed Publications (Prior Art)*

P102 (d) (1)—102 (a)—102 (b)

It appears safe to predict that no single section of P102 will be subject to more litigation than that of P102 (d) (1).<sup>35</sup> Designed essentially to eliminate controversy as to what is a "printed"<sup>36</sup> publication,

---

<sup>33</sup> *Anderson's Black-Rock, Inc. v. Pavement Salvage Co., Inc.*, 396 U.S. 57, 163 U.S.P.Q. 673 (1969).

<sup>34</sup> *Webster's Seventh New Collegiate Dictionary*.

<sup>35</sup> (d) The 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 invention was made by the inventor, or more than one year before the actual filing date in the United States of the application; or . . . S.643, §102 (d) (1).

<sup>36</sup> *Deep Welding, Inc. v. Sciaky Bros., Inc.*, 417 F.2d 12227, 163 U.S.P.Q. 144 (7th Cir. 1969), has held a typewritten report to be printed.

it adds a qualification as to which patents and publications may be considered as prior art. This qualification will undoubtedly haunt the patent law for years to come.

“Printed” publications were not singled out for special treatment in the 1952 Act due to the aesthetic values of the draftsmen. At the time that the 1952 Act was written it was not economical to print only a few copies of a document. Only large quantities could be justified. It was presumed, therefore, that if the publication was “printed” many copies would be available and it would not be onerous to hold an applicant to constructive notice of the contents of all printed publications. However, the certainty of the law was undone by technology. Photocopying and other quick copying methods now make it possible to make single copies of documents at a very low cost.

P102 (d) (1) effectively eliminates any controversy pertaining to this issue. Any patent or publication is a reference if it is in “Printed or other tangible form.” Such language would encompass any means of documenting that the subject matter was in existence. Typewritten documents, photostats, microfilm, handwritten letters, pictures, computer print out, tape recordings or any other conceivable permanent recording means is acceptable. As a substitute for “printed,” as justification for holding an applicant to constructive notice, P102 (d) (1) requires that the foreign patents and publication must be “reasonably available to the public of the United States.”

The difficulty with the phraseology of P102 (d) (1) rests not with its good intentions, but with its indefiniteness. “Reasonably available to the public” is just not precise enough. It could mean all things to all men.<sup>37</sup> When is something reasonably available? Is a single typewritten thesis in a library reasonably available? It is available but not necessarily reasonably available. It appears that the courts will be forced to decide the validity of patents based on considerations of the locations and numbers of copies of a publication. A single copy of a foreign patent may be reasonably available if it is filed in the Patent Office, yet not be reasonably available if it is located across the street from the Patent Office in the Arlington County Public Library.

Further evidentiary problems will be created. It is not uncommon for foreign patents to be received by the Patent Office on one date, sent to the group at a later date, and placed in the files at yet another date. Which date is controlling?

---

<sup>37</sup> Both N.A.S.A. and the A.E.C. have stated that “reasonably available” is uncertain and subject to no known standard. Hearings before the Subcommittee on Patents, Trademarks and Copyrights of the Committee on the Judiciary, U.S. Senate, 90th Cong., 2nd Sess., Part 2, at 719 and 742. [Hereinafter Hearings].

A final question with regard to "reasonably available" is whether a document may be reasonably available at one date and then become unavailable at a later date. Would a publication that was once available, but later unavailable at the time of the invention be a reference? P102 (d) uses the present tense in defining the available prior art.

It is possible that all of the above questions may be susceptible of a simple resolution. There is some basis in the legislative hearings that would indicate that the evil to be remedied by the "reasonably available" terminology may be to prevent disclosures which are physically inaccessible to American nationals from being considered as prior art.<sup>38</sup> On a lower scale of international relationships such a determination would also prevent the USSR, or other Communist countries from alleging prior inventorship, falsely documenting such prior art and thereby invalidating an otherwise valid United States patent. If this is the intent of the draftsmen it should clearly be set forth so as to prevent later litigation on all of the above issues.

Some concern has been expressed that the use of the term "before the invention was made by the inventor" in P102 (d) (1) and P102 (d) (3) will permit the use of an applicant's own disclosure of his invention against his application, even absent a statutory time bar. This concern is based on the fact that an invention is not "made" until after a reduction to practice, either actual or constructive. If diligence can be shown the invention is then considered made as far back as the conception. Therefore, it is argued, if the applicant is either nondiligent or he alters his conception after disclosure such a disclosure may be a bar.

Although the literal language of P102 (d) (1) and P102 (d) (3) would permit such a result it is not likely that the courts will take such a restrictive view. *In re Land and Rogers*, in interpreting similar language in 102(a) stated that one's own disclosure absent a time bar cannot be used as a reference against the inventor.

#### *U.S. Patent or Application (Prior Art)*

P102 (d) (2) —102 (e)

P102 (d) (2)<sup>39</sup> encompasses the status of 102 (e) that a United States

<sup>38</sup> *Id.* at 468-469.

<sup>39</sup> (d) The invention is identically disclosed or described in any of the following prior art:

. . . (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 invention was made by the inventor named in the application; or . . . S.643, §102 (d) (2).

patent is prior art as of its filing date. However, provision is made for including published United States applications as references. The publication of applications may arise due to the requirements of the Patent Cooperation Treaty. Under the treaty signatory nations will publish all applications within 18 months from the filing date, regardless of the stage of the patent examination.

The considerations present in finding that a patent is a reference as of its filing date are not necessarily present with a mere published application. The subject matter of the application may eventually prove unpatentable, either under P102 or P103 and go abandoned. Should the published application be treated differently than any other publication merely due to the different means of their arriving at a published state?

It might be argued that the answer to the above question must be yes, otherwise P102 (d) (2) and P102 (d) (1) would be partially redundant and it is a cardinal rule of statutory construction that every phrase of a statute be given independent meaning, if possible. However, the inclusion of published applications in P102 (d) (2) would eliminate the requirement that published United States applications be reasonably available as must be publications and foreign patents included under only P102 (d) (1). Whether or not this difference may be significant must await the eventual interpretation given "reasonably available."

#### *Prior Use and Knowledge (Prior Art)*

##### P102 (d) (3) — 102 (a)

P102 (d) (3)<sup>40</sup> makes "subject matter made known to persons in the art to which it pertains; or used by others in the country before the invention was made by the inventor" a bar to patentability. It is well settled that evidence of knowledge under 102 (a) must be accessible to the public.<sup>41</sup>

As with 102 (a), P102 (d) (3) does not specifically state that the

---

<sup>40</sup> (d) The invention is identically disclosed or described in any of the following prior art:

. . . (3) Subject matter made known to persons in the art to which it pertains, or used by others, in this country before the invention was made by the inventor named in the application; or . . . S.643, §102 (d) (3).

<sup>41</sup> *In re Schlitter and Uffer*, 234 F.2d 882, 110 U.S.P.Q. 304 (CCPA 1956), overruled on other grounds by *In re Borst*, 345 F.2d 851, 145 U.S.P.Q. 554 (CCPA 1965).

disclosure must be accessible to the public. However, it cannot be presumed that "public" will also be inserted in P102 (d) (3) as new considerations are present. The public as a whole was involved in 102 (a) while P102 (d) (3) focuses attention on a limited class of the public—persons in the art.

It would appear that P102 (d) (3) is directed to the situation present in *Corona Cord Tire Co. v. Doran Chem. Corp.*<sup>42</sup> in which an oral disclosure, accompanied by nonprinted reports, was made at a convention of skilled chemists by one other than the inventor prior to the time the invention was made by the applicant. The court did not have to reach the issue of whether such a disclosure would have been a sufficient bar.

What might P102 (d) (3) add to P102 (d) (1)? Firstly, oral disclosure, public as well as private, might be added since an oral disclosure, without more, is neither a publication, nor reasonably available. Secondly, secret disclosures of subject matter, such as under trade secret agreements, may fall within the exclusive ambit of P102 (d) (3). The final category is subject matter not secret, yet not reasonably available to the public. The exact scope of this last category rests on the eventual interpretation given "reasonably available" by the courts.

Is it reasonable, or desirable, that nonpublic disclosures be considered prior art under 103? Certainly, in a few highly specialized fields, such as perhaps the computer industry, virtually every person in the art may be the recipient of a particular secret disclosure. To allow such a disclosure to be prior art against an individual who had no actual knowledge of the subject matter and is not a person in the art requires adopting the rationale that only those in the art are going to make any meaningful contributions to that art. The presumption has proven to be historically wrong. Color film was invented by musicians while Adams, of battery fame, was hardly a trained scientist. A trained scientist never would have performed the *obvious* experiment that proved successful.

How would this provision be employed in the litigation of a patent? Will each side present a parade of witnesses testifying that the subject matter was known at some time in the past, despite lack of documentation? If it was known at least some documentation should be available.

How often after a breakthrough in an art do others in the art believe that the "breakthrough" was obvious? It is only a short easy step from

---

<sup>42</sup> 276 U.S. 358, 1928 C.D. 253 (1928).



"I should have thought of that" to "I knew that" with no question of the deep sincerity of the declarant in his belief that he actually did know.

Many other questions present themselves. How many persons in the art must know of the subject matter? Must it be substantially the entire class, a large portion of the class or merely more than one other? A requirement that a substantial number of persons in the art must know of the subject matter would make constructive knowledge of secret disclosures more palatable.

Does "in the country" modify both "made known" and "persons in the art"? In *Deep Welding Inc. v. Sciaky Bros., Inc.* the court emphasized the point that many Americans were at a foreign scientific convention where typewritten reports were distributed. There doesn't appear to be any reason for making any artificial distinctions based upon where the disclosure was physically made as long as the end result is that persons in the art in this country know of the subject matter.

Finally, it should be noted that P102(d) (3) refers to "subject matter" made known and not to "invention" as in 102(a). This change resolves the controversy of whether a disclosure requires a reduction to practice to be sufficient evidence of knowledge of the invention under 102(a) since no reduction to practice is required for a disclosure to be subject matter. Although this point is well settled in the CCPA<sup>43</sup> it is desirable to prevent the district courts from arriving at a contrary decision.

#### *On Sale or Public Use (Prior Use)*

P102(d) (4) — 102(b)

Perhaps no area of patent law in general, and Section 102 in particular, is in such a state of confusion as that of public use and sale.<sup>44</sup> This is due in great part to the companion cases of *Watson v. Allen*<sup>45</sup> and *In re Blaisdell*.<sup>46</sup> The same identical acts of the applicant that were held to be public use and not excused as experimental in *Blaisdell* were excused as experimental in *Watson*.

One commentator<sup>47</sup> has suggested that the only possible way of

<sup>43</sup> *In re Borst*, 345 F.2d 851, 145 U.S.P.Q. 554 (CCPA 1965).

<sup>44</sup> *Tractor Supply Co. v. Int'l Harvester Co.*, 155 U.S.P.Q. 420 at 429 (ND. Ill. 1967) and cases cited therein.

<sup>45</sup> 254 F.2d 342, 117 U.S.P.Q. 68 (D.C. Cir. 1958).

<sup>46</sup> 242 F.2d 779, 113 U.S.P.Q. 289 (CCPA 1957).

<sup>47</sup> Kayton, "The Year (1966) in Patent Law," *George Washington Law Review*, Vol. 35 (1967) pp. 720, 727.

reconciling *Watson* and *Blaisdell* and of making a meaningful determination of whether an act will be considered public use or excused experimental use is to ask whether it is the *claimed* invention that has been in public use. Since an invention is "made" upon a reduction to practice and a reduction to practice requires evidence that the invention operates for its intended purpose, until such operation is shown use will be excused as experimental. Any acts following such proof will be considered public use for starting the time running.

P102 (d) (4)<sup>48</sup> may be interpreted so as to obviate any difficulties with public use. Subject matter, and not the invention, is prior art if it is in public use for more than a year prior to filing. As discussed above an invention comes into existence only after reduction to practice. Therefore, experimental use is permitted. No such experimental use is required for subject matter to come into existence. Therefore, P102 (d) (4) may make *any* use of the subject matter more than a year prior to filing a bar.

The greatest change made by P102 (d) (4) results from the fact that "subject matter on sale" more than a year prior to filing is a bar. Subject matter, however, is regularly on sale prior to reduction to practice, such as in government contracts and R&D firms. The subject matter sold is the conception of the invention. The reduction to practice may not follow for more than a year. It would appear that P102 (d) (4) would prevent the patenting of such an invention.

A desirable method of clarifying the law on public use and sale would be to provide that such activity must follow a reduction to practice to be a bar. The law with regard to what constitutes a reduction to practice is fairly settled and could be readily applied to the on-sale and public-use issues.

A large measure of the confusion concerning P102 (b) public use is a result of the fact that very rarely are such issues presented before the CCPA. For the most part the district courts have been the only forums available. With adoption of S.643 and its re-examination provisions,<sup>49</sup> the CCPA may finally lend its calming influence upon this troubled body of law.

---

<sup>48</sup> (d) The invention is identically disclosed or described in any of the following prior art:

. . . (4) Subject matter on sale or in public use in this country more than one year before the actual filing date in the United States of the application; or . . . S.643, §102 (d) (3).

<sup>49</sup> S.643, CH. 18.

*Prior Invention by Another (Prior Art)*

P102 (d) (5) —102 (g)

The final category of prior art of P102 (d) is the invention of another before the invention was made by the applicant, provided the other has not abandoned the invention.

The inclusion of this category under prior art removes any doubt as to whether under the 1952 Act, 102 (g) is prior art under 103.<sup>50</sup>

P102 (d) (5)<sup>51</sup> presents a change in the law in that only abandonment, and not suppression or concealment, prevents the prior invention from being applicable against the late inventor. This may allow an inventor to use his invention as a trade secret and not apply for a patent until another files an application for the same invention. Since concealment and suppression of inventions are counter to interests of the patent system of making information available to the public, this change would lend credence to the position that failure to file within one year of a reduction to practice is abandonment. Otherwise concealment and suppression of inventions would be condoned.

SUMMARY

It is the hope of the author that this paper has pointed out topics of concern present in Section 102 of S. 643. The novelty provision of S.643 has been shown to be subject to a myriad of interpretations, each of which will be paid for in uncertainty of application and increased litigation. It is suggested that remedial legislative drafting is in order.

---

<sup>50</sup> See Turner, "Is Prior Invention by Another a Proper *ex parte* rejection . . . and Prior Art Under 35 U.S.C. 103? 52 J.P.O.S. 802 (1970).

<sup>51</sup> See note 20, *supra*.

## APPENDIX A

## (Proposed Section 102)

## §102. Conditions for patentability; novelty and loss of right to patent

An applicant shall be entitled to a patent on the invention defined in each claim of his application upon establishing by a preponderance of proof that the 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 invention; or

(b) The 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, but derived it from another; or

(d) The 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 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 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 invention was made by the inventor named in the application; or

(4) Subject matter on sale or in public use in this country more than one year before the actual filing date in the United States of the application; or

(5) An invention made in this country by another before the 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 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 with respect to the invention shall prima facie constitute abandonment.

## APPENDIX B

## (Section 102 of 1952 Act)

## § 102. Conditions for patentability; novelty and loss of right to patent

A person shall be entitled to a patent unless—

(a) the invention was known or used by others in this country, or patented or described in a printed publication in this or a foreign country, before the invention thereof by the applicant for patent, or

(b) the invention was patented or described in a printed publication in this or a foreign country or in public use or on sale in this country, more than one year prior to the date of the application for patent in the United States, or

(c) he has abandoned the invention, or

(d) the invention was first patented or caused to be patented by the applicant or his legal representatives or assigns in a foreign country prior to the date of the application for patent in this country on an application filed more than twelve months before the filing of the application in the United States, or

(e) the invention was described in a patent granted on an application for patent by another filed in the United States before the invention thereof by the applicant for patent, or

(f) he did not himself invent the subject matter sought to be patented, or

(g) before the applicant's invention thereof the invention was made in this country by another who had not abandoned, suppressed, or concealed it. 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 prior to conception by the other.



R&D, Technological Education, and  
Industrial Property: Policy  
Correlations for the 1970's

**A Special Conference**

# R&D, Technological Education, and Industrial Property: Policy Correlations for the 1970's

The Special Conference 432

Proceedings of the Conference 435

Welcome—L. JAMES HARRIS, Director, The PTC Research Institute; Professor of Law, The National Law Center of The George Washington University 435

Introductory Remarks—JAMES STACY COLES, Conference Chairman; President, Research Corporation 437

## PANEL OF INVITED EXPERTS

New Conditions and Problems of the "Knowledge Industry," National and International 439

Speakers: HENRY DAVID, Executive Secretary, Division of Behavioral Sciences, National Academy of Sciences 439

LAWTON M. HARTMAN, Special Assistant to the Director, National Science Foundation 443

GEORGE D. SUMMERS, Manager, Biomedical Programs, Fairchild Hiller Corporation 449

Cross-Questioning and Comment by Panel of Experts 454



New Challenges to Patent, Know-How, and Other Industrial- Intellectual Property Rights	460
Speaker: SYDNEY CARTER, Patent Attorney, General Motors Corporation	460
General Discussion	467
Luncheon	479
Master of Ceremonies: O. S. COLCLOUGH, Chairman of the Ad- visory Council and Director Emeritus, The PTC Research Institute	479
Speakers: BILLY M. HORTON, PTC Research Institute In- ventor of the Year for 1970; Technical Director, De- partment of the Army Harry Diamond Laboratories	480
JAMES H. WAKELIN, JR., Assistant Secretary of Commerce for Science and Technology, U.S. Depart- ment of Commerce	482
General Discussion	485
Antitrust and Competition Policy in New R&D Setting	488
Speaker: RICHARD E. DAY, Research Associate, The PTC Re- search Institute; Professor of Law, The Ohio State Uni- versity	488
General Discussion	492
Emerging Needs in Tax Policy Concerning Research and Educa- tion	500
Speaker: ARTHUR B. HANSON, Member, Advisory Council of The PTC Research Institute; Senior Partner, Hanson, O'Brien, Birney and Stickle	500
General Discussion	506

# TABLE OF CONTENTS

New Conditions and Problems of the "Knowledge Industry," National and International	439-459
Shift in Concept of Knowledge and Science	440-441
Subjective emphasis of knowledge	440
Disassociation of science from social values	440-441
Concern with Utilization and Consequences of Generation of Knowledge	440-441
Present Oversupply of Scientific Manpower	441; 449-450; 485-486
Problems of Western Knowledge-Generating Institutions	441-442
Confusion of purpose	442
Changes in demands for research	442
Skills of "closed systems" not applicable to "open systems"	442; 485
Public Support and Influence on Knowledge Structure	442
Market Determination of Relative Values of Knowledge Production	443
Scientific producers' values	443
Public consumers' priorities	443
Relation of the two sectors	443
Minimal Effect of Reduced Federal Support on R&D and "Knowledge Industry"	444
Growing Industrial Support Offsets Government Reduction	444
Distribution of Federal Funding	444-446; 451-452
Increase in funds for federal R&D laboratories	445
Duplication of government facilities in environmental R&D	445

---

Legislation producing excessive number of laboratories	445
Distribution by industry	445-446
Critical State of Natural Environmental Science	446-449
Dearth of knowledge to solve problems	446
Shortage of scientific manpower	446-449
Problem of coordinating university scientific resources with industrial systems techniques	447
Need for trained specialists adapting to broad multidisciplinary ecological problems	447-448
Need for cooperation between university and industrial scientists and engineers	448-449
Corporate Interests in R&D	449
Changing Attitudes Toward Science and Technology	449-452
Service to humanity	449-451
Status of private and public financial support	450-452
In academic institutions	450-451
Federal expenditures for R&D	451-452
How money is allocated: Industrial v. consumer production	452
International implications of R&D expenditures	452; 456-457; 474-475
Effect on U.S. technological leadership	452-453
Effect on U.S. economy	452-453
Japanese example	453; 456-457; 474-475; 483
Need for Cooperation Between Government, Industry and Academia	453-459; 482-484
Problem of Timidity in Decision-Making	453-454; 457

New Challenges to Patent, Know-How, and Other Industrial-  
Intellectual Property Rights 460-478

Problems of Transfer and Right to Use Technical  
Information 460-475

Storage and retrieval of information due to  
“knowledge explosion” 461-463; 472-473

Searching of prior art 461-463; 484

Patent law exceptions to antitrust laws 464-465; 468-472

Trade secret information 463-465; 467-468; 471-472; 473-475

Contractors’ Proprietary Rights in Government-Sponsored  
R&D 465-467; 492-493

Challenges in the Field of Copyright 472-473

Programs in Department of Commerce to Enhance Technology  
and Facilitate Its Transfer 482-484

Commerce Technical Advisory Board 483-484

Technology utilization 483-484

Effect on economy 483-484

Technology intensive areas 483-484

Labor intensive areas 483-484

Technology transfer 482-484

Technology assessment and the Patent Office 484

Antitrust and Competition Policy in New R&D Setting 488-499

Patent/Antitrust Law Trend 489-499; 506-513; 515-517

Antitrust incipency test 489; 498

Various interpretations of Rule of  
Reason 489-493; 496-497; 498; 512-513

Possibility of co-existence 490; 492-493

“Primary” and “Secondary” Patent Rights	490-491
Effect of Antitrust Limitations on R&D, Invention, and University Research	491-492; 506-515
Alumni assistance in university patent utilization	513-515
Licensing possibilities	513-515
Government Policy on Compulsory Licensing	492-493
Antitrust Relief for Cooperative Arrangements in the Public Interest	493-497
Trade association research	495-496; 497-498
Joint ventures and the public interest	496-498; 515-517

**Emerging Needs in Tax Policy Concerning Research and  
Education** 500-517

Congressional Amendments to Pre-1969 Tax Laws	501-506
Effect on Private Foundations	502-506
Complexity of Reporting System	502
Deterrents to Foundation Participation in Legislative Activity	502-503; 505
Rationale for Foundation Tax Exemption	503
Unrelated Business Tax Income	504-505
Antitrust and the Non-profit Organizations	508-510
Relations of Regulatory Agencies and Industry	510-511

## The Special Conference

This Special Conference was devoted to an area of major concern in the future technological progress and economic condition of our country: the exploration of how national priorities will have to be reordered and implemented to overcome the plight of the "knowledge industry"—R&D, higher education, especially science and engineering—because of such factors as the reduction of research funding, poor business conditions, unemployment among scientists and engineers, decline in graduate school support, dim prospects for new crops of graduates, the information explosion, and the great increase in employee mobility. A better understanding emerged from the Conference of the role and potential of industrial property, taxation and competition in meeting some of these challenges to the "knowledge industry."

Because of the timeliness and comprehensiveness of the subject of this Conference, we are publishing the proceedings in *IDEA*. We believe our Journal audience will welcome this broad-gauged treatment because of the economic, technological and international problems which are receiving increasing attention of late.

## **Conference Participants**

Carl Batz, Armour and Company  
Milton W. Bennett, Georgia Institute of Technology  
Theodore L. Bowes, Westinghouse Electric Corporation  
Joseph L. Brzuszek, Bailey Meter Company  
Albert A. Caretto, Jr., Carnegie-Mellon Institute  
Sidney Carter, General Motors Corporation  
George D. Cary, U.S. Copyright Office  
Robert B. Chapman, III, AAI Corporation  
O. S. Colclough, The PTC Research Institute  
James Stacy Coles, Research Corporation  
Horace B. Cooke, The PTC Research Institute  
Henry David, National Academy of Sciences  
Richard E. Day, Ohio State University  
Earl H. Dearborn, Miles Laboratories, Inc.  
Nicholas M. Esser, Chemetron Corporation  
Robert Fay, Fay, Sharpe & Mulholland  
Marcus B. Finnegan, Finnegan, Henderson & Farabow  
John L. Gray, Battelle Development Corporation  
John C. Green, The PTC Research Institute  
R. W. Hampton, Eastman Kodak Company  
Arthur B. Hanson, Hanson, O'Brien, Birney and Stickle  
L. James Harris, The PTC Research Institute  
Lawton M. Hartman, National Science Foundation  
J. K. Haskell, Hughes Aircraft Company  
Carl A. Hechmer, Jr., Pennwalt Corporation  
Philip Heiberger, E. I. du Pont de Nemours & Company  
Billy M. Horton, Harry Diamond Laboratories  
Robert M. Janowiak, Illinois Institute of Technology Research Institute  
John T. Kelton, Watson, Leavenworth, Kelton & Taggart  
George R. King, U.S. Patent Office  
Joseph M. Lightman, The PTC Research Institute  
Louis H. Mayo, Program of Policy Studies in Science and Technology,  
The George Washington University  
Willard Marcy, Research Corporation  
Edward V. McCarthy, Jr., The Foxboro Company  
Ralph E. Montgomery, The Pennsylvania State University

Helen Nies, Pattishall, McAuliffe & Hofstetter  
S. Chesterfield Oppenheim, The PTC Research Institute  
George Perazich, Economic Associates, Inc.  
Gerson S. Schaffell, Scientific Design Company  
William L. Scherer, Automobile Manufacturers Association  
Irving H. Siegel, The PTC Research Institute  
Donald R. Simpson, Suffolk University Law School  
R. J. Steinmeyer, Beckman Instruments, Inc.  
George D. Summers, Fairchild Industries, Inc.  
W. J. Wachter, W. J. Wachter & Associates  
James H. Wakelin, Jr., U.S. Department of Commerce  
James T. Wilson, Institute of Science & Technology, The University of  
Michigan  
Richard C. Witte, The Procter & Gamble Company  
Joseph Yahlom, The Technion-Israel Institute of Technology, Haifa



## **The Proceedings of the**

## **Special Conference**

**May 20, 1971**

**WELCOME**

**L. JAMES HARRIS**

On behalf of The PTC Research Institute of The National Law Center of The George Washington University, I welcome you to the Special Conference of Invited Experts on R&D, Technological Education, and Industrial Property: Policy Correlations for the 1970's.

This Special Conference has three major foci:

- (1) Incentives for innovation and invention;
- (2) Problems of the "knowledge industry" (that is, R&D and higher education, especially in science and engineering) due to the cutback in funds for research and development;
- (3) National priorities and their reordering or implementation to take account of (a) antitrust and competition policy in the new R&D setting and (b) emerging needs in tax policy concerning research and education, so as to alleviate the plight of the "knowledge industry" and provide new opportunities.

We called this Special Conference because of the national—even international concern—with the crisis in the "knowledge industry" reflected in the cutback in funds for R&D and the unaccustomed unemployment among scientists and engineers. This Special Conference is one of the major tools of research and education we at the Institute use to deal with problems of this nature.

This Conference is restricted to a relatively small group of highly informed individuals and to a limited number of observer specialists from a broad range of disciplines. The participants are strategically placed and have a need to know and from their experience have something to contribute to raise the level of knowledge.

This Conference is a teaching instrument. We are seeking to provide additional kinds of expertise. Here, sophisticated people can assemble in an appropriate setting and without embarrassment acquire extra schooling. In this type of meeting you do not spend too much time on orientation. With informed people speaking to informed people we can zero in to the state of the art and expeditiously develop "hard" information on the legal and economic incentive systems.

The proceedings of this Special Conference will be widely distributed after editing by the participants. We should like to emphasize that all participants will have an opportunity to edit their remarks before publication. Accordingly, will you please identify yourselves before speaking to assure proper attribution and please speak loudly and clearly to assure an accurate transcription.

In short, we want to encourage you to take advantage of this unique learning and teaching opportunity. Let us keep our comments pointed when possible to what is specifically under way. Let us try to develop "hard" material with respect to our resources of industrial property and to our potential opportunities under the antitrust and tax laws.

I shall conclude my brief welcome by quoting from the formal description in our publications of our Special Conferences:

The maximum benefit of the Conference will be derived from maximum interchange among participants. Sophisticated people will be sharing experience, opinions and insights. Although a limited number of observers have been invited in addition to the speakers, these observers are highly qualified people. Since all attendees are specialists, it is hoped that the exchanges will be free and uninhibited and that the informed opinions from different vantage points will provide new insights.

Dr. James S. Coles, President of Research Corporation of New York, is eminently qualified to chair our Conference today. He was formerly a chemistry professor and subsequently President of Bowdoin College, Maine. During the war he served as research group leader and supervisor with the Woods Hole Oceanographic Institution. He is a Fellow of the American Academy of Arts and Sciences and a member of the American Association for Advancement of Science and of the American Chemical Society. It is my pleasure to present to you Dr. Coles.

INTRODUCTORY REMARKS

JAMES STACY COLES

If we assume that for the foreseeable future our gross national product will continue to grow, it would seem that we must more wisely manage technology than has been the case for the past 50 years. During this period we have devoted much of our gross national product to war or defense preparedness, and to consumer goods—essential or luxury. But we have neglected other needs of our society, in areas such as local government, education, medical care, the judicial system, and the environment—needs of humanity itself. We have been totally ineffective in controlling population. It seems clear that major changes in the uses to which the gross national product is put are long overdue.

The general problem, common to most countries, is to use the fruits of economic growth to meet social wants effectively, and to minimize *undesirable* ecological impact created by growth. New national *and international* policies and controls are needed to give proper direction to this growth. Policy must encourage technology in which environmental impact and social consequence may be equally or more determining than economic efficiency or technical elegance.

Industry must plan on the basis of even longer range and broader scope in the development, manufacture, and marketing of its products. But society must set the standards and competitive nationwide ground rules, which hopefully can become worldwide. Rewards must be provided for the best results, not solely with respect to adequate profits for the manufacturer, but in terms of the total benefit/cost ratio for mankind.

Melding the resources of modern technology with modern social science in a systems-type approach may help provide solutions to complex problems ranging from the urban ghetto to the Arctic tundra. We are only beginning to appreciate the advantages, and recognize the limitations, of this developing use of technological analysis and planning. Development of means for measuring and monitoring the social performance of many of our institutions becomes a prerequisite for the emergence of successful participatory democracy.

Today's Conference is concerned with several limited but important aspects of this comprehensive long-range problem: R&D, technological education, and industrial and intellectual property. It has been conceived to bring together diverse viewpoints on these subjects, and to provide the opportunity to go into some depth concerning a few of the specific areas where change is taking place most rapidly. Dr. Harris in his note to invitees has clearly delineated the hope that our discussions

will lead to a more concerted effort to use our country's vast resources of humanity, intellect, property, and money to fulfill more adequately our social as well as our physical needs.

Our first panel has three very distinguished speakers, and I shall just introduce each of them in the beginning so as to not interrupt the course of their thought as they move on.

Dr. Henry David is a fellow refugee from a college presidency; a man of great distinction, he has been president of the New School for Social Research. He has been a professor of business at Columbia University. As a matter of fact, we were both on the faculty of the City College of New York in the Thirties, at the same time, although we didn't know one another then. He's been Executive Director to the National Manpower Council. This gives you some idea of the scope of his activity.

He very wisely saw the light and joined the scientists a few years ago; he has been with the National Science Foundation for several years—perhaps a decade—and he is now the Executive Secretary of the Division of Behavioral Sciences at the National Academy of Sciences.

We are very pleased to have Dr. David here on our program this morning.

Dr. Lawton Hartman is Special Assistant to the Director of the National Science Foundation. He is a graduate of Yale, with three degrees there—Bachelor's, Master's and Doctor's, in theoretical physics. He has taught physics at Yale, and he has also taught Chinese at Yale. I asked him how he happened to teach Chinese, and he said he had to earn his living somehow. But he has been with General Electric, with Philco, for some 15 years. He came to the Pentagon in 1962. He has been a Senior Specialist in Science Policy Research Division at the Library of Congress, and since 1967 he's been with the National Science Foundation.

Our third panelist, Mr. George D. Summers, who is the Manager of Biomedical Programs at Fairchild-Hiller, is a graduate of West Point. He's been in industrial research and development for some 13 years. He has a number of publications and patents. He's experienced in aircraft, missiles, spacecraft, physics research, medical, industrial, and so on. It's a wide range of activities, so he comes very broadly based.

The panelists will speak in the order in which they are listed in the program. Without further introduction, I turn the program over to Dr. David, who will proceed; and following him, there will be cross-questioning and discussion among the panelists and an opportunity for questions, discussion and comments from the floor. Dr. David.

## **New Conditions and Problems of the "Knowledge Industry," National and International**

**HENRY DAVID**

Thank you very much, Mr. Chairman. Ladies and Gentlemen: The Chairman will forgive me if I subtract seven and a half years from the sentence he gave me as a bureaucrat. I survived for two and a half years at the National Science Foundation.

Before I left my home this morning, my wife asked me what I was going to speak about, and I read with all the solemnity I could muster the title of this panel. "New Conditions and Problems of the 'Knowledge Industry,' National and International." And as a good loving wife should do, she said, "I wish you luck." (Laughter)

This is an impossible problem to handle, not only within the limits of the ten minutes each of us is given to begin with, but also within the time limits of the panel session as a whole. I think the best thing I could do is to establish five points of view—five perspectives—from which one might consider conditions and problems, none of them necessarily new, having to do with what we call the "knowledge industry." And I believe that what I am about to say holds for the Western world in general, as well as for the United States.

In questioning the word "new," I am diminishing the notion of

crisis, and reveal a bias. I do not think the knowledge industry, even though its practitioners so assert, is in a state of crisis. The crisis notion is, I believe, a function of a very short-range view. It is also a characteristic of the knowledge industry itself, which has high capabilities for identifying crises and problems. Professor Harris adverted to a knowledge explosion. It is also fair to mention that we've been living over the last 15 or 20 years in what could be called a time of "problem explosion."

The first of my five perspectives might be described as a shift in the perception of knowledge and, particularly, of what is called science. But this is not new. To a certain degree, the shift in the contemporary view of knowledge and of science is reminiscent of that of the latter part of the Eighteenth Century and most of the first third of the Nineteenth Century, reflected in the term "romantic." The new current today means a revived emphasis upon knowledge as being subjective rather than intersubjective and testable. We have a heavy emphasis upon the value of acute personal experience in leading one to truth. We have a heavy emphasis upon a symbolic world which is private—not necessarily interchangeable with the symbolic worlds of others, as is the intersubjective symbolic world within which the scientist works and through which he expresses himself.

Linked with this is an alteration in the value that is placed upon the knowledge we call science in the sense that it is no longer automatically tied to notions of human advance, to progress, and the like. We are for the moment repudiating much of the posture taken towards science, certainly from the middle of the Nineteenth Century on, and through the earlier decades of this century. During that time there was an automatic assumption that somehow science carried within it a very high social utility. The current mood, not necessarily the dominant one, calls attention to the disutilities of science.

Thus, one of the conditions is the way science and the business of producing scientific knowledge is viewed by the external world and is increasingly viewed by scientists themselves, many of whom seem to carry not only their doubts about what they are doing upon their own sleeves, but would also like to have others manifest that doubt as well.

That leads me to my second point—namely the heightened concern with the consequences of the generation of knowledge and its uses. This heightened concern appears not only outside the frame of the knowledge-producing industry but also within it. There is talk among scientists about the social responsibilities of science. This is a curious way to put the matter because an abstraction does not carry with it

responsibilities, social or otherwise. What they mean, of course, is that they are raising questions about the responsibilities of scientists, not in relation to the science they do but in the light of the flow of consequences from their work and the way they make their livings. So, they are beginning to grapple with the problem of "science assessment," as well as with that of technology assessment. This is most visible, of course, in certain aspects of scientific activity in the life sciences, where the prime object affected is man himself. Consequently, the issue that comes immediately to the surface is what change in the way man values himself will be set in motion by current and future advances in the biomedical sciences. To achieve the retardation of aging, to change genetic structure, to engage in genetic engineering, goes far beyond demonstrating the power of contemporary scientists and technologists. It also raises questions about the fundamental meaning of man, about how we are to think about received ideas concerning the sanctity of the individual.

A third condition has to do with people, that is, manpower. We are now compelled to recognize that we have lived for at least a quarter of a century with high demands for people whose business is knowledge—with its generation and utilization—and that what we had hoped for—that is, that supply would catch up with demand—is apparently taking place. This situation is less a function of changes in the funding of scientific activities than it is of demographic and other developments.

We may not quite have scientists coming out of our ears, but we no longer place a high premium on an array of policies and programs designed to increase the supply of scientific manpower. We are concerned now with finding useful functions in the job market for the highly skilled and acutely specialized people whom we produce. I regard present demand-supply relationships as short-run phenomena. Since I was originally an historian, I think of 10 or 12 years as short run and I would not be unduly troubled by recent changes in the demand for scientific manpower unless, of course, it affected my own employment situation. (Laughter)

The fourth point I want to mention has to do with the situation in which the knowledge-generating institutions of the Western world find themselves. These are obviously the colleges and universities and the large array of research capabilities that exist in both the private and public sectors, including the non-profits and the not-so-much-for-profit organizations with which you are familiar. And the one comment I would make is that, for a variety of different reasons, all of them are in trouble.

Some of them are in trouble because they have lost a sense of purpose, or a sense of purpose that is manageable. Some are in trouble because they have so many purposes that there is no way of properly deploying the resources necessary to fulfill them. This is a general statement about the situation in which many of our universities find themselves. Other knowledge-producing organizations are in trouble because their clienteles or their demands for research have altered as is largely true, for example, for the not-for-profit and profit research organizations.

Some are in trouble because the skills which were used with high success within a closed system—and by a “closed system” I mean the knowledge requirements of the Defense Department, for instance—are not so effective on the knowledge requirements of open systems which are poorly understood and in which control over all of the critical variables is certainly not easy and frequently impossible. A simple illustration of what I have in mind would be the difficulties that the Rand Corporation has, for example, in coping with urban problems research.

The fifth point I would mention has to do with the public nature of the knowledge industry. Historically, even though its output was used in both the private and public sectors—its inputs, essentially, came from the private sector. In this country, as well as in England, France, and elsewhere, a structure of public policies has now been devised which in effect says that it is perfectly appropriate to take public funds and use them to produce, disseminate, and apply knowledge. This has meant moving increasingly toward a single source of supply of the surrogates for resources—that is the dollars that are simply hunting licenses to secure manpower and institutional resources for producing and using knowledge. And that means that the knowledge industry as a whole is far more sensitive than it was, say, 30, 40, or 50 years ago, to fluctuations in public policy decisions, to programmatic decisions, and the like.

This situation is a major source of the present set of problems, although not necessarily a dominant one. In effect, the funds which are proxies for research and related resources can be turned off today by a roll-call vote in the Senate or the House. This is a simple fact of life. When the claims for funds for knowledge production reach present proportions in the order of more than \$18 billion, the proposed R&D budget for fiscal 1972, that is a large enough claim to raise questions in the eyes of those who want to make claims on public funds for other purposes.



The final point I would make flows from this notion that the knowledge industry is a public industry, for there are different markets in which the adjudication of the claims for knowledge-producing resources are being settled. There is a scientific marketplace, a knowledge marketplace in which debates are conducted under certain modest rules and questions raised about methodology, techniques, and the weight of the evidence. In this setting we want to know how observations were conducted, whether conclusions are supported by the data, and we contest with one another saying, "No, this is less true than that, and that is more true than this." In this marketplace we settle questions about the way we value certain kinds of knowledge.

There is another kind of marketplace in which knowledge becomes linked with public policy. Here the terms of reference for conducting debate are vastly different, and the debates are settled in terms of systems of preferred choices that are normative, value-laden. Many of us are now struggling with the problems of discerning or inventing better kinds of institutional relationships through which the producers and the consumers of knowledge can find more meaningful ways to engage with one another—in other words, to link these two marketplaces. In so doing, we appreciate how critical is the issue of relating research to policy formulation and how far we are from knowing how to handle it satisfactorily.

Mr. Chairman, I leave you with these points. They may provide a frame of reference within which the discussion can be conducted later. Thank you.

CHAIRMAN COLES: That's a very, very eloquent statement, Dr. David. That's given us a great deal to think about.

Dr. Hartman would you proceed?

LAWTON M HARTMAN

It's rather difficult, Henry, to follow the excellent statement that you've given.

DR. DAVID: But I don't have to.

DR. HARTMAN: I— (laughing)

DR. DAVID: Well, why don't you do what people always do when they review books? They tell the author he should have written a different book.

DR. HARTMAN: No, rather in trying to decide what to say here today, I thought of an old Taoist expression which goes roughly, "Those who talk a lot don't know what they're talking about; those who know, keep quiet." And, in that sense, I was indeed flattered to be asked to cover the new conditions and problems of the knowledge industry in ten minutes. I didn't think it was quite possible, and after listening to Dr. David I find that we're all at a disadvantage.

I wanted to talk about two points. I was intrigued by the emphasis placed in the announcement of this Conference on the apparently critical nature of funding and the attempt to tie the reduction in federal support of research and development funding to an emerging critical situation in the research and development or knowledge industry.

There are two aspects of this which I believe are worth mentioning. I don't for a moment believe that we are really suffering unduly, in the broad field of research and development, from the relatively small perturbations in federal funding in recent years. There are two reasons for this. One, industrial funding of research and development, with its own funds, has been growing at a rate considerably in excess of inflation; and though I haven't checked, I believe it's in excess of the growth of the gross national product. It now exceeds federal funding for research and development in industry by more than a billion dollars a year; and it has been growing relative to federal funding for quite a number of years.

Now, industry simply does not put something in excess of \$9 billion into research and development, including basic research, and continue to do so over many years and at a growing rate, without experiencing benefit from it in the marketplace.

Another aspect, however, of this funding, something that I have not seen mentioned generally, is the distribution of the funding by the federal government and what has happened to that distribution. Between 1969 and 1970, federal funding of research and development in current dollars reduced approximately 2.9 percent; and this reduction was shared by all sectors participating in research and development, except one—namely, research and development conducted by the federal government itself. It went up 2.9 percent. The universities, industries, not-for-profit organizations, even federally funded research and

development centers, suffered a decline, even in current dollars, while federal laboratories increased.

Now, there are two aspects of that. One, it's interesting to note that if the federal government had shared the reduction in funding that the other sectors of the economy were forced to absorb, it would have released, simply by redistributing the funds, of the order of \$180 million, an amount which would go far to assist the universities in their present financial situation.

Now, the other aspect is of course that there are an awful lot of federal laboratories. I made a study about five years ago, a rather impertinent study of federal laboratories conducting research and development on environmental pollution. And I found 192 such laboratories, federal in-house laboratories, claiming to do research and development on environmental pollution. When you examine the history of these laboratories, the date when they were formed, you find, surprisingly, that the total number is exponential in time. The growth curve shows that the rate of formation of laboratories directed to this one field of environmental pollution is simply proportional to the number in existence, which implies that very little planning goes into the decision to form a new laboratory.

Then if you look further, you find that the number of items of legislation, the enabling legislation that permitted these laboratories to come into existence, also, for many decades, has increased exponentially. And this all raises a question as to whether federal laboratories, which are absorbing a fairly substantial portion of the federal research and development budget, do not really constitute a research and development pork barrel.

Now, this is the type of problem that one can think about. I don't know what one does about it.

With respect to federal funding of research and development in industry, I think it is important also to note that about 79 percent of such funding goes to two industries—namely, the electrical equipment and communication industry and the aircraft and missile industry—which are, to be sure, exceedingly important. But at the same time, they represent a relatively small part of value added by manufacture. And so I think we have to recognize that the large bulk of American industry, representing approximately two-thirds of the total funding for research and development utilized by American industry, is fairly insensitive to federal funding of research and development.

Those two industries, in particular, are exceedingly research and development intensive, so that fluctuations in federal funding are

bound to be reflected in an unstable manpower situation. And I think it is in those two industries that we are most acutely aware of lay-offs of scientists and engineers, a most unfortunate thing to happen. But there's another aspect of that.

And for that I'd like to consider briefly an aspect of basic research that I think forms an interesting handle for a number of new conditions and new problems of the knowledge industry. I'm thinking here of a broad field that we might generally call "environmental science"—and by that I mean science addressed to the natural environment, the social environment being hopelessly more difficult. But considering only the natural environment of atmosphere and biosphere and hydrosphere and lithosphere and so on—we have reached a point today—and I unfortunately must take issue with one point that Dr. David made—that I believe is a point of very serious crisis.

It's a crisis of two kinds. With a burgeoning public concern over the environment, its status, its future, and man's possible intervention in it, and what the long-term consequences may be of such intervention, we are faced by the complete incapacity today of environmental science to answer, definitively and quantitatively, any single question you can ask about the environment. We've heard a great deal about technology assessment. The fact remains that it is impossible today to conduct anything but the first-order, most trivial types of technology assessment. Meteorology, oceanography, ecology—all of these fields are wide open for exploitation, and the demand is enormous. But we have a situation which we've never quite confronted before, where science is not capable, really, of contributing the kinds of knowledge and understanding that are required by the public interest at the present time—and for the foreseeable future, for that matter.

Now, the other side of this coin is that, at the time when certain industries are having to lay off scientists and engineers, there is a critical shortage of manpower all across environmental science. If you identify, for example, as I did, 87 specialties which, taken together, constitute environmental science, including everything from ecology to meteorology and so forth—within these 87 specialties there is a median of 20 Ph.D.'s doing research and development in the United States. That means that half of the specialties of environmental science at the present time have fewer than 20 Ph.D.'s working in them, and that at a time when we need to know a great deal more about the long-term climatic effects of fossil fuels, about how mercury gets into fish, about how DDT gets into penguins in the Antarctic, what really happens to the tundra if you disturb it, and so on. A whole host of such problems.

And so we have to distinguish very carefully, in connection with the public concern over the environment, those problems that can be handled almost in a trivial sense—don't put the sewage in the rivers, and that sort of thing—and the long-term consequences of what in fact we are doing.

Now, if this is a crisis—and many of us think it is—then the question arises as to how to approach the subject. And this raises a number of new problems of the knowledge industry. It raises the question of the role of the university. Fully two-thirds of the scientists in environmental science are in the universities; however, environmental science is “systems science,” an emerging concept that has not been characteristic of science over many centuries, where it has involved a principal investigator working on a grant, a scientist in his laboratory with his associates, his assistants and his students. Here we have systems science, where many specialties and skills and talents must be brought together, with enormous amounts of input data, with the most difficult types of mathematical computation, to solve problems which we really don't understand today—let alone be able to attempt definitive solutions.

But universities aren't put together quite this way. If I can adapt an old expression from Sir Arthur Eddington, “Verily, it is easier for the camel to pass through the eye of a needle than for academicians to cooperate with each other on a project.” So there is a very serious question here of imbalances. We have an imbalance between public need and the capability of environmental science. We also have an imbalance of a different kind. The universities have the scientific resources to tackle major problems of environmental science. They have no idea how to do it. Industry doesn't have any resources today, in effect, to handle environmental science; but they have superb ability and experience in handling major systems. The question is; how to put them together.

And we don't know. Whether it means an entirely new type of research center to be established in many places in the nation; whether they should be under the aegis of a university; or whether they should be a GOCO (government-owned company-operated) type of thing that has worked so well in atomic energy—these are questions to be resolved.

There's another problem that I'd like to mention with respect to the universities, because I think it is a possible danger that we could be walking into, and that is this matter of multidisciplinary, interdisciplinary type of activity. It's not entirely clear what these two terms

mean. I find it easiest to think of “multidisciplinary” as consisting of activities involving many disciplines and the people representing many disciplines, and “interdisciplinary” as being something associated with one’s private soul, and therefore having to do with a much broader type of generalist education, which may be a good thing but which may not lead to the kinds of people that programs of a multidisciplinary nature in universities, that are coming into being more and more, may need to achieve their objectives.

In particular, I think we have to look for people to be coming out at all levels of higher education not as generalists, not as people who are academic dilettantes, not people who begin their lives with jobs involving matters of science and public policy and the like, but as specialists—specialists who can do something well. I think, for example, a person who has gone through a graduate program in environmental science in the *very broadest sense*, could have a harder time becoming a competent contributing ecologist than a competent Ph.D. electrical engineer, or some other specialist, provided with a certain amount of transition time and guidance to learn the subject matter he is going to deal with.

The fundamental role of the university on the graduate level, in my judgment, insofar as it involves new manpower, is to continue to produce specialists of high quality. And in that regard, I think the university has a very serious job to do, and one that it does not always see mto be doing too well—namely, not encouraging too many people to go into fields where the future employment opportunities are certainly limited. The world can only handle so many physicists in elementary particle physics.

The difficulty that physicists, for example, are having in getting jobs, does not really seem to relate entirely to the number of jobs available. It relates rather to what they have been led to want to do, their aspirations, namely, academic research in the field of their degree. There are enormous opportunities for physicists throughout the country, if they wish to go and find them and do them; they just don’t want to do that kind of work, frequently. And it takes a year to get used to the new look.

Well, I’ve probably used up my ten minutes. I think there’s just one final point I’d like to make here, and that concerns the matter of attitudes. I think attitudes are simply going to have to break down. There is the traditional one of regarding people in the academic world as a bunch of—well, as Edward Teller once put it, he had been called an egghead, and he’d been called a longhair, and he’d never been able to reconcile the two. But there is also an attitude in the academic world

of looking down the nose, let's say, at people in industry. There is often a lack of a genuine mutual respect between scientists and engineers in universities and those in industry, an attitude that does not lend itself to the types of cooperative relationships that are simply going to be necessary if we're going to make environmental science pay off in the next decade or more.

Thank you, Mr. Chairman.

CHAIRMAN COLES: Thank you very much, Dr. Hartman. Mr. Summers?

**GEORGE D. SUMMERS**

In noting the quality and background of my fellow panelists, I quickly came to the conclusion that I represent the balance. I'm down on the firing line, and perhaps from that point of view, see things a wee bit differently.

Now, perhaps it would be sort of a summary point to start out by saying how our company may have in the last month indicated its confidence in the future of R&D. We had an annual stockholders' meeting, at which time the board of directors recommended a name change, which was duly passed. We are no longer Fairchild-Hiller; we are Fairchild Industries, Incorporated. And the point made was that we now are diversifying into more areas, such as real estate. So perhaps that gives you a clue of some thinking, at least in one company.

We've heard already—and we all know of some of the difficulties in the knowledge industry—the hundred thousand or so scientists and engineers walking the streets, and the many others who have simply switched professions in order to avoid that. We read of near bankruptcy and catastrophes in universities and colleges all over the land. Are we experiencing a mere bump in the road, as has already been suggested, that seems magnified by the smooth progress we've been making for the last decade or so in this field? Are we instead experiencing a well needed reassessment and readjustment of the goals of humanity, in which the knowledge industry will have an honored but necessarily

constrained part? Or might we be on the start of a modern equivalent of those antiscientific spasms that have surfaced from time to time in human history?

It's my belief that we in this knowledge industry are part of an inexorable forward and upward movement of technology in the service of man. Maybe that sounds a wee bit idealistic, and it gets all entangled with the profit motive, but many of our advances in history have come from the profit motive. Of course we know that progress is not preordained and that unfortunately we have to solve today's problems with today's organizations and with today's tools. So what are some of the conditions and problems? I've tried to divide some of my remarks into two different segments—one in the area of scientific higher education; the other in R&D. I think these can be separated.

One way to assess the status of higher education, in my opinion, is to examine its financial support. We've heard some numbers already, and I can apologize for the numbers I'm going to quote, which are not necessarily identical, but I didn't make them up. I got them from good sources.

It has been reported that the budget for support of scientific research and education in academic institutions was up 8 percent in 1969, and again in 1970. In constant-value dollars, this represents an annual increase of perhaps 4 to 5 percent. The figure must be contrasted with the increase in population growth in a year of about one percent and the slight decrease in the gross national product. Of this 8 percent annual financial increase, the federal portion was up 2.4 percent, for both '69 and '70. In terms of a constant-value dollar this represents a slight decrease. But I think to keep our perspective it must be remembered that direct and indirect federal monies account for about 40 percent of the total academic science budget. Looking to the future, Edward E. David, Jr., who is the new science advisor to the President—well, not so new; he's been in the office several months now—recently reported that the FY '72 budget requests a 14.7 percent increase in federal dollars for institutional support and research at colleges and universities.

It would thus appear to me that in this area, financial problems may and certainly do exist, but they may have their roots in empire building within academia, and in the timidity of responsible leadership to make selections and establish priorities, as was already pointed out by a member of the panel.

Now, as far as research and development: Within the knowledge industry, the research and development segment can be segregated in



one sense, in that there exist two sets of activities—one that pushes out into the new and unknown, and another set of activities that deals with repetitive services and the production of goods. Both of these are essential to the welfare of our nation. In the academic community, teaching is a major form of the repetitive service. In the industrial sector, mass production and distribution is your repetitive form. These activities contrast with the R&D activities where innovation and invention can lead to subsequent application of that knowledge to the economic and cultural utility of man. So where do we stand in our R&D commitment?

Let's look again at the financial figures. According to the National Science Foundation, and I guess I should clear this to be sure that these numbers are really true; but the total U.S. R&D expenditures for 1971 are expected to reach \$27.8 billion. This is 4 percent above the 1970 level. In constant-value dollars, this means that the national R&D effort paused along with the general economy in the last year or so; but note that this enormous amount of money represents about 2.7 percent of our gross national product. So a very valid question is, does this amount of money represent an optimal share of our national resources, or should it be adjusted higher or lower?

Within the overall R&D effort, about 14 percent is your basic research, 22 percent is your applied research, and your remainder, the 64 percent, for development. Of course, what goes into what category is a matter of semantics in too many cases. According to the figures that I have, over half of these R&D funds—roughly, \$15-1/2 billion—come from the federal government and, within the federal sector, the lion's share of the R&D funding comes from the Department of Defense. Forty-eight percent of our federal R&D comes from this source. Next, the National Aeronautics and Space Administration provides 22 percent; followed by the Department of Health, Education and Welfare, with 10 percent. The Atomic Energy Commission provides 8 percent of the federal R&D support, and the Department of Transportation 4 percent, the National Science Foundation 2 percent, and other agencies lumped together, 6 percent.

The FY '72 budget calls for an increase in overall federal R&D spending of 7.6 percent, up to a total of \$16.7 billion. And I think I've given enough of these statistics. Many people perhaps are not too interested in them, but they do tend to show a trend. Most agencies within the federal government will have increased R&D budgets, while NASA and the AEC will have modest declines next year. One must conclude that insofar as overall funding levels go, the share

devoted to research and development is not declining, but may be settling out into a constant portion of the gross national product.

As to how we should spend this money this has been brought up already. This is where the wild debate rages. It certainly is a valid point of contention, where we have to do some real, hard thinking. We're aware of the bitter attacks that have been made—these have been alluded to already—attacks on the R&D dollars. Usually, these attacks are directed against the military and space portion of it. Often the call is made for shifting priorities to housing, education and health. In general terms, what can we expect from our R&D dollars—not only the federal but the private sector?

Well, it's obvious. Just to review a few expectations for you: for the individual, new goods and services at a reduced cost compared to old ones, through more efficient means of production and new materials; and better means to diagnose and treat injuries and disease. R&D can also just simply fulfill the need for a creative outlet and a more satisfying life for people who are of that bent. For society, R&D can offer us a range of alternatives that simply do not exist today. It hopefully can free man from drudgery and lead him to a higher plane of living. It can point to solutions to today's insoluble problems and it can perpetuate itself and lead in turn to ever more progress through more R&D.

For the nation, R&D can allow us to survive and compete in world economic affairs. Rodney Nichols, a special assistant in the Office of the Secretary of Defense for several years and now Director of Program Planning and Development at Rockefeller University says, "Most economists agree that our principal, if not only, past advantage in international trade was our technological edge." And recently, Philip Bothe, in *Science*, reporting on a three-day seminar at the National Academy of Sciences, wrote, "Several speakers expressed concern that the United States is in danger of losing its world lead in high-technology industry. They suggest that trade balances may worsen, productivity may decline, unemployment may remain high, and the economy may stagnate unless a greater R&D effort is made."

At the same meeting Science Advisor David said he believed the country is losing its technological nerve, that the public is becoming increasingly alienated from rational ways of thought, and that we are losing our courage to experiment. He stated, "Already we see timidity in new undertakings. We require over-analysis before we are willing to find out what are the real possibilities. If these trends progress, our society will become dull and altogether stagnant."

We can see on every hand the value of the national R&D effort, but is money allocated to this purpose all that is required to assure the continued technological leadership of the U.S., to restore the deteriorating balance of payments, and to lead us into a rosy technological future? Well, of course not. Money is necessary, but not sufficient. There are many other problems, some of them mentioned. I'd like to mention briefly just two more, one of which has already been touched on.

I feel that by far the most serious national problem is the poor cooperation that exists between government, academia and industry. I feel that the welfare of this nation demands that within and between these segments of our society, we find ways for mutual planning, open communication, more efficient utilization of resources, adherence to truth and fair dealing. Is this too much to ask of the leaders of our society? Or do we really like it better with fragmented planning, excessive suspicion and secrecy, useless duplication of effort, distortion of data, and sharp and sometimes questionable dealings? If you've read much about the future of Japan, you'll see that there cooperation between industry and government has resulted in the current economic miracle that in the last 10 or 15 years has lifted that nation to the third place among nations in gross national product.

I think a second problem concerns Edward David's warning on timidity and over-analysis. A root cause of this problem may be our institutionalized systems, wherein the fear of consequences of a wrong move can paralyze individual initiative and cause a fall-back on committee decisions, or I think probably worse, dependency on decisions being eventually handed down from some Great White Father higher up in the organization. In government, an action item must often be coordinated through dozens of agencies, branches, departments, and so on. A civil servant knows that being right may not help much, but being wrong can ruin him.

In industry, the typical place for making your decisions is your profit-and-loss center at divisional level. Here, according to James Hillier, RCA Vice-President at the time this statement was made, "This does not provide the suitable climate for nurturing more than the most minor innovations." He says the basic reason centers on the fact that the division manager, the decision-maker, is almost universally judged on his end-of-year profit-and-loss statement. Not what he's doing for humanity, not what he's doing for the ecology or to the ecology, but end-of-year short-term return on investment. Thus, this man, a key

man in American industry, has relatively little scope, money, or manpower to tolerate any substantial risk. And so our risk must fall back to the federal sector—and now you have the beginnings of a problem.

Of course, in the academic community, the price of a wrong position can be a lifetime branded as a second-rate researcher or a hare-brained thinker. Under such constraints as these—and these are the various segments of our knowledge industry—we may have created a breed of timid men who cannot afford to make more than a minor mistake. Although the line between risk and foolhardiness is often cloudy, I think as a society we must find a way to encourage and reward individual initiative and have some tolerance of the mistakes that will inevitably occur. When mistakes are not tolerated, there will be little initiative, and without initiative, there will be no progress.

So to conclude, in an era where the knowledge industry has settled down to perhaps a more or less static percentage of the gross national product, it behooves us to be more efficient in utilizing the resources placed at our disposal by society. Some of our problems are of our own making, and we must solve them by responsible leadership and enlightened management. Some of our problems relate strongly to the government, and here we must find new mechanisms for cooperating toward common goals. Other of our problems, of course, may spring from the spirit of society and the institutions that we have created.

O.K., problems we have; but problems can be overcome. The knowledge industry is far from sick, but it must retain confidence in itself, and the future. We in the knowledge industry are the keepers of vital assets of our nation and of our race. Education is the key to a better future, and research and development is the cutting edge of the knife we use for carving out our destiny.

#### **CROSS QUESTIONING AND COMMENT BY PANEL OF EXPERTS**

**CHAIRMAN COLES:** Thank you very much, Mr. Summers. I think you touched on one point which might provide a take-off for the other members of the panel. You spoke about the poor cooperation among the government, academia, and industry; and I think we have representatives here on the panel and in the room where there might be some

comment upon the cooperation which exists among government, academia and industry, because that certainly is a key to this. You mentioned Japan, and of course in Japan so far as I can see, the industry is almost identical with government; they operate very close to hand-in-hand, but what do you think about that, Dr. David?

DR. DAVID: I don't know. In other countries the degree of, quote, "cooperation"—whatever that might mean—that they believe obtains among these three sectors of a society in the United States, is highly envied. You know, we have much higher rates of mobility among the three, from government into the industrial sector, from the industrial sector into the government, and from both of these into the university world, the academic world, than takes place elsewhere.

I don't know how the government could be more cooperative than by picking up 40 percent of the operating budgets of academic institutions, for practical purposes. Could there be any way of exercising a greater measure of cooperation than by placing a certain set of policy decisions and research decisions in the hands of academics who are invited to render peer judgments on research support? The chief performer of R&D for the government is the private industrial sector. All of the high science and technology industries have been nurtured, to put it mildly—some even created and sustained—by public funds. If these are not the terms of cooperation, I do not know what they are. So, I do not quite see what you are talking about in that regard. If you say there is no common, universal plan, there is no doctrine for a common set of priorities, that there may be duplication of efforts in certain fields, you are right, but I think we would be badly off if there were no duplication, no elements of competition. I thought that what is highly valued in this society is a set of pluralistic values. Do you want to play God? Do you want to write the terms of reference for national objectives and national will? If you propose to do that, I will reject you. (Laughter.)

What is wrong, as you discern it, and where are the terms of correction? I do not mind remedying adverse situations, but I do mind attempts to remedy mythologies. I want to have them dispossessed, taken out of the system. If you talk with people in England, they say, "If we could only have the same mode of interaction that you have in the U.S. between the government sector, the university sector, and the business sector, by God, we would have it made!" And they have taken as their model for effective linkages, the United States. So, either their perceptions are absolutely cockeyed, or else the speculations you have made are open to question. No doubt, I have overplayed my hand, but for obvious reasons.

DR. HARTMAN: I wonder if the answer doesn't lie somewhere in the middle. I certainly share your feelings about the value of the way in which we have done things, but I believe that there is another aspect to cooperation that we've come to call by a different name. We call it "national programs." Where there exists a sense of crisis, somehow the resources of the nation are brought together in planned, managed, coordinated activity to solve these problems of crisis.

We have seen this thing in the Manhattan District during the war. We have seen it in a different sense in the formation of NASA, when we decided we should go to the moon. There are many possible national programs, which place the monkey squarely on the back of the federal government, because even in the most cooperative ventures, somebody has to call the shots. So I think that cooperation in the sense of somebody, namely government, deciding what the priorities are, through the processes of determining the public interest, as government does, leads to a type of activity which perhaps in many areas we have not seen enough of.

I understand, for example, that in Japan this combination of industry, government, and financial institution specifically aims at penetrating international markets, in quite a different sense from the normal give and take of the marketplace.

Now, national programs provide for cooperation of one sort. Apart from that, we have, as I think Dr. David so eloquently put it, a certain sense of values of a different sort that have become important to the wellbeing of this nation.

DIRECTOR HARRIS: Mr. Chairman, may I ask a question? Would you use different criteria for the penetration of foreign markets than you would on the national scene?

DR. HARTMAN: I think this problem is much too complicated for me to attempt. It is concerned with so many things that are not related to research and development, such as the balance of payments problem. We have the large growth or proliferation, if you will, of multinational and international corporations, where parts of corporations compete with each other across international boundaries. We have activities by foreign governments in tariff subsidies. We have this Japanese situation. There are many types of such things.

I don't believe I should be responsive to that question. I don't know. I just don't think that research and development is seriously deficient with respect to the international trade position of the United States. I think it is complicated by many other factors.

DIRECTOR HARRIS: Well, you mentioned Japan, and they're a vigor-

ous nation—R&D-wise. When we talk about the transfer of technical information, we're constantly talking about sending the information abroad, helping these other nations. At our Institute we've had discussions of the need for a reverse flow—for example, a serious problem with countries like Japan is how we might encourage them to send more technical information to the United States. We now can use some of *their* know-how, and perhaps this is true in other countries that have developed to a point where their know-how, in certain technologies, may be more advanced than ours. And so I was wondering whether you were also directing your attention to the relevant international problem which is equally urgent. Some sort of domestic cooperation may be even more acceptable in certain American quarters if it improves our trade positions with foreign countries.

DR. HARTMAN: Well, whether we would have access to such information from foreign nations or not, I think we come back to a much more fundamental point—the one that Mr. Summers described so well, namely, this area of timidity. I really don't think that the problem of whether we do or do not get certain types of information from foreign nations or from our own laboratories is really the issue. I think Mr. Summers hit on a very important matter.

MR. SUMMERS: I'd like to throw out the additional thought here that perhaps we can use as an example in this area. Dr. David is challenging my position, and it would seem to me that perhaps the current controversy over the method of implementing the National Cancer Crusade is one small example, perhaps, of problems within the bureaucracy—not using that as a derogatory term. We have on the one hand very powerful political factions who want to break this National Cancer Crusade out, as a separate Manhattan-type project, put it under a powerful man reporting, I believe, directly to the President, spending an initial \$400 million additional per year, rising at the rate of one or two extra hundred million per year for the next several years. On the other hand, another faction would like to continue what we have done under the National Cancer Institute, going forward exactly the same way and spending more money.

On one hand you have the directed effort. On the other hand you have this area, that was touched on here, of duplication of effort, scientists going their own way, following their own interests, in the present pattern of the National Institutes, which has been criticized by the other side. So here is just one homey example of the area of controversy within the federal establishment itself.

DR. DAVID: I wonder if I might pick up on that, Mr. Chairman, and

“unpack” this little story that you have put on the table. First, what is at issue is “declared public policy.” And the way in which we state public policies in order to have a sufficiently large number of interested constituencies resonate to them, so that the necessary support is provided, is to express them in some metaphor, or to state them in highly ambiguous terms. No one fusses very much if you say that it is the declared intention of the government of the United States to maintain high levels of employment. That is the language of the Employment Act of 1946. But it matters whether you mean by that 6 percent unemployed, 4 percent unemployed, or 2 1/2 percent unemployed. The act does not, you know, declare for full employment. That is another kind of concept, and the act would never have been adopted if that language had been insisted on.

We have another public policy that is expressed in the notion of conducting a war against poverty. If you went out of your way to misname a policy to find the most misleading conception of what is involved, you would settle upon “war against poverty.” Incidentally, we also conducted a “war” against the depression in the Thirties. The language was the same. As a matter of fact, many of the people who first manned that “crusade” came out of the military.

All right. Now, what can one possibly mean by a “crusade against cancer”? You recall the Children’s Crusade? What citadels in the Near East are we taking by storm? The rhetoric establishes a set of objectives that renders the enterprise self-defeating. All right. The point that you made about agreement represents a nice illustration of what I said about the two marketplaces in which differences are resolved. There is no mode for accommodation between a man who wants to make political hay with an election in ’72, and a group of scientists who say that the problems of cancer have to do with problems of life. As I indicated, we just do not know the best way to grapple with issues of this kind.

It should be clear that it does not make much sense to take the Apollo project or the Manhattan bomb project as models for ways of coming to grips with certain problems. There the critical problems, as you know, were not scientific. They were essentially technological, and the issues were how to move from the known base of science to a set of steps that had to be taken technologically—which in turn raised some very fundamental scientific problems.

The absence of agreement is not necessarily the failure of cooperation. I always worry about the term “coöperation,” because I remember the remark that Averell Harriman once made about people with



whom he was dealing: "My God, I told them that I was willing to cooperate. Why the hell don't they do what I want?" (Laughter)

CHAIRMAN COLES: That being the case, I've got to cooperate with the program which has been set up here that I'm going to use. Before I recess the group for a coffee break, is there anyone on the floor who has something which he just wants to be sure to get out before we go off for coffee? If not, we'll have a break now for coffee.

\* \* \*

CHAIRMAN COLES: Professor Harris had word yesterday that Mr. George Frost, who is listed on the program as our next speaker, would be unable to be here because of some emergency at General Motors. But to substitute for him, is Mr. Sidney Carter, who is also from the Patent Section of General Motors Corporation. Mr. Carter is a senior attorney. He's been there for some 19 years. He's had responsibilities in patent prosecution, licensing, general contracting. He's a former patent examiner. He's been an Air Force and government contracting officer in the Patent Branch at the Wright-Patterson Air Force Base.

Mr. Carter tells me that he will speak on the same general subject as listed here on the program, of new challenges to patent know-how, other industrial and intellectual property rights. And knowing that he has not had a great deal of time to prepare for this, why, we can look forward to having really a down-to-earth input from directly off the top of his knowledge, which is very extensive in this area. Mr. Carter.

## **New Challenges to Patent, Know-How, and Other Industrial-Intellectual Property Rights**

**SIDNEY CARTER**

Thank you, Mr. Chairman.

What I'd like to do is, without apologizing, merely say that, with the benefit of the thoughts of George Frost, plus my own between the hours of 9:30 last night and about 10 this morning, flying most of the time, one way or another, I have prepared something which will touch at least on the general areas of problems covered by the title of the talk. And of course I'm hoping that the free-wheeling discussion will touch on the other aspects which have been either lightly brushed or not brushed at all, and we hope that we can come out with something that's mutually beneficial in our discussions. So without further ado, let me proceed.

Those of us who are engaged in handling practical problems associated with patents and technical information are largely dealing with two items. One is the transfer of technical information; the other is the right to use technical information. Perhaps the most useful contribution we can make to the proceedings today is by expressing a few observations on the effect current developments have had and can be expected to have on these two items.

One of the principal current developments is the so-called knowledge explosion. The President's Commission on the Patent System expressed much concern on this problem in 1966. Their focus was in large measure directed to the patent administration problem of searching before patent issuance. The explosion has received greater prominence, however, with respect to the general problem of storing, indexing, and retrieval of a quantity of technical information that is far beyond the capacity of available library facilities.

Our impression on this problem is that it is serious. But not nearly as serious as some have suggested. Now, don't forget, this is speaking from the standpoint of corporate practitioners and dealing with the day-to-day problems involving patents and know-how. Each day we deal with the consequences of patents that issue without adequate prior art before the patent examiner. It is easy to say that these patents should not issue, and that there is something wrong with a system that leads to the large numbers of such patents. To those who are faced with these patents, however, the matter is more one of degree than kind, and the situation is not as critical as theory might suggest.

Why is this so? In the first place, industry has long been concerned with patents that have issued without the Patent Office knowing the best prior art. No matter what kind of an examining system we have—and it will vary from period to period and commissioner to commissioner and load to load through the years—at best, the examining system is only one which approaches some degree of perfection. Anyone wishing to confirm the fact that not all of the best prior art is turned up in the Patent Office need only look to the law reports—for example, the Supreme Court decisions in the '31 to '40 decade—and in there, these matters can be demonstrated very clearly as being a system which at best is imperfect.

Therefore, if a patent charge is asserted, the matter becomes one of pick-and-shovel investigation, so to speak. In the first instance, this does not involve needle-in-the-haystack types of digging into the available publications. Rather, emphasis is placed upon the more easily and readily available materials such as classified U.S. patents and information available from the engineers and scientists working in the field. Our experience was and continues to be that this sort of investigation is the most fruitful—and in most instances provides the necessary prior art to handle the particular problem.

To be sure, there are instances where we engage in extensive searches in the literature and otherwise. These can be exceedingly time-consuming and expensive. But this, too, is nothing new. It's been done

before. This is not to suggest that we should all relax in some comfortable assumption that people are seeing a problem that does not exist. We are not subscribing to any thought that the Patent Office should not get the very best prior art possible. On the contrary, we think that the major work can and must be done to provide more effective ways to retrieve and use the mountains of technical information that are constantly accumulating.

These observations may be surprising, and since they do conflict with what may seem obvious, perhaps an explanation is in order. Our concerns are with the handling of issued patents. We operate under the rules of law which have been built up through large numbers of judicial decisions. In most cases, careful analysis will show that the judicial rules make very good sense.

The following is a quick examination and enumeration of some of the more important of such rules, as viewed from the standpoint of the practitioner.

One of the basic rules is that, where the patent examiner does not consider an item of prior art, the usual presumption as to patent validity is severely curtailed. The effect of this rule in cases where we do searching of the sort that the Patent Office might do in theory, and should have done, is quite beneficial. The result is that by some diligent searching through the prior art, references turned up not cited in the course of prosecution, and pertaining directly to the patented invention, are given great weight by the court in terms of evaluating the validity.

Another basic rule being given greater emphasis today than in the past, is that the patent applicant owes a duty to the Patent Office to come forth with the pertinent prior art known to him. There are many questions of judgment that arise on whether, in a given instance, prior art should be called to the attention of the patent examiner. We do feel, however, that the emphasis on this item in recent years has had the effect of somewhat reducing, but not eliminating, unfortunately, the instances where patent examiners are uninformed of important prior art.

Finally, the fact is that some forms of prior art never have been readily available to the Patent Office. The easiest example is public use material. No patent office anywhere is able to locate the public uses or public knowledge, since all that can be done is to search the available records of prior issued patents and publications; and as indicated, this is done to a greater or lesser extent. Since a rather large number of cases involve this sort of prior art, it cannot be expected that the

document storing and retrieval problem would affect the situation in any real manner. The labor of research and investigation remains the same.

In our view, therefore, this is one of the major reasons why the problems of the patent lawyers have not been affected as much as the theory might suggest.

Turning now to a somewhat different subject that is of concern to us. Some years ago, the Supreme Court decided the case of *Sears v. Stiffel*, 376 U.S. 225 (1964). The facts and substance were these: Stiffel had designed a very distinctive and attractive pole lamp. It had received a great deal of success in the marketplace. Stiffel had obtained a design patent on the lamp. When Sears brought out a copy of the Stiffel lamp, Stiffel brought an action for infringement of the design patent and for unfair competition.

The trial court held the design patent to be invalid. The court of appeals affirmed this judgment. However, the court of appeals reversed the trial court's refusal to enjoin manufacture and sale of the lamp. The court reasoned that the very distinctive lamp was one that, under Illinois state law, could not be made and sold without trespassing on the right of Stiffel to be free from such exact competition. The Supreme Court reversed the court of appeals. The basic holding, though not everything that was said by the Court, was that the lamp was not covered by a valid patent, and therefore could be manufactured and sold by anyone. The Court reasoned that the patent law provides the only exception from the general rule that anything in the public domain may be copied and manufactured by the public at large.

Our personal view is that *Sears v. Stiffel* is sound law, and that any other judgment by the Supreme Court would have been most unwise. However, from the point of view of this Conference, perhaps a more important aspect is that the language used by the Supreme Court in *Sears v. Stiffel* has led to an extension of the case to a different field—namely, unpublished technical information, trade-secret type of information not known to the public.

This point can best be illustrated by reference to the case of *Painton v. Bourns*, 309 Fed. Supp. 271 which was decided in 1970. In that case, Painton brought suit in the Southern District of New York, for a declaratory judgment to the effect that it was free to use technical information supplied by Bourns under a trade secret license. In substance, the license provided for royalty payments in electronic components that were not covered by any patent, and included a provision under which Painton, the licensee, could cancel. Painton did cancel,

and argued that by such cancellation, it had the right to manufacture and sell the product royalty-free.

The trial court regarded the United States patent laws as covering the sole way that inventors can receive payment for their inventions. In the words of the court, "Our patent policy of strict regulation of inventors would be undercut if inventors could enforce agreements for compensation for alleged secret ideas without being required to submit these ideas to the Patent Office, and thereby eventually have the ideas disclosed to the public." The trial court further made the following statement: "This court holds that federal patent law requires an inventor to submit his ideas to the Patent Office before he can compel consideration for the use of his idea."

We are happy to report that the Court of Appeals for the Second Circuit reversed this aspect of *Painton v. Bourns* decision in its ruling on April 27th. We probably have not heard the end of the *Painton v. Bourns* matter, but even if we have, it still deserves a good deal of attention. Frankly, the trial court opinion in the case is difficult to understand. To be sure, one can take the position that the patent law is exclusive and supersedes the law of trade secrets. The trial judge was right in pointing to *Sears v. Stiffel* case, and some subsequent Supreme Court decisions, as containing some language that might support this theory. But in the practical world, we look at this matter quite differently. And it is this approach that warrants our consideration at this meeting.

On the one hand, I think that we have and should continue to have, an absolute rule that anyone can make products that are in the public domain and either unpatented or unpatentable. This is an essential element of competition. The whole theory of the patent law is that when the conditions of patentability are met, we should grant the exceptional right to exclude others for a limited period of time. It is implicit in this law, as the Supreme Court has pointed out, that absent these conditions, there should be no right to exclude others.

On the other hand, however, this rule should not apply to products that are not in the public domain or to aspects of products that are not in the public domain. Anyone concerned with product manufacture and sale soon learns that there is much technical information not publicly available which is required to manufacture and sell a product. This ranges from trade secrets and know-how, to such items as detailed engineering and dimensional definition, as well as inspection and test

procedures—which represent a substantial investment of time, money, skill, and facilities.

The easy example is the famous case of *Tabor v. Hoffman*, 118 N.Y. 30 decided by the New York Court of Appeals in 1889. In this case, core patterns had been made for the manufacture of a pump. The pump was in public use, but the patterns contained items of necessary taper and clearances, and some of the features of know-how that resulted from the experience in manufacture of the product. These items were not obvious in the examination of the pump itself, and were not in the public domain. The court upheld the legal interest in the trade secrets involved.

A similar, more recent holding was handed down in the case *Schreyer v. Casco Products Corp.*, 88 U.S.P.Q. 515, 90 U.S.P.Q. 271, about 1957, I would guess. In that case the court upheld the developer's interests in a complete set of drawings covering a steam iron, where this set of drawings had been delivered to Casco in order to consider the question of licensing and manufacture. After some negotiation, the matter fell through, and apparently copies of drawings were either made or the set used; but at any rate, production was entered into by Casco and suit was brought. The defense was made that these can be readily reverse-engineered—the drawings, that is—from the product. And the court held that that may be true, but that until you do that, you have no right in manufacturing the product; that the drawings represented substantial investment and interest by the inventor.

From a practical point of view, we simply must have ways to buy and sell technical information, and this is even more important—not less important—in the case of unpatentable items. Speaking for myself, and for George, I have little doubt that the court of appeals ruling in *Painton v. Bourns* will either settle this fact, or lead to further court rulings that do so; and this will be all to the good.

In the next few minutes, I'd like to carry forward George's thoughts to the decreasing expenditures of the government in the field of research, development and engineering.

Our experience in contracting with the government has shown that there is greater recognition currently over contractors' proprietary rights in technical data than had existed prior to 1965. This results from the government's recognition through the Armed Services Procurement Regulation of the distinction between privately developed data and data directly resulting from the performance of research, development and engineering under government contract. Thus, the

private investment during these lean years of government sponsorship, is reasonably assured of recognition; and I do mean that from a practical standpoint.

In any future contracting with the Department of Defense and other agencies such as NASA, we believe that the same in substance applies to patented inventions. I would submit that the trend of reduced expenditures in this field will be reversed within the not-too-distant future. This by reason of the increasing threat of Russian penetration in the Middle East as well as elsewhere in the world, and by reason of the Russian aggressive pursuit of leadership position in developing a tremendous buildup of tactical defensive and offensive weapons and systems. The response must be made. It's only a matter of time before the response is made, things being the way they are.

And I might also add that we really have faced such austere budget conditions in the past, both shortly after World War II, and then sometime in the late Fifties. At the risk of being dubbed as Pollyanna, I would like to refer to the fact that in my observation, our operations in this country in the social sphere as well as in the political seem to operate like a pendulum. You are always going, somehow or other, between extremes. And while we are at a low point from this standpoint, this too shall pass, and we'll find ourselves back in the area where expenditures for development and research will be increased, where the demand for engineers will grow, and where response will similarly grow. There may be some pains in the meantime, but I think it will all come out right in the end. We've managed up till now, and I think we will. Thank you, Mr. Chairman.

CHAIRMAN COLES: Thank you very much, Mr. Carter. That's a very interesting presentation, and certainly in terms of the intellectual property, your remarks pertaining to trade secrets are of extreme pertinence.

I think this perhaps refers to something that Dr. David was speaking about in the initial panel discussion, of the knowledge industry and products of knowledge, which comes over into intellectual property, and how you are able to protect this intellectual property.

Mr. Carter's talk is open for discussion and also the remarks of the earlier panelists. Would you identify yourself before you speak each time, please?



## GENERAL DISCUSSION

IRVING H. SIEGEL: Irving Siegel, on The PTC Research Institute staff. I wonder if Mr. Carter would direct himself briefly to the decision of *Lear v. Adkins*, 359 U.S. 653. I don't raise this point simply because we want to burden the discussion with more legal references. Rather, there is an important principle which I think represents an important new challenge, in accordance with the title of the session. This challenge is indicated, for example, in the ability of a manufacturer, who has already acknowledged the inventiveness of an inventor's contribution by paying him royalties for many years, suddenly to claim that there is no inventiveness in the achievement, and therefore to cease paying royalties.

I feel this notion strikes very deep into the heart of the concept of inventor rights embedded in the Constitution.

MR. CARTER: Yes. Of course that's directly involved in what we've been talking about. As a matter of fact, the *Lear v. Adkins* decision was a direct lead-into, and of course referenced in, the *Painton v. Bourns* case. The logic of the court in *Bourns* was based on the fact that the holding in *Lear v. Adkins*, as interpreted by the court, was to the effect that public policy demanded that patents which were invalid be wiped clean from the docket of patent holdings of the nation, and that this, of course, is based upon the philosophy—upon the recognition of the basic philosophy that the patent is an exception to the antimonopoly and free competition concepts of the nation.

Going from that step, or that basic premise, with which, I think, few of us will take direct issue, the court in *Bourns* then looked at the fact that the *Lear v. Adkins* decision permitted the cancellation of the—not the cancellation of the agreement—but rather, permitted the non-payment of the royalty which was due. And in looking at those two things, the court then realized in its own mind—jumping some steps along the way—it felt that its decision was impelled, by reason of the fact that if an inventor was to be placed in the position as in *Lear v. Adkins* of not receiving the royalty negotiated for while at the same time the licensee is able to operate under the patent, that then it would be logical in the minds of inventors and innovators not to license, not to patent, and to fall back on trade secrets as a defense and as a protective mechanism.

So the next step that the court took in *Bourns* was to say, "Well, we

can't have that. So we'll just force the issue and say that trade secrets just don't exist unless you've applied for patents." I don't think the court ever got to the point of saying what happens when the patent is applied for and it fails; and it doesn't issue, which then leaves it as an unpublished bit of information. Then what happens?

But I guess the court was not too concerned about such questions. It was just a gut reaction that I think resulted in the decision.

I feel that there is something to be said on both sides. Let me say from our own practical standpoint, when we write licenses in General Motors, and have done so long before *Lear v. Adkins*, we never provided that the licensee may not contest the validity of the patent. This was always possible, and we always looked to being able to do that where we were being licensed.

It just seems to me that a proper course in recognition of all of the interests involved in this big issue would be that we continue along the line that *Lear v. Adkins* has set down, which is that you shall not provide by contract or otherwise for the non-contesting of validity, merely because you're a licensee. Continue that, but at the same time, require that the licensee, when he does that, renounce the license so that he is no longer free to operate; and so leave the parties in the position they were before the license, which is that if you manufacture, you're subject to a suit for infringement, and let the chips fall where they may. It seems to me that's the only logical solution to that problem.

CHAIRMAN COLES: Yes, Ted.

THEODORE L. BOWES: I'm T. L. Bowes, Westinghouse, Pittsburgh. Sid, I heard you say that the patent laws were an exception to the antitrust laws. Now, there have been several speakers and several writers recently, who have pointed out that patents go back to the Constitution. The first patent act was in 1790. The Sherman Act didn't follow until a hundred years later.

Now, did you mean that the Sherman Act, for instance, provided by its terms or by implication that henceforth the patent law was considered an island within the sea of antitrust? Or that, really, there is a dividing line between the two, and patents have their place; but you shall not use patents as a means of violating the antitrust laws? Or something else?

MR. CARTER: Well, I think that you've raised a basic philosophical question there. I'm not so sure that—from a practical standpoint, again—I'm not going to answer your question directly, Ted. (Laughter.)

From a practical standpoint, I'm not sure that it really matters.

Certainly not in today's environment. This is good, law-journal subject matter, but not realistic, from a practical standpoint, it seems to me, what with the views taken by the Department of Justice and the decisions—those which are or can be pointed out by some as good decisions. And perhaps it can be argued that so many of these to which I allude as good decisions are in fact mixed, and here's where I fall short, because I'm not as academically grounded as my very good teacher, Professor Oppenheim, or George Frost, in the case law. But it seems to me that it's true that many of these so-called good decisions in the antitrust field involve issues in the so-called per se violations of the antitrust laws, and so have impacted and affected patents. Nonetheless, it seems to me that in today's environment, whether the chicken or the egg came first doesn't really matter. The patent is viewed as something which is a statutory grant and an instrument for exclusion, and as an instrument for exclusion it inherently means that it has a competitive impact and a control effect; and as such is therefore subject to scrutiny, at least from the standpoint of whether or not it is fulfilling its valid functions as an instrument of technological development and competition.

I myself feel that the antitrust law is to be viewed like a land mass surrounded by a water mass, and that there are boundaries; but like the land-water interrelationship, these boundaries shift from time to time, and bits of the land mass slip into the water, and the waves lap up onto the shore. And there are high tides and low tides and so on. And as a result, there is not a very clear interface, and these are the areas which make for the development of the law.

This is what the Department of Justice is looking for, cases in the shade areas with a bit of this per se violation taint, in order to come up with a decision which takes another step in the direction that the Justice Department is attempting to pursue. Professor Oppenheim.

S. CHESTERFIELD OPPENHEIM: Well, Sidney, it pains me to say that I cannot fully subscribe to what you said. (Laughter)

Mr. Chairman, is it proper for me to comment in reply?

CHAIRMAN COLES: By all means.

PROFESSOR OPPENHEIM: Since I am on record regarding patent license limitations in an article entitled "The Patent-Antitrust Spectrum of Patent and Know-How License Limitations" to be published in the next issue of the PTC Journal, *IDEA*, what I say here touches on several of the points treated fully in my article.

My basic concern is with the pronouncements of officials of the Department of Justice Antitrust Division on patent-antitrust issues. I

am not so much concerned with the corpus of judicial decisions on patent license limitations because I think that in general they are quite favorable to the patentee. The source of the present controversy comes from the Antitrust Division's challenge to certain well settled case law—including three Supreme Court decisions.

For example, the 1926 *General Electric* decision of the Supreme Court sustained a first-sale price restriction in a patent license. The 1938 *General Talking Picture* case sustained a field-of-use license restriction. And the 1947 *Transparent-Wrap* case upheld an assignment grant-back in a patent license.

The fundamental fallacy, in my view, is in the criteria announced by the Antitrust Division for testing the legality of patent license limitations. The head of the Division, Richard W. McLaren, announced the following criteria: Is the particular license provision justifiable as necessary for commercial exploitation of the patent rights? Second, are there less restrictive alternatives which are more promotive of competition?

Those are antitrust considerations which are being wrongly substituted for the patent policy criteria. If the Antitrust Division is able to prove what I call plus elements of antitrust violation beyond the lawful, exclusive rights of the patentee, then the Division would be on sound ground. The patent grant is a right to exclude others from making, using and selling the patented invention. The patentee may, of course, grant a license to practice the invention.

One glaring example of the Antitrust Division's erroneous criteria is the exclusive license situation. There isn't a glimmer in any court decision which has questioned the legality of an exclusive license granted at the unilateral option of the patentee. There may, of course, be very important reasons why the licensee will accept only an exclusive license. For example, he may not wish to undertake the development of a new product unless he gets an exclusive license. The patentee may not have the incentive or capital to market the patented device himself.

Tested by the Antitrust Division's criteria, the patentee would have to justify the exclusive license as being essential. He would have to show also that he does not have available to him less restrictive alternatives which are more promotive of competition. Again I say that those criteria are not relevant to patent policy, although they may be of some relevance to antitrust policy if the exclusive license is part of a scheme to restrain trade beyond the lawful patent rights. A patentee is not obligated to promote competition. Justice Douglas is certainly not soft

on patent rights and he explicitly said that the patent grant gives the patentee the right to be free from competition.

What are some of the plus antitrust elements to which I referred? A combination or conspiracy between two or more patentees or with their licensees; a tying clause which ties to the patented invention unpatented subject matter beyond the scope of the patented invention; resale price control imposed on one who purchases the patented article pursuant to an authorized first sale or an attempt to restrict such a purchaser from selecting his customers on resales. Those are genuine antitrust prohibitions.

The recent speeches of Antitrust Division officials for the first time formulate antitrust criteria for testing patent license limitations in a way that places antitrust policy above patent policy instead of an approach which seeks to accommodate one policy to the other. If the patentee stays within the area of his exclusive patent rights inherent in the grant, he should not be subject to purely antitrust tests. As Ted Bowes said this morning, the patent laws were on the books one hundred years before the Sherman Act. In 1918 the Supreme Court in the *Motion Picture Patents* case held that there is patent misuse when the patentee restricts trade by a tying clause outside the scope of the patent grant. The patent bar and antitrust counselors know that the antitrust plus elements I have mentioned expose the patentee to suits under the Sherman, Clayton and Federal Trade Commission Acts like any other owner of property rights.

When Thurman Arnold was head of the Antitrust Division, the patent-antitrust suits he instituted were mostly cases involving international cartels. Those were genuine illegal per se antitrust violations. The *General Electric* lamp and tungsten carbide cases and the *National Lead* case illustrate that category. But Thurman Arnold did not question the right of the patentee to exact a full reward so long as he does not step outside the circle of his exclusive patent rights. If you look at a report published in 1956 by the House Subcommittee dealing with patent-antitrust, you will find that it supported exclusive patent rights and contained nothing like the present Antitrust Division's criteria which confuse patent policy and antitrust policy in a way that creates unwarranted inherent conflicts. It is thus understandable why the patent bar is seeking Congressional amendments to counteract the conflicting views of the Antitrust Division.

In the area of trade secrets, my article shows at length that the Antitrust Division is on sound ground. Mr. McLaren has stated that he will use a Rule of Reason approach to trade secret and know-how

license limitations which are ancillary to the lawful primary purpose of the agreement. Judge Friendly's recent opinion in *Painton v. Bourns* in the Second Circuit differs from the fallacious dictum of Justice Black in his dissenting opinion in *Lear v. Adkins*. That dictum would extend the scope of federal preemption on the false reasoning that patent policy precludes licensing of trade secrets for royalty payments. My article discusses that issue in detail.

CHAIRMAN COLES: Thank you very much.

GEORGE D. CARY: Mr. Chairman? George Cary, Washington, D.C. I'm not going to ask for equal time to discuss this problem, as my good friend Professor Oppenheim just did with his usual scholarly eloquence. But I would feel that it might be important to note, since we're on the subject of new challenges to intellectual property, that the subject of copyrights gets in here, in the picture, itself.

Again, as I say, I'm not going to go into this extensively, but briefly, the new technology has been quite a problem with copyright proprietors in recent years. I have only to mention the Xerox machine, for example, as one source of a great deal of headaches with authors and publishers. The computer has been another source. There's much talk of storage of data, copyrighted text material, for example, and output either in the printed form or by means of a television screen in connection with the use of this in educational fields, teaching systems, library interconnections, and the like.

Another challenge is the problem of cable television, which the Supreme Court in a recent case indicated does not violate the performance rights of the copyright law when it broadcasts or transmits, rather, a copyrighted program, which it takes off the air from a commercial television station.

Then we are now beginning to see an area in the field of satellite broadcasting, which does have international implications. All of these problems could be the subject of an extensive discussion itself; but I couldn't rest easy if I didn't at least let the record show that there are challenges to intellectual property in another area—that is, the field of copyrights.

CHAIRMAN COLES: Yes sir.

ROBERT M. JANOWIAK: Janowiak, with IIT Research Institute. I'm particularly also interested in another challenge, which is developing and has been handled thus far mainly on a contractual basis. This is the whole burgeoning software industry in the computer field. I was wondering if Mr. Carter or any of the other participants would care to venture any new challenges or directions they might see for this multi-

billion dollar industry, such as protection rights, directions, future.

CHAIRMAN COLES: I think this is not unrelated to what Mr. Cary was speaking of earlier. Mr. Carter?

MR. CARTER: The problem is a serious one. You know, the copyright bill in Congress has been pending quite a number of years, and it just hasn't made any progress, for the simple reason that it's just these areas that are bogging it down. Special study committees have been set up, and hearings, and I guess there will be more of them. And the problems between the theory of whether you assert the control at the publishing—originating level—or whether you assert the control at the user level, is a serious problem; there's much conflict.

And the picture is so muddy, the problems relating to user in terms of the automatic relay and retrieval systems—accessible by telephone and telegraph and what have you—so that anybody and everybody hooked into the system can obtain the information—all of these, and xerography, as you point out, are serious problems. It doesn't seem at this stage that there is any clear trend. It just seems like being at the heart, or in the eye, of the hurricane—all is quiet, but all around it there's turmoil, and there's no real direction.

JOSEPH M. LIGHTMAN: Joe Lightman, Research Associate with the Institute; International Economist with the Department of Commerce.

Mr. Carter, where a licensing contract has been concluded in the U.S. for trade secrets, or unpatented technology, if the licensee decides to make unauthorized use of the technology or otherwise do something with that technology that's not provided for in the contract, is that contract enforceable as such against that licensee in the light of the court decisions you mentioned? Also, what has been your recent experience, in light of these U.S. court decisions with respect to enforcement of licensing contracts for trade secrets and unpatented technology with foreign firms, particularly those in Western Europe and Japan?

MR. CARTER: First, with regard to the possibility of a contract providing for the use of trade secrets, and the use then being outside of the license use and provided-for use, it seems to me, with the support now of the overruling of the *Bourns* case, I know of no cases which would preclude the assertion of a suit to restrain the use, or to collect damages for the use which is outside of the limits of the license. I think that there are other questions which would be brought to bear in any such action, and this is where the parties can themselves, in effect, make the law, which could result in more and more of this land mass dropping off into the water and disappearing into the waves—the land mass being the protecting and protected area.

They would undoubtedly look to the effect of the relationship, the effect of the desired restriction, other aspects of the contract and agreement, which could get into the true antitrust violation situations.

At any rate, we learn hard. And therefore I think that it's inevitable that a suit can be brought; as a matter of fact, the *Westinghouse* case, licensing in Japan, is one of these situations that the Department of Justice is looking toward as a stepping stone to achieving its desired position as announced by the policy makers of the Department of Justice, McLaren and others.

But as I say, from the pure point, if you can write a pure agreement, of the use of technical know-how, the question always comes up, "Is there a time limit? How long does this express or implied restriction go on? Does it go on in perpetuity?" A patent will expire in 17 years, or whatever, but know-how—inherently there are no automatic limits. So that is another real area of question. What do you do with time? How do you provide for that in the agreement?

All these things would be considered, I think; but to answer your question purely and simply, yes, I think an action can be brought.

MR. LIGHTMAN: The right of contractual enforcement seems to be about the only protection left in this context.

MR. CARTER: Well, that is a real protection from the standpoint of operation in industry. These are real values, and I might say that maybe it's surprising to some people, but General Motors Corporation on balance is a receiver of technology. And that isn't to say that we don't have a mass of our own technology and know-how and trade secrets, which we have, use, and make available to others on a licensing basis. We're careful about these things of time, et cetera, when we write such agreements.

Going over to your next question, yes, I think that the licensing of technology overseas is a real point, and it's of real value, and it certainly has been one which has been valuable up to now. The PTC in its past studies has shed real light on that; and I think, on balance, technology has been flowing out of the country in licensing. It's probably time that we recognize that there is something on the other side too, and maybe lose a little of our arrogance in that regard and seek out that which we can really use. I think there's more of that taking place now, with Japan, for example, where there are other reasons for doing it, of course. But there are these new Japanese interrelationships with 30 percent and 40 percent part ownerships and so on, whatever MITI will permit and allow. So there are now opening up channels for technology flow which didn't exist before and which weren't sought out before.



And in view of reduced government-sponsored research and development programming, it seems to me that this is a fertile area for applying our technology, for getting a return on our investment in direct dollars, and also getting a return on our investment in terms of the technology flowing back to us.

MR. LIGHTMAN: It's my understanding that some Western European laws, such as in the U.K., France and Germany, offer a substantial degree of statutory protection for trade secrets and proprietary know-how.

MR. CARTER: Well, we do know this. Our experience tells us that—and maybe General Motors is the exception—we tend to look on technical information and know-how with a lesser degree of seriousness than the foreign counterparts and companies. It seems to me that in all of their general relationships, social and otherwise, secrecy is a great thing. It's long been recognized as one of the standard procedures, diplomatically and otherwise. And these great conspiracies and the cartels and what have you—all of this is a part and parcel of the same thing.

We, as I say, don't think we have tended in that direction. We've been more direct, more straightforward; we tend to be more naive in approaching our licensing relationships with foreigners, and that's something we have to be careful of, in that techniques are different from what we are used to. We tend to be sensitive in that area and try to correct it, knowing our faults.

CHAIRMAN COLES: Any further comments or questions at this time?

DR. HARTMAN: I'd like to ask a fairly naive question, for someone who doesn't know about patent law.

Some years ago I noticed some statistics which indicated that the number of patent applications in the United States per scientist and engineer, was tending downwards, while simultaneously the number of scientific and technical publications per scientist and engineer was increasing. Now, is this trend in fact continuing; and, second, in view of the rapid new product development and obsolescence that we see as a result of research and development, is the patent process in fact becoming somewhat less productive as time goes on, as a useful mechanism, in contrast to rapid exploitation and so forth?

MR. CARTER: Well, I don't know the relative relationship of numbers that you allude to, but I've always suspected this idea of measuring by numbers; and, for whatever it's worth, it's true that U.S. patent applications are filed not only by domestic, but also by foreign originators. Certainly the number of applications have been on the up-trend in this

country continually, and the number of patents issued have been on the up-trend continually, and both seem to have no limit in growth.

As necessary, the process of examination accommodates to the handling of larger numbers of applications, as best it can, without getting completely deluged and drowned in the mass. But it certainly seems to me that our concept of the patent as an instrument within the law, our concept of protection, going back to the common law, of that which a man creates remaining his, the common law copyright, the trade secret, et cetera,—it seems to me that all of this is really not diminishing. I also subscribe to Professor Oppenheim's very fine analysis. There are threats which always have to be guarded against, as Professor Oppenheim stated so beautifully.

I think that the system is viable today. I think that it's alive and growing; it's used, and I think the Congress recognizes it, and I think the Department of Defense has gotten to recognize it, albeit grudgingly because of its own immediate purposes and drives. No, I think it's a real system. I think it's here to stay.

As a matter of fact, the trends are all the other way, because, taking our opposite numbers, like Russia, for example, they have tended to adopt our ways of protecting the innovator and creating incentive, et cetera.

DIRECTOR HARRIS: May I add a footnote to that?

MR. CARTER: Yes, sir.

DIRECTOR HARRIS: Sid, we did some studies on that very subject at the Institute. Among these studies, one by Dr. Sanders published several reports on the upgrading of patented inventions here and abroad. The conclusions that he reached—this report was published in *IDEA*—that the patent examination is getting stricter, that inventions are getting more complex, and consequently—and these are only some of the reasons he cites—you find that fewer patents are being issued, the trend is in that direction, relatively speaking.

I would suggest that those who might be interested in pursuing this subject—and this was, I believe, the thrust of your question, Dr. Hartman, wasn't it?—should check *IDEA*. In Dr. Sanders' article on upgrading of patented inventions here and abroad, you will find some very informative data.

CHAIRMAN COLES: Thank you. We're going to have to conclude after one more comment. And I want to have Henry David have a chance to make a comment, because he can't be back with us this afternoon, and this is the only chance we'll have to hear some of the things which have come to him from this more recent discussion.

DR. DAVID: In connection with this last discussion, I am impressed by my ignorance, and will use it as a springboard to make a brief statement about the word "intellectual." It struck me, as I listened to Mr. Carter's informative presentation and the subsequent discussion, that the most powerful intellectual ideas or instruments are not expressed in property right terms.

In the case of those notions, those conceptions, which seem to have shaped and reshaped our picture of ourselves and our picture of the world in which we live, property right dimensions seem to be nonexistent or minimal. I just wondered how, for example, Mr. Lenin, who invented an effective operational model for bringing about a revolution, could express its property rights aspect in terms other than copyright. (Laughter.) Or, for example, the difference between the powerful effects on our view of ourselves and our deepest motives, for which we're indebted to Freud. The distance between these effects and Mr. Freud's income as a result of his publications is measurable in light years.

The problem of how one translates the capacities inherent in intellectual and other inventions into property rights upon which a return is claimed I find oppressively difficult. It just strikes me that looking ahead into the future, we will have to say that some very powerful intellectual tools, considered from the perspective of the public good, will not be amenable to treatment in property right terms. Thus, it will be feasible to patent machines which register environmental changes but wholly infeasible to patent the ideas which would give man the basis for regulating his relationship to the biosphere. We are already troubled by the variety of conflicts that arise because the notion of protecting property rights is incompatible with notions about the general welfare or the public good. And there situations will increase, not diminish.

I offer those as speculative thoughts, not to disturb you, but to suggest that the future may hold these issues in it. Thank you.

DIRECTOR HARRIS: I take Dr. David's statement simply to mean that many fundamental or basic ideas which affect human affairs deeply lie outside the realm of property—and that he prefers that the situation should continue.

The notion of protecting great ideas by some kind of incentive system—similar to the intellectual property systems now in effect—has been suggested many times in one form or another over the years. One of the basic problems of protecting and encouraging the products of invention and authorship is the intangible nature of these "proper-

ties." Also, the subjects for protection are disparate in nature, i.e. artistic creations as compared with useful machines. Another problem is the danger of monopolizing the laws of nature or the thoughts of men. A further difficulty is to provide a fair measure of payment to the innovator for his contribution.

To meet these problems, the law developed to take account of the particular factual situation and to provide a remedy within feasible boundaries. The diversity of these "properties" has evolved different substantive laws and remedies to accommodate the unique characteristics of the intellectual property involved. At common law and subsequently by legislation, these legal doctrines also sought to harmonize private interests with the all-important public interest. To do all this, the law must first specifically identify what it is to protect. In the intangible property field it may cover a machine, a process of manufacture, a composition of matter, or a literary or artistic creation. There is also the law of unfair trade to insure that market rivalry is "fair." Other legal concepts, such as those relating to contract may also be involved.

After identity has been accomplished, the emphasis on application in some tangible form—whether technological or artistic—is intended to provide a yardstick for determining the interest of the inventor or author as well as the public interest. This is not rigidity, but rather feasible flexibility, subject to expansion or contraction based on social, economic, legal, political and other value judgments. Patents, trademarks, trade secrets, et cetera, may be utilized to protect at least a portion of the great idea—that part amenable to legal protection. Since incentives are needed to provide inventive contributions that would enhance the quality of life and the leisure and welfare of our citizens, the intellectual property systems must provide their "fuel to the fire" even here.

One additional point: Certain forms of intellectual property are used for other than financial remuneration. For example, there are those who use the copyright solely to protect the integrity of their contributions.

If some feasible means were devised to protect great ideas per se without the necessity of reducing them to some form of application, I believe it would receive very favorable consideration, indeed.

CHAIRMAN COLES: I know there are other people who would like to respond to this, but I think this is a good note on which to adjourn for cocktails and lunch.

Room three, next door.

## Luncheon Session

O. S. COLCLOUGH

My name is Colclough; I am Chairman of the Advisory Council of The PTC Research Institute. It's my privilege to preside at this luncheon, and I'm asking if he'll come stand beside me—Mr. Billy M. Horton. Needless to say, this is one of our memorable occasions. Billy M. Horton is the Technical Director of the Harry Diamond Laboratories of the Department of the Army. I could talk about him a great deal—originating in Texas, receiving his Bachelor's Degree from the University of Texas, later his master's degree from the University of Maryland. I think because of the occasion that this is, however, that I would rather say just a few words about something else.

Mr. Horton is the inventor of a system of fluidics—tough word to say—or fluetrics, if you prefer to say it that way. This system uses fluids for gases in lieu of conventional electrical current, having no moving parts and no conventional elements to wear out or change values. Basically, it is an amplifier used as a control mechanism. Examples of its application have been in the laboratory construction of digital and analog computers, an entire family of medical life-saving and/or life-supporting devices in which his inventions have been used by those who developed the system—such as the army artificial heart pump, the army respirator and related medical devices, and the military field of fuzes in fuzing systems.

He has received other awards before this one today—the Arnold O. Beckman Award by the Instrument Society of America in 1960; the U.S. Army Research and Development Award in 1965; John Scott Award in 1966—an international award received by people such as Madame Curie; Department of Defense Distinguished Civilian Service Award in 1967. The possessor, the owner of what's being discussed today has outstanding patented inventions.

I'm sure that everyone who has accepted the invitation to be here today at The PTC Research Institute's Conference on a broad basis, and with all my respect and admiration for our Research Staff and our office secretaries—the three ladies down there—agrees that it is a great privi-

lege and honor to present to him The PTC Research Institute of The George Washington University's Inventor of the Year Award—Billy M. Horton, for the year 1970, in recognition of the dedication to his inventive art, and for outstanding executive achievement under the United States patent system. Signed by Lloyd Elliott, President of The George Washington University, L. James Harris, the distinguished Director of The PTC Research Institute, and myself, as Chairman of the Advisory Council. I think you all join me in congratulating and honoring this gentleman. (General applause)

**BILLY M. HORTON**

I feel highly honored that The PTC Research Institute has seen fit to confer this Award upon me. To be permitted to join a list of inventors for whom I have great admiration is somewhat humbling. I hope that such innovations as I have been able to make in the past, and I hope to continue to make, will justify this recognition, this honor, which I deeply appreciate. This is particularly satisfying to me because in my present position a great deal of my energy is required in my working together with other groups—larger groups. But, as Jack Rabinow says, the best thing you can do for any inventor is expose him to problems. Jack is one of those for whom I have great admiration.

Now, we have plenty of problems in today's society, and many of them require inventions. Unfortunately, these initiatives, or these inventions, are not entirely in the physical science field, which is the area in which I do most of my thinking, and some of them are quite difficult to sell. But it does turn out that there are plenty of problems in physics, in engineering and the scientific application area. Somehow or other I feel it appropriate to mention some of the areas that have caught my fancy in the past few years, and a little bit about the impetus for my interest.

I'm currently working part-time, mostly in my basement, on a high pressure machine which I think will make it possible to achieve extremely high pressures over larger volumes than have previously been achieved. I'm also working on a ratcheting open-end wrench, which is self-adjusting. That was motivated by skinned knuckles, I think, (laugh-

ter) with a little impetus given by the need for a self-adjusting wrench which can accommodate both American and metric sizes, all within one wrench. The motivator for the next one was the problem which afflicted a friend of mine. He has homonymous hemianopsia—that's a long word for being unable to see in one-half of the total visual field even with both eyes.

Then the most recent thing that's caught my fancy is a foldable structure, which oddly enough, was inspired by seeing some of the devastation in Corpus Christi caused by the hurricane they had last summer. I observed that some of the oil tanks which were crushed were folded in such a way as to increase their rigidity. I think I've been able to use this and make a light-weight, inexpensive structure.

One more thing—I'd just like to say that I'd rather be Inventor of the Year than President. (Laughter) (Applause)

ADMIRAL COLCLOUGH: Thank you so much, Mr. Horton. Now, ladies and gentlemen, it is my privilege to introduce a distinguished gentleman with a wide range of interests in matters that concern all of us, as is evidenced by our PTC Research Institute Conference today, and evidenced by its publications.

I don't want to be accused of bias, but I just have to refer to the fact that he has considerable past relationships with the United States Navy. He received his Bachelor's Degree from Dartmouth and he's just given up, after nine years, I think it is, membership on the Board of Overseers of Dartmouth. He received his Master of Arts from Cambridge University, a Ph.D. in physics from Yale University. He served as Assistant Secretary of the Navy for Research and Development, which is right down our alley. And because of the time element, without further ado, it is my privilege to present to you The Honorable James R. Wakelin, Jr., the Assistant Secretary of Commerce for Science and Technology. Mr. Secretary.

## **Programs in Department of Commerce to Enhance Technology and Facilitate Its Transfer**

**JAMES H. WAKELIN**

I'd like to visit with you for a few minutes on some problems of common interest, and for which I have certain responsibilities in the Department of Commerce. These fall within the jurisdictions of the National Bureau of Standards, the Patent Office, the National Technical Information Service, the Office of Telecommunications, the Office of Environmental Affairs, and the Office of Product Standards.

Now, the thrust of our programs in the Department of Commerce, as I see it, is to try to exploit the usefulness of science and technology particularly with respect to how it affects our economy. There are a number of areas in which we have a great interest, and in which we are doing a great deal of work. One of the most important is trying to determine what programs should be started in Commerce to enhance technology and to facilitate its transfer, not only in our country, but between both developed and developing-nations. As implied by two units I named earlier, I also have Department-wide responsibility for environmental affairs—the balance between technology and ecology—and the whole range of domestic and international product standards.



We're very fortunate to have a Commerce Technical Advisory Board, whose members are from industry, academia, science, and general interests. There are about 15 on the Board now. These men advise me and the Secretary with respect to the course of science and technology in the Department, and particularly the application of technology to increase our productivity.

These are gentlemen who have been referred to as my argumentative College of Cardinals, because they are not bashful about telling me when I'm wrong. To give you an example of the issues with which the Department deals, take the conversion of our country to the international metric system. As you probably know, right now we're about 10 percent converted, so to speak, in certain areas. So-called conversion to the metric system would not mean 100 percent conversion, but instead would mean that the metric system would be the predominant measuring system.

Britain is about half-way through with her program of conversion to metric. We're becoming now an island on the old British system of weights and measures, and I think the general feeling is that we should seriously consider going metric, probably in about ten years. I can't anticipate what the Secretary is going to submit with respect to his recommendations when the report goes to the Congress, probably within the next couple of weeks, but I would suspect that we ought to increase the tendency to use the metric system.

If that is his recommendation, I think this will have a good effect on our international trade in balance of payments and things that we export abroad.

Now, with regard to technology enhancement or utilization, there's been a lot of discussion, as you know, about how one might estimate the importance of technology to our business health, both nationally and internationally. There are many issues which bear on productivity, including requirements for the cost of labor, certain restrictions, anti-trust among them, labor practices, and, in essence, what is being asked of technology. Internationally, technology is being asked to take up that slack between our cost of labor and another country's cost of labor. If the Japanese, for example, have roughly half the cost of our labor, then our technology has to be twice as effective, forgetting materials.

We have had a favorable balance of trade in most of the areas which we call "technology intensive." These include aircraft, computing equipment, and some of the solid state and electronic equipment. We've had a very high negative balance of payments—balance of trade—in the so-called "labor intensive" areas.

A technology intensive product area in which we do have a high negative balance of trade is the automotive industry. Another is the telecommunications field. And certainly, in the latter, it's because we Americans do not always go abroad as a team, government along with the industrial and commercial people. When our private sector people go abroad, they meet government representatives and industrial people together, acting as a team. This is another indication of the need for a better companionship between government and industry in this country as well as abroad.

In technology assessment, which lies at the base of what we might do in technology, the U.S. has a great capability in our patent system to assist in assessing technology of the United States in certain trade areas compared to equivalent areas abroad. I'm sure that Mr. Schuyler, the Commissioner, is going to take an ever deeper interest in technology assessment as his program of automation in the Patent Office proceeds.

Our main job in Commerce Science and Technology is to try to find out what technology offers by way of productivity—how we can increase productivity on a national scale in technology intensive products in order to keep ahead, hopefully giving us a positive balance of trade in our international relations.

Commerce Technical Advisory Board is considering studies which it might undertake which would be of value in planning our technology policies and programs. A CTAB report of two years ago on transfer of technology among developed countries was quite useful. Now CTAB is preparing to study the transfer of technology to developing countries.

The prospect of our country's keeping a favorable balance of trade in the order of \$1.7 billion to \$2 billion, when you add up the pluses and take out the minuses, is going to depend heavily on technology. The President is most anxious to transfer technology to developing countries and also to assist us in enhancing our technological ability in this country. It's going to be a tough job. I'm not sure what kind of positive program we should adopt but I am sure that we should do something much more active than we have had to date.

The gap is narrowing between the positive export balance and the negative import balance. This, of course, is fundamental and lies at the stake of our standard of living.

ADMIRAL COLCLOUGH: Thank you, Mr. Secretary. I'm sure you've revived and activated the minds of all of us, mentioning some of the

problems we face in the future. The PTC Research Institute hopes and, we believe, it can contribute to solving some of them.

Shall I just say, "Stand adjourned"? Next door, all hands.

## GENERAL DISCUSSION

CHAIRMAN COLES: Gentlemen, Mr. Robert Chapman is going to have to leave a little later, but he has a point he made in private to Henry David, and he would like to have a chance to make that point to the group.

ROBERT B. CHAPMAN: I appreciate the Chairman giving me this opportunity. I would prefer to stay here, but let's say I'm just borrowing two minutes from whatever discussion I might have gotten into later.

I'd like to emphasize the statement that Dr. David made at the beginning that "we must manage our technology better" and that "we've devoted too much of our GNP to defense and consumer products." It's very profound and offers a lot to think about. Later on, he made the statement that we have a big problem in converting our technology, which has been used in the closed system, to use in an open system. And you realize the difference—a closed system being a contract system such as the DOD system, and an open system being a system where you try to get the whole society to solve urbanology or transportation or whatever it may be. And I would also hope that you gentlemen are aware of the J curve and what it portends—and don't try to tell me that it doesn't portend anything because the President is talking to us every day about what last month's GNP statistics portend.

The J curve, which results if you plot man's progress, shows that we only have about 20 years to solve these major problems. I would like to say in response to George Summers that I'm not so much concerned with solving the human cancer problem. I'm not at all sure that it's humane to carry people on physically the way we're doing now when their mental powers and their ability to live a whole life goes down. I am very concerned that we solve our social cancer.

We are far from solving our social cancer which is increasingly putting people outside the system who can't cope or have no useful

purpose—no way of exchanging their labor for an income other than welfare or a guaranteed income. We've now created a new deprived class, and this new deprived class I would like to point out has been understated. The total number of people that were let out of the defense and space technology industries from the summer of 1969 to the coming June is three million. The total number of engineers dislocated is not 100,000. That may be the number walking the streets, but it's closer to 450,000 improperly employed.

Now, these are not insignificant problems. These are not problems that you can shrug off lightly. Do you realize that the total engineering work force is around 900,000. So we dislocated one-half of it in a one-half year period. The total work force of the United States is 88 million and we dislocated over 3-1/2 percent of it.

I personally have done a great deal about this privately, and I have made it known to the President's economic advisors that I personally do not think that the society can recover from this reduction in force. We face a very bad 1971. We do not face an increasing '71. It is not growing right now.

I would point out as my last statement—what social responsibility do we have as leaders for these people who have been dislocated and have been rejected? What kind of an immoral act is it for us to have in 1958 and 1959 and 1960 persuaded hundreds of thousands of young men to become engineers and scientists and go to the expense in money and time of becoming technically equipped and then in 1969, overnight, with no announcement or no plan whatsoever, to reject them?

And I will point out that there are three great social losses. In the first place we are not getting the value out of those people's capabilities. They aren't being used for anything. They are not being used for defense or space or urban technology or biomedology or whatever it may be. The second problem is that these people were prize wage earners. They were not only engineers and scientists. They were technicians—highly skilled, blue-collar workers, et cetera, et cetera. The money for social purposes was coming from them. We have not yet found what the impact is going to be on the federal income by the fact that we took 3-1/2 percent of the most affluent part of the society and put it out of business.

The third point, gentlemen, when you talk about turning back to technology programs, four or five years from now, is that our young people have seen this lesson, and we are going to have a great deal of difficulty persuading our young people to make the same mistake of becoming engineers and scientists. Now, we have a very serious social

problem, and I hope you consider it in your discussion period later on.

CHAIRMAN COLES: Thank you very much, Mr. Chapman. That's a very good point and very interesting point. It will give us all much cause for thought.

We'll go on now into our afternoon program; and our first speaker is Richard E. Day. He is on the research staff of The PTC Research Institute; a member of the National Conference of Commissioners on Uniform State Laws; University of Pennsylvania, Wharton, Bachelor of Science in Economics; University of Michigan Law School, J. D. with distinction; has been with two law firms; taught at the University of North Carolina Law School; he is now Professor at the Ohio State University Law School since 1964.

Professor Day is going to speak on Antitrust and Competition Policy in the Research and Development Setting.

## Antitrust and Competition Policy in New R&D Setting

RICHARD E. DAY

I might say that I came in a little late this morning—in the middle, in fact, of Mr. Carter's well-thought-out, well-prepared paper—and I somehow had the feeling that I was in the wrong place at the wrong time and doing the wrong thing. In my conversation with Lou Harris I was told that this was going to be a panel discussion, and that he would permit me to have a few minutes—not more than 15—to make a few opening remarks.

And then, when Mr. Carter finished, my old friend, professor and mentor in antitrust law, Professor Oppenheim, stood up and extemporaneously gave my speech, only much better than I had prepared it.

About that time I was contemplating whether to feign sickness or whether I was actually sick perhaps. (Laughter)

I tried to figure out a way that I could get back to my room, and during the lunch hour, write a speech that would come up with Mr. Carter's speech, and somehow perk it up so that I could do as well as Professor Oppenheim did off-the-cuff. Finally, I decided it was no use and I came back just in time to hear the dinner speeches, and I'm glad I did.

Well, I guess from this you can tell at least that Professor Oppenheim and I are in agreement, or, more properly, that I agree with him. That may not be too surprising since he was my teacher and I have always had a great deal of respect for his views on antitrust.

I might also add that my feelings on this matter—my support for the patent law as well as the antitrust law—is not that I'm anti antitrust. I do believe that there is a trend now in the current enforcement policies and some of the statements that I have heard and read from the Department of Justice and the Federal Trade Commission, and of course, we ever have to worry about private litigants.

As far as the intrusion of antitrust on sound patent law principles, I agree with the analogy that Mr. Carter referred to this morning. I thought it was very apt, maybe more apt than he intended it, that patent law is like an island in a sea of antitrust. The problem that I see now is the possibility of this great sea of antitrust eroding the patent law to the point that it may become virtually nonexistent some day. Maybe that's an alarmist kind of a viewpoint. Down deep in my heart I really don't believe that's going to happen, but I think that something is going to have to be done to prevent it from happening. If the antitrust insipieny test continues to be expanded into patent law, I would say that there is at least a possibility, if not a real probability, that this could very well come close to being a reality.

Professor Oppenheim mentioned the Rule of Reason as espoused by Mr. McLaren and by his predecessor, Professor Turner. Perhaps Mr. McLaren, Professors Turner, Oppenheim and I would agree that the Rule of Reason is the basic antitrust policy as, I think, best put by Judge Taft in *Addison Pipe* and later by Justice White in *Standard Oil* and its progeny. The only problem is that we have to define our terms—what do you mean by the Rule of Reason? It is at this point that I depart from views of Professor Turner and Mr. McLaren. Mr. McLaren's statement of the Rule of Reason, as applied to patent licensing, is as follows:

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?

And he concludes,

Where the answer to the first question is no, and to the second is yes, we will consider bringing a case challenging the restriction involved.

Now, this is not a new idea, and it's not limited to patent licensing. This is an interpretation of the Rule of Reason which has been advocated in antitrust by Professor Turner and others for some time. I disagree with it there, too. I think that this is an improper interpretation of the Rule of Reason in antitrust, as well as patent law.

I would like to go one step further, as Professor Oppenheim did this morning, and, again, point out—and I think this is not insignificant—the Constitution provides for the Congress to pass a law for promotion of inventions. There is nothing in the Constitution about antitrust. The first Congress did pass a patent law, predating the first antitrust law by 100 years. I don't think that the Congress meant by any means to repeal the patent law by passing the Sherman Act. It is worth noting that the Clayton Act Section 3 is the only antitrust law that specifically refers to patents.

Therefore, I believe that it is reasonable to conclude that we have two viable public policies which are not in conflict, or should not be in conflict if properly interpreted. I think that we have room for antitrust laws as a general rule and I think we also have room for a specific area of promoting the useful arts in the patent law. And I don't see why one has to eat up the other.

I think that it is important to distinguish between what another Day—Rufus Day—has called “primary” patent rights and “secondary” patent rights. The patentee's right to exclude others from making, using or selling his patented invention is a “primary” right. And I think that anything that involves nothing more than this right to exclude is, in fact, not subject to the Rule of Reason. I think this is one place where we get off the track. Just as “non-ancillary” restraints of trade, or “naked” covenants not to compete are per se illegal under the antitrust laws, this patent right to exclude is a long standing public policy, promoting the public interest and should be per se legal. I think that it's wrong to apply an antitrust test—even the Rule of Reason—to conduct that relates solely to this primary right of exclusion.

Now, the catchy part is that when you go beyond these primary patent rights to “secondary rights,” or perhaps I'd call them “ancillary restraints,” then you get into the Rule of Reason area. I think the best example of overstepping the Rule of Reason—the one that everyone knows—is the *Motion Picture Patents* case, where the patent was used as a lever to extend the patent “monopoly” to another area. When you get into ancillary restraints you get into a question of the application of the Rule of Reason. The question then is: are these ancillary restric-



tions reasonably necessary to effectuate the lawful main purpose of securing to the patentee the benefits of his patent.

To sum up then, when we talk about the basic rights of exclusion, for example the right to assign your patent, I think that the assignment should be at least presumptively lawful. By contrast, in the assignment and licensing areas, for example, the McLaren Rule of Reason test would raise such questions as : if you license one do you have to license others? If you license one for one field of use do you have to license all others in that same, or other, fields of use? If you license at one price do you have to license—the Robinson-Patman Act philosophy—to everybody on equal terms?

These matters seem to me to be directly within this basic right to assign or license which, at least presumptively, should be lawful. And it's only when you impose restrictions on the assignees or licensees, such as resale price-fixing, tying, or covenants not to compete, that you should properly come within the antitrust question of whether or not the practice is reasonably ancillary to effectuate the purpose of the patent law to give the patentee the full benefit of his patent. I don't want to be misinterpreted here. This is not to say that by assigning or licensing a patent, or acquiring a patent, you cannot be guilty of violating the antitrust laws. Obviously, a patent may be used as an instrument in an overall plan, or a conspiracy or combination in restraint of trade. In the hard-core antitrust cases that Professor Oppenheim referred to this morning, the antitrust laws should apply with full force. But when I speak of these primary rights as presumptively legal I mean that when all you have is a simple licensing arrangement or assignment, et cetera, it should be lawful, at least presumptively.

Now, some of the cases were talked about this morning and I'll save the actual cases for the questions since I was instructed that the direction that this panel would take would be determined by your questions from the floor. And perhaps I should just leave it off at that as far as my general statement. I would just like to point out that as far as the topic says, "Antitrust and Competition Policy in the R&D Setting," at the University we are very much concerned with matters of antitrust application to patent law and research and development. In fact, what has happened, and the direction that the law takes concerning assignments and licensing of patents probably affects us—people like us—in the research end of it more than it would the business inventor. As I see it, the inventor who is in the business of producing what he invents isn't going to be hurt as much by restrictions on his licensing ability, and the public is not going to suffer as much in that

case as in the case of the University or private research foundation, because the latter normally are not in the business of developing the market for the inventions on which they secure patents. Instead, they have to rely on their licensees or assignees to develop the market. In determining whether antitrust limitations will hurt the incentive to invent, the effect on the development of the patent commercially cannot be ignored. I don't think that these are two separate, mutually exclusive considerations. After all, if the noncommercial inventor has no way to commercially exploit his patents, he would have less incentive to invent. So I think the two go hand in hand on this.

Well, I've used more than my time, but at least these are some general thoughts that I have.

## GENERAL DISCUSSION

CHAIRMAN COLES: This presentation is now open for discussion. I think we have Mr. Carter who is here and General Hanson who you'll hear later as members of our panel.

Mr. Carter, do you have any comments on this?

MR. CARTER: Well, I was wondering as Dick was talking about this concept of antitrust as it relates to patents. You always get to talking about the intent in the antimonopoly policy and about the free competitive purposes of our system. And then at the same time you turn around—I'm referring to the government now—and in implementing its government contract operations will adopt practices and procedures which narrow the direct right of the patent grant to exclude others. For example, the Department of Defense regulations, and now the proposed Department of Transportation regulations, include the concept of compulsory licensing under inventions to which the government gets a license, where it is judged in the interest of the public health, safety and welfare.

Here is an area where, it seems to me, there is no question of antitrust or any other statutory philosophy being in conflict with the patent law and its purposes. Here is an area where the government steps in and erodes a part of the exclusivity of the patent grant simply on the broad basis of public health, safety and welfare, however this

might be interpreted, which interpretation might also include antitrust applications.

Now, how would you feel about that, Dick? Do you feel that this is a Rule of Reason type of approach? The taking of this right was argued by industry when negotiating such regulations, but compulsory licensing was adopted and it's been used in patent rights clauses for several years now since 1964, and no real problems have arisen out of it as far as I'm aware.

Do you feel that the adoption of this right is a proper application of the Rule of Reason?

PROFESSOR DAY: I'm not sure whether I understand you—the particular situation you're talking about. I can visualize several possibilities. One is where the government is supporting research. I think then they would have the right, as anybody who hires an employee to do research does, to determine the result of the patent issue—what should happen with it. If a particular agency of the government wants to support a particular kind of research, the fact that it's paying the bill, I think, gives it the right to determine whether it wants to license generally, or what rights, if any, the inventor should have. I think there may be an employee/employer relationship to take care of some of those situations to which you refer. I also think you're referring to such matters as the provision in the Environmental Protection Act which would require compulsory licensing where, in the public health or safety area, a patentee's invention is crucial to the public health or safety. For example, I suppose that if General Motors did invent an efficient emission control device for automobiles, and it was the only one that had it, and it then became a matter of protecting the public, I think that under extreme circumstances at least, that provision would provide for compulsory licensing.

But there you have another public policy, and although I have addressed myself to antitrust and patent law, I also recognize that there are other policies which have to be reconciled with both.

DIRECTOR HARRIS: Mr. Chairman, Dick—may I ask a question? Remember at lunch we talked about the arrangement among the automobile manufacturers for R&D on antipollution devices that the Department of Justice objected to? Do you think there should be some kind of a legal absolution whereby companies can get together on an arrangement to develop a device that doesn't have a good commercial market, but is needed in the public interest? This morning we spent a lot of time discussing the social issues involved in R&D today. If this is the direction we are going, don't we have to take account of it legally?

Do you think that there is a possibility that the government might recognize this new climate and permit cooperative R&D arrangements among corporations for this limited public interest purpose?

GENERAL HANSON: Let me make a comment on that, Jim. Looking around this room I think nearly everyone here remembers a greatly lamented affair about 30 years ago called World War II. During the course of that war you should remember that, among others, the oil companies were permitted to pool resources in order to feed the requirements of our defense establishment, and they were granted a limited exemption from the antitrust laws at that time in order to meet that requirement. The exemption was taken off immediately following the war, and the antitrust division proceeded to go ahead and continue their courses of action against them. One of them resulted in the founding of a large research fund called the Petroleum Research Fund which is administered by the American Chemical Society.

I see very little difference in theory of granting that type of exemption under war emergency conditions as opposed to granting a similar type exemption if the ecology condition is such that it demands it. And I don't know how you feel about it, Dick, but it seems to me they have some relationship to each other by analogy.

PROFESSOR DAY: I think that in an area such as President Nixon's all-out attack on cancer research there has to be some way to have some cooperation. Now, of course, the mechanism may be important here. If you operate through an agency such as NIH I think maybe that might be one way to do it. If you just have independent private businesses who are in the area and who are making a business of the product, the invention, then you run into a problem. If competitors are excluded from this research program, or at least if everybody doesn't have some way of being cut in, then you do get into a purpose and effect problem. If your purpose is to develop new technology for the public interest in a particular area—health, safety, welfare, or whatever—you may defeat that purpose by having a close group of companies, in effect, getting the full benefits by their cooperation and excluding others. I think that situation might call for some kind of licensing as a condition to permitting this kind of cooperation. And I don't mean compulsory licensing without royalties. I mean reasonable royalties for those who are unable or incapable to join this cooperative venture.

Of course, you have things like this going on right now with universities and private research foundations, where businesses do come in and support research in these areas, and then the question is: would such cooperative efforts of these various companies using these independent,

public, or semi-public agencies be an unlawful combination or conspiracy? I don't think it should be, but you do get into some areas there where, if you permit that sort of thing, maybe as a *quid pro quo* there should be some requirement for licensing where the effect, absent licensing, would be to adversely affect competition and not really promote the art.

DIRECTOR HARRIS: Well, if there were licensing open to all in this kind of an arrangement do you feel it would be perfectly legal?

GENERAL HANSON: It depends on who gave it its blessing, who attended the wedding. (Laughter)

PROFESSOR DAY: That wasn't the original question. I think the original question was: would this be a good idea to permit this sort of thing?

DIRECTOR HARRIS: Go one step further. I'm trying to commit you.

PROFESSOR DAY: Well, you cited the automobile industry case, and cases are still pending there. I suppose we may know someday whether that sort of thing is legal.

GENERAL HANSON: The Department of Justice, of course, entered a consent order in that case which prohibited this sort of exchange.

PROFESSOR DAY: And I think General Hanson just put his finger on it. It depends on who puts his blessing on it. Obviously the Department of Justice didn't like what was going on. Now, maybe there were other things there. It's a consent order, and we may find out in these pending cases that these were only methods of accomplishing a conspiracy not to produce an emission control device, for example. And I'm not saying that's the case. But this may be the kind of situation that the Department of Justice was after. And I'm not saying that the Department of Justice in the situation we're describing would necessarily say it's bad. I suppose from what they have done just on face value, you certainly might be afraid that they'd say that.

VOICE: May I ask what's probably a naive question since I'm not legally trained? What about these trade association laboratories such as the Portland Cement Association which has research laboratories?

PROFESSOR DAY: Well, I think that's a very good example of a way that you could do this contrary to the way the Department of Justice charged the automobile industry was doing it. It seems to me that if you have an association—a trade association, a research association or whatever—you may satisfy the requirements of trade association cooperative efforts generally where there is a legitimate purpose, such as to promote the public welfare—in cancer research, automobile emissions or whatever—and the organization is not a closed organization. Where membership is open for others to participate under reasonable condi-

tions, it seems to me that this could very well be a lawful, cooperative venture where it's not for the purpose and doesn't have the effect of restraining trade or monopolizing in this area as a result of cooperative combination competitors.

GENERAL HANSON: In line with that comment I would like to add another statement on the Petroleum Research Fund only because I'm thoroughly familiar with it. When the major oil companies, not all of which were U. S. citizens, but included Shell and the Dutch—some other organizations, were required to divorce themselves of any control of the Universal Oil Products Company, the Universal Oil Products Company was later sold to the public and the Petroleum Research Fund was established. One of the requirements of the courts in establishing the fund under the trust agreement that had been drawn to create it was that any patents that were derived from research administered by the American Chemical Society and created by the scientist who received the grants under this fund had to be in the public domain. This is one of the requirements of that particular agreement. And this goes back to 1946, which, in our rapidly moving history of these days, is a little ahead of its time, perhaps. But it touches upon the type of thing you're talking about, I believe, in this business of what-do-you-do-in-these-major-problems-that-arise. You also have the problem of adjusting and competing constitutional pictures. You're got two justices on the Supreme Court who would say that the First Amendment is an absolute. Nobody can encroach on free speech, free press, free religion unless it's a labor union.

This pair of justices, I think, are entirely wrong. I think all of the amendments to the Constitution and all the provisions of the Constitution have to be weighed one against the other. And they have to be weighed in the minds of where we find ourselves at a given time. And this is where, I think, your patent system under its constitutional protection has to find itself when it gets into the field of antitrust or other areas.

PROFESSOR OPPENHEIM: In light of the context of the discussion I think one of the most important instrumentalities for promoting R&D compatible with antitrust is the joint venture. Dick has properly alluded to various aspects of that, but I'm thinking of a joint venture among partners who may even be competitors although some of them may be complementary in the sense that they're noncompetitive in diverse areas—like a conglomerate joint venture.

The Supreme Court, interestingly enough, as Dick knows, in the *Penn-Olin* case set forth in the opinion of Justice Clark a great listing

of the Rule of Reason criteria that have to be evaluated in the joint venture which he held was also within Section 7 of the Clayton Act as a sort of a merger, not precisely the same as an outright acquisition. And he outdid Justice Brandeis in opening the doors to an extended Rule of Reason inquiry.

It seems to me it isn't a question of the size of the venture. It isn't a question of collective power of the venture being great. As I see it, the basic doctrinal significance lies in the willingness of the joint venture with due protection of the patent rights that they pool and put in the venture, and protection of pooled trade secrets and secret know-how, to end up with an open-end licensing program. There are a good many joint ventures, for example, where some of the joint ventures' only interest lies in licensing income. Those ventures are not engaged in the commercial marketing of the end products or the apparatus of the venture or what not. But whatever it is, it seems to me that the best safeguard under a Rule of Reason for a joint venture with competitors—even if the venture has almost monopoly power of the art by reason of their patents—is to be sure that they have an open-end licensing program on a nonexclusive, reasonable basis.

I think when you take note of the fact that the joint venture partners put their risk capital into the venture as an investment, that they are entitled to some differential treatment. For example, perhaps they are entitled to royalty-free use as against royalty-bearing licenses of the interchanged patents and trade secrets granted to companies which are not parties to the joint venture.

So it seems to me that in cases of that sort the basic question is: is the public benefiting from the fruits of the lawful purposes of the joint venture?

I'm against compulsory licensing unless antitrust violation is found. I think it ought to be very limited. It may be employed in atomic energy ventures, let's say, or in health and safety inventions, as you say, Dick. It seems to me that industry can get ahead of that by making sure that industry itself, in its own program, opens it up in a way that protects the investing interest of the venturers at the same time diffusing as widely as possible the public benefits by giving all responsible applicants licenses at reasonable royalty.

CHAIRMAN COLES: I think we'd better move along to the others of our afternoon panel.

PROFESSOR DAY: Could I make just one comment on this—a very brief one? Obviously, Oppie and I agree with each other on this, I'm happy to say. I wish you were still giving me grades.

I think that what you said is supported in the trade association cases where the other industry members, not members of the association, should be given the benefits of that association on payment of reasonable fees to cover the expenses and the costs of the association activities.

I'd like to point out that this is a dangerous area because, as Professor Oppenheim has stated, the joint venture in *Penn-Olin* was held to be within Section 7 of the Clayton Act. I also want to point out to you that Mr. McLaren has stated that—and we have cases—a patent is an asset which would come under Section 7. And he has gone further and said that a patent license is also an asset which should come under Section 7 of the Clayton Act.

As you know, Section 7 of the Clayton Act states that an acquisition by a corporation in commerce of the stock or assets of another corporation in commerce is unlawful where the effect *may be* substantially to lessen competition or *tend* to a monopoly. You don't have to prove actual effects on competition—you don't have to prove actual monopolization or actual restraint of trade. It's merely a reasonable probability that this may happen. The "may be" test, the insipieny test.

So when you apply this insipieny test to a patent assignment or license you can see that you don't apply the Rule of Reason we've been talking about because you don't have to determine whether there is an undue restraint of trade. The only question is whether there is a reasonable probability that this "may" happen.

Now, I'm not going to take any more time with this; but once you start thinking in this direction, what happens to your licensing and your assigning and your joint ventures? If you follow that through, what happens again is you're going to have the antitrust tail wagging the patent dog, or to use Mr. Carter's metaphor, those waves are going to lap up until that patent island is going to crumble into the antitrust ocean.

**PROFESSOR OPPENHEIM:** Professor Day is perfectly right. We call this a swinging door—a revolving door. All of you have had the experience of going through a revolving door. You go through the revolving door with your basic patent rights which you think protect you. Just as you think you're getting out into the street along comes antitrust with a pincer movement and you're back in that revolving door. You never quite escape. (Laughter)

**GENERAL HANSON:** Why not be perfectly candid, Oppie, and state that the Antitrust Division by its approach is trying to repeal the constitutional protection of the patent system? It's that simple. You know it and so do I.



PROFESSOR DAY: The result may be close to that if you applied Section 7 tests to licensing of patents, for example, instead of, as I advocated in my opening comments, treating that as a separate right granted by statute. If, following the public policy in the patent statute, merely granting a license or assigning a patent should not be subject to the test of the Rule of Reason, then certainly they should not be subject to an insipieny test.

CHAIRMAN COLES: Well, I hate to break in and cut this very interesting discussion, but I know that our next speaker has other engagements and so we'd like to move on to him.

General Hanson is a native Washingtonian, almost. He went to school at Cornell University and William and Mary where he received his B.A. & B.C.L. degrees; has been a member of the Maryland, Virginia, D.C. and Supreme Court Bars for some 24 years; has been very active in the civic affairs in Washington, the Smithsonian Institution, the National Geographic Society, and Cathedral School. I'll just abbreviate this by saying I don't have to tell you he's been active in the Marine Corps Reserves today, and he is off on duty for the Marine Corps later on this afternoon.

He is going to speak to us on the Emerging Needs in Tax Policy Concerning Research and Education.

## Emerging Needs in Tax Policy Concerning Research and Education

ARTHUR B. HANSON

If I may I'm going to stand up. Some of you folks who patented this cloth I'm wearing did not put an anti-wrinkle factor into it and you sit on it for awhile and it falls apart. This is the new all-purpose, all-seasons, Marine uniform which becomes official uniform in 1975. By that time, hopefully, we will have a new, all-purpose, all-seasons Marine uniform and I will be retired and won't have to worry about it. Some other character will.

I'm awfully sorry to have to leave early and I'm sorry I couldn't be with you earlier today, but I got made a president of the Marine Corps Reserve Policy Board for the Secretary of the Navy. And I must say that it's always a pleasure to involve myself with the governmental function even in the military industrial complex just to find out how confused we really are. (Laughter)

And the last two weeks have been rather interesting; I have a session with the Commandant of the Marine Corps and the Secretary of the Navy at 4:00 this afternoon. So I haven't got much time. That will save you lots of problems.

Mr. Chairman, Director Harris, I've been asked to speak to you on Emerging Needs in Tax Policy Concerning Research and Education, and I suppose the reason for it is that by circumstance I represent a great number of organizations in the scientific and educational field who are involved in research and development and are involved with the Internal Revenue Service and, unfortunately, on occasion involved with the Antitrust Division.

I would make one comment before I go into what I want to say about that. I don't understand why the patent system which has its founding in our Constitution should be any less exempt from the enforcement of the antitrust laws than our professional football, professional baseball and even the newspaper business which I also have a rather deep interest in.

In any event, let's go to the subject of the tax picture as it concerns research and education as we find it today. Now, I think you all are aware of the fact that in 1969, as of December 31st, an unusual date, the Congress of the United States disgorged a tax bill, and I say "disgorged" because it had to be just that kind of an operation which has as part of its purposes a complete restructuring of the tax laws as it relates to research and education or, put in other terms, for the scientific and educational field. And there is no question that the approach to foundations and the scientific picture was produced by great abuses made by those who sought to use the benefit of the existing laws prior to 1969 for personal gain and, oftentimes, research of a peculiar nature, such as sending seven Congressional assistants around the country after their Senator, unfortunately, was shot and killed out in California.

These are all part and parcel of the hearings up on the Hill that related to this tax law. And these abuses, as so often happens, produced an overkill in this field. Today you find, with government research money drying up, that the universities and the foundations are hard put—under the present climatology in the tax field—to come forth with a proper disposition of their funds in a fashion which gives you an easy climate in this area. On the other hand, I'm a strong believer that when the pendulum goes one way, it'll go back. And I want to address myself to the problems involved here.

You have, of course, a situation where you have money problems in the country today and in a—what one might term—a "declining economy." You certainly have unemployment problems. And in the field of aerospace science you have areas such as California, Texas and the state of Washington which have taken rude buffets in the field and are causing great dislocations of people.

On the other hand, some do not recognize that those people never had it so good; they were too quick to recognize the bad side of the picture. Many of these people are being very gainfully employed in their same field in the private sector as opposed to the governmental sector. And under our economy I'm one of those who believes this is important to us.

Now, one of the biggest problems produced by this amendment to the tax laws has been the amount of paper work involved in merely trying to comply with the reporting system that private foundations are now required to keep up with. This has placed the economic burden on the private foundations of having to hire a number of accountants and clerks merely to keep up with the government's requirements for reporting for fear that the executive officer of the foundation will go to jail. And it's really just that simple. The reporting system they created is monstrous. Some of us are trying to do something with that. We have, fortunately, a rather humane general counsel to the Internal Revenue Service at the moment. He is endeavoring to bring some light to bear on these matters and get these regulations simplified and also make them reasonably intelligible, so that you'll know what to do. I do not really believe he's going to be successful. The system doesn't seem to want that kind of success.

These organizations now are fearful of what they do in the public sector particularly. They're fearful of making statements in areas where they have expertise. You have a statement of law now that if you're a 501 (c) (3) organization, which is the scientific, educational side, you cannot participate in any legislative activity. Now, nobody has interpreted what that means. Under the old law you could not have any particular amount of your resources devoted to this, and they never really reached anything but a rule of thumb that maybe 5 percent was enough to be substantial. They used the term "substantial," and as any lawyer would be able to tell us, you tell me what substantial is and what's insubstantial and I would say it depends on which court you went before as to how that would be defined. Five cents might be substantial to a fellow who had 10 cents in his pocket, but five million dollars might not be substantial to a foundation with \$300 million in its pocket. But five million dollars obviously is a substantial amount of money.

These are the kinds of areas you're in. But today these people are not permitted to devote any of their resources to legislative functions. This means that many of these people are fearful of even appearing on Capitol Hill in matters in which they are expert.

I have always advised the organizations I represent that if they really want to appear before any legislative body, whether it be local, state or national, that there's no real problem in obtaining an invitation because I found that legislators are universally willing, if you tell them you're on their side. And you can usually find somebody on every side of every question on the Hill—you tell them you're on their side and they'll get you an invitation to appear. And if you're invited to appear then you are not devoting any of your funds and time and effort to a legislative matter. You are being asked to appear as an expert. Keep that in mind. You say, "Well, that's just semantics." But it isn't really. Get invited. Don't break the door down. Then you're not hurt on that.

You people have got to be able to do this type of thing and you should not be hampered by tax policy in not being able to do it, because the things that you're seeking to do here may be some of the very things that you're interested in for the benefit of the public in the fields of ecology and of patent law. In all these areas you should be able to take your message to these legislators and keep them from putting sand in the works of time against things that will assist the people of our country.

I won't bore you with a lengthy discussion of the history of exempt organizations, but you can go all the way back to the reign of Queen Elizabeth in England and you will find the first reference to the same subject. And basically the reason for exemption and the reason that science education and things of this nature are given these exemptions is because you are relieving the government of your nation of a burden which otherwise the general public would have to assume.

Now, that may sound a little far-fetched, but that, truly, is the history of it in a capsule. And I think when you recognize that the work that you do in this area is of that nature, you shouldn't try to hide your light under a bushel. You ought to get up and try to get Mr. Wilbur Mills and the other geniuses who have initiated tax legislation to recognize the overkill that they put into the last legislation because it has had a stultifying effect on your ability to get funds for the things you wish to do in this field.

Right today we are attempting within this particular organization, The PTC Research Institute, to get some money to fund a study of the copyright law. Now, most of you gentlemen are interested in patents, some in trademarks and probably very few in copyrights. But you had best recognize that, in the field of software and the computer business, and in the field of retrieval in information, the copyright provisions

now pending before the Congress of the United States, upon which we do not expect any action until another year at least goes by and I wouldn't guarantee it then, will have a very, very strong effect on your ability to carry on the functions in that field. Now, we have structured a research program, and I'm going to try to get it funded, which will give people a chance to really understand the impact of this. I'm frank to say I don't think there is anyone in this country who really recognizes the far-reaching effect of the proposed revisions to the copyright law.

This Institute, I think, can do a great service if we can get it funded. It's going to cost \$50,000 or \$60,000 or so. In the old days we used to be able to go to certain people and say, "We need this to make a study of this legislation." Now you find people saying, "Legislation, my God, we don't want to touch it with a ten-foot pole." Fortunately, I've been able to persuade some people to do this, and you're going to discover that we'll get this money because it obviously is not what you would call an action program. It's a study program. So long as it isn't an action program you're not involved with it. But that's just an example of what we're talking about.

Now, I want to run through a couple of notes here because I don't want to take too much of your time on this, but—one of the very interesting facets that's come up under the new law is the approach to unrelated tax income, unrelated business tax income. They find that the advertising revenues in some organizations which obtain advertising only in the field in which they're working is unrelated business and that any income from there, if it presents a net income, is now taxable at the normal corporate rates.

Right there in some smaller organizations you have dried up their real source of funds that they could devote to research. A case was called to my attention yesterday. In fact, I was consulted by people unnamed who have an income of \$100,000 and some a year from a publication that they have sent only to their membership, and the income is derived from ads their members put in. They don't get them from anyone else. They've now been held to be a totally business-oriented organization, yet I will say that they involve every ham radio operator in the world. And they are going to go out of business if this ruling stays in effect. They've found that the structure of their entire operation which they, for years, have felt was rendering a public service in the fullest sense, is now rated solely as a business one. And I can assure you they're not very businesslike.

This is the kind of thing that happens when the tax people or the

antitrust people take a particular thrust at a business organization or a nonbusiness organization and cripple it by what I term "overkill." And I think the Antitrust Division is guiltier of this than even IRS.

As you all well know no one can operate a magazine or a newspaper or any public information service on subscription prices alone because the price would be out of your reach. I know of no individual, for instance, who buys the *Chemical Abstract* service. The subscription rate for it is now up to about \$2,500 per year. Pretty good subscription rate. The only people who can buy that document are corporate organizations where their laboratory uses them.

I'm waiting for the Internal Revenue Service to come in and tell me, "Sorry about that. That's purely a business matter even if that is the basic chemical research document for the entire world." I'm expecting them to come in and say, "We're going to tax it at the corporate rate." So we then make the subscription rate \$5,000 apiece. I don't know. This is a tough area. We know, for instance, that at the National Geographic Society we're waiting the day when the Internal Revenue Service comes in and tells us that our entire book publication field is a business. Although we send these books only to members of the Society and we give them to them for about 10 percent over cost, the effect of taxing us on that income is going to be substantial, and probably the National Geographic Society could stand it better than most. But they're now devoting at that Society in excess of \$5 million a year to research, grants to universities, to institutions around the country, and to museums. And if this happens to them that pool of research money will dry up.

This has been a very hasty overview of this picture, but I suggest that you will find that if it continues on its present trend, the Internal Revenue Service without any vicious approach to life, is going to hamper further the scientific and educational research in this country without even realizing that they're doing it because when we tried to say this in the Committee hearings up on the Hill we were bludgeoned with the example of some wealthy folks who had created private foundations. We were bludgeoned with the Ford Foundation's problems. You may as well face it. This was one of the institutions that created some of the hottest fire against us all. We were bludgeoned with these problems and the committees paid no attention to anything we had to say on the good side. I don't think they really believed the fact that there are literally 700-800 institutions in this country which are put together without any commercial or economic interests solely

for the purpose of sponsoring research and education in some private field or other.

Mr. Chairman, I thank you for letting me step in here for a moment. I'll be glad to try to answer any questions that anyone might have for all of eight minutes. Yes?

## GENERAL DISCUSSION

J. L. BRZUSZEK: General Hanson, my name is J. L. Brzuszek from the Bailey Meter Company of Cleveland. I just wondered if this "overkill" that you refer to, as an attribute of the antitrust department, is having a material effect in this country on the grade or quality of inventiveness, or has it been directed primarily to other situations where antitrust is actually an issue?

GENERAL HANSON: Well, I think philosophically we can discuss that question for a long time, and I'm not saying that to try to turn you off. Obviously, the Antitrust Division would state that it only endeavors to go in and go against those who are violators of the law, but in their philosophy of law enforcement the Antitrust Division is dedicated to the fact that the price covered, the second-rate seller, the guy who operates out of his hip pocket is their preferred friend. And you may as well face that—I've lived here all my life. I'm one of those strange critters who was born here. Dick Day spoke kindly of the Antitrust Division. I've know it under Democratic administrations, under Republican administrations, but many of the people there, as in all government departments, have been there for 30-40 years. Their philosophy doesn't change.

When Judge Barnes and Professor Oppenheim were running the Attorney General's National Committee to Study the Antitrust Laws back in the 50's, they didn't even get to the tip of the iceberg. Sorry about that.

PROFESSOR OPPENHEIM: I'm not sorry because if we had to get at the whole iceberg the Committee would still be at it. (Laughter)

GENERAL HANSON: That's right. I think it's time to have another Committee to take a look at it. I think the antitrust laws are not



assisting competition. I think, if anything, they are restricting competition. But I'm afraid our's is a voice in the wilderness.

Obviously, where corrupt business people go into competitive business practices violating the antitrust laws they ought to be brought to book. But, in turn, a conciliation process in that field has a whole lot better effect in my opinion than the other. I happen to believe most businessmen I've known have been pretty honest guys.

I don't think that really answers your question.

MR. BRZUSZEK: I think so. I think I'm primarily concerned about the judiciary in my question because they ultimately decide validity, and I was interested in what perspective you knew the high rate of invalidation of patents and perhaps the antitrust situation as a carryover.

I wanted to know if perhaps that was what you were directing your "overkill" remarks to.

GENERAL HANSON: Well, in the patent field—I'm not a patent lawyer so forgive me for anything I misstate in the field—but in the patent field there are those who believe many things are patented which truly should not be. I don't think this is news to any man here. And I think perhaps some of your problems lie there, and also the great majority of your judges who sit on these cases are not expert in the patent field. And oftentimes, with complete respect, the presentation of cases in the federal courts leaves a great deal to be desired because they're overcome with the technicality of the case and by the time the judge, who's not a patent expert gets in there, he's struggling to find out what in the name of heaven they're talking about, and not always do they get good light cast upon it. That, again, is only a philosophical answer, but it does approach what you're talking about.

I'll leave quick before anybody says anything more. Thank you very much.

CHAIRMAN COLES: Thank you very much, General. Very interesting, particularly since one or two of us here are a 501 (c) (3) organization and have some problems of our own. And everything you said about them is correct.

Other general discussion of either one of these papers—we can say anything we want after General Hanson leaves now. He's not here to defend himself. (Laughter)

DIRECTOR HARRIS: May I ask you a question? Research Corporation has been dealing with a great number of universities and you do a lot of licensing, too, don't you?

CHAIRMAN COLES: Yes.

DIRECTOR HARRIS: Have you been running into any antitrust problems?

CHAIRMAN COLES: I'd like to ask Dr. Marcy who is our Vice President for Patents and is more familiar with this to respond to that question. The question was: Have we been running into any problems with antitrust in licensing at the universities?

WILLARD MARCY: I think the answer to that is yes.

DIRECTOR HARRIS: Well, what sort of problems? Do they involve certain licensing limitations?

DR. MARCY: All sorts of problems. It's rather difficult to generalize on something like that. We try very hard in our operation to observe both the letter and the spirit of the antitrust laws.

Recently we've been involved with foreign licensing where the antitrust laws are giving an impact overseas, and these complications are rather complex. So far we've been pretty lucky in contrast to some other licensing organizations. But in a fluid situation as with antitrust legislation where you can't predict what's going to happen tomorrow almost anything can happen.

DIRECTOR HARRIS: Is it because of peculiar arrangements among people that you are dealing with or because of license limitations in the license itself? What is the factor that people should be aware of and be careful of? Are there any caveats that you can tell us about?

DR. MARCY: Well, you can list every item if you intend to be careful of every one of them. Territorial restrictions, field of use restrictions—these are very important.

Manufacturing in one country and shipping into another country where no patent protection exists is difficult to resolve.

DIRECTOR HARRIS: In other words, very similiar to what other organizations have? There seems to be no difference.

DR. MARCY: No real difference. I don't know that I'm responding to the question very well, but I'm being a little vague because there are so many facets to it.

DIRECTOR HARRIS: Well, what I had in mind is that perhaps you would have some sort of leeway because you represent universities, representing academia rather than commercial firms—you weren't engaged in pure commercial arrangements. But you don't?

DR. MARCY: The universities deal in these areas, or some have, so they're going to be subject to the same laws as the commercial operations. I don't think there are really any major differences.

DIRECTOR HARRIS: Because they're thought of as operation for profit

in this regard. It's not a non-profit operation. You're out there to make a dollar and so you have to—

CHAIRMAN COLES: There's a difference in that. The university is subject to the same laws that anyone else is subject to. And in the matter of handling patents we've been very alert to the antitrust laws and have tried always to act in conformity with them as long as we could tell what they were which is sometimes difficult. So far they've caused us little difficulty. We've never been involved with any type of litigation or had any action brought against us at any time or any question raised that I know of. On the other hand, a very distinguished university research foundation took a different attitude towards certain aspects of this than we did and has been brought to trial and has had a judgment rendered against them on this. And that was a university much more directly concerned. I think it's a 509 (a) (2) or (a) (3) type organization.

DR. MARCY: But that doesn't mean that we won't have something served on us tomorrow. Under this Section 7 we were talking about I guess anybody could have something served on him.

CHAIRMAN COLES: I don't think the university is really any different from a commercial operation just because of the non-profit thing.

How do you feel, Ralph? Ralph Montgomery from Penn State is here.

RALPH E. MONTGOMERY: The only thing I can say is that Penn State looks to Research Corporation to handle these problems for us. (Laughter)

CHAIRMAN COLES: A little louder so we can pick it up on the recorder.

MR. MONTGOMERY: I was saying that we have never been involved with the problem directly, but our patents are handled either through the Research Corporation or the Battelle Development Corporation. And we have them worry about these problems for us.

DR. MARCY: Well, we do worry about them for you. (Laughter)

We tend generally to lean over backwards to be on the safe side. I'm not sure in the long run this is a proper position to take. It could tend to stultify our operations and it tends to withhold from the public benefit some of the things that otherwise would be out there sooner. I'm not sure that this causes a complete repression, but it does delay things a great deal because one has to be very open-minded about what may happen to you. You can't think about all these things happening to you on the spur of the moment. It takes a long time to get an overview of all the possible factors which should be considered.

Marcus Finnegan, who was here earlier, developed something for us which is a little different from our usual licensing approach. This concerned a patent pool involving two industrial companies and ourselves. The question that Mr. Finnegan addressed himself to was: How do you sublicense these patents to the two companies involved plus the rest of the industry on a nonexclusive basis and be fair about it?

So far this has worked out well in the United States, but now we've come to the problem of licensing this set of patents or their corresponding patents in foreign countries. We have one particular foreign company which wants to use the patents to manufacture itself, then ship the products to other companies in other foreign countries for incorporation of the products into a third product and import the final product into the United States. Now, how do you handle that? This is a rough situation.

DIRECTOR HARRIS: John—John Gray, I'm just wondering—what's been your experience? Has it been any different?

JOHN L. GRAY: No, I think that what Will has said is the same as the experience in the Battelle Development Corporation. There are two areas of difference between an organization like Research Corporation or Battelle Development Corporation and a manufacturer-licensor. We don't manufacture anything, so we're different from an ordinary product-making organization in that respect when you consider it from an antitrust standpoint. The other area of difference relates to the fact that quite often the time that we license is perhaps a few years after conception of the invention. The normal length of time from conception to any kind of significant market penetration for a major innovation is usually at least 10 years and more like 15 or more. When you consider the fact that there might be another four to six years of developmental effort involved subsequent to our licensing, the problem that we have is trying to forecast what the antitrust laws are going to be like 10 or more years from now when our licensee has that success in the marketplace. This tends to make us more conservative.

DR. MARCY: Well, John, do you think that with the laws the way they are now, this tends to stretch out the time that it takes to get products on the market?

MR. GRAY: I think it's a deterrent. In fact, I'd expand it to say that one of the things that I find as a long-range problem in industry, in the area of introduction of new technology in the form of new products in this country, is the increasing problems that we have with regulatory agencies, not only the Antitrust Division, but the FDA and two or three others. Instead of being in partnership with industries, they tend to

block the introduction of new products. My personal experience is that you have less of that in Europe and Japan.

DR. MARCY: Our experience is the same. The FDA situation is a special case in point, and anybody in the drug or the pharmaceutical industry is pretty rabid on this point. The thalidomide problem, which occurred less than 10 years ago, has been a major factor in causing FDA to tighten up its regulations. We have a product in the public health area which caused much concern to the FDA people, in this case, I think, quite irrationally. They are simply not going to take any chances. They are going to require an awful lot of investigative work to settle this case and it will cost in the neighborhood of a couple of million dollars just to get the clinical data necessary to satisfy the FDA requirements. It doesn't seem as though that kind of thing is necessary. This product won't be on the market at all if the company and industry don't cooperate in doing what FDA says to do.

Now, I can understand FDA's point of view, and I think the FDA is a most vital organization. I think it's necessary to have an action corps, but it is not necessary for them to develop an adverse position.

CHAIRMAN COLES: Dick, we've had an interesting session this afternoon. Our program calls for a coffee break now, but I think we better just run right on through and then have a cup of coffee before some of us rush off to catch airplanes and things of that kind.

MR. BOWES: I'd like to raise something which hasn't been touched on here. Most of us know that there were some hearings last week connected with some amendments to S.643. Largely, the subject matter of the hearings were the so-called Scott Amendments which essentially are designed to sanction many of the existing long-standing patent license restrictions.

On the one side we have heard a lot of speeches, we have read writings from the Department of Justice officials, particularly Mr. Stern and Mr. McLaren. At the hearings in particular a number of law school professors opposed the Scott Amendments. Several of them we might call members of the antitrust bar who are not patent attorneys. These opponents were talking in generalities and were talking about the academic approach of the law professors who were talking philosophically, and on that theoretical basis you can make a very fine sounding statement.

Businessmen, however, are not interested in philosophy or an academic or intellectual approach to patent licensing. The businessman has a specific problem. The licensee usually has a particular infringement problem which troubles him, and all he wants is relief from that

infringement. He doesn't care much for having a license to do anything he wants all over the world and so on. He wants a specific type of license. The licensor doesn't want to be clairvoyant and have to determine whether he can get royalties for all possible uses of inventions. So he, too, usually is interested in only the particular situation. So when a businessman talks about patent license practices he's talking about the technicalities of the business.

Looking back again at the remarks on the Scott Amendments, by and large, the people opposing them have not had business experience and have not done negotiating and also, it seems to me they just don't understand the business aspects of patent licensing—the practical problems. So where does this go? I don't know, maybe you don't agree, but there is a gulf. Do you see any way of bridging it?

PROFESSOR DAY: I guess I would have to agree with you that there is a gulf in some ways between some of those who testified against the Scott Amendments and people like myself who don't agree with that position.

I'm not so sure that it's necessarily bridgeable by practical experience alone. I take issue with the whole philosophy of it as well. I live in an ivory tower, too. I don't have day-to-day patent problems in the sense of writing patent applications and negotiating licensing agreements as such, but to me the comments that I've heard this afternoon substantiate my philosophical position. All of these antipatent philosophies, fortunately, have not as yet been put into practice in the courts. And when I spoke with some alarm earlier I was talking in terms of what could happen if these philosophies were effectuated.

It seems to me that this kind of extreme antitrust application could have very adverse consequences on research and development. The people who speak strongly of antitrust enforcement in patent licensing matters generally justify it philosophically on the grounds that the incentive to invent would not be hurt, and that the public would benefit from a wider dispersion of the inventions.

I take issue with that basic premise because as I tried to say earlier I think that the commercial development and utilization of patents is closely tied to the incentive to invent. Consider the comment a minute ago that you're worried about what's going to happen in the future if you license a particular way and therefore you play it safe and you do things that maybe you shouldn't do economically speaking or in the public interest even, simply to avoid the antitrust laws. If, for an example, the narrow Rule of Reason that I oppose were adopted as a general rule in the courts you would always be faced with second

guessing—long after the fact perhaps—in a law suit to determine whether or not there were, in fact, more reasonable alternatives which could have accomplished your purpose. And it's not based upon whether at the time of your actions it appeared to be a reasonable licensing arrangement to permit you to benefit fully from your patent. At the time of suit you may be found to have gone too far simply by hindsight saying: "Well, as it turned out there was a more reasonable way to do that. You didn't have to grant just two licenses. You may have been able to accomplish your purpose by granting three." You know, that kind of an approach.

And I think in this merger area the result could be even worse, because under the so-called backward sweep doctrine of the *DuPont-GM* case you would look at an acquisition of a patent or perhaps a patent license at the time of suit. And if, at the time of suit, it appears that there *may* be this adverse effect on competition then it becomes illegal at that time, even though, if tested at the time of the license—maybe 12 or 15 years ago—it was perfectly lawful, as far as any probable adverse effects on competition.

So when you put all these things together you could have some Draconian effects. Whether you call it overkill or just strong antitrust encroachment upon the patent area, it seems to me that such an approach could have a stultifying effect not only in the licensing and utilization of patents for the public benefit, but also in the incentive to invent itself.

DIRECTOR HARRIS: Mr. Chairman, may I ask a question of Dr. Marcy?

Sometime ago we had a paper in *IDEA* on the possibility of utilizing alumni to support the development of patented inventions at universities, and to provide assistance in patent utilization, licensing, et cetera. Have you given any thought to some kind of an arrangement where alumni could be of help to you?

DR. MARCY: I'm sorry. I didn't see the paper so I'm not exactly sure what it says. But are you speaking now of alumni of a given university?

DIRECTOR HARRIS: That's right.

DR. MARCY: Let's say, for example a man who graduates from Columbia University and then goes out into the business world and starts or manages a business and having him somehow or other get involved?

DIRECTOR HARRIS: Right.

DR. MARCY: Well, I probably shouldn't say this, but alumni are not always very reliable. (Laughter)

They have a vested interest in one thing. They have a vested interest in their school. They have a vested interest in their own affairs. They have a vested interest in the companies that they're involved with, and sometimes they make decisions as alumni rather than as uninvolved third parties. I think other things being equal I'd just as soon go to a third party somewhere and have him help.

I don't know exactly what special talent alumni could bring to bear in this area. It's a decision-making area and decisions that are made are then carried out by other people.

**DIRECTOR HARRIS:** I was thinking that he might be more interested in taking a risk.

**CHAIRMAN COLES:** He might be more amendable to taking the risk. Therefore, these are new things.

**VOICE:** Also, supporting a piece of research with the possibility that eventually he would be a preferred licensee. He'd get first crack at it.

**CHAIRMAN COLES:** Just to respond to this as a former college president who has dealt with a lot of alumni, I just wanted to dissociate myself from his general description of alumni and attitude towards them. (Laughter)

The alumni I know have—I would like to see as licensees would be the ones who are more astute businessmen and they're going to make any decisions they have on the basis of good business judgment and economic prognostications and things of that kind. And about all you could say for them would be that they might give you a little bit better hearing when you first went to see them on your first interview about something. Beyond that if it's not good business why they shouldn't be interested in it, and I don't think they're going to be interested in it.

**DR. MARCY:** I think you're saying what I should have said. I agree with you 100 percent. I think this is the thing. Alumni are just alumni—not any different from any other people. A good businessman, a man with astute business judgments whether he's an alumnus or not—that's the man that one should deal with. I don't think it pays to search out an alumnus in particular.

**MR. JANOWIAK:** It may make sense to categorize the two kinds of things you go to alumni after, so to speak. There's fund seeking; that's a bona fide good arm-twisting thing for universities to do with successful alumni. Now these could be restrictive or unrestrictive depending upon the specific situation. But in the business deal that he's talking about, I think, both parties ought to approach on a business basis. If the



person was an alumnus the hearing would be a little bit better, but most of the university administrators I know would not want to mix the two.

MR. GRAY: The university might let an alumnus know sooner about a development which might be in his particular specialty. Suppose this alumnus wanted an exclusive license and there is no reason for having an exclusive license. I would certainly recommend that he not be treated any differently than anybody else except that maybe he might be the first licensee to be signed up. You wouldn't give an exclusive license unless there was really a good reason for it.

VOICE: I think the danger of going in this direction is that you're liable to find yourself in the position of having to do business with an alumnus when he is not necessarily the best licensee. You open yourself up to some conflicts of interest charges, too.

CHAIRMAN COLES: I might say when people ask me how I find being at Research Corporation after being the president of a college I say, "Well, I don't have any alumni to deal with." (Laughter)

MR. BOWES: Mr. Chairman, I'd like to inquire about a comment that Professor Oppenheim made. I believe he said that in his opinion the best way to avoid compulsory licensing was to license everybody. And that does sound to me a little bit like averting death by committing suicide. You brought this up in the context—

PROFESSOR OPPENHEIM: Ted, I'm glad you brought that up because I believe you got the impression I approved compulsory licensing in patent pooling arrangements. On the contrary, I have always been against compulsory licensing which, as you know, is a Supreme Court approved remedy in certain litigated antitrust decrees entered when the government proves antitrust violations.

I was referring to an interchange of patent rights. This may be part of a joint venture that may necessarily involve reciprocal patent licensing by the partners in the joint venture. The patentee, who is not a party to a pooling of his patents with other owned patents, has an option, acting unilaterally, to license or to refuse to license. Mr. McLaren, the head of the Antitrust Division, has explicitly taken that position. A recent President's Commission report proposed that once a patentee grants a license, he should be under a duty to grant comparable licenses to others. This is an unwarranted derogation of the exclusive rights of the patentee.

In a patent interchange, the participants who pool their patent rights are entitled to be rewarded for their investment risks. Hence, even if

outsiders are granted royalty-bearing licenses, the participants in the pool should be entitled to royalty-free reciprocal licenses since they are contributing their patents to the pool.

I think, Ted, that you may have been concerned about a proposition in the Attorney General's Antitrust Committee Report of 1955 to this effect: if the patent pool included all products and processes which gives the interchange a monopoly position in the field of the pool, this should not be considered a violation of Section 2 of the Sherman Act if the pool has a primary lawful purpose. But the Committee did recommend that where such monopoly results, the pool should license all responsible outside applicants at reasonable royalties and without discrimination. That, of course, would most likely be an exceptional situation since most patent interchanges do not monopolize the art.

DR. SIEGEL: It should be of interest that the Small Business Act (as rewritten in 1958) nominally encourages the formation of joint research ventures by small firms, specifically offering exemption from anti-trust prosecution. Very few such ventures, however, seem to have developed.

PROFESSOR OPPENHEIM: It is not safe to generalize about the anti-trust status of joint ventures. Each one should be judged on its particular set-up and facts. Indeed, in some situations there might be little inducement or benefits in a joint venture, whereas in other situations, a joint venture may be in the public interest as well as for the benefit of the parties.

In *Penn-Olin* the Supreme Court approved a Rule of Reason approach to a joint venture to determine its legality under the Sherman Act. If the joint venture has main lawful purposes and is motivated by legitimate business needs without intent to suppress outside competition, it should be free from antitrust prohibitions. It is wise to avoid restrictions on production and price in patent licensing by the joint venture.

A joint venture is desirable when no one company would be willing to go it alone in capital investment and risk-taking. When each party has patent rights complementary to those of the other parties, the risks are shared. Sometimes a joint venture is created for the purpose of obtaining revenues only from patent licensing, rather than from engaging in manufacture and sale of products.

Reference has been made to the overall antitrust enforcement picture regarding patent licensing. I think it is important to bear in mind the enforcement attitudes in the antitrust field of the Antitrust Divi-

sion and the Federal Trade Commission—the Department of Justice on the executive level and the FTC on the administrative and quasi-judicial level. The judicial attitude toward patent rights is also important to evaluate. Furthermore, the public attitude toward the patent system and patent rights is significant. These moods may change.

I pointed out this morning that the present Antitrust Division's view toward patent license restrictions is not favorable. I also find that many antitrust lawyers, who have not had experience in patent-antitrust cases, or some law teachers who likewise have not dealt with such problems, are apt to regard the patent grant as a monopoly which unduly restrains competition. That view overlooks the constitutional objective of giving the patentee limited-time exclusive rights as a means of inducing disclosure of the invention and its claims and also inducing investment of risk capital.

The patent grant is therefore a public welfare limited-time monopoly for contributing an invention which is new, useful and nonobvious. It is regrettable that there is at times confusion between the antitrust restraints beyond the patent rights and restraints on competition which the Constitutional provision and the Patent Code sanction as restraints within the scope of the valid patent grant.

DR. SIEGEL: Although the subject of this Conference is inexhaustible, we do tend to cover some parts of the relevant terrain more often or more thoroughly than other parts that also merit attention. This tendency, the complexity of our subject, and the multiplicity of interconnections and ramifications—all underscore the need for "policy correlations" that motivated the Conference call in the first place. None of us, unfortunately, is sufficiently interdisciplinary to treat research and development, technological education, and industrial property with equal authority. Still worse, none of us is sufficiently gifted with wisdom as well as knowledge to advise society how to make an elephant of the parts that we see.

Looking back over my notes of this exhilarating and also troubling day, I find that I have asterisked points made by each of the speakers—and by commentators from the floor. Too many ideas will strive for priority in an environment that is unstable, evolving, not really predictable, and heavily populated with competing wills.

What is to be done? Surely, political decision will not wait on discussions of this group or any other assemblage. Every piecemeal decision that is taken, every action relating to a fraction of the total area of concern, has implications for the rest of our enormous subject, for the

relevance of any attempted integrated program design, and for the options still open for future decision and action.

If we look at the matter too closely, it always seems too late to worry about the future; and this observation may provide some basis for optimism. After all, man has lived in open systems throughout history; and he is destined to live in increasingly complicated ones. Furthermore, he is a problem-solving animal, or at least a problem-posing one. Accordingly, he looks for "closure" of open systems, tries to supply the missing element or assumption or value that leads to a tolerable answer, solution, *modus vivendi*.

The search for closure will obviously involve trial and error, and such policy correlations as are devised for the 1970's will involve compromise. At a minimum, all who have participated in this Conference are for that reason better equipped to contribute to the process as citizens, professionals, and officials of private or public organizations. In addition, the Conference suggests the desirability of establishing commissions for broadly representative, collective, and continual grappling with the issues on which we have touched today. Two kinds of commissions are indicated. One would deal with narrower aspects of our Conference theme, and the other variety would deal with it more comprehensively. For example, the discussion of patent and antitrust issues that we have heard here suggests a need, perhaps, for establishing another Attorney General's committee, such as the one that functioned in the early 1950's. On the higher level of integration, we seem to need more groups that try to discern a proper pattern of national priorities. The Eisenhower committee on goals comes to mind; and so does the one established by President Nixon under Professor Moynihan, which reported on the memorable date of July 4, 1970.

Of course, committees are only available, rather than decisive, weapons; we should not expect easy closure by a method of delegation. Indeed, one might suspect that too many committees already exist—that we are already "overcommitted" as a nation—and that we cannot hear ourselves or each other above the Babel, babble, or battle. Fresh in memory also is the failure of the President's commission concerned with patents to anticipate some of the governmental actions taken, and issues emerging, after the publication of its report. But we must go forward with the crude or limited instruments that we have, and with the benefit of the insights provided by the widely representative panel of speakers to the privileged few who could be here today.

Many others in this group may draw future inspiration, as I know I

shall, from recollection of Billy Horton's final remark at lunch—that he would rather be Inventor of the Year than President of the United States.

CHAIRMAN COLES: That is a very thoughtful summary, Dr. Siegel.

I think at this time with these very eloquent statements of Professor Oppenheim and Dr. Siegel that it's probably time we should adjourn the Conference. And I can't help but thinking in adjourning that we're all going to leave here and we're going to weigh our own public spirited and thoughtful convictions against the selfish prejudices of those on the other side. (Laughter)

DIRECTOR HARRIS: May I thank the Chairman, the speakers and all the participants for a very informative and provocative Conference. You will receive your remarks for editing before publication. I know our level of information has risen as a result of this meeting and we will all want to give serious consideration to the many suggestions which were made—and our publication also will make these proceedings available to the larger public.

Thank you again. The meeting stands adjourned.

---

## NOTES

---

---

### New Film on "The Way of Invention" Available

"The Way of Invention," a new film in the Institute's series of "Living Archives of Inventors" is now available for purchase by interested individuals and organizations. Those interested in purchasing the film can view it at the Institute's headquarters. Copies are approximately \$140, exclusive of shipping costs, and can be ordered through The PTC Research Institute of The George Washington University, Washington, D.C. 20006.

The one-hour, five-minute audiovisual film records the highlights of a day of exchange between five outstanding inventors which took place at Smithsonian Institution. The five inventors are Robert Adler (radar, TV/FM systems); J. Presper Eckert, Jr., (computer systems); Jack Rabinow (electronic equipment); Richard R. Walton (textile processes); and Vladimir Zworykin (TV iconoscope).

Sponsored jointly by the Institute and the Smithsonian, this is the first of a series of one-hour

films planned by the Institute to provide clear and memorable impressions of outstanding living inventors portraying the circumstances under which their inventions originated and were applied. The film series underscores the relation of the industrial property systems to the protection and marketing of products of the mind.

This film program affords an opportunity for researchers, students, professional people, business administrators and the general public to examine firsthand the techniques employed by recognized creative individuals and to record the reactions of these creative people as they contact other outstanding creative minds.

The series serves three major purposes: (1) makes available an educational instrument for universities, television, business, etc., (2) provides living archives for posterity, and (3) honors leading creative people in a unique way during their lifetimes.

## Selected Papers from the Institute's Fifteenth Annual Conference to be Published

Selected papers by key speakers at the Institute's Fifteenth Annual Conference on "Enterprise Under Stress: Changing Premises and New Responses," will be published in the Conference Number 1971 issue of *IDEA*. The Conference was held at the Shoreham Hotel in Washington, D.C. on October 20th.

This year's Conference considered the risks attendant on the introduction of new products and the social requirements for enhancing the quality of life and the material welfare of our people. Particular attention was given to national and international problems due to technological hazards (such as pollution of the environment) and to consumer protection. The role and potential of R&D, industrial property and competition was stressed as a means of meeting these current and emerging challenges, while at the same time observing the new constraints on R&D and on industrial property.

Robert W. Cairns, Deputy Assistant Secretary of Commerce for Science and Technology moderated the morning sessions on "New Context for Research" and "New Circumstances for Industrial Property."

The afternoon session on "New Setting for Antitrust and Unfair Competition" was moderated by John C. Bodner of Howrey, Simon, Baker and Murchison.

"Consumerism and 'Old-Fashioned Commercial Honesty,'" the Kettering Award Address presented by 1970 Recipient Walter J. Dernenberg, internationally recognized scholar in industrial and intellectual property, highlighted the luncheon session held in his honor. Among the distinguished guests attending the luncheon was former Supreme Court Justice Tom C. Clark.

The key speakers were Henry David, Executive Secretary, Division of Behavioral Sciences, National Academy of Sciences; Joseph S. Whitaker, Coordinator of Environmental Affairs, Union Carbide Corporation; Corwin D. Edwards, formerly Head of Bureau of Economics, Federal Trade Commission; S. Delvalle Goldsmith, Ladas, Parry, Von Gehr, Goldsmith & Deschamps; Allen C. Holmes, Jones, Day, Cockley and Reavis; and Robert Pitofsky, Director of the Bureau of Consumer Protection, Federal Trade Commission.

## Paul E. Kritzer Wins 1971 Patent Office Society Award

Paul E. Kritzer, a student in the Georgetown University Law School, was chosen to receive the Patent Office Society Student Award for 1971 for his paper entitled "Copyright Protection for Sports Broadcasts and the Public's Right of Access."

The Award, consisting of a citation from the Institute and an honorarium contributed by the Society,

was presented to Mr. Kritzer at the annual Patent Office Society banquet held November 6. A citation was also given to Lewis Anten for his paper, representing The George Washington University, entitled "What's New with Novelty." Both papers are published in the "Student Papers" section of this issue.

The Award program is open to the law schools in the District of Columbia.

## Edited Proceedings of "Fraud" Clinic to Appear in *IDEA*

The edited proceedings of the Institute's recent Clinic on "Avoiding Fraud on the Patent Office," held at its headquarters in Washington, D.C. on November 18, 1971, will be published in *IDEA*.

Based on the key presentations of four experts, the Clinic concentrated on the major questions of how, when, and to what extent the applicant's own data should be disclosed to the Patent Office and prior art should be disclosed to the Office; and what counsel the litigating lawyer can give on how such data should

be disclosed.

Chairman of the Clinic was Frank Neuhauser of General Electric Corporation. The principal speakers represent four different points of view. Paul A. Rose, Union Carbide Corporation spoke as a soliciting attorney; Albert C. Johnston, Keith, Johnston and Isner as a litigating lawyer; Jack Rabinow, Control Data Corporation, as inventor-research director; and P. J. Federico, Cushman, Darby and Cushman as a former member of the Patent Office staff.



# An Empirical Study of Cost Factors in Patent Litigation

L. JAMES HARRIS\*, TERRY M. CHUPPE\*\*  
AND LE MANH TRI\*\*

## APPROACH

THIS IS THE THIRD PHASE OF A SERIES of surveys conducted by the Institute designed to draw together factual information and expert opinion on reducing the delay and expense in patent litigation while maintaining patent reliability. In Phase One of this study, The PTC Research Institute sent a pilot questionnaire to a sample of 65 patent experts in industry and private practice seeking their opinion and data based on their experience with respect to (1) the patent system in effect today and (2) reaction to a proposed Dual Patent Program

---

\* Director, The PTC Research Institute; Professor of Law, The National Law Center, The George Washington University.

\*\* Mr. Chuppe is a Research Associate with the Institute. He and Mr. Tri are Financial Economists in the Office of Policy Research, Securities and Exchange Commission. The views expressed herein are those of the authors and do not necessarily reflect the views of the Commission.

suggested as a long-range proposal for the future.<sup>1</sup> From the responses to the pilot survey, Phase Two of the study evolved. In that phase questionnaires were sent to a larger sample of patent attorneys to obtain more detailed information on total costs as well as a clearer insight of the composition of total costs in litigated cases.<sup>2</sup> In addition to supplying basic cost data, the responses directed our attention to certain key factors having special impact on litigation expense and we were apprised of explicit cost-cutting opportunities that respondents believed they could have taken in their cases and yet have accomplished the same results.

#### SCOPE OF CURRENT SURVEY

For the Third Phase of the Cost of Patent Litigation Study, questionnaires were sent to a sample of litigating attorneys listed in published reports on the federal courts in the years 1967 to 1969. The questions<sup>3</sup> were developed from the responses to the Institute's earlier surveys in this area. The attorneys included in the sample were requested to answer questions for each case with which they had been associated which terminated by settlement, judgment or dismissal in 1970.

As a means of reducing delay and expense in the litigation of patent cases, respondents to the Institute's earlier surveys most often advocated that (1) greater use be made of the Pre-trial Conference; (2) more cases be decided on the basis of Summary Judgment motions; (3) greater attention be given to Separation of Issues; (4) limitations be placed on Discovery procedures; and (5) judges be better educated on technological and on patent matters. Some form of *res judicata* was

---

<sup>1</sup> L. James Harris, "A Dual Patent Program: To Increase Patent Reliability and Decrease Litigation Costs," *IDEA*, Vol. 13, No. 1 (Spring 1969), pp. 1-24; and L. James Harris, *IDEA*, Vol. 13, Conference Number 1969, pp. 51-59; 93 and 94.

<sup>2</sup> L. James Harris and Terry M. Chuppe, "Cost of Enforcement of Industrial Property Rights: An Analysis," *IDEA* Vol. 14, Conference Number 1970, pp. 77-88; and L. James Harris, "The Cost of Patent Litigation Study: Current Status and Future Direction," *id.*, pp. 63-75. In addition to the mail questionnaires, approximately 300 patent decisions from 1965 through 1969 included in the U.S.P.Q., involving those factors most often referred to by respondents as areas of cost-cutting opportunity, were reviewed. Also a sample of Cleveland attorneys were personally interviewed to explore certain questions in depth.

<sup>3</sup> A copy of the questionnaire is appended hereto.

avored, but less frequently.<sup>4</sup> The questions contained in the current survey were intended to explore the above five aspects of patent litigation more thoroughly with litigating attorneys on very recent cases in which they were personally involved. The questionnaire was also designed to test the hypothesis, based on information obtained in the earlier surveys, that early introduction of the judge into pre-trial proceedings was beneficial in patent cases.<sup>5</sup> Respondents were asked questions relating to the composition of patent litigation expense, time involved and the relationship of the stake to the procedures utilized. The pleading of fraud on the Patent Office or the raising of an antitrust defense was also explored since the earlier surveys suggested that patent trials are often concerned with and protracted by these issues.<sup>6</sup>

#### RESPONSES TO THE CURRENT SURVEY

The rate of response to the third survey in the Institute's Cost of Patent Litigation Study was good—approximately 30 percent. Fifty-seven attorneys provided information on 82 patent cases that were terminated by settlement, judgment or dismissal in 1970. The other responses received were from local counsel or from patent attorneys with cases in progress who did not have a case terminated during 1970 and, therefore, could not be included in our sample.

As expected, of the four "pre-trial" procedures (i.e., Discovery, Pre-trial Conference, Separation of Issues, Summary Judgment) receiving major attention in the questionnaire, Discovery was most heavily relied upon in litigation. Overall, 90 percent of the respondents indicated that Discovery had been utilized in their cases and, in most instances, their adversary sought to make use of this procedure too. Next to Discovery, the most utilized procedure was the Pre-trial Conference. It was employed in about half the sample cases, being required in many instances by local court rules. Motions for Summary Judgment and for Separation of Issues were sought far less than relief by Discovery or Pre-trial Conference. Motions for Summary Judgment

---

<sup>4</sup> Scattered support was expressed for a final judicial determination of patent validity or invalidity (see Harris, *supra* note 2, at pp. 74-75), and *Blonder-Tongue Laboratories, Inc. v. University of Illinois Foundation et al.* (402 U.S. 313; 2 L.Ed. 2nd 788; 91 S.Ct. 1434; 169 U.S.P.Q. 513) would appear to be a significant step in the direction advocated by some.

<sup>5</sup> Harris, *supra* note 2, pp. 63-75.

<sup>6</sup> See Frederic B. Schramm, "Cost of Enforcement of Industrial Property Rights: A Report of Interviews," *id.*, p. 93 at pp. 105-106

were reported in about one-fourth of the cases and for Separation of Issues in approximately one-third.

#### COST AND TIME FACTORS

The total cost of litigation as well as the breakdown of such costs into components were analyzed in the earlier phases of this study.<sup>7</sup> The current survey sought to obtain cost data from litigating attorneys primarily on the elements of litigation most often mentioned by respondents to our previous questionnaires as offering the best cost-cutting opportunities. Before discussing these specific cost factors, it would be useful to highlight at this point some of the Institute's earlier findings on the cost of litigation.

In the previous surveys, the total cost of patent cases analyzed ranged from under \$25,000 to several million dollars.<sup>8</sup> Outside counsel was found to be the principal source of cost for each component of litigation expense<sup>9</sup> regardless of the total cost of the particular case. For simple cases, however, the cost of house counsel tended to increase.

With regard to selected components of total cost,<sup>9</sup> Discovery was the largest—whether undertaken at the initiative of the respondent or at the initiative of the opposing party. In the relatively simple case, where total costs in most instances were less than \$50,000 (but in some cases up to \$100,000), Discovery tended to be somewhat less significant, although still the principal expense.<sup>10</sup> Generally, total Discovery expense (i.e., items (3) and (4) in footnote 9) ranged from 25-40 percent of total costs, the breakdown of expenses varying with the particular circumstances of each case. As was true for other items, most Discovery costs were related to outside counsel. After Discovery the largest expense was for trial, followed by the investigation of prior art and the nature of the alleged infringing act. For the relatively simple case, the direct expense of time in court was nearly as large a component of cost as Discovery, averaging about one-fifth of the total. Legal studies and

---

<sup>7</sup> Harris and Chuppe, *id.*, at pp. 81-84.

<sup>8</sup> *Id.*, at p. 80.

<sup>9</sup> Respondents were asked to break down their total costs into the following components: (1) Investigation of prior art and the nature of the alleged infringing act; (2) Legal studies and evaluations; (3) Discovery undertaken at the initiative of reporting party; (4) Discovery undertaken at the initiative of opposing party; (5) Direct expense of time in trial court; (6) Cost of preparing briefs; (7) Cost of appeals; (8) and other expenses.

<sup>10</sup> *Supra* note 2 at p. 83.

evaluations and the cost of preparing briefs each were found to average approximately 10-15 percent of total expense. When the costs of preparing briefs were combined with the direct expense of time in trial court, they exceeded Discovery.<sup>11</sup>

As noted earlier, the current phase of this study sought to obtain and relate cost and other data primarily with respect to (1) Discovery, (2) the Pre-trial Conference, (3) Separation of Issues, (4) Summary Judgment—areas referred to by respondents to the Institute's earlier surveys as having the greatest cost-cutting potential. We also wanted to relate these to the conduct of the trial. Table I summarizes the cost data (supplied by respondents with respect to 82 cases they were personally involved in which were terminated by settlement, judgment, or dismissal during 1970) associated with each of these procedures and with the conduct of the trial. Table II provides information on the amount of time spent on each procedure (other than the conduct of the trial).

For respondents supplying cost data on Discovery, the figures were generally in the \$5,000-\$25,000 range, although in a number of instances they exceeded \$100,000. The amount of time spent on Discovery was usually from one week to less than a month; however, in about 15 percent of the cases as much as six months or more were devoted to it.

Of the 30 respondents who provided Pre-trial Conference costs,<sup>12</sup> more than one-half estimated it at less than \$1,000. In contrast, less than 15 percent of the respondents had Discovery expense of under \$1,000. Typically, the time spent in Pre-trial Conference was less than a week, although it was not uncommon to consume up to a month. Likewise, the expenses incurred by Separation of Issues and Summary Judgment procedures was usually less than \$1,000; occasionally it was substantially higher.

The cost of the trial itself, including the related expense of preparing briefs, tended to be somewhat higher than Discovery expense. Expenses related to the conduct of the trial were most often in the \$10,000-\$50,000 range (as shown in Table I). However, in nearly one-third of the cases for which respondents supplied information, the cases were terminated before trial. Although respondents were not asked for the amount of time they spent in actual trial, they were requested to estimate how long it took to litigate the case. The most frequently mentioned duration for an entire case was from one to four years, but it was not unusual for cases to extend for longer periods, including one

---

<sup>11</sup> *Id.*, at p. 84.

<sup>12</sup> As indicated in Table I, in 16 additional instances the Pre-trial Conference procedure was utilized by respondents, but the related costs were not reported.

TABLE 1  
DISTRIBUTION OF SPECIFIED LITIGATION COST FACTORS  
FOR 82 PATENT CASES INCLUDED IN THE PHASE-THREE SURVEY

Costs (thousands)	Procedure Utilized				
	Discovery	Pre-Trial Conference	Separation of Issues	Summary Judgment	Conduct of Trial
N.A.*	6	36	54	51	25
Under \$1.0	9	16	7	7	0
1.0 - 4.9	9	7	3	3	4
5.0 - 9.9	13	5	0	0	9
10.0 - 24.9	13	1	1	1	11
25.0 - 49.9	3	1	1	1	12
50.0 - 99.9	5	0	0	0	2
\$100 and over	3	0	0	0	4
N.R.**	21	16	16	10	15
Total Using Procedure:	76	46	28	25	57

\*N.A.—Not applicable because procedure was not utilized.

\*\*N.R.—Costs not reported although procedure was used.

TABLE 2  
DISTRIBUTION OF TIME SPENT ON SPECIFIED PROCEDURES FOR 82  
PATENT CASES INCLUDED IN THE PHASE-THREE SURVEY

Time Factor	Procedure Utilized			
	Discovery	Pre-Trial Conference	Separation of Issues	Summary Judgment
N.A.*	6	36	54	51
Less than one day	2	7	5	4
One day to less than one week	14	17	5	8
One week to less than one month	28	13	4	11
One month to less than six months	16	2	2	2
Six months to less than one year	6	2	1	3
One year and more	2	0	0	0
N.R.**	8	5	11	13
Total Cases Using Procedure:	76	46	28	25

\*N.A.—Not applicable because procedure was not utilized.

\*\*N.R.—Costs not reported although procedure was used.

instance of ten years. Generally, the expenses associated with cases in the current phase of the study are akin to those classified by respondents in previous phases as relatively simple cases—with overall expenses generally under \$50,000 and in some cases up to \$100,000.

Most respondents felt that there was a relationship between the use of a particular procedure (e.g., Discovery) and the stake involved, and the greater the possible financial loss, direct or indirect, the more likely the client would allow for greater expenditures. Although there were some few who felt the financial stake had no relation to the procedures utilized, it is doubtful clients would allow costs to proliferate if the potential return did not warrant the expenditure. Regarding remuneration to litigating attorneys, fees based on the number of hours spent on a case were most common, followed closely by a retainer or salary basis.

#### DISCOVERY

Attorneys who responded to the Institute's earlier surveys indicated that Discovery appears to educate parties in advance of trial, prevents surprise at trial, and assists in ascertaining truth and preserving testimony. Discovery can apparently expose the relative strength of the parties and improve the chances of settlement where the costs have not yet run very high and attorneys are experienced and can evaluate the situation. Despite these benefits, patent attorneys find that Discovery is often not a simple, convenient or inexpensive way of obtaining facts,<sup>13</sup> and have generally suggested—albeit with some reservations—that Discovery be simplified and certain aspects eliminated. For example, attorneys interviewed in the Cleveland area are generally agreed “that Discovery practice was costly and that savings could be effected if there were a way of reducing the amount of Discovery taken without interfering with the arriving at facts.”<sup>14</sup>

Generally, the responses to our most recent questionnaire supported the Institute's earlier findings on Discovery, although there was somewhat less concern associated with its duration. A likely reason is that the cases in the current survey were less costly and relatively less complex than those analyzed in the earlier surveys which were directed to certain patent “experts” who were often engaged in—and long remembered—complex cases in which financial stakes were high and resistance strong. In contrast, the current questionnaires were sent to litigating

---

<sup>13</sup> Harris, *supra* note 2 at pp. 65-68.

<sup>14</sup> Schramm, *id.* at p. 95.

attorneys listed in published reports on the federal courts for the three-year period 1967-1969, comprising their cases terminated in 1970, and include relatively few of the "difficult" cases alluded to by respondents to the earlier surveys.

With respect to the 76 cases in the current survey where Discovery was utilized, approximately 40 percent of the respondents indicated that it had a major effect on the judgment in the case. About 60 percent thought it had educated the parties in advance of trial and assisted in ascertaining truth. Fewer than one-third suggested that it shortened the trial or eliminated issues, and about two-fifths felt that it prevented surprise at the trial.

Nearly all of the 35 respondents who indicated that Discovery had an effect on settlement thought that it had exposed the relative strength of the parties and 40 percent of these indicated that the potential costs of Discovery had exerted economic leverage to promote settlement. About two-fifths of all the respondents found fault with the Discovery tactics of their adversary. For example, complaints were voiced to extensive use of interrogatories, vague and indifferent answers to interrogatories, ignorance of federal procedures with regard to Discovery, prolonged Discovery beyond the point of reasonableness, and using it as an harassing tactic in order to promote settlement. Most respondents felt that Discovery proceedings were introduced at the appropriate time; however, about 10 percent thought that earlier introduction could have induced settlement.

With regard to the role of the judge, one-half of the respondents indicated that they filed motion for court help. The outcome, however, varied with the particular circumstance of each case. Most respondents felt the amount of judicial time spent on the procedure was reasonable and that the judge's intervention usually improved the trial process. A majority believed the judge's intervention in Discovery proceedings made the attorneys better prepared. One-half of the respondents indicated that the judge had previous experience in patent cases.

#### PRE-TRIAL CONFERENCE

The Pre-trial Conference was utilized in over half of the cases reported in the current survey. Respondents were dissatisfied with the tactics used by their adversary in less than a quarter of these cases and approximately the same number indicated that either they or their adversary filed a motion for court help, with mixed results. Very few



felt the amount of judicial time spent on the procedure was unreasonable. More than half were of the opinion that the judge's intervention during the procedure made the attorneys better prepared. The Pre-trial Conference, in many instances, was influenced by local court rules and use of the procedure was often required; some local courts have rather strict rules concerning the Pre-trial Conference. Most respondents who utilized the Pre-trial Conference think it educates the parties in advance of trial and prevents surprise. About one-third felt it had resulted in a shorter trial. However, less than one-fifth felt that the Pre-trial Conference had a major impact on the judgment in the case. In contrast, more than 40 percent of the respondents who utilized Discovery reported that it had a major impact on the judgment.

#### SEPARATION OF ISSUES

Procedure for the Separation of Issues was reported in one-third of the patent cases terminated during 1970 for which we received completed questionnaires. One-fourth of the 28 respondents who used this procedure thought that the judge's intervention made the attorneys better prepared. Less than one-fourth indicated that it encouraged settlement or enhanced the quality of the trial (e.g., preventing surprise, assisting in the ascertainment of truth or shortening trial). Only one respondent felt that the amount of judicial time spent on the procedure was unreasonable.

#### SUMMARY JUDGMENT

The Summary Judgment procedure was utilized in one-fourth of the cases reported in the survey. Although, as illustrated in Table I, this procedure can be relatively inexpensive, it nevertheless was utilized less frequently than either Discovery, the Pre-trial Conference or Separation of Issues. As in the Separation of Issue procedure, very few respondents indicated concern with the tactics of their adversary and nearly all felt that the amount of judicial time consumed was reasonable. More than one-third of the respondents who used this procedure believed it encouraged settlement. Judges appear to be overcautious in using this technique in patent cases. Whether because of the technical complexities of the art involved or their lack of experience with such cases, they

usually require demonstration before the trial court—even where credibility is not involved and there is no issue of fact.<sup>15</sup>

#### ANTITRUST AND FRAUD ON THE PATENT OFFICE

The use of the antitrust and fraud on the Patent Office defenses were referred to as an area of abuse by respondents to the Institute's earlier questionnaires and personal interview surveys. Attorneys were generally of the opinion that the additional time and effort required in proving and defending against fraud was an unnecessary and growing abuse,<sup>16</sup> that when fraud is pleaded a defendant could prevail by simply citing the prior art instead. It appears that many trials can be protracted by not trying an issue first that can dispose of the case,<sup>17</sup> particularly by not separating out peripheral issues such as antitrust or misuse.<sup>18</sup> Certain aspects of antitrust litigation require numerous witnesses and Discovery is rendered exceedingly extensive and expensive. In a single infringement case, cited as an example, a hundred depositions were required on its antitrust aspects.<sup>19</sup> Moreover, when a defense of fraud on the Patent Office is pleaded the patentee may not only be subjected to antitrust charges but also to the inference of collusion and may be forced to continue the litigation if only to vindicate himself.<sup>20</sup>

The number of respondents who indicated that antitrust and fraud on the Patent Office were issues in cases terminated during 1970 was high. This was not surprising in view of the fact that the Institute's earlier studies showed that this was a growing problem. In more than one-half of the 82 cases, antitrust violation or fraud on the Patent Office was pleaded. In the majority of cases where such pleas were made, either numerous additional witnesses were required or these defenses prolonged litigation in some other manner. Extensive Discovery was required in more than one-third of these cases. There were other litigation detriments: the briefs and trial were lengthened considerably, the number and complexity of issues to be decided were increased and the taking of numerous depositions, including those of examiners, was required. The extensive and growing antitrust and fraud on the

---

<sup>15</sup> Harris, *id.* at pp. 64-65; lack of familiarity with the relevant technology and the need for expert testimony have been cited by courts as the principal basis for denying motions for Summary Judgment, Peter D. Rosenberg, *id.* at p. 91.

<sup>16</sup> Harris, *id.* at p. 71; Schramm, *id.* at pp. 105-106.

<sup>17</sup> Harris, *id.* at p. 71.

<sup>18</sup> Harris and Chuppe, *id.* at p. 85.

<sup>19</sup> Schramm, *id.* at p. 105.

<sup>20</sup> Schramm, *id.*; IDEA, Vol. 15, No. 4 (Winter 1971-72), p. 675.

Patent Office pleading surfaced in our previous surveys and confirmed in cases terminated during 1970, and the implications of this situation with respect to the integrity and value of the patent right, suggests that this aspect of patent litigation merits further study.

#### FINDINGS AND RECOMMENDATIONS

Overall, the responses of litigating attorneys to the current phase of the Institute's Cost of Patent Litigation Study were more constructive than critical of patent litigation practice. Generally, they were less concerned about changing the rules than with making them work better. The cases reported on in this phase of the study were not as complex and protracted as the cases referred to by the patent experts in our previous surveys and interviews. This no doubt was a major factor in moderating the strong complaints we previously received of excessive costs and undue expenditures of time on litigation. Since we found that the stakes involved, whether economic, psychological or ethical, had a direct bearing on the pre-trial procedures used and expenditures made, perhaps it is the high-stake case that is largely responsible for excessive litigation costs and requires special consideration by the Bench and Bar.

Adequate preparation and fair and frank dealing among professionals were frequently advocated.<sup>21</sup> Although respondents suggested various devices for reducing the cost of Discovery, they appeared to be just as (and sometimes more) concerned with assuring that its benefits be preserved. Of considerable importance is the fact that over 40 percent of the respondents who employed Discovery—a pre-trial procedure that had been utilized in most cases—believed it had a major effect on the judgment in the case, and over 60 percent stated that it had some beneficial impact. Over half the judges presiding in these cases were experienced in patent litigation and even more were interested in the subject. Apparently patent cases are assigned to judges who like to try them.<sup>22</sup> Two-fifths of the respondents did voice complaints with the tactics of their adversaries and one-half of the respondents filed motions for court help. Most felt judicial time spent was reasonable and the judge's intervention made the attorneys better prepared—a finding which coincides with that in previous phases of this study.

One of the major hypotheses in our current survey—a theory based on the information we previously gathered—was that the introduction of the judge into the Discovery procedure at the earliest stages of the

---

<sup>21</sup> Also see John W. Malley, *supra* note 2, pp. 114-115.

<sup>22</sup> Harris, *id.* at p. 72.

litigation would reduce the cost and make the procedures more effective. The findings in the current survey support this proposition. One judge assigned to each case and brought in at the outset, as strongly favored by respondents, would educate him on the particular subject matter of the case as the litigation proceeds. If this is combined with the fact that patent cases are generally assigned to experienced or interested judges, the current impression that there is a lack of comprehension on the part of judges trying patent cases would probably be reduced to a minimum.

The responses to the questions on Pre-trial Conference coincided with those on Discovery. The opinion that the judge's intervention made the attorneys better prepared is also in accord with the results of the study of Pre-trial Conference procedure of negligence cases in the state of New Jersey made by Professor Maurice Rosenberg<sup>23</sup> of Columbia Law School. Although the respondents in our study appear to agree that the judge-controlled Pre-trial Conference is beneficial, they report that the procedure has relatively less impact than that of Discovery; more than 40 percent of the respondents utilizing the procedure felt that Discovery had a major impact on the judgment as compared with less than one-fifth in Pre-trial Conference. This could be attributed to the fact that the Pre-trial Conference is generally postponed until shortly before trial when the main issues have been hammered out and most of the money and time on pre-trial procedure spent. This explanation would support the argument for earlier introduction of the Pre-trial Conference and the earlier introduction of the judge into any other pre-trial procedures of the case.

There may be another advantage to bringing the judge in earlier. Reference to local court rules was most often referred to in responses on Pre-trial Conference. Formal introduction of the judge apparently requires additional procedural guidelines to assure expedition and the best use of the judge's time. Although some objection was voiced to local rules because of their sometimes unique character, the early introduction of rules aimed at conserving time of the Bench should also prove beneficial to the Bar, particularly if counsel is adequately prepared.

Separation of Issues was used in approximately one-third of the cases reported. Although less than for Discovery and Pre-trial Conference, this is not an inconsiderable number for this procedure since care must be exercised not to unduly fractionate the trial of a case. Two of the issues included in the reports as good candidates for Separation were

---

<sup>23</sup> Harris, *id.* at p. 68.

antitrust and misuse, particularly since their intrusion in infringement cases had increased substantially, burdening these cases with mountains of economic and other antitrust evidence. Other suggestions for Separation were for the most part to obtain the benefit of a dispositive issue such as prior public use.<sup>24</sup>

In cases involving antitrust and fraud defenses additional witnesses, extensive Discovery, lengthy trial and briefs, and an increase in complexity and number of issues were reported. "Separate out the antitrust or misuse defense and have the case tried first on a determinative issue," was one revealing way the suggestion was offered. Since both fraud on the Patent Office and the antitrust-misuse defense may involve, directly or indirectly, either intent<sup>25</sup> or inequitable conduct,<sup>26</sup> another approach (based on our interpretation of respondent sentiment) would be to seek the cooperation of counsel, through the medium of the judge, to simplify and clarify the issues, with a minimum of paper work, so the parties could know specifically what they were accused of as soon as possible sans elaborate procedure and voluminous documentation.

Good faith was particularly stressed in fraud on the Patent Office cases. Great care was advised in raising this issue because of the serious implications involved both legally and ethically. Although the defendant's attorney owes it to his client to raise every legitimate defense he can, the pleader should be reasonably certain of the facts—and should recognize that this type of pleading carelessly indulged in may boomerang. Once fraud is pleaded there might be a problem for defendant if he subsequently wants to settle.<sup>27</sup> Courts have not yet penalized defendants for losing on a fraud defense, but with the growing popularity of this defense and its indiscriminate use, the climate is likely to change.

Summary Judgment was utilized in only one-fourth of the cases reported. There is evident a reluctance of judges to make Summary Judgment determinations in patent cases. Some attorneys believe that simple cases, the good candidates for such determinations, are generally settled by the parties themselves. However, more than one-third of those using this technique thought it encouraged settlement. Summary Judgment appeared to be favored by those who were willing to chance the motion for the sake of expedition and economy if there was no

---

<sup>24</sup> Also see Malley, *id.* at pp. 117-118.

<sup>25</sup> *Cataphote Corp. v. DeSoto Chemical Coatings, Inc.*, CA 9, 450 F.2d 769; 171 U.S.P.Q. 736 (1971).

<sup>26</sup> *Norton v. Curtiss CCPA* (1970) 433 F.2d 779; 167 U.S.P.Q. 532 (1970).

<sup>27</sup> *IDEA*, Vol. 15, No. 4 (Winter 1971-72), pp. 679.

genuine issue of fact, the opposition counsel was willing to cooperate on the case fairly and squarely, and there was sufficient time to prepare and present argument so that there would be a determination on the merits not likely to be reversed on appeal.<sup>28</sup>

The major recommendations that evolve from the current study on reducing cost and delay in suit and increasing patent reliability fall into four categories. They are:

With Respect to the Large-Stake Case—

- (1) Both Bench and Bar be alert for the large-stake case and apply the other recommendations which follow with special care to such a case.

With Respect to Counsel—

- (2) Counsel be more frank and open with each other so they and courts cooperate in carrying the case forward.
- (3) Counsel be candid at the outset with client on potential costs, and advise with him concerning the overall implications of possible economies in the suit.<sup>29</sup>
- (4) Counsel be adequately prepared early in the case, including knowledge of local court rules.

With Respect to Judge—

- (5) Pre-trial Conference be introduced earlier.
- (6) The judge be introduced into Discovery and other pre-trial procedures earlier and, if possible, each case assigned to a particular judge.

With Respect to Procedures—

- (7) More attention be directed to simplifying and reducing issues.
- (8) Paper work be reduced and elaborate procedures eliminated (e.g., substituting oral presentation for written briefs where possible).
- (9) More specific pleading to reduce burden on Discovery.<sup>30</sup>
- (10) Discovery procedures, such as written interrogatories and requests for admissions, be carefully prepared to avoid aimless and prolonged investigation.
- (11) Reasonable limitations be placed on Discovery, avoiding undue hardship on the parties by the limitations adopted.

---

<sup>28</sup> Also see Malley, *supra* note 2 at pp. 118-120.

<sup>29</sup> Also see Francis C. Browne, *id.*, pp. 111-112.

<sup>30</sup> Also see Malley, *id.* at pp. 115-116.

- (12) A determinative issue be tried first.
- (13) Facts be carefully checked before introducing antitrust, misuse, or fraud defenses.
- (14) Summary Judgment be used in appropriate cases, allowing time for sufficient preparation.

Some of the recommendations do perhaps point in a different direction from certain changes that have been introduced into Rules of Civil Procedure in recent years. Also, the results do not necessarily correspond with the opinions held by a number of members of the Bar and critics of the system. The data herein gathered and the findings and recommendations, which reflect a cross-section of experience, may modify their views.

APPENDIX

THE PTC RESEARCH INSTITUTE  
THE GEORGE WASHINGTON UNIVERSITY

QUESTIONNAIRE

Please answer the following questions with respect to cases *terminated* by settlement, judgment, or dismissal during 1970.

	DISCOVERY	PRE-TRIAL CONFERENCE	SEPARATION OF ISSUES	SUMMARY JUDGMENT
1. Did you seek the procedure (i.e., Discovery, Pre-trial Conference, Separation of Issues, or Summary Judgment)?	Yes__No__	Yes__No__	Yes__No__	Yes__No__
a) How* and why?				
b) What results did it yield?				
2. Did your adversary seek the procedure?	Yes__No__	Yes__No__	Yes__No__	Yes__No__
a) Did you find any fault with his tactics?	Yes__No__	Yes__No__	Yes__No__	Yes__No__
b) If "Yes", what was it (e.g., procedure used for harassment, etc.)				

---

\*Check box if standard or form interrogatories were used

DISCOVERY

PRE-TRIAL  
CONFERENCE

SEPARATION  
OF ISSUES

SUMMARY  
JUDGMENT

3. Did you or your adversary file motion for court help? Yes\_\_No\_\_ Yes\_\_No\_\_ Yes\_\_No\_\_ Yes\_\_No\_\_

What was the outcome?

4. What is your estimate of the amount of *judicial* time that was consumed in this procedure?\_\_\_\_\_

a) Do you think the amount unreasonable? Yes\_\_No\_\_ Yes\_\_No\_\_ Yes\_\_No\_\_ Yes\_\_No\_\_

b) Did judge's intervention make attorneys better prepared? Yes\_\_No\_\_ Yes\_\_No\_\_ Yes\_\_No\_\_ Yes\_\_No\_\_

c) Did judge's intervention help to settle case, shorten trial time, or improve trial process?

d) Was the judge experienced in patent cases? Yes\_\_No\_\_ Yes\_\_No\_\_ Yes\_\_No\_\_ Yes\_\_No\_\_

5. Approximately how much time did you spend on the procedure?

6. Approximately what were your dollar costs on it?

7. What effect, if any, did the stake involved have:

a) on your use of the procedure? Explain

b) on your adversary's resistance to it? Explain

8. Did local court rules have any effect on the procedure? If "Yes", in what way? Yes\_\_No\_\_ Yes\_\_No\_\_ Yes\_\_No\_\_ Yes\_\_No\_\_



	DISCOVERY	PRE-TRIAL CONFERENCE	SEPARATION OF ISSUES	SUMMARY JUDGMENT
9. Did the use of the procedure have any effect on settlement? **	Yes ___ No ___	Yes ___ No ___	Yes ___ No ___	Yes ___ No ___
potential cost exerted economic leverage	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
exposed relative strength of the parties	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
other	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
10. What effect did the procedure have on quality of the trial? **				
a) educated you in advance of trial	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
b) prevented surprise at trial	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
c) assisted in ascertaining truth	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
d) Had i) a major effect or ii) a minor effect on the judgment in the case	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
e) i) shortened trial or ii) eliminated issues	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
f) i) helped or ii) hindered obtaining an injunction	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
g) tended to i) increase or ii) decrease amount of recovery	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
h) introduced i) irrelevant evidence, ii) unnecessary witnesses or iii) extraneous issues	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
i) other	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

\*\*If "Yes", please check one or more boxes. If "other" box is checked, state the effect in space next to the word "other".

	DISCOVERY	PRE-TRIAL CONFERENCE	SEPARATION OF ISSUES	SUMMARY JUDGMENT
11. If the procedure had been instituted earlier, what difference would it have made in disposition of the case? **				
a) judge would have been better educated on subject matter	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
b) judge would have been better able to obtain agreement of counsel that proof be made inexpensively	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
c) would have promoted settlement	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
d) other	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
12. Was the material or your objective obtainable other than by the procedure? If so, how?	Yes___No___	Yes___No___	Yes___No___	Yes___No___
13. What changes would you advocate so these procedures could have been better employed in this case? *				
a) would have preferred a time limitation on the procedure	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
b) would have preferred that the procedure be handled by a special officer of the Court with appeal to trial judge	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
c) other	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

\*\*If "Yes", please check one or more boxes. If "other" box is checked, state the effect in space next to the word "other".

\*\* Please check one or more boxes. If "other" box is checked, state the effect in space next to the word "other".

GENERAL QUESTIONS

14. Was your client a) the owner of the patent (s) Yes\_\_No\_\_  
b) the plaintiff\_\_or defendant\_\_
15. Do you believe that early and continuous control of the proceeding by the same judge who would have tried the case would have increased the speed and reduced the cost of litigation? Yes\_\_No\_\_
16. Was an antitrust defense or fraud on the Patent Office pleaded? Yes\_\_No\_\_  
a) did this require numerous additional witnesses? Yes\_\_No\_\_  
b) did this require extensive discovery? Yes\_\_No\_\_  
c) did the defense prolong litigation in any other way? Yes\_\_No\_\_  
If "Yes"? how?  
d) if fraud was pleaded, was inventor aware that claims read on work previously done? Yes\_\_No\_\_
17. Did the question of separation of issues come up in any other context in this case? Yes\_\_No\_\_  
If "Yes," how?  
If "Yes", were the issues divided so that those tried first could dispose of the case? Yes\_\_No\_\_
18. What were the dollar costs of the trial, if there was one, in this case?\_\_\_\_\_
19. Was the case decided in your client's favor? Yes\_\_No\_\_. If not, what was the decision?
20. Did you appeal the case? Yes\_\_No\_\_, or move for a new trial? Yes\_\_No\_\_
21. Was the trial court's decision sustained? Yes\_\_No\_\_  
If not, what was the appellate court's decision? \_\_\_\_\_
22. How long did it take to litigate this case? \_\_\_\_\_
23. Were you and your client satisfied with the outcome of the litigation? \_\_\_\_\_
24. Were you on a contingent fee\_\_\_\_\_or a retainer\_\_\_\_\_or salary basis?

# Experience Aspects of USSR Industrial Property Rights Protection\*

## INTRODUCTION

U.S. TRADE RELATIONS WITH THE USSR CONTINUE TO IMPROVE. While this situation is evident in trade statistics (Table 1), it is also reflected in the growth of licensing and technical interchanges and of patent and trademark protection between the two countries (Table 2).

Although there are basic divergencies between the economic organization of our free enterprise system and the Soviet "command economy," there is nevertheless an underlying uniformity in the two industrial property systems. This uniformity, manifested by governmental adherences to the "Paris Union" International Convention for the Protection of Industrial Property, has, actually, enhanced our trade relations with that country. The Convention's obligations on member countries to effect uniform standards of international patent and trademark procedures and to accord special advantages in this context to each other's nationals, have eliminated barriers that might otherwise militate against U.S.-USSR trade. This compatibility in industrial property rights protection may be strengthened by both governments'

---

\* This report was prepared by an Institute research team consisting of John C. Green, L. James Harris and Joseph M. Lightman.

TABLE 1  
U.S. EXPORTS TO AND IMPORTS FROM EASTERN EUROPE AND COMMUNIST AREAS IN ASIA, 1964-1970, AND JANUARY-JUNE 1971

COUNTRY	[THOUSANDS OF DOLLARS]									
	1964	1965	1966	1967	1968	1969	1970	JAN.-JUNE 1971		
	EXPORTS, INCLUDING REEXPORTS <sup>1</sup>									
TOTAL	339,926	140,010	197,738	195,260	215,024	249,288	353,645	202,812		
East European Areas	339,923	140,009	197,737	195,258	215,024	249,286	353,644	202,810		
Albania	19	8	166	56	8	18	4	16		
Bulgaria	5,020	3,613	3,631	4,219	4,036	4,645	15,294	3,521		
Czechoslovakia	11,338	27,685	37,336	19,155	13,956	14,363	22,512	23,909		
East Germany	20,211	12,413	25,152	26,329	29,047	32,373	32,545	12,770		
Estonia	.....	.....	.....	.....	2	.....	2	.....		
Hungary	13,753	9,327	10,053	7,570	11,194	7,252	28,263	15,805		
Latvia	1,807	.....	.....	.....	.....	.....	.....	387		
Lithuania	.....	.....	.....	.....	1	.....	.....	.....		
Poland	138,066	35,417	52,988	60,825	82,375	52,694	69,915	36,964		
Romania	5,156	6,385	26,686	16,796	16,680	32,394	66,399	36,923		
USSR	144,553	55,161	41,725	60,308	57,725	105,547	118,710	72,515		
Communist areas in Asia	23	21	21	22	.....	2	1	2		
China, including Manchuria	23	21	21	21	.....	2	.....	.....		
Outer Mongolia	( <sup>2</sup> )	.....	.....	.....	.....	2	1	.....		
North Korea	.....	.....	.....	.....	.....	.....	.....	.....		
North Vietnam	( <sup>4</sup> )	( <sup>4</sup> )	.....	.....	.....	.....	.....	.....		

Table 1 is continued on page 544

TABLE 1 (Continued)

TOTAL	GENERAL IMPORTS									
	102,305	141,590	182,179	179,814	200,755	197,819	226,514	120,973		
East European Areas	98,516	137,496	178,668	177,224	198,429	195,457	225,775	120,703		
Albania	102	113	109	335	283	396	151	134		
Bulgaria	1,177	1,666	2,529	2,814	3,731	1,598	2,431	1,995		
Czechoslovakia	12,706	16,741	27,695	26,241	23,756	24,063	23,892	12,397		
East Germany	6,686	6,537	8,194	5,647	5,934	8,018	9,394	5,301		
Estonia	96	13	113	55	67	20	72	17		
Hungary	1,693	2,092	2,985	3,884	3,848	4,077	6,224	4,241		
Latvia	418	12	18	34	16	9	16	724		
Lithuania	4	33	8	32	5	2	( <sup>3</sup> )	2		
Poland	54,202	65,861	82,948	90,960	96,871	97,835	97,946	57,564		
Romania	1,272	1,836	4,655	6,176	5,553	7,966	13,425	5,670		
USSR	20,160	42,592	49,414	41,046	58,365	51,473	72,224	32,658		
Communist areas in Asia	3,789	4,094	3,511	2,590	2,326	2,362	739	270		
China, including Manchuria	477	463	102	181	( <sup>3</sup> )	24	1	2		
Outer Mongolia	3,312	3,631	3,490	2,409	2,326	2,338	738	268		
North Korea										
North Vietnam	( <sup>4</sup> )	( <sup>4</sup> )								

<sup>1</sup> In these tables, the term "reexport" refers to an export from the U.S. of foreign origin goods. Elsewhere in this report, "reexport" refers to the shipment of U.S. origin goods from one foreign country to another.

<sup>2</sup> Figures shown include printed matter under general license and shipments to diplomatic missions of friendly foreign countries.

<sup>3</sup> Less than \$500.

<sup>4</sup> Not reported separately.

NOTE: Exports are shown by area of destination. Imports are credited to the area in which the merchandise was originally produced, not necessarily the area from which purchases and shipments were made. General imports represent merchandise entered immediately upon arrival into merchandising or consumption channels plus commodities entered into bonded customs warehouses for storage.

United States exports to North Korea were embargoed July 1950, and those to People's Republic of China, Manchuria, and Outer Mongolia were embargoed the following December. On Mar. 1, 1951, general export licenses to East European areas were revoked and the requirement of prior approval by license was extended to cover all exports to this area. On July 26, 1954, exports to North Vietnam were embargoed. Since mid-1954 the policy with respect to exports of nonstrategic goods to East European areas has been liberalized to some extent. In particular, a less restrictive policy with respect to Poland has been pursued since August 1957, and with respect to Romania since July 1964. On April 26, 1956, a general license was established authorizing the export without a validated license of certain commodities to Albania, Bulgaria, Czechoslovakia, East Germany, Estonia, Hungary, Latvia, Lithuania, Outer Mongolia, Poland, Romania, and the USSR, and in 1965 to the Maritime provinces of the USSR. This authorization was subsequently extended to additional commodities. In June 1971, a list of commodities eligible for export to the People's Republic of China under general license was published, and other commodities were made eligible for consideration for validated licenses. Pursuant to the Trade Agreements Extension Act of 1951, benefits of trade agreements tariff concessions were withdrawn from the USSR and other East European areas and an embargo was imposed on the import of certain furs from People's Republic of China and the USSR.

Imports from North Korea and the People's Republic of China were placed under license control on December 17, 1950, through the Foreign Assets Control Regulations of the Treasury Department. On May 5, 1964, license control of imports from North Vietnam was added to these regulations. In June 1971, a general license was established authorizing importation without restriction of goods from the People's Republic of China. Under the regulations in effect prior to June 10, 1971, the importation of goods from the People's Republic of China was prohibited without license by the Treasury Department, and it was generally contrary to the policy of that agency to license such imports, except goods for noncommercial purposes which, effective December 22, 1969, were permitted by general license. Some items of People's Republic of China origin, however, continued to appear in the statistical records of U.S. imports. In U.S. import statistics, goods originating in the People's Republic of China are credited to that country regardless of the last country from which they were shipped.

Source: U.S. Department of Commerce, 97th Quarterly Report, 3rd Quarter 1971, *Export Control* (November 15, 1971).

TABLE 2

## U.S.-USSR MUTUAL PATENT AND TRADEMARK FILINGS AND REGISTRATIONS

U.S. Activity in USSR						
	1965	1966	1967	1968	1969	1970
Patent applications	87	165	347	423	492	512
Patent registrations	2	3	35	65	82	199
Trademark applications	83	79	156	202	166	164
Trademark registrations	56	60	97	182	205	124

  

USSR Activity in U.S.						
	1965	1966	1967	1968	1969	1970
Patent applications	215	112	427	329	438	403
Patent registrations	28	66	115	95	159	218
Trademark applications	1	—	2	1	1	—
Trademark registrations	—	—	1	—	1	—

Source: World Intellectual Property Organization.

recent adherence to the World Intellectual Property Organization (WIPO), and by their eventual adherences to an international trademark registration agreement and the Patent Cooperation Treaty.

#### THE RESEARCH PROGRAM

The PTC Research Institute has had a research program under way for a number of years on the industrial property rights systems in Eastern Europe. The results of this research have been published in reports on pertinent laws, regulations, and legal decisions, as well as on applicable international arrangements and their impacts on East-West trade.<sup>1</sup> In the latest phase of this program, the Institute is seeking insights into experiences of Western nationals in acquiring and enforcing industrial property rights in Eastern Europe. A great deal of material is now available on Eastern Europe's patent and trademark laws and regulations, but not too much is known about day-to-day operating procedures and experiences in most of these countries,

<sup>1</sup> For list of articles published in *IDEA*, through Vol. 10, No. 4 (Winter 1966-67), see Institute publication *Patents, Trademarks and Copyrights in East-West Trade—What do you know about . . .* Guides to Institute Research. Subsequent articles are: "Inventors' Certificates and Industrial Property Rights," *IDEA*, Vol. 11, No. 2 (Summer 1967); "Domestic and International Trade Aspects of the USSR Trademark System," *IDEA*, Vol. 12, No. 2-3 (Summer-Fall 1968).



particularly regarding foreign prosecutions. The Institute, in this current project, has thus endeavored to provide factual and analytical information on these subjects for interested American businessmen, inventors, and legal practitioners. This information, supplementing that already available on the countries' patent and trademark laws, should provide to interested parties fuller insights than previously available on the practicalities of applying for and enforcing industrial property rights in that area.

#### THE RESEARCH APPROACH

As a sampling base for this survey, the Institute selected a group of leading international patent and trademark attorneys in Western Europe with experience in handling industrial property rights matters for Western clients<sup>2</sup> in Eastern Europe. These attorneys were sent a questionnaire soliciting views relative to their experiences on matters Western nationals have to deal with, other than compliance with the laws and regulations themselves, in securing patent and trademark protection in that area.

The questionnaire (Appendix A) sought insights on five basic aspects of their experiences in Eastern Europe, namely, the treatment accorded Western applications (expeditious processing, examiner cooperation, final grants, and differences in treatment of Eastern European nationals); the protection available against infringements; the adequacy of compensation in licensing; the usefulness of patents, and trademark registrations; and the desirability of obtaining inventors' certificates. The recipients were also asked to provide a case study on problems encountered in applying for and enforcing industrial property rights, and for any general comments on Eastern European attitudes affecting Western nationals' abilities to secure and enforce such rights.

Replies were received from 35 practitioners located throughout Germany, France, Belgium, Netherlands, Italy, Norway, Sweden, Denmark and Switzerland. A number of the replies included supplementary material which either explained the responses in considerable detail or presented a comprehensive discussion of the subject. The following data and analyses on the USSR derives from these replies. A report on other Eastern European countries, also derived from the questionnaire replies and now in process of preparation, will appear in a forthcoming issue of *IDEA*.

---

<sup>2</sup> Clients in the U.S. include not only business concerns but patent and trademark attorneys representing U.S. business interests.

## EXPERIENCES AND ATTITUDES IN THE USSR

Virtually all of the respondents had submitted applications for filing in the USSR or had otherwise had some experience relative to patent and trademark practice on behalf of their clients in that country. The more comprehensive replies came from France, Germany and Sweden.

A summary of the basic features of Soviet patent and trademark laws appears in Appendix B.

*Treatment in Application Processing and Registration*

Most of the respondents felt that patent and trademark applications filed with the Committee on Inventions and Discoveries,<sup>3</sup> through the USSR Chamber of Commerce, were processed in a satisfactorily expeditious manner. Typical of most responses was that of the attorney who stated:

I have filed several patent applications in the Soviet Union. Notwithstanding the difficulty of translation, the applications have been filed quite expeditiously within the Convention periods. Official actions are issued in Russian language and the periods set for reply are generally short. However, by a careful prosecution of the cases, I have been able to obtain the patent in many instances.

One firm did believe that the processing was "slow," noting two to three years between filing and registration.

As to cooperation of Soviet examiners in allowing access to references, answering questions, and facilitating other desired contacts, French and German respondents had the more satisfactory experiences, compared to the others in the sampling base. One French firm remarked:

An examination on novelty and patentability is conducted, and we can add that the discussions with the Examiners are quite open; the Examiners are well-qualified, and we recommend interviews which facilitate the allowance of the applications.

Another noted that ". . . for Frenchmen there is no difficulty to have more time to answer the examiner. The USSR Chamber of Commerce in Moscow gives all references I need."

German attorneys characterized their experiences in terms of "ade-

---

<sup>3</sup> The Soviet "Patent Office"; all applications must be filed through the USSR Chamber of Commerce's Patent Bureau.

quate cooperation" and "no difficulties" with USSR examiners. An attorney with extensive experience in that country elaborated as follows:

It has now become common practice that the applicant will discuss matters [on first rejection] with the examiner until one of them gives way. Sometimes, these discussions can last for years and usually it is the applicant who gives up because the economic interest in the invention will, by the time, probably have been lost in 98 percent of cases. Lengthy discussions with the examiner, however, also have their good points for the applicant because, like in all countries, the examining procedure is being further developed and the Soviet Patent Office, I should like to say as one of the few patent offices in the world, is prepared to admit its own faults and to correct them. We have seen that applications that had unjustly been rejected were reinstated after years and that patents were finally granted on them.

Other respondents generally reflected the above views regarding their experiences with Soviet examiners, except two attorneys who were very critical. One said that examiner cooperation was "Definitely bad." Another remarked:

The Soviet Union seems to represent one end of the scale.<sup>4</sup> The communication between applicant and patent office is unsatisfactory, partly due to language difficulties. There is a noticeable un-sureness and in consequence in the administration. The ability of the Board of Appeals is said to be of varying degree.

There were no difficulties or problems reported by respondents in securing final patent grants and trademark registrations, once the applications were allowed, the fees paid, and the material published. There were complaints, however, about the unusually high fees for final registrations and for annual maintenance of patents in force.

The respondents reported, in general, that they were not aware of any differences in Soviet treatment of Western applications and those received from Eastern Europe. None stated that they had experienced discriminatory treatment.

### *Infringement Proceedings*

The respondents were also unaware of any infringement of their clients' patents in the USSR. Only one trademark infringement case—

---

<sup>4</sup> [With respect to variations in procedures of Eastern European industrial property rights protection systems.]

*Gevaert-Agfa*<sup>5</sup>—was mentioned. The situation on lack of infringement experiences is perhaps best explained by the respondent who was of the view that:

. . . there is a socialist moral sense which inhibits plants from committing an act of infringement with full knowledge. It is generally felt that there is no necessity to "borrow" from abroad, especially capitalist countries. It would be contrary to the Russians' pride. As the enterprises have to inform the planning commission on any new development, they first investigate whether there is anything against it. Furthermore, they check whether according to prior world art this introduction may possibly be obsolete and a new development may be in progress in international techniques that might be preferable. I can imagine acts of infringement to be committed by Soviet plants only if matters are unclear and if errors have occurred in the bureaucratic procedure between application, production and examination. Infringements of patent rights are not considered a minor unlawful act in the Soviet Union as, for instance, drunken driving with us. The responsibility of the individual plant manager is too great, penalties are too high and the interest is low. It cannot be foreseen how matters will stand once the new process of liberalization and transfer of responsibility to the individual enterprises is established. I am convinced, however, that even then we should not expect any sharp increase in patent infringement proceeding from zero to one hundred percent.

#### *Adequacy of Compensation in Licensing*

The Institute sought to determine whether Western patent and trademark owners had had difficulty in securing adequate compensation where licenses had been negotiated voluntarily with State enterprises, or where the State had ordered compulsory licensing, or had otherwise made use of their property rights without authorization.

Most of the respondents reported little experience of their own in licensing contacts with Soviet enterprises. Presumably, their clients had conducted the actual licensing arrangements with State enterprises through other channels. Some respondents noted that the Soviets were hard bargainers but once they signed, such agreements were carefully observed and fulfilled.

#### *Views on Desirability of Patent and Trademark Protection in USSR*

Most of the respondents agreed that it was worthwhile to have such protection in Eastern Europe. A few singled out the USSR in this

---

<sup>5</sup> For details on the case, see "Domestic and International Trade Aspects of the USSR Trademark System," *supra* note 1, p. 805.

context by noting the particular desirability of securing patents and trademark registrations in that country to facilitate sales of the relevant goods.

It was generally agreed that in the USSR patents would not only be valuable as exclusive rights to prevent others from using the subject matter, or making, selling, and importing products thereunder, but also in establishing legally recognized proprietary rights for licensing activities with State enterprises. Use of patents for advertising purposes was also considered by certain respondents as a highly worthwhile purpose. The importance of trademarks to Western firms in the USSR as marketing, advertising, and quality indication tools was also emphasized. Growing possibilities for consumer selectivity, facilitated by trademarks, and enhanced by increased availabilities in the USSR of consumer goods from domestic and foreign sources, was readily apparent to the respondents.

#### *Views on Desirability of Securing Inventors' Certificates*

The practitioners generally did not believe it worthwhile for Western nationals to apply for inventors' certificates.<sup>6</sup> Reasons included renunciation of proprietary rights in the invention, remuneration too small, and benefits inapplicable to Westerners (status, better housing, promotions, etc.).

Some, however, did mention cases where it had been to their Western clients' advantage to secure inventors' certificates in the USSR. In one instance, the client had undertaken a technical assignment and sales agreement with a State enterprise and had initially applied for an inventor's certificate on pertinent subject matter "only to give a legal basis to the agreement." Others noted that their clients had applied for inventors' certificates on food and pharmaceutical products, for whatever compensation might be obtainable, since such subject matter is not patentable. One attorney suggested that if a Western firm's basic interest in the USSR was market penetration, and it "wants to demonstrate its own products, its trade name and its economic possibilities," the firm might find it expedient to apply for inventors' certificates "which are cheaper economically" than patents.

Cases were also brought to the Institute's attention where foreign owners of Soviet patents had converted them into inventors' certificates,

---

<sup>6</sup> For history and explanation of inventors' certificates, see article "Inventors' Certificates and Industrial Property Rights," *supra* note 1.

primarily because of the high patent maintenance fees. Such owners, finding that they could not sell or license their patents in the USSR, in effect, turned the inventions over to the State for inventors' certificates in the hope that they might eventually receive some remuneration, if used. There are no fees for acquiring or maintaining inventors' certificates.

### *Case Studies and General Comments*

The case studies and comments received from respondents elaborated primarily on Soviet examining procedures. While the attorneys generally had no complaints about the cooperation received from Soviet examiners, their views on examiners' competence were mixed. Experiences were also described on patenting in specialized fields and on trademark registrations. Excerpts of the respondents' views on these subjects follow:

#### Administrative Aspects of Examinations

. . . in Russia, as distinct from other Eastern European countries, examiners take a less legalistic approach to what constitutes invention, as we are used to. This may be due to the normal practice of dealing with inventors' certificates. However, as the principle of the law does not differ, careful wording in the application and additional explication of the inventive legal concept is apt to overcome misunderstandings on the side of the examiner.

\* \* \*

In Moscow I have often had problems stemming from the tendency of the Russian Examiners to force Applicant to limit his claim to the embodiment described for the purpose of exemplifying the inventive idea. Also disturbing is their inclination to refuse sub-claims and their way of construing the unity rules. . . . I am convinced that the major reason of the unsatisfactory and "jerky" practice in Moscow is not offensive in nature but caused by unsatisfactory professional training and lack of long-time experience which shows up as an uncertainty as to how to judge patentability issues. They are simply underdeveloped.

\* \* \*

In the USSR much work has to be done here since the USSR Chamber of Commerce does not usually play the part of a correspondent. The results are much better if correspondence takes place in Russian.

## Technical Aspects of Examinations

The examination proceedings are very well carried on by the examiners who appear as competent and qualified persons. However, . . . the grant relating to the cosmetic compositions requires the execution of toxicologic and allergic tests but the clinical tests have been suppressed on such above mentioned points. The examiners of the Soviet Union are very severe.

\* \* \*

A client filed a Russian patent application for a flax treating machine. The patent was granted but immediately confiscated by the Russian State. The compensation was approx. D. gld. 5000.—! [sic] Nothing could be done to change the situation. This experience dates from before the second world war.

An inventor filed in Russia a patent application for paving bricks. The application was rejected because in Russia the roads are only paved with asphalt but not with bricks!

A patent application in Russia was rejected because its subject matter had already been applied in Russia in the village of L. It was impossible to check whether this was true. We could not even trace where the village of L. was situated!

\* \* \*

In one of my patent applications filed in the Soviet Union the examination proved to be of a rather low standard. I informed the Patent Office on the prior art very accurately and it was obvious that the invention differed essentially from what was known as prior art. Nevertheless, the application has been rejected with reference to a French patent the subject of which was exactly equivalent with the prior art referred to by me. (Then I appealed from the decision and obtained a favourable result before the Board of Appeals.)

\* \* \*

As a rule, the quality of examination [in the USSR] may be termed good in varying nuances. The examination of chemical inventions, for instance, is very good, the organic ones taking the lead followed by inorganic chemistry, plastics, dye colors, dyeing procedures, chemical engineering, electrical engineering, and finally inventions dealing with medicine.

\* \* \*

In Russia the practice as to uniformity of the invention is very strict. High requirements for technical progress and inventiveness. . . In the pharmaceutical field many details are required on the activity in special fields of medicine.

## Trademark Procedures

As to infringements we could enforce a registered trademark in Russia rather quickly by writing to the competent ministry.

\* \* \*

. . . in Russia matters of trademark cases are treated with the greatest fancy and unpreciseness. Unexplained procedure is a cause for unexplained monetary charges difficult to justify and impossible to discuss with the Russian Administration, completely anonymous.

## CONCLUSIONS

The information obtained from the Institute's sampling base is enlightening relative to patent and trademark prosecution experiences in the USSR. It is readily apparent that the USSR is adhering to the spirit as well as the letter of the "Paris Union" Industrial Property Convention. No respondent complained of discriminatory treatment, or of inaccessibility to Soviet administrative or judicial procedures, or of denial of Convention benefits. The type of complaints that were received, such as those related to examiner competency, technical strictness, high costs, and communication difficulties, are not peculiar to "command economies" but may be applicable to many patent systems outside of Eastern Europe. Procedurally, it was evident from the replies that there were no insuperable administrative peculiarities affecting foreign acquisition of industrial property protection. Although foreign applicants might be faced with some difficulties in claims specifications and in translations, there were, on the other hand, no special problems indicated by reason of State enterprise philosophies.

While inventors' certificates continue as the dominant form of inventor recognition in the USSR, it is evident that the Soviets are upgrading the importance of patents in that country to foreigners. There are clear indications from the respondents' comments that the Soviets are conscientious about affording to Western patent and trademark owners full and effective recognition (1) of exclusive rights in their patent grants and trademark registrations and (2) of protection against their infringement, in the USSR.

Nothing in the replies suggested a negative attitude towards seeking industrial property rights protection in the USSR. The attorneys generally believed that trade factors should be the governing considerations. Not at all mentioned were negative considerations based on possible compulsory licensing, expropriation or other impairment of



such rights. The respondents were not without criticism of various aspects of Soviet procedures. However, this did not detract from an overall awareness, inherent in the replies, of Soviet policy respecting Western-owned patent and trademark rights. There were no concerns apparent from the replies that the USSR would not afford equal treatment to Westerners or abide by the "Paris Union" Convention's commitments.

#### APPENDIX A

#### THE PTC RESEARCH INSTITUTE OF THE GEORGE WASHINGTON UNIVERSITY

##### QUESTIONNAIRE ON SITUATION RE EXPERIENCES IN EASTERN EUROPE

1. How would you characterize, generally, the treatment accorded in those Eastern European countries with which you have had experiences (please identify countries), with specific reference to:
  - a. expeditious processing of applications?
  - b. cooperation of examiners and other Patent Office personnel in allowing access to references, answering questions, facilitation of other desired contacts?
  - c. opposition proceedings involving:
    - i. an East European national?
    - ii. a national from other communist regimes?
    - iii. a national of another Western country?
  - d. final granting of the patent and/or trademark registration?
  - e. other obvious differences in the Eastern European countries you have identified between the treatment accorded to applications of other bloc nationals and nationals of Western countries?
2. Please describe any experiences you have had to indicate whether or not Western patent and trademark owners have been able effectively to protect their patents and/or registrations against infringements.
3. Please describe if you are aware whether such owners have had difficulties in securing adequate compensation in:
  - a. ordinary cases where licenses have been negotiated with State enterprises:
  - b. where the State has ordered compulsory licensing by the patent owners:  
or
  - c. where the State has otherwise made use of industrial property rights of foreign nationals:
4. Please explain whether you do, or do not, believe it is worthwhile at present for Western firms to apply for patent and/or trademark registrations in Eastern European countries.
5. Please explain whether you do, or do not, believe it worthwhile at present for Western firms to apply for inventors' certificates.  
Also note your experiences as to whether or not Western firms have benefited from use of inventors' certificates regarding compensation and protection of rights.

6. We would be interested in a brief description of any particular case study you may wish to offer with respect to problems encountered:
  - a. in applying for and obtaining a patent or trademark registration, and/or
  - b. in enforcing such a right against infringement or other usurpation:
7. We would appreciate receiving any other general comments you may wish to offer on Eastern European attitudes affecting Western nationals' abilities to secure and enforce industrial property rights in any or all of the countries with which you have had experiences.

## APPENDIX B

### SALIENT FEATURES OF USSR PATENT AND TRADEMARK LAWS

#### Convention Membership

"Paris Union" International Convention for the Protection of Industrial Property (Latest text adhered to is Revision of Stockholm in 1967)  
World Intellectual Property Organization

#### Patent Law Features

Law's effective date: May 1, 1959  
Patent Duration: 15 years from application filing date  
Novelty Disqualification: If invention known anywhere  
Novelty Examination: Yes  
Opposition: None  
Compulsory Working: None in law  
Compulsory Licensing: None in law  
Non-patentable subject matter: Medicinal and chemical products and foodstuffs;  
inventions contrary to law or morality

#### Trademark Law Features

Law's effective date: June 23, 1962  
Registration Duration: 10 years from application filing date  
Examination: To determine if registered in the country; or otherwise excluded  
under the law from registration  
Opposition: None  
Compulsory Use: None in law  
First Registration Accords Exclusive Rights: Yes  
First User: Not entitled to recognition of rights if mark not registered

# The Commercial Value of Patented Inventions

RICHARD L. SANDOR\*

## SUMMARY

THE PURPOSE OF THE CURRENT RESEARCH has been to determine the value of inventive activity by a direct method and to compare a direct and indirect approach. The results suggest that the direct method is reliable. The results are consistent with the original attempts to determine the value of inventive activity. An indirect method developed by F.M. Scherer is incompatible with the direct method.

---

## INTRODUCTION

PATENT STATISTICS HAVE FREQUENTLY BEEN USED in the growing body of empirical studies concerned with inventive activity and related areas. Their advantages and disadvantages have been a constant source

---

\* Assistant Professor, School of Business Administration, University of California, Berkeley. The author wishes to thank the National Science Foundation and the Institute of Business and Economic Research of the University of California for their generous support.

TABLE 1

Net Gain Or Loss From Patent	In Current Use		Past Use		Never Used	
	Num- ber	Per- cent	Num- ber	Per- cent	Num- ber	Per- cent
(1)	(2)	(3)	(4)	(5)	(6)	(7)
Total Number	23	23	8		8	
Percent		100.0		100.0		100.0
Gain	22	95.7	7	87.5		
over \$1,000,000	2	8.7				
\$500,000-1,000,000	2	8.7	1	12.5		
\$100,000-499,000	5	21.7				
\$50,000-99,000	3	8.7	2	25.0		
\$15,000-49,999	4	17.4				
\$5,000-14,999	6	26.1	1	12.5		
Under \$5,000	0	0	3	37.5		
No gain or loss	1	4.3			3	37.5
Loss			1	12.5	5	62.5
\$3,000-4,999					2	25.0
\$5,000-9,999					1	12.5
\$10,000-25,000					2	25.0

of debate.<sup>1</sup> The availability of the data is one of the principal reasons for its use in various research efforts. Alternatively, the fact that these statistics do not reflect quality differences in the inventions which they represent is a severe handicap. Research devoted to determining the value of the underlying inventiveness would be extremely useful in evaluating past work which used patent statistics and might help in suggesting topics for future investigation. In a seminal article which appeared in this journal, Sanders, Rossman, and Harris<sup>2</sup> published findings on the value of patented inventions. In subsequent research Scherer<sup>3</sup> developed an indirect procedure for determining the value of inventive activity. The research devoted to determining the value of patented inventions appears to be limited to the direct survey procedures of Sanders and the indirect of Scherer. The current research attempts to shed further light on the commercial value of patented inventions in the following two ways: (1) reporting the findings concerning the value of patented inventions from a subsequent independent sample and comparing those to the results of Sanders, and (2)

<sup>1</sup> See, for example, Jacob Schmookler, *Invention and Economic Growth* (Cambridge: Harvard University Press, 1966).

<sup>2</sup> Barkev S. Sanders, Joseph Rossman, L. James Harris, "The Economic Impact of Patents," *PTC J. Res. & Ed. (IDEA)*, Vol. 2, No. 3 (September 1958), p. 340.

<sup>3</sup> F. M. Scherer, "Corporate Inventive Output, Profits, and Growth," *Journal of Political Economy* (June 1965).

TABLE 2

Utilization Status	Number	Approximate Net Gain Mean	Number	Approximate Net Loss Mean
In Current Use	22	353,769	0	
Used in past	7	85,895	1	170,000
Never used	—	—	5	9,530

determining if results of the indirect and direct procedures are compatible. During the course of the latter, Scherer's model will be slightly modified.

The population used in this study is the same as Scherer's sample which consisted of 448 firms on *Fortune's* list of the 500 largest industrial corporations. There were 365 firms in this group having one or more patents assigned to them in 1959. In particular, 31 had exactly one patent, while the remaining had two or more. One or two participants were selected at random from each of the particular firms. Questionnaires concerned with the particular sampled patent (s) were sent to the firms. Follow-up letters and questionnaires were sent to the firms which did not respond to the original inquiries. There were 282 questionnaires returned from 159 firms.

Among other things, the questionnaires requested information on the utilization status of the sampled patent and the cumulative profitability of the patent.<sup>4</sup>

Data regarding profitability was supplied for 39 patents. Of the 39, 4 had zero profits, 5 had losses and the balance were profitable. The mean value of profits for the entire group of inventions was \$209,583. This figure represents the firm's estimate of cumulative profitability of the invention from initial use to 1965. The results of the questionnaire are further summarized in Tables 1 and 2. Tables 3 and 4 represent the findings as reported by Sanders *et al.* There is a striking amount of

---

<sup>4</sup> The specific questions were "3. Is the patent currently being used in production (use in production refers to making or selling the patented invention or used in the production of goods and services) —yes—no . . . has it been used in production?—yes—no." And "14. If the patent is being used, please estimate the total pre-tax net gain or loss which has occurred to the present time (net loss means all expenses incurred inventing, patenting, and/or developing the sampled invention for commercial exploitation, plus market survey costs plus actual production costs, less the total income realized to date from sales, royalties, inventory, etc. derived from the sampled patent. Net gain represents the excess of income from sales, royalties, inventories, reduction of costs, etc.—all the expenses incurred in inventing, patenting, and/or developing the sampled invention for commercial exploitation, plus survey costs etc. plus actual production costs) —gain—loss."

similarity in the findings. The net mean gain for those patents in use was \$577,000 for Sanders and \$353,769 for the current study. The approximate net gain for those patents which were used in the past was \$72,000 for Sanders' study and \$85,895 for the current study. The figures regarding patents never used and those showing losses are less similar. It is difficult to determine how comparable the results are

TABLE 3<sup>5</sup>

Net Gain or Loss From the Patent	In Curent Use		In Past Use		Never Used	
	Number	Percent	Number	Percent	Number	Percent
(1)	(2)	(3)	(4)	(5)	(6)	(7)
Total: Number	81	81	53	53	147	147
Percent		100.0		100.0		100.0
Gain:	65	80.2	24	45.3		
over \$1,000,000	5	6.2	—	—		
\$1,000,000-\$500,000	7	8.6	1	1.9		
\$499,999-\$100,000	6	7.4	2	3.8		
\$99,999-\$50,000	3	3.7	4	7.5		
\$49,999-\$15,000	14	17.3	4	7.5		
\$14,999-\$5,000	13	16.1	6	11.3		
under \$5,000	7	8.6	2	3.8		
net gain/no amount	10	12.3	5	9.5		
No gain or loss	8	9.9	18	33.9	27	18.4
Loss:	8	9.9	11	20.8	120	81.6
under \$500	—	—	—	—	8	5.4
\$500-\$999	—	—	1	1.9	27	18.4
\$1,000-\$1,999	1	1.2	—	—	15	10.2
\$2,000-\$2,999	—	—	1	1.9	14	9.5
\$3,000-\$4,999	1	1.2	—	—	12	8.2
\$5,000-\$9,999	1	1.2	2	3.8	16	10.8
\$10,000-\$25,000	1	1.2	6	11.3	14	9.5
over \$25,000	3	3.9	1	1.9	2	1.4
net loss/no amount	1	1.2	—	—	12	8.2

<sup>5</sup> Sanders *et al.*, *supra* note 2.

TABLE 4<sup>6</sup>

Utilization Status	Number	Approximate Net Gain Mean	Number	Approximate Net Loss Mean
In current use	55	\$577,000	7	\$88,000
Used in the past	19	72,000	11	14,000
Future use	—	—	23	12,000
Never used	—	—	108	4,500

<sup>6</sup> *Ibid.*

TABLE 5<sup>8</sup>

RESULTS OF REGRESSIONS: LAGGED PROFITS ON PATENTS, GIVEN OTHER VARIABLES

Year	Given 1955 Sales and Slope Dummies	
	Partial r: $\pi_{ti}$ on $P_i$	Regression Coefficient (Profit Dollars per Patent)
1955	.145	71,830 (26,300)
1956	.224	118,340 (27,500)
1957	.116	51,640 (23,700)
1958	.268	147,070 (28,300)
1959	.039	22,780 (31,300)
1960	.188	105,220 (29,500)

<sup>8</sup> *Ibid.*

because the sample sizes were different for the two studies. The current research deals with a distinctly larger group of firms.

It should be noted that Table 4 has been modified so it is comparable to the current research and facilitates the comparison of distributions. The distributions of gains for those patents being used have certain similarities. The percentages of patents with gains of over \$500,000 is small in both cases. The current research has a greater concentration of inventions with gains from \$100,000 to \$499,000. In the current sample the inventions which were used in the past were more profitable and those which were never used exhibited less losses. However, the small sample size makes it impossible to draw any definitive conclusions.

The first part of the last section of this paper will be devoted to describing Scherer's model and to summarize his results. The regression model hypothesized is given by

$$\pi_{ti} = a + (b_1 + \sum_{j=2}^m b_j d_{ji}) S_{si} + cP_{si} + u_i$$

where  $\pi_{ti}$  is the dollar volume of profits of the  $i^{\text{th}}$  firm in period  $t$ ,  $P_{si}$   $S_{si}$  is sales  $d_{ji}$  is an industry dummy variable and  $u_i$  is an error term. It was proposed that profits were a function of patents conceived in an

TABLE 6

RESULTS OF REGRESSION: LAGGED PROFITS ON PATENTS, GIVEN OTHER VARIABLES

Year	Given 1955 Sales and Slope Dummies	
	Partial r: $\pi_{t1}$ on $P_1$	Regression Coefficient (Profit Dollars per Patent)
1955	.069	73,266 (56,484)
1956	.18477	228,267 (65,084)
1957	.16407	193,847 (62,475)
1958	.32810	368,583 (56,885)
1959	.23186	264,164 (59,411)
1960	.14066	155,356 (58,619)

earlier period. Scherer was also interested in the effect of patented inventions holding firm size constant and industry structure constant. The empirical results of the Scherer study are presented in Table 5.

The coefficient in Table 5 can be interpreted as an estimate of the profitability of a typical patent. As Scherer indicates "Considering the adverse effect of the 1958 recession on 1959 profits, the 1958 figure of \$147,000 in after-tax profits per patent seems to be the most suitable candidate as the equation 1 estimator."<sup>7</sup> He continues to point out some of the difficulties in interpreting the results because of statistical difficulties such as multicollinearity.

However, it is not really the total number of patents which a firm has assigned to it which increase profit but only those which are used. The aggregate number of patents may tend to over- or underestimate the effect of inventive activity on profits. If the independent variable was the number of patents being used, then the coefficient in equation 1 would represent the profitability of an average patent being utilized. Since the proportion of patents being used is not independent of firm size, the original model had the econometric difficulties associated with error in variables.

The current research was devoted to reformulating the hypothesized

<sup>7</sup> Scherer, *supra* note 3.



regression model by substituting the number of patents being used by the firm for the total number of patents assigned to the firm. For purposes of this study the firm sizes were classified into deciles. The use rate within the decile was then computed. In order to obtain an estimate of the number of patents used, the latter number was multiplied by the number of patents the firm had. This procedure certainly has many drawbacks. However, in previous studies it has been shown that firm size and use rate were definitely related. Because of the limitations of this method, the results should certainly be considered as suggestive rather than conclusive. The first regressions were run using the use rates in the sample and then applying these use rates to the entire Scherer sample. The results are summarized in Table 6.

Although the results appear to be very similar to Scherer's, it must be recalled that the model is somewhat different. This indicates that the average used patent given the slope dummies is 368,583. Since the use rate for the entire sample was .52, this suggests that the average value of all patents with Scherer's original formulation is approximately \$191,662.

Accounting for differences in use by firms of different sizes results in a new estimate of the average value of a used patent. Since large firms have lower use rates, the weighting scheme results in less importance being given to the patents of larger firms and more importance given to the patents of smaller firms. The result is to raise the estimated average value of used patents.

It is now interesting to compare the results of the direct and the indirect method. The former indicated that the cumulative gain before taxes was \$353,769 and the latter indicated an annual gain after taxes of \$368,583. This suggests that the two methods are not compatible. There is insufficient evidence to determine if either of the methods is valid. It is apparent that future research devoted to developing alternative but consistent methods of determining the value of patents is indicated.

# Patent Statistics As a Surrogate for Spending: A Case Study of Patents Relating to Acoustics and Noise Abatement

MARY A. HOLMAN\* AND JAMES T. BENNETT\*\*

## INTRODUCTION

STATISTICS ON PATENTING ACTIVITIES have been used to analyze a number of important political, social, and economic questions. Patent statistics have provided insight about such diverse matters as concentration and monopoly control, the effectiveness of corporate investment policies, geographic differences in the stringency of interpreting anti-trust laws, and changes in the direction of technology as it relates to economic growth.

The purpose of this article is to show another use for patent statistics—as a surrogate for expenditure data in the absence of information about past spending patterns for research and development. A surprising finding of the study is that the private sector of the economy has probably spent much more money on research and development than the federal government in at least one area that relates to the

---

\* Associate Professor of Economics, The George Washington University.

\*\* Assistant Professor of Economics, The George Washington University.

TABLE 1

ESTIMATE OF FEDERAL SPENDING FOR PROGRAMS RELATED TO NOISE, FISCAL YEARS 1968 TO 1971

Federal Agency	1968	1969	1970	1971	Total
NASA	b	21.6	24.7 <sup>c</sup>	22.3	103.3
Department of Transportation	10.0	3.2	5.3	8.9	
Department of Defense <sup>a</sup>	b	2.1	2.7	2.5	
Health, Education, and Welfare	0.8	1.0	1.1	1.4	
Department of Commerce	0.2	0.3	0.4	0.5	1.4
Housing and Urban Development	0.3	0.3	0.5	1.0	2.1
Department of the Interior	b	b	0.5	0.5	1.0
Total	11.3	28.5	35.2	37.1	112.1

<sup>a</sup> Primarily spending by the Air Force.

<sup>b</sup> Not available.

<sup>c</sup> Includes \$4.67 million for NASA Acoustics Facility.

Sources: Data for 1968 and 1969 from Stanford Research Institute, Long Range Planning Service, *Noise Pollution Control* (Menlo Park, California: October 1970), p. 6. Data for 1970 and 1971 from an unpublished report, Cabinet Committee on the Environment, Subcommittee on Noise, Secretary of Commerce, Maurice H. Stans, Chairman (1970).

preservation of a high quality environment. That research area covers problems relating to noise and its abatement.

The first part of the article presents information about private and federal expenditures for noise-related activities. The second part of the article shows how patent statistics can be used to estimate the relative size of R&D expenditures for noise-related problems in the public and the private sectors.

#### *Federal Expenditures for Noise-Related Problems*

Although federal spending for noise-related research activities has been growing in recent years, the total for fiscal years 1968 through 1971 is estimated to be slightly more than \$110 million. As the data in Table 1 show, between 60 and 70 percent of total federal spending for noise-related problems was made by the National Aeronautics and Space Administration, primarily for research and development activities for the Quiet Engine Program and also for the Super-Sonic Transport (SST) Program before it was cancelled.

An unpublished report prepared by the Subcommittee on Noise of the Committee on the Environment indicates that in fiscal year 1970 about 95 percent of total federal spending for noise-related activities

was directed toward problems associated with aircraft noise.<sup>1</sup> The share going to aircraft noise was about 85 percent of the total in fiscal year 1971. This means that in recent years less than five percent of federal spending on noise-related programs has been directed toward highway, industrial, and other noise abatement programs. The Long Range Planning Service of the Stanford Research Institute forecasts that federal spending for aircraft noise abatement will decrease in relative importance as the federal government allocates more resources to reduce other sources of noise.<sup>2</sup> In contrast to R&D spending for noise abatement, the federal government spent \$163 million on air and \$829 million on water-pollution control and abatement activities in fiscal year 1970, according to the first annual report of the Council on Environmental Quality.

### *Private Spending for Noise-Related Problems*

Although a few estimates have been made for individual programs, no estimate presently exists on the amounts that private industry has spent either for research or for other programs that relate to noise-abatement problems. For example, the Air Transport Association of America estimates that the airlines and aircraft manufacturers spent about \$200 million for the research, development, and installation of noise suppressors for the first commercial jets.<sup>3</sup> Some other examples of the kind of information about private spending for noise reduction include the two following case studies that do not relate to R&D expenditures: spending at a General Electric plant and at a paper mill.

At a General Electric plant in Evandale, Ohio, there was a large office area adjacent to the factory. The advertising and product information employees who worked in the office were distracted by noises emanating from the factory and complained about the unusually high noise levels. The plant's industrial hygienist agreed that they had a legitimate complaint and decided to re-suspend the ceiling, soundproof the doors, and acoustically treat the walls. The cost of these modifications was about \$10,000.<sup>4</sup>

---

<sup>1</sup> Cabinet Committee on the Environment, Subcommittee on Noise, Secretary of Commerce, Maurice H. Stans, Chairman, Unpublished Report Prepared in 1970.

<sup>2</sup> Stanford Research Institute, Long Range Planning Service, *Noise Pollution and Control* (Menlo Park, California: October 1970), p. 6.

<sup>3</sup> *Air Transport Association of America, A Fact Sheet on Aircraft Noise Abatement* (January 20, 1970).

<sup>4</sup> Large Jet Engine Division of General Electric, correspondence with the National Bureau of Standards, Building Research Division (Summer 1970).

Another industrial noise-abatement project took place at an eastern paper mill that installed a wood chipper to speed up production.<sup>5</sup> The chipper cut logs into small chips and blew them from the chipper room into digesters through a system of pneumatic tubes. The operator who monitored this process was exposed to noise levels well above all hearing-damage risk criteria. To solve this problem, a booth was constructed from which the operator could monitor the chipper. The amount spent for this action was around \$2,500.

### *Patents As a Surrogate for Spending*

Patented inventions are an important output of research and development expenditure. The literature on research and development as well as economic growth reveals that patented inventions have been used as a measure of scientific and technological output. The principal justification for using patenting activity as a measure of scientific progress is that a patent passes a recognition or acceptability test (i.e., examination in the Patent Office) for describing an invention that does in fact contribute something new. Because of the lack of available data on spending, patents are used here as a surrogate of research input or expenditures rather than as a surrogate for output, i.e., the value of research and development expenditures.

The use of patented inventions as a measure of spending for noise-related problems is not precise for a number of reasons. First, there is no way to know whether the cost of an "average invention" remains the same over time. Second, there is no way to ascertain if the ratio of spending to inventions, and then the ratio of inventions to patents in a given firm or sector of the economy, remains constant over time. Third, studies indicate that there is wide variation among business firms and also among nonprofit institutions and agencies of the federal government to file patent applications on invention disclosures. Finally, it is impossible to identify and then relate patents issuing in any given year with R&D expenditures in some earlier year. Although a patent application usually pends for two-and-a-half years in the Patent Office before it issues (provided Patent Office criteria for patentability are met), some inventions are processed through the Patent Office more rapidly than others. Also, many patents cover inventions that are improvements on components of larger products and processes with the R&D expenditure covering the entire product or process that is developed.

---

<sup>5</sup> *Science and Technology* (October 1969), p. 38.

Despite these weaknesses, patents are the result of research and development effort; and they must in some way mirror changes in levels of manpower and dollars going into a given area of research. In part, this reflects the fact that in early 1970, the Patent Office established a priority program for antipollution inventions. The Patent Office reports that a year after the inception of the program, 380 patent applications covering antipollution techniques and devices passed through the Patent Office's examination and processing within eight months after application (as compared with the usual two-and-a-half

TABLE 2

NUMBER OF UNITED STATES PATENTS ISSUED IN PATENT OFFICE SUBCLASSES THAT RELATE TO ACOUSTICS OR NOISE-ABATEMENT DEVICES, 1959-1970

Patent Office Class or Subclass

Year	Chemical <sup>a</sup>	Metal Working <sup>b</sup>	Buildings <sup>c</sup>	Gas Separation <sup>d</sup>	Power Plants <sup>e</sup>	Acoustics <sup>f</sup>	Fluid Sprinkling, Spraying & Diffusing <sup>g</sup>	Total
1959	61	14	h	h	8	48	h	131
1960	29	28	h	h	6	69	h	132
1961	36	39	h	h	5	52	h	132
1962	36	31	h	1	24	44	h	136
1963	22	26	h	h	12	88	h	148
1964	38	21	h	1	8	58	h	126
1965	50	62	3	2	222	86	h	225
1966	35	53	8	3	24	61	h	184
1967	24	46	4	4	18	51	2	149
1968	20	45	5	3	24	58	h	155
1969	56	42	8	h	18	57	3	194
1970	46	34	3	4	22	72	2	183
Total	453	441	31	18	201	744	7	1,895

<sup>a</sup> Class 23 Subclasses: 284 (Chambers and Stacks) and 288 (Catalytic).

<sup>b</sup> Class 29 Subclass: 157 (Gas and Water).

<sup>c</sup> Class 52 Subclasses: 144, 145, 404, 405, 406, and 407.

<sup>d</sup> Class 55 Subclass: 276 (Noise Attenuation).

<sup>e</sup> Class 60, Subclasses: 29 (Exhaust Treatment) and 30 (Fluid Mingling).

<sup>f</sup> Class 181, Subclasses: 30, and 33 through 72.

<sup>g</sup> Class 239, Subclass: 265.13 (Reaction Mortar Discharge Nozzle) with Retractable Noise Suppressing Steam Divider.

<sup>h</sup> No issues.

Sources: Compiled from data in United States Patent Office, *Index of Patents*, 1959-1969, and United States Patent Office, *Official Gazette*, 1970.

years). The accelerated process program has two important objectives: First, to increase the speed at which these inventions get into use by industry; and second, to make new information available to others as soon as possible.<sup>6</sup>

Tables 2 and 3 present information about the growth in the numbers of patents issuing in Patent Office subclasses that are related to acoustics or to noise-abatement devices. The relevant subclasses were selected by a Patent Office examiner with many years of experience in the field of acoustics. The data in Table 2 give the number of patents issuing in seven broad fields (chemical; metal working; buildings; gas separation; power plants; acoustics; and fluid sprinkling, spraying, and diffusing) between 1959 and 1970. It must be emphasized that these patents are Patent Office subclasses which are most likely to cover inventions relating to noise-abatement devices. Without examining each patent disclosure, it is impossible to know whether they do in fact cover noise-abatement techniques.<sup>7</sup> The data in Table 3 give the average increase in the number of patents issuing in each year (the coefficient of  $t$  for the linear equations) and the rate of growth in the number of patents that issue (the anti-log of the coefficient of  $x$  for the logarithmic equation). All of the coefficients are positive, which indicates that the number of patents issued is increasing over time. The low  $r^2$ 's for a number of the classes suggests that the fit of the equation is not good and the equation is not adequate for forecasting changes in the level of patent activity in those classes. The purpose of this analysis, however, is not to forecast changes in the numbers of patents in these subclasses. Moreover, with increased federal and private concern over noise-related problems, it is reasonable to assume that the numbers of inventions in these subclasses will increase more rapidly in the future. This is especially true if the Patent Office continues its priority program for antipollution inventions and the federal government increases its R&D activities in environmental research.

---

<sup>6</sup> "Patent Office Approves 380 Anti-Pollution Applications Under Priority Program," *Commerce Today*, Vol. 1, No. 2 (March 8, 1971), p. 30. The Patent Office does not have a classification of these inventions by field, i.e., those covering air, water, solid waste, noise, etc.

<sup>7</sup> Although each invention was not analyzed closely, the data-collection process indicated that class 29 (metal-working—subclass 157) and class 60 (power-plants—subclasses 29 and 30) contained a large number of patents that covered devices for air-pollution control relating to exhaust from different kinds of motors. It is believed that class 23 (subclasses 284 and 288) contained the largest number of inventions that did not relate explicitly to noise abatement, and that class 181 (subclasses 30 and 33 through 72) contained the largest number of inventions relating to a number of different kinds of noise-abatement devices and techniques.

TABLE 3

GROWTH IN UNITED STATES PATENTS ISSUED IN PATENT OFFICE SUBCLASSES THAT RELATE TO ACOUSTICS OR NOISE-ABATEMENT DEVICES, 1959-1970

Field	Growth in Number of Patents Per Year (Linear Regression)	Growth Rate in Percent Per Year (Logarithmic Regression)	Patent Class 1959-1970
Chemical <sup>a</sup>	$y = 605.38 + 29.95t$ $r^2 = .50$	$y = 2.80 + .02x$ $r^2 = .48$	23
Metal-Working <sup>b</sup>	$y = 462.44 + 68.45t$ $r^2 = .86$	$y = 2.71 + .03x$ $r^2 = .88$	29
Buildings <sup>c</sup>	$y = 443.67 + 29.86t$ $r^2 = .11$	$y = 2.57 + .04x$ $r^2 = .18$	52 <sup>l</sup>
Gas Separation <sup>d</sup>	$y = 124.42 + 25.72t$ $r^2 = .74$	$y = 2.12 + .05x$ $r^2 = .76$	55 <sup>j</sup>
Power Plants <sup>e</sup>	$y = 620.95 + 7.76t$ $r^2 = .63$	$y = 2.79 + .01x$ $r^2 = .58$	60
Acoustics <sup>f</sup>	$y = 111.35 + 4.51t$ $r^2 = .36$	$y = 2.04 + .02x$ $r^2 = .42$	181
Fluid Sprinkling, Spraying, and Diffusing <sup>g</sup>	$y = 200.33 + 10.44t$ $r^2 = .41$	$y = 2.30 + .02x$ $r^2 = .44$	239 <sup>k</sup>
All Subclasses Except 23	$y = 83.38 + 5.65t$ $r^2 = .48$	$y = 1.92 + .02x$ $r^2 = .53$	All Subclasses (except #23) #33
Mufflers and Sound Filters <sup>h</sup>	$y = 17.03 + .10t$ $r^2 = .05$	$y = 1.17 + .01x$ $r^2 = .13$	
All U.S. Patents Issued	$y = 45862.95 + 1644.58t$ $r^2 = .50$	$y = 4.67 + .01x$ $r^2 = .50$	Total All Patents Issued

<sup>a</sup> Class 23, Subclasses: 284 (Chambers and Stacks) and 288 (Catalytic).

<sup>b</sup> Class 29, Subclass: 157 (Gas and Water).

<sup>c</sup> Class 52, Subclass: 144, 145, 404, 405, 406, and 407.

<sup>d</sup> Class 55, Subclass: 276 (Noise Attenuation).

<sup>e</sup> Class 60, Subclasses: 29 (Exhaust Treatment) and 30 (Fluid Mingling).

<sup>f</sup> Class 181, Subclasses: 30, and 33 through 72.

<sup>g</sup> Class 239, Subclass: 265.13 (Reaction Mortar Discharge Nozzle) with Retractable Noise Suppressing Steam Divider.

<sup>h</sup> No issues Subclass 33.

<sup>l</sup> From 1965-1971.

<sup>j</sup> From 1962-1971.

<sup>k</sup> 1969 omitted.

Source: Compiled from data in United States Patent Office, *Index of Patents*, 1959-1969, and United States Patent Office, *Official Gazette*, 1970.



The data in Table 3 show that all United States patents were growing at about 2.3 percent per annum between 1959 and 1970. Patents relating to noise in class 60 (power plants) and those in subclass 33 (mufflers and sound filters) of class 181 (acoustics) were growing at about the same rate as all United States patents. Subclass 33 is the largest subclass in the acoustics area. Inventions in other subclasses that relate to acoustics or noise-abatement devices are growing more rapidly than the number of total patents issued. For example, the relevant subclasses in chemicals; fluid sprinkling, spraying, and diffusing; and acoustics (except mufflers and sound filters) are growing at a rate of 4.7 percent per annum. Noise-related patents in metal-working are growing at 7.2 percent each year and those in the building class at about 9.6 percent per annum.

Tables 4 and 5 show patent activity for noise-related inventions from a different point of view—the ownership of inventions at time of issue. Although the stringency varies among the different federal agencies and also among private businesses, both the federal government and private companies usually require inventors to assign titles to patents to the

TABLE 4

PERCENTAGE DISTRIBUTION OF UNITED STATES PATENTS ISSUED IN PATENT OFFICE SUBCLASSES THAT RELATE TO ACOUSTICS OR NOISE ABATEMENT DEVICES, BY ASSIGNEE 1959-1970

Year	Type of Assignee				
	Federal Government	Individual	Foreign	Large Business <sup>a</sup>	Other Business
1959	4	18	12	34	32
1960	1	27	10	33	29
1961	1	21	19	27	32
1962	0	25	13	31	31
1963	1	19	10	30	40
1964	1	16	13	45	25
1965	2	25	15	32	26
1966	1	20	10	32	37
1967	1	17	15	33	34
1968	2	17	16	30	35
1969	0	18	16	31	35
1970	1	14	27	29	29

<sup>a</sup> Among the *Fortune 500* in 1970.

Sources: Compiled from data in United States Patent Office, *Index of Patents*, 1959-1969, and United States Patent Office, *Official Gazette*, 1970.

funding organization. The data in these tables reflect the relative amounts of R&D spending on noise-related problems undertaken by the federal government, individuals, and business, during the past decade or so. Table 4 gives a percentage distribution for all relevant subclasses in the seven broad Patent Office classes. Table 5 gives the number of patents, by assignee, in subclass 33 (mufflers and sound filters) of class 181 (acoustics).

The data displayed in both Table 4 and Table 5 strongly suggest that the private sector of the economy has been much more active than the federal government in R&D on noise-related problems. During the entire 12-year period, the federal government acquired titles to less than 5 percent, and in most years no more than 2 percent, of all of the patents issuing in these subclasses. The same kind of distribution of patents between the federal government and private industry existed before World War II when the federal R&D effort was just beginning to grow.

*Another Estimate of Federal R&D Spending on Noise Abatement in the 1960's*

In 1968, the National Bureau of Standards prepared a report for the Task Force on Noise of the Federal Council on Science and Technology.<sup>8</sup> The report tends to confirm patent statistics which show that most R&D on noise abatement was in the area of applied research and development and was undertaken by private industry. According to the report, the federal government funded almost no research in the field of acoustics apart from acoustical research associated with defense requirements. Based on a review of the *Commerce Business Daily*, the report identifies an expenditure of \$259,000 between 1963 and 1967 sponsored by the Federal Housing Administration.<sup>9</sup> The report also lists two contracts of an undetermined amount for noise reduction in hospitals funded by the Public Health Service between 1963 and 1967.<sup>10</sup> The report stated that in the late 1960's, the national effort of the United States on noise pollution and its abatement was so far below that of the Canadian government that the United States would have to

---

<sup>8</sup> Internal Memorandum from the National Bureau of Standards to the Members of the Federal Council on Science and Technology, Task Force on Noise (February 20, 1968).

<sup>9</sup> *The Commerce Business Daily* is a publication of the federal government that lists contract proposals and also contracts awarded by the federal government.

<sup>10</sup> Internal Memorandum from NBS to FCST, p. 18.

TABLE 5

NUMBER OF UNITED STATES PATENTS ISSUED IN CLASS 181 (ACOUSTICS), SUBCLASS 33  
(MUFFLERS AND SOUND FILTERS), BY ASSIGNEE, 1959-1970

Year	Type of Assignee					Total
	Federal Government	Individual	Foreign	Large Business <sup>a</sup>	Other Business	
1959	0	0	2	2	4	8
1960	1	6	2	3	2	14
1961	1	4	2	6	6	19
1962	0	6	3	5	4	18
1963	0	3	4	9	22	38
1964	0	1	2	9	5	17
1965	0	3	2	5	9	19
1966	0	5	3	5	5	18
1967	0	2	1	3	6	12
1968	1	1	2	3	2	9
1969	0	1	3	8	4	16
1970	1	4	6	5	5	21
Total	4	36	32	63	74	209

<sup>a</sup> Among the *Fortune 500* in 1970.

Sources: Compiled from data in United States Patent Office, *Index of Patents*, 1959-1969, and United States Patent Office, *Official Gazette*, 1970.

accelerate its research effort by "one hundred fold" to match the then existing Canadian program on a per capita basis.<sup>11</sup> Although the report probably neglected to account for all studies sponsored by the federal government because of the complicated nature of R&D procurement, it does strongly suggest that the federal government did not have a positive program in the area of noise pollution and its abatement in the 1960's.

#### SUMMARY AND CONCLUSIONS

As illustrated by the case study on noise abatement, measures of research and development expenditures in the area of noise pollution are fragmentary at best. Patent statistics, however, can be employed as a useful surrogate for R&D effort because patents are the end product of research and, therefore, are indicative of changes in both manpower and expenditures in a given research area. Although it is difficult, if not

<sup>11</sup> *Ibid.*, p. 16.

impossible, to ascertain the *level* of spending by private businesses, the federal government, and other organizations, at a given *point in time* from patent data, the statistics reveal meaningful information about the *relative* R&D effort of various organizations and the federal government as well as the *changes* in manpower and spending through time.

In the case of noise-pollution research, the patent data suggest that the private sector of the economy has committed much more R&D effort to noise abatement than the federal government. In view of the large spending programs of the government for water- and air-pollution research as well as research in general, this finding is rather surprising. The conclusion drawn from the patent data is supported by other evidence which suggests that government-sponsored R&D for noise abatement has been minimal in the recent past. This research also suggests that a careful analysis of patent statistics can provide useful information regarding R&D effort in an area in which alternative sources of data are meager.

## STUDENT PAPERS

---

By making available student papers, students will receive an incentive and our readers will appreciate the evidence of scholarly development in the fields of interest. These papers are carefully reviewed by the Editorial Committee and other specialists, and helpful suggestions are made to the students as part of the educational function of *IDEA*. The Research Institute invites educational and research institutions to submit informative student manuscripts on the patent, trademark, copyright, and related systems.

# Statutorily Decreed Awards for Employed Inventors: Will They Spur Advancement of the Useful Arts?\*

FRANKLIN C. HARTER

### INTRODUCTION

ON JANUARY 22, 1971, REPRESENTATIVE JOHN E. MOSS of California introduced a bill<sup>1</sup> with the stated purpose of creating "a comprehensive

---

\* This paper was submitted by the author in partial fulfillment of a course in patent law in The National Law Center of The George Washington University. He is at present employed in the Law Department Patent Section of Whirlpool Corporation, Benton Harbor, Michigan.

<sup>1</sup> H.R. 1483, 92nd Cong., 1st Sess. (1971) (hereinafter cited as H.R. 1483).

federal system for determining the ownership and amount of compensation to be paid for innovations and proposals for technical improvement made by employed persons." As indicated by this statement of purpose, enactment of the proposed legislation could substantially alter the prevailing policies and practices of American employers vis-à-vis their employed inventors. To be more specific, passage of the bill would end the all but universal practice among major corporations of requiring each employee involved in research and development and associated fields to sign a uniform, comprehensive assignment contract<sup>2</sup> which establishes the respective rights of the employee and employer with regard to subsequent inventions.

Having swept away the employment contract as a means of allocating invention rights, the legislation would substitute therefor a statutory basis for defining the respective rights of employee and employer. The employer, under this statutory basis, would be granted rather extensive rights to claim an interest in an employee's invention, provided he acted timely in accordance with a procedure set forth in the bill. In return, the employee would be accorded a legal right to compensation from his employer. The legislation would also provide for the establishment of tribunals for settling disputes between the employer and employee, thus assuring the latter his day in court.

Introduction of the comprehensive Moss bill was no doubt prompted by increasingly adamant demands from employed inventors and their professional organizations, notably the Society of Professional Engineers, that a complete reevaluation be made of the present practice of requiring unilateral preassignment of patent rights as a condition of employment. Some advocates of this reevaluation argue that the preassignment contract deprives the employed inventor of an alleged "natural right" to a reward for his genius.<sup>3</sup>

Other advocates of possible change, although not necessarily the type of change embodied in the Moss bill, express concern over whether or not the patent system in today's economy is still effectively carrying out its traditional functions of stimulating a high rate of technological innovation and channeling it into areas most useful to society.<sup>4</sup> They

---

<sup>2</sup> See, e.g., O'Meara, *Employee Patent and Secrecy Agreements*, N.I.C.B. Study in Personnel Policy No. 199 (1965).

<sup>3</sup> See, e.g., Robert J. Kuntz, "Patent Rights for Employee Inventors." An article from an unspecified publication in the *Congressional Record* (January 22, 1970), at H191-2.

<sup>4</sup> See, e.g., John C. Stedman, "The Employed Inventor, The Public Interest, and Horse and Buggy Law in the Space Age," 45 *New York University Law Review* 1 (March 1970).

note with alarm that inventive output in the United States has not increased anywhere near in proportion to the increasing amounts of money and manpower being expended on research and development.<sup>5</sup> This rapidly mounting concern over the possible malfunctioning of our patent system, which many equate with its failure to provide a direct stimulus to the actual inventor due to extensive use of the preassignment contract, has led to some activity in the halls of Congress,<sup>6</sup> the latest of which is Mr. Moss's proposed amendment to Title 35, United States Code.

In this paper, the author will set forth his reasons for concluding that enactment of the Moss bill at this time would be ill-advised. This conclusion rests primarily on the contention that operation under a statutorily decreed award system of the type proposed, in the absence of a change in attitude by corporate management, would fail to increase the incentive to innovate among employed inventors. This is not to say that action, be it legislative or otherwise, which would increase this incentive is not highly desirable. Indeed, the author feels there is an urgent need for further study in this area so that truly effective action may be taken. As John C. Stedman has stated in a recent law review article:

It is premature to make firm specific recommendations for action in the absence of much more information and understanding than we now possess. The forces that operate upon employed, as well as independent, inventors are many, varied and complex, and it behooves us to tap them all and not just concentrate on one or two while ignoring the others.<sup>7</sup>

#### STANDARD USED TO EVALUATE THE MOSS BILL

The desirability of a given legislative proposal obviously depends in large part on the criteria used to evaluate that desirability. This

---

<sup>5</sup>*Id.* at 22.

<sup>6</sup> For Congressional activity in this general area, see:

—H.R. 5918, 89th Cong., 1st Sess. (1965);

—S. 789, 89th Cong., 1st Sess. (1965);

—*Hearings on S. 2157 and H.R. 2383 Before the Subcomm. on Patents, Trademarks and Copyrights of the Senate Comm. on Judiciary*, 84th Cong. 2nd Sess. (1956);

—*Hearings on S. Res. 70 Before the Subcomm. on Anti-Trust and Monopoly of the Comm. on the Judiciary*, 89th Cong., 1st Sess. (1965); and

—Maltby, "A Government Patent Policy for Employee Inventors," 21 *Federal Bar Journal* 127 (1961).

<sup>7</sup> *Supra* note 4, at 23.

observation is especially pertinent here since the author may be using a somewhat different yardstick to measure the Moss bill than are its sponsors. To be more specific, in introducing the subject bill in the House, Representative Moss utilized an article written by Robert J. Kuntz which was said to describe the need for such legislation. The article notes that the *World Book Encyclopedia* definition of a patent includes the following:

France adopted its first patent legislation in 1791. It believes that the patent law should be based on the idea that the *inventor's right is a natural right*. (Emphasis by Mr. Kuntz.)

Further on in the article, it is stated:

The California Society of Professional Engineers considers the rights of an inventor to be intrinsic in nature.<sup>8</sup>

As these excerpts indicate, the Kuntz article stresses the need for such legislation as a means of securing for the employed inventor an alleged natural right to a reward for his genius.<sup>9</sup>

With all due respect, it is submitted that in emphasizing the employed inventor's natural right, Mr. Kuntz misconceives the underlying goal of our patent system. While French patent law may well be based on a theory that, according to principles of universal equity, an inventor has an exclusive property in his invention,<sup>10</sup> such has never been the case in common law countries. As stated by Anthony W. Deller in his well-known work on patent law:

Independent of statute law, however, no such right [an inventor's right to an exclusive property in his invention] existed at common law. . . . The exclusive right to use an invention after disclosure can exist only by virtue of some statute law enacted by the legislature as the representative of the people.<sup>11</sup>

---

<sup>8</sup> *Supra* note 3, at H191.

<sup>9</sup> In fairness to Mr. Kuntz, the author notes that his article does indicate that preassignment of invention rights by employed inventors results in a loss of incentive. Hence, the Kuntz article does recognize the other side of the coin; namely, that such contracts may be slowing down the rate of technological advancement in the United States.

<sup>10</sup> A decree of the French National Assembly in 1791 declared that "not to regard a discovery in industry as the property of the discoverer would be to attack the rights of men in their essence." See Coryton, *The Law and Letters Patent* (1855); and Renouard, *Traite des Brevets d'Invention* (1825).

<sup>11</sup> Anthony W. Deller, *Deller's Walker on Patents* (2nd ed., 1965), at 37.



Further on in the same work, it is noted:

The right which an inventor obtains is a creature of statute whereas an inventor has no exclusive right to his invention at common law.<sup>12</sup>

As these quotes suggest, the primary goal of the United States patent system is not to secure any sort of natural right to an exclusive property in an invention. Rather the primary goal is to promote a rapid rate of national economic development by relying on a combination of two factors. First, technological activity in fields useful to society is encouraged by holding out the "carrot" of patent protection. Second, in exchange for and as a condition of that protection, society, through the patent system, demands full disclosure of the invention.<sup>13</sup>

A moment's reflection will reveal that if the Moss bill is thought of merely as providing a statutory mechanism which may be utilized by an employed inventor to extract compensation from a possibly reluctant employer, it may well be desirable since it does provide such a mechanism. On the other hand, if one adopts the viewpoint that the Moss bill is desirable only if it provides a positive spur to technological progress, then more searching questions must be asked. For example, in light of recent data from the behavioral sciences, will the legislation provide a meaningful reward which will actually stimulate creative activity? Will the activity fostered be in areas useful to society? If management is opposed to legislation such as the Moss bill (which the widespread use of preassignment contracts indicates it probably is), what are the chances that any reward at all will be provided in view of possible loopholes in the bill?

These and many more questions must be answered before a sound appraisal of the bill's desirability can be made. The next section of this paper will consider some of these issues in a bit more depth.

#### REWARDS PROVIDED BY THE MOSS BILL AND THEIR EFFECT ON INNOVATIVE ACTIVITY

Before attempting to predict the practical impact of the Moss bill on technological development in the United States, something must be said about the factors necessary to get inventors, employed or otherwise,

---

<sup>12</sup> *Id.* at 46.

<sup>13</sup> For a statement of this position by Judge Giles S. Rich, see *In re Nelson and Shabica*, 47 CCPA 1033, 126 U.S.P.Q. 242 (1960), at 251.

to invent. Although there is certainly no universal agreement in this area, most commentators would probably concede that invention involves at least two basic components: namely, the creative ability to invent coupled with the motivation to use that ability.<sup>14</sup> As a working definition of creative ability, the following one suggested by Irving H. Siegel is appropriate:

. . . a disposition or ability to discover significant novel facts or principles or to generate significant novel ideas, distinctions, or combinations.<sup>15</sup>

Since the Moss bill is obviously not intended to increase this latent ability to invent, no more need be said with regard to it.

Turning now to the motivational factor in the inventive process, we can no doubt all agree on at least certain basic requirements which must be satisfied by any reward system designed to increase the incentive to invent. First of all, the reward which is provided must be truly *need-satisfying to the recipient*. Despite the obviousness of this requirement, it is an important one to keep in mind, since those establishing reward systems for inventors often fail to appreciate that a reward which would be desirable to them may not be need-satisfying to the intended recipient in his particular situation.<sup>16</sup>

Next, the *inventor himself must believe that he has a good chance of getting the reward* if he engages in the behavior to be encouraged. Recognition of this requirement makes it apparent why the proverbial trip to Hawaii awarded yearly to one engineer out of five thousand has little incentive effect. A third consideration to keep in mind, and perhaps the most important one in evaluating the probable operation of the Moss bill in the modern corporation, is expressed in the following language by James N. Mosel:

. . . it is really management's behavior toward inventors which carries the real reward. It is not management's words. There frequently develops a discrepancy between what management's words prescribe for people to do and what its own behavior in fact makes it worthwhile for them to do.<sup>17</sup>

---

<sup>14</sup> See James N. Mosel, "The Employee Inventor, A Psychologist's View," 47 *JPOS* 507 (1965). This is an address given by Dr. Mosel at a seminar entitled *The Employee Inventor* which was conducted by Prof. L. James Harris and sponsored by the Commemorative Committee of the 175th Anniversary of the United States Patent System.

<sup>15</sup> Irving H. Siegel, "Employee Creativity and Organizational Aims," *IDEA*, Vol. 9, No. 3 (Fall 1965), at 403.

<sup>16</sup> See *supra* note 14, at 508-509.

<sup>17</sup> *Id.* at 509.

The importance of this consideration as it relates to the Moss bill will become apparent in a later portion of this analysis.

One more point deserves mention before we get down to specifics. If the Moss bill is to carry forward traditional patent system goals, it must not only stimulate innovative activity, it must stimulate that activity in *fields useful to society*. Perhaps this is what Jay W. Forrester had in mind when he said:

If published papers and filed patent applications are the only sources of reward, then creativity takes the form of new ideas without any filtering of good new ideas from bad new ideas. If the motivation is to serve society either because of financial gain or public acclaim, then emphasis is focused on useful new ideas and discarding bad new ideas becomes as important as creating good new ideas.<sup>18</sup>

Let us now consider the statutory allocation of rights between employer and employee should the proposed legislation be enacted. Under the bill, which is virtually a carbon copy of legislation in effect in West Germany since 1957,<sup>19</sup> both patentable subject matter and "proposals for technical improvement" are covered. Inventions are classified as (a) "service" inventions, which relate in designated ways to the employee's work, and (b) "free" inventions, which are unrelated to the employee's work.<sup>20</sup> Regardless of classification, the employee must offer his invention to his employer,<sup>21</sup> subject to payment of compensation should his employer claim the invention.<sup>22</sup> The amount of compensation is specified to be the "fair market value of the employer's right to the invention adjusted to reflect the following factors: (1) the position and duties of the employee, and (2) the degree to which the operations of the employer contributed to the making of the invention."<sup>23</sup>

---

<sup>18</sup> Jay W. Forrester, "Environment and Invention," *IDEA*, Vol. 13, No. 2 (Summer 1969), at 281. This is an acceptance speech delivered by Dr. Forrester on April 17, 1969, in Washington, D.C., at a reception in his honor as Inventor of the Year, an award presented to him by The PTC Research Institute.

<sup>19</sup> For excellent discussions of the West German employed inventor legislation and its operation, see:

—James W. Brennan, "The Developing Law of Employee Inventions," *PTC J. Res. & Ed. (IDEA)*, Vol. 6, No. 1 (Spring 1962), (hereinafter cited as Brennan).

—Fredrick Neumeyer, "The Law of Employed Inventors in Europe," Study No. 30, 87th Cong., 2nd Sess. (1962).

<sup>20</sup> H.R. 1483, *supra* note 1, § 402 (4), (5).

<sup>21</sup> *Id.* at §§ 411 (a), 431 (a).

<sup>22</sup> *Id.* at §§ 412, 431.

<sup>23</sup> *Id.* at § 414 (a).

The bill further authorizes the Secretary of Labor to issue regulations including specific rules to ascertain the amount of compensation to be paid for service inventions.<sup>24</sup> Should the employer use a proposal for technical improvement, he is obliged to compensate the submitter under rules similar to those pertaining to inventions.<sup>25</sup> Strict time limits are imposed upon the employer's offer of compensation and the employee's rejection thereof if he deems it unsatisfactory.<sup>26</sup> Controversies are to be resolved either through an arbitration board located in the Patent Office or through court proceedings.<sup>27</sup>

Under the above system it appears that the usual reward for an invention made in the course of employment would be some measure of monetary compensation. This follows since an employed inventor generally would be working in a technical area relevant to his employer's business; hence, most employee inventions would be of the "service" variety. Experience under the German system bears out this conclusion. In 1960, for example, 80 percent of the 34,577 patent applications filed in West Germany were filed on behalf of German employees.<sup>28</sup>

Since most employee inventions will give rise to a claim for the payment of money under the proposed legislation, it behooves us to make the following inquiry: Assuming employers pay the statutorily envisioned amount for an employee "service" invention, will such a cash payment provide the need-satisfying reward essential to stimulate further creative effort? Although one is tempted to answer "of course" to this inquiry, recent data from the behavioral sciences should make us leery of hard and fast answers to the question posed.

Let me be more specific. In a survey conducted by Joseph Rossman relating to rewards and incentives for employee-inventors, questionnaire cards were sent to 1118 employed inventors. Of the 385 inventors who filled in and returned the cards, 96 indicated they felt cash payments or bonuses would encourage the production of inventions.<sup>29</sup> It would seem that if cash payments were such an obvious stimulant to creative activity, more employed inventors would have indicated the fact when asked for their opinion. In the same article, Dr. Rossman

---

<sup>24</sup> *Id.* at § 439.

<sup>25</sup> *Id.* at § 432.

<sup>26</sup> *Id.* at §§ 414 (b), 431, 432.

<sup>27</sup> *Id.* at §§ 437, 438.

<sup>28</sup> Brennan, *supra* note 19, at 85.

<sup>29</sup> Joseph Rossman, "Rewards and Incentives to Employee-Inventors," *PTC J. Res. & Ed. (IDEA)*, Vol. 7, No. 3 (Fall 1963), at 448.

discussed the results of a government survey involving more than 3000 scientific and engineering employees engaged in industrial research. The survey revealed that pay ranked number six in order of importance among 15 factors contributing to job satisfaction.<sup>30</sup> Although a factor contributing to job satisfaction may not have a corresponding effect in the more specific area of spurring creative activity, it seems likely that there is a high degree of correlation.

When management opinion is sampled as to whether cash payments stimulate innovations, actions speak louder than words. We have already noted that U.S. corporations almost universally utilize employee preassignment contracts. Rossman concludes based on his survey of management practices:

. . . it is the general policy of most companies to regard the salaries paid R&D employees as full consideration for the assignment of inventions made during their employment using the time and facilities of the company. Only a few companies pay any substantial amounts or make special awards.<sup>31</sup>

Further on Rossman notes:

Practically all U. S. companies replying. . . indicated that incentives of their R&D employees were not impaired because companies took title to their patented inventions.<sup>32</sup>

While the reader may be tempted to discount somewhat the validity of the employer's viewpoint on this matter due to its self-serving ring, one consideration should be borne in mind. Presumptively at least, inventors are hired to invent. If experience among the few companies who do give substantial cash awards for inventive output indicated that such payments had a strong motivating effect, it seems that the forces of competition would move other companies to adopt similar programs to get the most out of their employed inventors. The fact that most U. S. companies have not seen fit to do so may lend some credence to their viewpoint.<sup>33</sup>

Looking to more disinterested viewpoints on what factors encourage

---

<sup>30</sup> *Id.* at 448-49.

<sup>31</sup> *Id.* at 435.

<sup>32</sup> *Id.* at 447.

<sup>33</sup> In considering this point, the reader should note that a typical mission-oriented company may not, in point of fact, wish to stimulate its employed inventors to the maximum possible degree for a variety of reasons to be explored later in this paper. This factor could easily account for management reluctance to adopt a monetary reward system even though it had proven successful at another company engaged in a similar line of business.

innovation, the ones usually stressed are those relating to the so-called "creative environment," not those relating to increased use of direct monetary awards. A typical statement of this "managerial science" viewpoint is provided by Harry Levinson who stresses the importance of setting up "a reward system which fits the scientist's values." These values are said to include greater autonomy of choice of projects for senior scientists, more challenging assignments, opportunity for association with high-caliber colleagues in a "creative intellectual atmosphere," recognition of productive performance, provision of merit salary increases and status promotions, and availability of parallel ladders of "research" and "administrative" advancement.<sup>34</sup> Further comments on ways to promote creativity have been made by a psychologist-social scientist, Harold Guetzkow. Mr. Guetzkow states:

A dispersed distribution of authority within a firm provides more occasions for innovation, creative decision making, especially when the decentralized unit exists within a diversified firm and possesses relatively objective criteria in terms of which its output may be appraised. . . .

The greater the organizational slack [flexibility], with its increased capability of absorbing errors and ethos for risk-taking, the greater the propensity for innovation. . . .

The communication system of an organization may be tuned so as to provide materials for creative activities without depriving members of the organization of time for creative work.<sup>35</sup>

Significant with regard to these comments on the management of employed inventors is the fact that neither commentator listed direct monetary compensation for inventions as an important consideration.

In reflecting on the material presented above, it should be borne in mind that the author is not arguing for the correctness of any particular viewpoint. Rather, the important point is that a significant number of knowledgeable people apparently do not rank direct monetary awards high on their list of factors which spur innovation. This should at least prompt one to think twice about the wisdom of enacting the Moss bill if the legislative purpose is taken to be advancement of the useful arts via the provision of a need-satisfying carrot to the employed inventor.

---

<sup>34</sup> Harry Levinson, "What an Executive Should Know About Scientists," *Think* (September-October 1965), at 6-10.

<sup>35</sup> Harold Guetzkow, "The Creative Person in Organizations," in G. A. Steiner ed., *The Creative Organization* (University of Chicago Press, 1965), at 35-45.

ADVANCEMENT OF THE USEFUL ARTS UNDER THE  
MOSS BILL REWARD SYSTEM

Bearing in mind the point just made, let us now assume that money will stimulate creativity. In other words, assume that a direct cash payment to an employee each time his employer claims a service invention will have a significant effect in motivating further innovative effort. In addition, assume that employers act in accord with the spirit of the Moss bill (an assumption to be examined shortly) and give each employed inventor a cash payment reflecting the fair market value of the employer's right to the invention adjusted by the factors indicated earlier. Given these two assumptions, will technological development progress more rapidly in the U. S.?

Before answers can be attempted to even a few of the many subissues raised by this question, some generalizations must be set forth regarding the inventive process in the corporate environment. First of all, it is obvious that more is needed than just clever ideas before the useful arts advance one inch. The ideas must be practical in the sense that they can be put to use for society's benefit. They must come to light in an environment where they will be received with enthusiasm, for only then will sufficient company resources be devoted to their development and marketing to bring them to fruition. Hence, an employee invention must "fit in" with the present and future goals of the corporation if it is to get off the ground.<sup>36</sup> It follows logically that any reward system designed for employed inventors which will advance the useful arts must encourage practical ideas in line with present or future company activity.

Another factor which must be reckoned with in evaluating a reward system for employed inventors is that the evolution of a new and useful

---

<sup>36</sup>The author has serious doubts whether the practical requirement referred to here is a wholly desirable one. Such doubts are prompted by his agreement with a clinical psychologist, M. L. Stein, who spoke at a University of Chicago seminar on *The Creative Organization*. Mr. Stein, based on experience in research laboratories, expressed doubt that industry really wanted creativity or "would know what to do with it." He felt that administrators had a "cash register philosophy of creativity" that biased them toward short-range projects and away from "what will be profitable five or ten years from now." Agreement with these comments prompts the author to express his viewpoint that a system which would somehow bring the more far-out inventions made by employed inventors to the public's doorstep would be highly desirable. However, despite this view of what would be desirable, any realistic evaluation of how the Moss bill will operate must recognize the facts as they are today and one of these facts is that employed inventor ideas rarely get off the ground if they don't match short-run company goals.

product rarely, if ever, springs full blown in the inventor's mind. Rather, it usually involves a myriad of small inventive steps wherein one engineer builds on what another has done.<sup>37</sup> Furthermore, many people in addition to the inventors get involved in the development process before the product comes to the marketplace. An official at Bell Telephone Laboratories has estimated roughly that "it takes 14 times as many people to make something out of inventions as it does to invent them."<sup>38</sup> In view of this, one must recognize that cooperation between many employees, both technical and nontechnical, is necessary if the mission-oriented company is to get the job done. Hence, any competition among employees must be kept at a constructive level.<sup>39</sup>

Bearing in mind these considerations, let us now return to the original questions posed regarding the effect of legislation on the corporate research effort, assuming money will stimulate innovation and that the corporation will fork it over. As noted earlier, the Moss bill seeks to provide compensation in an amount depending on the market value of the invention to the employer adjusted to reflect (1) the position and duties of the employee, and (2) the degree to which the operations of the employer contributed to the making of the invention. No regulations are set out in the Moss bill to ascertain the amount of compensation in specific cases under these broad standards. Rather, this complex problem is left for later resolution by the Secretary of Labor.

Since the Moss bill itself is very similar to present West German legislation, it is reasonable to predict that our Secretary of Labor would borrow from similar regulations set up in West Germany to determine the amount of compensation in accordance with the legislative purpose. Summarily stated the compensation "formula" under West German regulations involves first a calculation of the invention's "value" to the employer which equals the amount the employer would be obliged to pay for the invention if bought from a free inventor. The compensation due the employee-inventor is generally a fraction of that value, termed the "share factor," which is determined by considering the following three items:

- (1) The manner in which the task was presented to the employee. If the employee demonstrated great initiative in setting for himself the task which ultimately led to the in-

---

<sup>37</sup> See P. G. Peterson, *The Creative Organization*, *supra* note 35, at 152.

<sup>38</sup> J. R. Pierce, *PTC J. Res. & Ed. (IDEA)*, Vol. 7, Conference No. (1963), at 98.

<sup>39</sup> See *supra* note 15, at 422.



vention, this factor is high entitling the inventor to a greater reward. However, if the invention resulted from carrying out a specifically assigned project wherein directions for performance were narrowly set, this factor is lower.

- (2) The resources of the company employed in making the invention. Here the employee is entitled to a greater slice of the pie if his invention resulted from activities over and above his normal duties in that the employer's contribution in furnishing resources and equipment, information, suggestions and so on was minimal.
- (3) The duties and position of the employee in the corporation. Under this factor, the employee's reward is smaller if he has a greater opportunity to inspect the production techniques and technical developments within the company, is in a higher position in the company, and makes a high salary.<sup>40</sup>

Review of these factors indicates that they do provide a reward in accordance with the broad standards of the Moss bill given above. But query, will a reward based in amount on these factors encourage progress of the useful arts under the realities of corporate life? Remembering our assumption that individual monetary reward will increase inventive productivity, it follows that, in engaging in such activity, the employed inventor will consciously channel his inventive effort so as to maximize his reward under the regulations. If he does, the above reward system will stimulate creativity outside the employed inventor's generally assigned line of work using the smallest quantum of company supplied resources. Furthermore, the highest paid technical people, who may well have the largest degree of creative talent, will be the ones receiving the smallest reward. Query, whether such a reward system will best mobilize corporate resources and creative talent for the task of advancing corporate goals.

In rebuttal to the above point, advocates of the Moss bill may validly point out that it might be highly desirable to stimulate invention in areas not directly related to the employer's line of business. After all, doesn't it make good sense to stimulate the General Motors product engineer who has been designing a door handle for the last ten years of his life to do something new? Perhaps yes, but we must keep in mind that the goal of the patent system involves more than just generation of good ideas. If the employed inventor is stimulated to come up with an idea outside his generally assigned area of responsibility using resources

---

<sup>40</sup> See Brennan, *supra* note 19, at 68-83.

not supplied by the company, the company might think twice about claiming it for two reasons: first, the compensation due the employee for such an invention would presumably be high and, second, its usefulness to the company might be rather low. Should the company reject the idea allowing it to become "free," would the inventor be able to develop and market it on his own in view of the astronomical cost of such activities in today's economy? Would he even pay the price of patenting the idea so other people could build on it? If these questions were to be answered in the negative, it is rather doubtful that the useful arts would advance more rapidly, regardless of how many good ideas are stimulated.

Continuing under the above critical assumption that management will grant a meaningful amount of compensation for a claimed invention, another unknown under the Moss bill is its probable effect on the cooperative effort necessary among corporate employees, both technical and nontechnical. As might be expected, corporate managers almost unanimously predict that such legislation will foster destructive competition among members of the "research team."<sup>41</sup> Obviously, the theory here is that if an employed inventor consciously has in mind that he will receive a handsome reward for a significant invention, he will be more secretive regarding his work in an effort to avoid sharing it with a potential coinventing colleague, or, worse yet, losing it altogether to a fellow engineer who beats him to the punch. A statement by management in this vein is provided by a vice president of Bell Telephone Laboratories in charge of long-range program planning:

One might question how, in an apparently loosely hung activity such as this transistor program, with its great opportunities for valuable inventions, one can avoid destructive rivalries. Scientists and engineers are human beings, and human beings by nature are competitive. I believe that destructive factors in competition are greatly mitigated by two of our policies. . . . The policy of making no special awards for inventions but of considering an invention as one meritorious performance to be lumped with all others in the administration of salaries reduces the incentive that leads to dog-in-the-manger thinking.<sup>42</sup>

Of perhaps even more significance than management's opinion in this area is the fact that many employed inventors are in agreement with it.

---

<sup>41</sup> See Albert S. Davis, Jr., "A Piece of the Action," *International Science and Technology* (December 1963), at 49-53.

<sup>42</sup> Ralph Brown, "The Transistor as an Industrial Research Episode," *The Scientific Monthly* (January 1955), at 46.

Even Mr. Kuntz, in his article describing the need for the Moss bill, recognizes this when he states:

Many engineers have been sufficiently "conditioned" that they even support the employer's position that preassignment of all invention rights is moral and just as a consideration of salary paid.<sup>43</sup>

Among the more distinguished inventors expressing a distrust of special awards for patenting is William Shockley, a coinventor of the transistor.<sup>44</sup> Dr. Shockley's view on this matter seems especially pertinent in view of an example given by Mr. Kuntz stressing the gross unfairness of Bell Laboratories' policy of giving each of the inventors of the transistor (which, of course, includes Shockley) only \$1.00.<sup>45</sup> Another prominent inventor, Jack Rabinow, expresses his views in this area as follows:

. . . Why should inventors think they deserve special compensation because they invent only once in a great while, while everyone else has to work hard every day. . . . It seems to me that the product of human labor, whether physical or mental, should be treated more or less equally in a qualitative sense. There are, of course, degrees to the quality of labor and if you're a great inventor you deserve a great salary. But to say that something changes in the quality of the employer-employee relationship, that because you're an inventor it is necessary not only to pay you a salary but you should get a special reward for every separate invention, is nonsense. How about the mathematician who discovers a new theorem? Does he not deserve a special reward even though he can't patent it? How about a physicist who discovers a new law of nature? . . . I have always believed that an inventor is important to our society, and I take great pride in being known as an inventor, but I do not believe he should be treated differently from the rest of the human race. I think inventors should get all they can in a competitive society, such as ours. And if all they can get is a good salary, then that is all they deserve.<sup>46</sup>

As suggested by Mr. Rabinow's comments, in addition to potential rivalry among employed inventors per se, there is also a danger that cooperation will be lessened between technical people and those support workers not in a job conducive to inventive activity as a result of awarding extra money to inventors only. Surely the man who has just

---

<sup>43</sup> *Supra* note 3, at H191.

<sup>44</sup> William Shockley, "A Case on the Development of Transistors," *The Creative Organization*, *supra* note 35, at 130-140.

<sup>45</sup> *Supra* note 3, at H192.

<sup>46</sup> Jack Rabinow, "The Employee Inventor, An Inventor's View," 47 *JPOS* 469 (1965), at 472-73. This is an address given by Mr. Rabinow at the seminar, *The Employee Inventor*, *supra* note 14.

labored long, hard and successfully to work the bugs out of a production line designed to mass-produce the practical embodiment of a day-dreaming inventor's latest brainchild is within his rights in asking what qualifies the inventor for a special reward, but not him. Advocates of the bill might respond that Article I, Section 8, of the Constitution puts the inventor in a special category. There are at least two answers to this nice legal distinction. First of all, as explained earlier, Article I, Section 8, is not intended to safeguard a natural right. Second, and more important, can it realistically be expected that citing the content of Article I, Section 8, to the weary support worker is going to satisfactorily answer his question? The latter question practically answers itself.

In concluding this portion of the analysis, the reader should bear in mind that the potential dangers pointed out above would arise only if the money payment provided by the Moss bill were to be truly of the need-satisfying variety worth fighting for. Granting this, one is led to the realization that advocates of the proposed legislation who dismiss possible disruptive effects on cooperative effort as a myth, or only of minimal importance, are implicitly assuming that the reward is not worth competing for. If this be true, it seems that they are left open for the argument that their assumption also precludes the reward from being significant enough to prompt creative effort, unless it is contended that the carrot provided by the Moss bill is strong enough to stimulate innovation, but too weak to engender rivalry.

At best, this seems to be a rather fine line to walk.

#### MANAGEMENT RESPONSE UNDER THE MOSS BILL

Moving on now to what is perhaps the most significant problem underlying the Moss bill, the assumption expressly made in the preceding section that management will grant money payments in accord with the spirit of the proposed legislation will be more closely examined. In doing so, the factors determining management's behavior toward inventors will be considered first with the aid of a very perceptive paper authored by Irving H. Siegel. Dr. Siegel notes that, contrary to popular belief

... the pursuit of profit or other key objectives does not automatically or naturally inspire the improvement, diversification, or substitution of processes, materials, and product lines. The speculative benefits derivable from innovation may not beckon all managements

as strongly as the more certain benefits expected from routine operations. In short, we should not take for granted the receptiveness of all organizations to technical activity, their capacity to utilize it extensively and effectively, or their ability to exploit happy accidents that could lead away from familiar paths (including familiar technical paths). Company advertisements for scientists and engineers have doubtless encouraged a wrong opinion that industry is enthusiastically organizing safaris of serendipity.<sup>47</sup>

M. I. Stein, a clinical psychologist speaking at a University of Chicago seminar on *The Creative Organization* was considerably more blunt when he expressed doubt that industry really wanted creativity or "would know what to do with it." He went on to state his feeling that administrators had a "cash register philosophy of creativity" that biased them toward short-range projects and away from "what will be profitable five or ten years from now."<sup>48</sup>

While these comments may not comport with the popular view of how industry utilizes its creative resources, a moment's reflection will reveal why they most likely indicate the true state of affairs. To be specific, probably most would agree that a mission-oriented company must make a consistent profit to stay in business. This need to operate profitably necessitates reliance on small product innovations from year to year rather than development of truly far-out ideas. P. G. Peterson, President of Bell and Howell, has made the point rather well:

As you probably know, most products that are introduced on the market are rather minor changes from year to year, and built into the existing product is an enormous, a staggering, investment in tools, know-how, dies and equipment. One of the characteristics of basic technological change is that the start-up cost, so-called, is truly enormous, because you have to start all over again, let us say, with your tools. Whereas a product change in a camera might cost us \$100,000, a major innovation might cost us \$4,000,000.

I suspect that one of the reasons these changes do not take place is that in computing what it costs to make the change versus how much they will sell, management decides they are better off not making the change.<sup>49</sup>

As these comments point up, major innovative strides don't necessarily go hand in hand with profitability. Rather, the type of innovator that the corporation is really seeking is most likely the one who can

---

<sup>47</sup> *Supra* note 15, at 405.

<sup>48</sup> M. L. Stein, *The Creative Organization*, *supra* note 35, at 94-95.

<sup>49</sup> P. G. Peterson, "Some Approaches to Innovation in Industry," *The Creative Organization*, *supra* note 35, at 190.

consistently come up with rather minor product changes or, as Mr. Peterson has put it, make "minor adaptations of things you know how to do."<sup>50</sup>

Recognizing this, it makes perfect sense that management's present reward systems are geared toward encouraging consistent small steps in familiar product areas, rather than encouraging major innovative strides in tangentially related areas. But note that small steps in assigned product responsibility areas are just the ones which would lead to the smallest measure of compensation under the Moss bill. Thus, engaging in activity which would cause the employed inventor to "get ahead" in terms of job status, salary, responsibility and so probably would not lead to significant monetary awards under the statutory scheme. In view of this, would management even be called upon to award any significant special awards under the Moss bill? The answer here depends in large part on whether the employed inventor would respond to the reward system carried in management's actual behavior toward him or the one which would arise as a legal right via enactment of the Moss bill. Let us look into this area.

First off, we can perhaps all agree that management today, by and large, considers salaries paid to R&D employees as full consideration for their inventive efforts. The all but universal practice of requiring preassignment of patent rights for a nominal consideration certainly establishes this as a fact. Furthermore, one should recognize that the correctness of this viewpoint can be argued for in rather ringing terms. In addition to Mr. Rabinow's comments above, consider the following statement by Albert S. Davis, Jr.:

The research director, having recruited across the year's graduating classes, promoted to research assignments a dozen men whose post-graduate courses have been paid for by the company, and having stolen three top steroid chemists from a competitor, may understandably feel that these men are hired to be inventive—not to do routine bench work. This conclusion is reinforced when he looks over several million dollars' worth of laboratory and specialized research apparatus and reflects on the fact that only one in ten, or fifteen, or a hundred of his men's patentable inventions will really pay off and that the others have to be carried as dead weight. His opposite numbers in corporate planning, production, marketing, sales and finance also tell him in firm, round tones that their efforts have contributed at least as much as the inventor's.<sup>51</sup>

Whether or not one agrees with this management attitude is not the important consideration for purposes of present analysis. Rather, the

---

<sup>50</sup> *Supra* note 37, at 152.

<sup>51</sup> *Supra* note 41, at 52.

important point is to recognize that this attitude is a fact of corporate life which must be taken into account in analyzing the effect of the Moss bill.

Given this widespread attitude, it defies common sense to assume that mere enactment of the Moss bill will lead to significant special patenting awards if management can find a way to avoid it. Is there an avoidance mechanism in the Moss bill? The author feels there is, when the proposed legislation is evaluated in the context in which it must function. The bill provides that the employer and employee shall agree on compensation "within a reasonable period of time prior to the expiration of three months after a notice of allowability" from the Patent Office. Failing this, the employer "shall determine the compensation and pay the employee and shall give the employee a substantiated written declaration of how the amount of compensation was determined." If the *employee doesn't object* within two months, the *employer's determination becomes binding*.<sup>52</sup> Given this arrangement, query, whether the bill's enactment would result in any more than a nominal, perfunctory payment to an inventor about the time of notice of allowance.

Granting that it runs counter to management's true feelings to give significant special patenting awards, one must at least concede that management will attempt to grant nominal awards, despite the legislation. When management does hand down its final, nominal offer, will a dissatisfied employee exercise, within the two-month time period, his legal right to appeal to the Patent Office Arbitration Board or the courts? In predicting an answer here, Dr. Mosel's observation is highly pertinent: to wit, ". . . it is really management's behavior toward inventors which carries the real reward."<sup>53</sup> This actual behavior, as noted earlier, is going to result in rewarding the man in terms of recognition, responsibility, salary, job status and so forth. Common sense tells us that this is the reward which will influence the employee's conduct. Obviously, the employed inventor does not put management in a frame of mind to provide this reward as manifested through actual behavior by dragging it before a tribunal in the Patent Office or bringing it before a court charging unfair treatment. Rather, since employed inventors—at least by and large—most likely perceive the actual reward in corporate life to be that of "getting ahead" in the organization, they will probably accept management's decision rather than jeopardize its good will.

---

<sup>52</sup> H.R. 1483, *supra* note 1, § 414 (a), (b).

<sup>53</sup> *Supra* note 14, at 509.

Is there any evidence to back up this skeptical prediction of how employers and employees will conduct themselves under the Moss bill? In reporting on the operation of the West German legislation, James W. Brennan notes as follows:

Petitions to the Arbitration Board [by West German employed inventors dissatisfied with the award granted by their employer] have been disappointingly few. Of these, a large portion, estimated at 75-85%, have been filed by former employees who have quit their employer. Based on this estimate, only 15 of the 62 cases submitted to the Board in 1960, involved cases in which the complaining employee was still employed. It would be a remarkable testimony to the generosity of the employers if it could be believed that of an estimated 27,600 patent applications filed on behalf of German employees in 1960 [80% of the applications originating in Germany], in only 15 cases was the employee not fully satisfied with the compensation granted by the employer. If the registered design applications are included in this estimate, the testimony becomes even more remarkable and less believable.<sup>54</sup>

While the author regrets his inability to find more recent data on experience under the German law, he doubts that the picture has changed much in view of the circumstances surrounding the employee-employer relationship. In view of such circumstances, operation under the Moss bill seems most likely to result in a reward system wherein the employed inventor would get \$2.00 at the time notice of allowance is received in addition to (or in place of) the \$2.00 he now gets when he assigns his patent right to the company.

#### CONCLUSION

This paper has examined some of the potential pitfalls which could prevent the Moss bill from providing a significant spur to technological progress in this country. While some of these pitfalls are no doubt mere "boogeymen," their total impact militates strongly against enactment of the Moss bill until we know more—a lot more—than we now do about what is happening in this field. This is not to say that action which would bring forth more from employed inventors is not highly desirable. However, to be truly effective, such action must not only encourage the employee to create, it must also stimulate his boss to welcome that creativity and utilize it for society's benefit. Herein lies the primary reason why, in practical operation, the Moss bill may be doomed to failure.

---

<sup>54</sup> Brennan *supra* note 19, at 85.



## FORUM

---

---

Although the primary purpose of *IDEA* is to communicate the research work of the Institute, it also serves as an educational vehicle for the exchange of informed opinion. The positions taken by the authors of papers and notes in this section are not necessarily those of the Institute. It is hoped that the material published in this section will stimulate researchers to undertake further study of the issues.

### Functions, Costs and Fees of the U. S. Patent Office

JERRY COHEN\*

#### SUMMARY

THE FEES CHARGED BY THE U.S. PATENT OFFICE for examination and at various other occasions, and annual budgets for Patent Office operations, are remote topics for review outside government intramural accounting groups. But they should be of concern to a wider group than government accountants because they have a great deal to do with the quality of the patent system itself—a subject which does not appear to suffer from inattention.

---

\* Attorney, Charles Hieken Law Offices, Waltham, Massachusetts.

This paper analyzes the operation of the Patent Office into segments which may warrant different financing treatment—coverage of the costs of certain operations in whole or in part through user fees and coverage of others through appropriations. The broader context of government financing is presented to show the realistic limits of Patent Office financing proposals and, last but not least, the cost problems of the various Patent Office “customers” are considered.

The Patent Office Fee Bill of 1965 more than doubled the fee rates which had been unchanged for the prior three decades. It might have been supposed that this settled things for at least another decade. But it really didn't settle anything; and now the pending patent law recodification legislation includes a provision that the Patent Office shall be 65-75 percent *self-supporting* (a term which will be defined below but the percentage figure preceding it can, for the moment be taken to mean that fees must go up again).

The only thing that has changed since 1965 is the dawning of the age of consumerism. It is appropriate to set a search for value received as the theme of this cost inquiry.

---



---

#### PREMISES AND BACKGROUND

##### *The United States Commitment to a Patent System*

A patent system is not an inevitable part of a nation's political or economic structure.<sup>1</sup> A nation adopts it as a matter of free choice and from time to time may reaffirm the choice by retaining its patent system after critical searching examination. In the United States the choice was made in the Constitution<sup>2</sup> on a basis of essentially unanimous assent.<sup>3</sup> After critical searching examination by blue ribbon commissions in the 1930's,<sup>4</sup> '40's,<sup>5</sup> '50's,<sup>6</sup> and '60's,<sup>7</sup> the patent system

---

<sup>1</sup> Machlup, *An Economic Review of the Patent System*, Study No. 15 of the Senate Subcommittee on Patents, Trademarks and Copyrights (1958); *c.f.* Melman, *The Impact of the Patent System on Research*, Study No. 11 (1958).

<sup>2</sup> U.S. Const., art. I, § 8 (8).

<sup>3</sup> Federalist Papers, No. 43.

<sup>4</sup> Temporary National Economic Commission. Hearings, 1938-1941, Part 1, pp. 1-252, and Part 3, pp. 835-1148.

<sup>5</sup> The National Patent Planning Commission, c. 1945.

<sup>6</sup> The Attorney General's Committee to Study the Antitrust Laws—Report of March 31, 1955.

<sup>7</sup> *Report of the President's Commission on the Patent System* (Washington, D.C.: G.P.O. 1966).

has been reconfirmed as a benefit to the economy and a proper vehicle for the just reward of inventive contributions to the useful arts.<sup>8</sup>

### *The United States Commitment to an Examination System*

A patent issued without examination and limit of scope would hinder rather than advance the useful arts.<sup>9</sup> A patent issued without a presumption of validity would be a meager inducement to disclosure and investment.<sup>10</sup>

There has been widespread public rejection of any suggestion that the United States should shift to a registration system.<sup>11</sup> The Patent Office will remain a necessary institution to implement our examination system in its present form or in some modified form of the future such as the hybrid examination/registration system embodied in "deferred examination."<sup>12</sup>

### *Present Role of the United States Patent Office*

The present tasks of the Patent Office which are of significance in evaluating its financial needs involve:

- (1) Searching of prior art incident to examination.
  - (a) Reviewing prior published U.S. patents in a rigorous manual search effort based on a written table of classification supported by a classified U.S. patent collection.
  - (b) A similar search of foreign and U.S. patents and non-

<sup>8</sup> In addition to studies by the above commissions, the Senate Judiciary Committee has sponsored a series of studies reported in monographs published by the Committee.

<sup>9</sup> A hindrance expressed most colorfully in *Atlantic Works v. Brady*, 107 U.S. 192 (1882).

<sup>10</sup> There is no question but that early and complete disclosure is of basic importance to the carrying out of the purposes of the patent system, although the more relaxed disclosure standards of other countries must make us wary of the notion that ours is the only sound approach. Investment in the patented invention (as opposed to investment in research which might lead to a patentable invention), while urged as basic [Oppenheim, *Federal Antitrust Laws*, p. 767], has a less clearly recognized position in the Congressional plan for carrying out the Constitutional purpose of the patent system.

<sup>11</sup> *Supra* note 7. Examination has gained acceptance in France whose registration system is being phased into an examination system. The advent of the Patent Cooperation Treaty makes examination on a delegated basis available to countries which would not have attempted to establish one themselves.

<sup>12</sup> While deferred examination will be rejected *de jure* in any patent recodification of the near future, its *de facto* acceptance is assured by such external influences as an 18-month waiting period for examination of applications by foreign applicants under the Patent Cooperation Treaty.

- patent literature through informal classification and in more cursory fashion.
- (c) Miscellaneous search efforts including searches in standard texts, particularly in the chemical field, pilot programs in computer searches and foreign exchange of search reports, random citations of art through interference, appeal and public use proceedings.
- (2) Processing patent applications for the initial benefit of applicants.
    - (a) Affording filing dates to applications and receiving amendments.
    - (b) Processing applications through examination procedure and affording a forum for prosecution.
    - (c) Issuance of patents.
    - (d) Post-issue processing (reissue, certificate of correction, interference).
  - (3) Examination of patent applications.
    - (a) Review as to form; classification of application claims.
    - (b) Comparison to prior art.
    - (c) Application of law and prior art; conduct of examination.
    - (d) Administrative appeal procedures.
    - (e) Interference contests.
  - (4) Public representative role.
    - (a) Establishment of regulations as to form of patents and examination and shaping substantive patent law through administrative rulings of precedent value.
    - (b) Defense of appeals to courts.
    - (c) Recommendations to Congress and the Administration.
    - (d) Participation in international patent planning.
    - (e) Collection and publication of patenting statistics.
    - (f) Public education and limited advice to inventors.
  - (5) Processing applications and patents for the initial benefit of the public.
    - (a) Maintaining a collection of issued U.S. patents and file histories, foreign patents, nonpatent literature.
    - (b) Distribution of printed U.S. patents at low cost.
    - (c) Access to other documents.
    - (d) Notification of new patents through *Official Gazette* and related index.
    - (e) Updating patent information.

- (6) Assignment recording, indexing and public access.
- (7) Technical information storage ("data base") and public service.
  - (a) Classification activity.
  - (b) Acquiring printed prior art.
  - (c) Processing new acquisitions into classified search files.
  - (d) Maintaining examination and public search facilities.
- (8) Building capabilities for technical information storage.
  - (a) Research and development.
  - (b) Cooperative arrangements with other countries.
- (9) Building capability for examination.
  - (a) Quality control.
  - (b) Cooperative arrangements with other countries.
- (10) Support.
  - (a) Recruitment, training, development, maintenance, orientation supervision and leadership of (i) examining corps and clerical personnel, (ii) public service personnel, and (iii) administrative and supervisory staffs.
  - (b) Facilities and equipment acquisition and maintenance.
  - (c) Budgeting and planning.

(Note—Trademark functions are included.)

For fiscal 1968, costs and income were approximately as follows:

TABLE I

Costs		(\$ million)
I—Examination and issuance of patents		\$25,134
II—Establishment and maintenance of search files		3,034
III—Information dissemination		8,760
Total		\$36,928
Income		(\$ million)
I—(a) Filing fees*		\$ 7,638
(b) Issue fees*		9,274
(c) Appeal (and brief) fees		555
(d) Other		30
Subtotal		\$17,497
II—Charges		
(a) Patent copies		\$ 2,568
(b) Record reproduction (about)		1,150
(c) Recording assignments		300
(d) Other (about)		1,476
Subtotal		\$5,581
Total		\$23,078

\* Including extras.

It is hard to plot trends in view of the reorganization of the Patent Office on December 1, 1969 and a consequent reshuffling of its accounts. But total costs, as might be expected, trend upward sharply and at a faster rate than total fee income.

TABLE 2

Fiscal Year	Operating Costs (\$ million)	Fee Income (\$ million)
1966	\$33,507	\$18,146
1967	35,534	23,666
1968	38,571	24,526
1969	42,576	25,456
1970	49,367	26,278

Issue and filing fees for patents provided about \$11 million in FY 1966 and \$18 million in FY 1970. However, the number of patent applications filed was 93,022 in FY 1966 and 100,116 in FY 1970, and the patents issued were 66,243 in FY 1966 and 66,339 in FY 1970.<sup>13</sup>

#### *The Future Role of the United States Patent Office*

The functions described above may also include some of the following modifications and additions in the future:

- (1) Acceptance at face value of search report of a foreign patent office or international patent search agency.
- (2) Conduct of search effort in the U.S. for use in a search report without examination.
- (3) Splitting of search and examination functions.
- (4) Referral of search questions (for specific cases or search requests of a general nature) to outside public and private agencies. This may also include search tasks of a continuing nature patterned after, for instance, the Defense Metals Information Center (operated by Battelle Memorial Institute under Department of Defense contract to serve the information needs of the defense community re high-temperature-use metals).
- (5) Expanded post-issue processing in quasi-opposition proceedings and increased use of reissue proceedings.
- (6) Establishment of patent of addition (or other new matter), protection, and publication as a means to partially close the 20-year gap between patent expiration and state of the art.

<sup>13</sup> Commissioner of Patents, *Annual Report—Fiscal Year 1970*.

- (7) Preapplication proceedings to receive and record disclosure documents for use in establishing priority and/or defense publication (one trial program is now in progress).
- (8) New forms of post-issue proceedings in the nature of referral from district courts trying infringement matters.
- (9) Examination of international applications leading to a Certificate of Patentability.
- (10) Consolidating separate information sources to provide—in response to a simple request for a patent copy—a document photo-composed currently, drawing (from high-speed automatic data processing storage) up-dated information as to basic classification (international), cross-references, references cited and classes searched in original and subsequent proceedings, subsequent patents citing the instant patent, foreign counterparts, assignment history, proceedings in the courts and Patent Office involving the patent directly, “related patents” lists, as well as the patent document itself as originally issued and as modified through subsequent proceedings.
- (11) Processing international applications.
- (12) Substantial reduction of assignment recording (and of recording fees) due to assignee filing under patent law revisions.
- (13) Recording license interests.
- (14) Becoming a more effective clearinghouse for sale and licensing of patents.
- (15) Improved prior art searching for the public either directly or through better cooperation with private searching firms.

A Patent Office offering these additional functions may be no more expensive than the present Patent Office (to the government, the patent applicant, or prior art searcher) in the long run, taking into account the long-range economy of data-processing methods (present and projected), and considering the economy of volume by buying search work from more efficient depositories of information (in specific fields), and international division of effort. However, in the short run it is clear that substantially increased spending in administrative and research and development operations is necessary to bring about the implementation (or at least an informed rejection) of the additional functions. It is of equal importance to the increased allocation of money for these purposes that the increased allocation be made pursuant to a long-range commitment to maintaining excellence in the operation of

the Patent Office and to take advantage of opportunities offered by technology and international cooperation to upgrade that definition of excellence.

#### FINANCIAL STRUCTURE OF THE U.S. PATENT OFFICE

Most Patent Office fees are fixed by statute.<sup>14</sup> Services covered by the statutory fees include essentially all of those directly related to examination and issue. Also included are several services not so directly related, such as patent copy sales and recordation of assignments and related papers.

Some fees may be set by the Patent Office.<sup>15</sup> Some of the more important services covered by these fees include: Selling copies of foreign patents and nonpatent publications; selling certified copies of applications; making and correcting drawings; registering of attorneys and agents; and performing searches of Patent Office records. It is expected that a number of additional services may be available to the public in the future where the fees would be fixed by the Patent Office. In addition, it is anticipated that greater requests and demands will be made for copies of documents and records under the public information section of the Administrative Procedure Act.<sup>16</sup>

All operating funds for the Patent Office are obtained from Congress by appropriation. The Patent Office proposed budget must be submitted to the Secretary of Commerce first, and then the Bureau of the Budget for approval, before it is incorporated into the President's printed budget for submission to Congress. This process requires the anticipation of budgeting needs more than a year and a half in advance. Supplemental appropriations can be obtained during a current fiscal year, but requests must again be approved by the Secretary of Commerce and the Bureau of the Budget, and considerable justification must be presented. Congress, of course, must then appropriate funds before they become available.

#### PROBLEMS IN OPERATING UNDER THE PRESENT SYSTEM

- (1) The system lacks flexibility. The Patent Office is unable to respond adequately to public requests for new services and

---

<sup>14</sup> 35 U.S.C. § 41 (a).

<sup>15</sup> 35 U.S.C. § 41 (b).

<sup>16</sup> Freedom of Information Act, Pub. Law 89-487 of July 4, 1966, 5 U.S.C. 552. One abortive attempt was made to use the act to break down the long standing confidential treatment of pending applications. In re Campbell, 170 U.S.P.Q. 354.



for the increasing demand and volume of requests for existing services.

- (2) The system is not based on an analytically determined, desirable cost recovery rate. There is no clearly stated resolution of the conflict between the public policy on cost recovery versus the public benefits of a patent system.
- (3) It is too difficult to obtain fee increases to cover rising costs. Years of legislative effort may be required.
- (4) Appropriations required for growth of examining operation are difficult to get. When they are granted they are used to meet rising demands for existing services.
- (5) Relative size of application and issue fees has been criticized. Some critics feel the whole fee structure should be reviewed and possibly restructured.

#### DEFINING THE ISSUES

The first order of business in any analysis of the issue of Patent Office financing is to mark the pitfalls of sloganeering which have in the past blocked promising attempts to reason through the problems involved.

#### *Cost Recovery Rates*

"Cost recovery rate" is a nonformal term used to indicate the ratio of Patent Office income through "user charges" (a formal term), and other receipts, to actual costs of operation or budgeted costs in a given fiscal year or other measuring period, past or projected. The ratio is usually multiplied by 100 and expressed as a percentage. A general expression of the same consideration is the extent to which the Patent Office is said to be "self-supporting."

Now this represents a semantic trap to the unwary viewer who has neglected to ask "Who recovers?"; "Who is the self that is supported?" The Patent Office does not support itself at all. All of its receipts are paid into the U.S. Treasury. All costs of the Patent Office are paid by the U.S. Treasury.

The terms "cost recovery rate" and "self-supporting" indicate that the patent system (or at least that portion of the patent system operated via the Patent Office) imposes itself on the American public purse and sense of economic and social priorities only as a small net imposition to the extent that the rate is slightly below 100 percent, and as a great

imposition to the extent that the rate is substantially below 100 percent. The conventional wisdom then goes on to the assumption that a self-supporting agency is welcomed more favorably by Administrative and Congressional budgetary authorities and can more readily get approval of its budgets. Such a narrow view of American public policy formulation and implementation has some support in logic and experience, but not to the extent that it can be accepted as a working theorem.

Congress has not committed the Patent Office to any specific cost recovery rate in the past. In this century, the rate has been as high as 110 percent and as low as 33 percent without giving offense.<sup>17</sup> Congressional attention has focused, and properly so, on such matters as the quality of Patent Office service and patent examination backlog. The most recent legislation on fees,<sup>18</sup> was reported out of the Senate Judiciary Committee with the comment (by Senator McClellan, chairman of the patent subcommittee), that in approving the bill, the Committee was not required to decide whether the Patent Office should be self-supporting.<sup>19</sup> The fees provided in that legislation taken together with projected costs of that time would have offered 74 percent "cost recovery" which the Committee felt was reasonable (without indicating whether a higher or lower percentage would be unreasonable).<sup>20</sup>

### *Public Benefit*

If Administration officials sometimes overstate the need for increased cost recovery, it is equally true that inventors' groups and Bar associations are insensitive to the reality that some degree of cost recovery is a necessity fixed by broader contexts of history and organization.

In hearings on Patent Office legislation, the argument is made that the public benefits of the patent system are such that the Patent Office cost recovery rate should be essentially zero. The argument usually incorporates an analogy to zero recovery rate activities of the Department of Agriculture.<sup>21</sup> Congress has never responded to the argument. The consistent pattern of Congressional action (or inaction) must be taken as acceptance of cost recovery to some degree.

---

<sup>17</sup> See "Patent Office Fees," Hearings on H.R. 10966 (April 19, 1962), 87th Cong., 2nd Sess., p. 99. The 118% years were 1906-1907. Cost recovery was over 80% from 1900-1942 and declined to 32% by 1961.

<sup>18</sup> 75 Stat. 259. The bill was H.R. 4185, 89th Cong., 1st. Sess.

<sup>19</sup> 89th Cong., S. Rept. No. 301, p. 8.

<sup>20</sup> *Ibid.*

<sup>21</sup> See e.g. Testimony of Fritz G. Lanham, Hearings on H.R. 4983 and 6175 (June 3 and 17, 1955), 84th Cong., 1st. Sess., p. 77.

Looking at federal agencies as a whole, several indications of a cost recovery trend are found. The Independent Offices Appropriation Act of 1952<sup>22</sup> provides:

It is the sense of the Congress that any work, service, publication, report, document, benefit, privilege, authority, use, franchise, license, permit, certificate, registration, . . . provided by any Federal agency . . . to or for any reason . . . shall be self-sustaining to the full extent possible [through user charges] . . . [which shall be set by agency heads and] fair and equitable taking into consideration direct and indirect cost to the Government, value to the recipient, public policy or interest served and other pertinent facts. . . and paid into the Treasury as miscellaneous receipts. . .

It is estimated that for fiscal year 1968 user charges produced \$2.09 billion in revenue out of total federal government revenue of \$155.8 billion (1.4%). Since 1962, user charge revenue has increased at a faster rate than total federal revenue.<sup>23</sup> A Presidential Memorandum<sup>24</sup> to all heads of departments and agencies affirms the concept of user charges as good economics and good government.

User charges are inappropriate for wholly public functions, e.g. national defense, but are appropriate and clearly national policy to the extent a chargeable private beneficiary of government activity can be identified and adequately distinguished from related public benefits following the criteria of the 1952 Act. In this vein a more thoughtful view of Patent Office activities can be developed. The patent examiner who causes patent claims to be narrowed is performing no less a public function than those performed by examiners of the Internal Revenue Service, Federal Trade Commission, Interstate Commerce Commission, or Food and Drug Administration. The sale of patent copies at 50 cents to the scientific and industrial communities has the same balance of public and private benefits as the sale of other technical literature to these same purchasers by the Federal Clearinghouse for Scientific and Technical Information (at \$3.00). However, the sale or transfer of a patent to a patent applicant to expedite examination involves a different balance of public and private benefits.<sup>25</sup>

---

<sup>22</sup> 31 U.S.C. § 841.

<sup>23</sup> Annual Progress Reports have been issued by the Office of Management and Budget.

<sup>24</sup> May 17, 1966.

<sup>25</sup> Patent Office operations are classified in the User Charges program under "Permits" along with fees for admission to practice before the tax court, easement grants on public lands, permits to graze in national forests, fishing licenses, registration of securities.

Despite the fact that user charges are as old as our republic, the issue has not been the focus of substantial analysis until recent years. Thus some fundamental points are still unanswered. Chief among these is the question of "overhead" allocation. Having determined that a given activity confers more private than public benefits and that its direct costs should be recovered through user charges, how shall indirect costs related to the activity be treated? Shall costs of the Patent Office research program be allocated pro-rata among wholly self-supporting activities such as patent copy sales and partially self-supporting activities such as patent examination? Or shall we recognize that the research work involves an entirely public benefit and allocate *no* portion of costs to be recovered out of user charges.

### *High Fees*

When is a contemplated increase in Patent Office fees too much of an increase? Taking into account all the factors involved a fair answer is that the contemplated increase is too high if the raised fee structure will discourage patenting activity to a significantly greater extent than the present fee structure.<sup>26</sup>

In studying fees as a deterrent to patenting activity, it is misleading to focus on the fees alone. Essentially all patenting activity involves cost of legal service which according to recent Bar association surveys run from \$350-\$1000 for filing a patent application and can involve several hundred dollars for additional patent prosecution effort. On the other hand, it must also be recognized that recent changes in Patent Office procedures have increased the number of patent applications that must be filed to protect what the inventor might view as a single inventive concept; thus, the cost effects of the fee structure are multiplied.

### *The Indigent Inventor*

Despite the fact that a majority of patent applications are assigned to and filed by profitable corporations deducting (directly or through depreciation) Patent Office fees from taxable income, the individual inventor, acting directly or through a closely held corporation and committing his personal resources to the patenting process, is an

---

<sup>26</sup> The Senate Judiciary Committee (Sen. McClellan) has said: "In view of the fact that all other expenses involved in securing a patent, most notably legal fees, have increased since 1932 without any reduction in the number of applications filed, the committee does not agree that the adjustment of fees provided in this bill will discourage invention. . . ." Report, *supra* note 19 at p. 9.

important client of the patent system. Certain individual inventors of limited resources, who prosecute their own applications or persuade a patent attorney to represent them without present payment of fees, are invoked as the principal reason for minimizing Patent Office fees. It is suggested that on the level of public policy analysis, this is a red herring.

The Patent Office should not be held to the level of effectiveness which its poorest client can afford. It is an illusory benefit to the indigent inventor to hold fees to his ability to pay if the result is a less effective patent system to protect his invention.

The answer to the problem of the "indigent inventor" is direct funding based on his status. It is not without precedent in American public policy to draw valid distinctions based on status. The examples range from the "forma pauperis" and assigned counsel of our criminal justice system to small business loans and preferences. Any consideration of Patent Office fee structure should take into account methods of subsidizing the filing of patent applications by certain individual inventors and corporations. Such subsidy could come through direct grants and loans or tax credit. It would also be reasonable to have the Patent Office grant fee concessions in such cases, but this form of cashless subsidy is (a) contrary to modern intragovernmental accounting practice, and (b) would have to be made available to foreign patent applicants to comply with treaty commitments,<sup>27</sup> whereas direct subsidy discrimination does not offend the treaty (compare the status of European export subsidies under customs treaties). Some existing forms of subsidies are (a) allowability of patent costs as reimbursable overhead to government contractors,<sup>28</sup> (b) tax provisions,<sup>29</sup> (c) the Small Business Investment Corporation Program,<sup>30</sup> and the like.

### *Revolving Funds*

Each federal agency is interested in establishing a revolving fund of its receipts. The Patent Office interest in such a fund was expressed with sufficient persuasion before the President's Commission on the

---

<sup>27</sup> Paris Convention 1883 (Lisbon Text—1958), Art. 2.

<sup>28</sup> TRW Systems, Inc., ASBCA #11,499 (1968).

<sup>29</sup> See generally, *Technological Innovation: Its Environment and Change*. Dept. of Commerce 1967.

<sup>30</sup> As well as other benefits of the Small Business Act, and Small Business Investment Act including loans for patenting costs, antitrust exemptions for R&D pools, patent and technology licensing, cooperative patenting programs.

Patent System that the Commission recommended authorizing the Office to establish a revolving fund of all its receipts to support its operation.<sup>31</sup> Such a concept, if applied to all agencies, would result in an inefficient allocation of total government resources; accordingly, an agency seeking a revolving fund should be able to show special merit in its request—either in the nature of the agency's mission or in the singular appropriateness of the revolving fund method to fit the agency's operation.

There are some 150 revolving funds and trust funds in the federal government structure and the annual gross business of these funds is about \$100 billion.<sup>32</sup> The revolving funds are broken down into two major categories:

- (1) *Public enterprise funds*—These funds provide an assured (read “politically secure”) source of support for certain grant, loan and guarantee programs such as the Commodity Credit Corporation, Federal National Mortgage Association, Federal Farm Mortgage Corporation, Small Business Administration Disaster Loan Fund, Defense Production Guarantees, Federal Savings and Loan Insurance Corporation, Tennessee Valley Authority Fund, St. Lawrence Seaway Development Corporation, and in some instances provide an administrative expedient for dealing with the public on a large scale, e.g. Federal Tax Lien revolving fund.
- (2) *Intragovernmental funds*—e.g., Government Printing Office revolving fund (GPO charges other agencies for printing service to reimburse the fund).

Generally, the use of a revolving fund involves a greater degree of budgetary discretion to the agency and is used in support of a 100 percent cost recovery rate, but not necessarily (e.g., the Post Office revolving fund is closely controlled by Congress and user charges must be supplemented by annual appropriations).

The agency revolving type funds most nearly analogous to the type which might be used by the Patent Office are those of (a) the National Bureau of Standards (a revolving public enterprise fund); and (b) the Federal Clearinghouse for Scientific and Technical Information (a trust fund, similar in effect to a revolving fund). These funds are available to activities of the agencies as a whole, and are accompanied by Congressional policies of setting user charges to make the agencies

---

<sup>31</sup> *Supra* note 7, Recommendation XXVII.

<sup>32</sup> Annual reports appear in appendices to the annual U.S. Budgets.

self-sustaining (in the finer sense of the term). These agencies (both branches of Department of Commerce) are not obliged to recover overhead costs incurred outside their own bailiwicks, but are obliged to recover costs such as reserves for equipment depreciation and accrued leave of their own personnel.

It is interesting to note as a matter of history that the Patent Office had a revolving fund which was abolished by Congress in 1932.

### *Maintenance Fees*

Such fees have been proposed for the U.S. Patent Office from time to time and were considered in Congressional hearings leading to the enactment of increased basic fees (without the addition of maintenance fees) in 1965. The Senate report indicates a Scotch verdict on the issue.<sup>33</sup> The Patent Office arguments as to the desirability of deferring costs for the inventor were equally balanced with Bar association arguments as to the increased handling costs and confusion to the inventor and to outsiders as to the status of a patent during grace or forgiveness periods allowed for delinquent payments. The balance was finally swung against the proposal by the impending appointment of a President's Commission; it was stated that no radical changes should be made at that time. Since then, the Commission has met and given its report, and the context in which the maintenance fee issue was argued in 1965 remains unchanged.

One additional argument which has not been clearly expressed is that enactment of relatively modest maintenance fees opens the "political floodgates" and eventually establishes a vehicle for the imposition of unduly high maintenance fees such as those found in the German fee structure (some \$3000 over the life of a patent). Also, maintenance fee structures of foreign countries are related to the working requirements of foreign countries. The United States does not have a working requirement. It may be useful to estimate the efficacy of such fees. If maintenance fees were to be adopted as a means of deferring required basic fee increases, the following schedule of maintenance fees enacted now would have that effect up to about 1990: \$100, \$200, \$300, and \$400 at 4, 8, 12 and 16 years from filing, respectively.

For purposes of this estimate a patent term of 20 years from filing and a two-thirds cost recovery policy have been assumed. It has also been assumed that the percentage of patentees willing to pay maintenance fees will be about 75 percent after 4 years, 40 percent after 8

---

<sup>33</sup> *Supra* note 19 at p. 9, Conclusion 3.

years, 20 percent after 12 years and 5 percent after 16 years. This estimate makes little allowance for cost increases and does not allow for new Patent Office functions.

#### ANALYSIS, CONCLUSIONS AND QUESTIONS

- (1) Uncertainty as to national priorities and policy is at the core of the several problems outlined above. The Patent Office needs guidelines from Congress endorsing its own ambitious (and worthwhile) plans for maintaining an excellent examination system and setting policy on who will pay the cost of implementing these plans.
- (2) Patent Office charges are one small segment of the financing problems of the small inventor. The total problem requires solution through financing means external to the Patent Office. The Patent Office cannot solve the total problem through holding low fees.
- (3) Patenting activity of large and small inventors needs study to determine the degree of passing-on of Patent Office fees to American consumers. If and when such fees become a widely diffused indirect general tax, it will be time to lower these fees and substitute appropriations derived from direct taxation in a progressive tax structure for the regressive structure of indirect taxation. U.S. patenting and invention exploitation by foreign interests will also require careful study.
- (4) The Patent Office has a complicated mission which includes many functions having analogy to several different agencies and fitting the framework of several conflicting policies. However a functional breakdown can be made and the appropriate financing of specific functions or groups of functions are then easily stated within the framework of existing practice and consensus view.
- (5) The examining function of the Patent Office is conceptually divisible into two distinct functions—first, examination for the benefit of the public to screen out overbroad patent claims; second, examination for the benefit of the applicant to grant a valid patent. The first fits a pattern suitable for support through appropriation, the second is suitable for user charges. However, the two conceptual functions are



carried out together in what is, mechanically, a single examination function. Considering the relevant issues and public policies discussed in this paper, a 50 percent cost recovery rate is appropriate. The examination function pool so covered (at 50 percent recovery) includes examiner salaries, benefits, and accrued leave, examining group direct supervisory and support personnel operations and facilities (including examiner search files and recruitment and training of examiners) and a pro-rata share of indirect support. The requirements of the examination function should determine the total pool.

- (6) Increase in fees (and in appropriations) will be necessary at shorter intervals (i.e. greater frequency) than in the past due to growing rate of increase of costs (e.g. salary increases set by Civil Service policy uncontrollable by the Patent Office). It is not reasonable to attempt to exempt the coequal patrons of the examination function—taxpayer and inventor—from the natural effects of inflation and growth.

#### RECOMMENDATIONS

- (1) Patent Office financing should be considered with respect to specific functions as outlined above. Overly refined breakdowns for purposes of analysis can be regrouped for purposes of implementation.
- (2) Legislation should be sought by Bar groups setting out the sense of Congress that:
  - (a) it is national policy to maintain the Patent Office at a high level of efficiency and setting quantity and quality goals for Patent Office operation;
  - (b) recognizing the essentially public-benefit nature of the patent examination system as a whole;
  - (c) setting cost recovery guidance for various grouping of Patent Office functions based on existing public policies of such functions, specifically (i) 50 percent cost recovery for examination; (ii) 100 percent cost recovery for public information; (iii) zero cost recovery for administration, research and development, and support functions except to the extent allocated to (i) and (ii) as overhead or presented to Congress as specific projects with an integral user charges financing plan.

Such "legislation" can be sought in connection with the next budget and appropriations cycle and/or in connection with pending patent law recodification.

- (3) The Patent Office should seek specific permanent legislation giving it the means to meet Congressional guidelines as to cost recovery while also meeting Congressional guidelines as to quantity and quality of work output. It would require delegation of power to set charges which are now statutory to meet 100 percent cost recovery guidelines. It would also require a revolving fund as to services of a simple ministerial nature whose costs are dependent on public demand, e.g., sale of patent copies. As for meeting partial cost recovery guidelines, the appropriateness of mechanisms will depend on the external limits of the Patent Office's ability to cut spending when appropriations are reduced. Such external limits include Civil Service tenure and pay policies and the need for stability in Patent Office operations.

However it has to be emphasized that any guidelines presented now as to cost recovery are applicable to present conditions of Patent Office operation and are derived from an analysis of present Patent Office functions. A significant change in the nature of Patent Office operations or the addition of a significant new function should not be slavishly followed by an increase in fees. Instead the guidelines should be reconsidered in view of the change. Congress and the people are properly interested in any such change and should pass on a plan of financing presented simultaneously with the proposed change.

In Congress, the presently active patent bill (born a patent reform bill, but now reduced by consensus abrasion to a recodification with minor adjustment), S.643, was favorably reported out of the patent subcommittee to the Senate Judiciary Committee and contains a fee section providing

**§ 41. Patent fees**

(a) The Commissioner shall charge the following fees:

(1) On filing each application for an original patent, except in design cases, \$65; in addition, on filing or on presentation at any other time, \$10 for each claim in independent form which is in excess of one, and \$2 for each claim whether independent or dependent which is in excess of ten. No fee shall be charged for the filing of claims in a patent during reexamination under section 191 of this title. Errors in payment of the additional fee may be rectified in accordance with regulations prescribed by the Commissioner.

(2) Except in design cases, for issuing each original or reissue patent, \$100; in addition, \$10 for each page (or portion thereof) of specification as printed, and \$2 for each sheet of drawing.

(3) In design cases:

a. On filing each design application, \$20.

b. On issuing each design patent: For three years and six months, \$10; for seven years, \$20; and for fourteen years, \$30.

(4) On filing each application for the reissue of a patent, \$65; in addition, on filing or on presentation at any other time, \$10 for each claim in independent form which is in excess of the number of independent claims of the original patent, and \$2 for each claim (whether independent or dependent) which is in excess of ten and also in excess of the number of claims of the original patent. Errors in payment of the additional fees may be rectified in accordance with regulations of the Commissioner.

(5) On filing each disclaimer, \$15.

(6) On appeal under section 134 of this title, for the first time from the examiner to the Board of Appeals, \$50; in addition, on filing a brief in support of such appeal, \$50.

(7) On filing each petition for the revival of an abandoned application for a patent or for the delayed payment of the fee for issuing each patent, \$15.

(8) For certificate under section 255 or under section 256 of this title, \$15.

(9) As available: For uncertified copies of specifications and drawings of patents (except design patents), 50 cents per copy; for design patents, 20 cents per copy; the Commissioner may establish a charge not to exceed \$1 per copy for patents in excess of twenty-five pages of drawings and specifications and for plant patents in color; special rates for libraries specified in section 13 of this title, \$50 for patents issued in one year. The Commissioner may, without charge, provide applicants with copies of specifications and drawings of patents when referred to in a notice under section 132.

(10) For recording every assignment, agreement, or other paper relating to the property in a patent or application, \$20; where the document relates to more than one patent or application, \$3 for each additional item.

(11) For each certificate, \$1.

(12) for publishing a pending application, under section 123 of this title, \$100; in addition, \$10 for each page (or portion thereof) of specification as printed, and \$2 for each sheet of drawing.

(b) The Commissioner may reduce the fees under subsection (a) (2) of this section up to 50 per centum upon the condition that an additional copy of the specification is submitted in machine readable form in accordance with regulations established by the Commissioner.

(c) The Commissioner may establish charges for copies of records, publications, or services furnished by the Patent Office, not specified above.

(d) The fees prescribed by or under this section shall apply to any other Government department or agency, or officer thereof, except that the Commissioner may waive the payment of any fee for services or materials in cases of occasional or incidental requests by a Government department or agency, or officer thereof.

(e) The Patent Office shall recover by fees not less than 65 per centum of the costs of operation of the Patent Office. When such recovery consistently falls below this percentage, the Commissioner shall transmit to the Congress his recommendations for an adjustment of the fee schedule.

**§ 42. Payment of patent fees; return of excess amounts**

All fees shall be paid to the Commissioner, who shall deposit the same in the Treasury of the United States in such manner as the Secretary of the Treasury directs, and the Commissioner may refund any sum paid by mistake or in excess of the fee required.

These tentative provisions reflect the impact of some of the underlying considerations outlined in this paper—the self-supporting and user charges concepts, flexibility for the Patent Office, revolving fund, and maintenance fees. Some of the other concepts, such as clearer policy for quality of the product sold and more refined allocation of the user charges to specific users, may also require attention before the bill becomes law.

## Book Review

Mayers, Harry R., *Drafting Patent License Agreements* (Washington, D.C.: The Bureau of National Affairs, Inc., 1971), 268 pages, \$25.00.

Mr. Mayers' book is written as I think a practical legal guide should be written—clearly, carefully, concisely, based on broad experience, containing much useful information, in the context of related areas of the law, with just the right amount of sage philosophy to provide color and moral purpose for the endeavor.

A philosophical preface leads the reader to a very pragmatic, orderly and comprehensive table of contents—and this philosophical realism is the measure of what follows. The author returns again and again in the various sections of the book to the practical and to the philosophical aspects of licensing agreements. With a minimum of verbiage, examples of simple as well as highly involved licensing provisions and arrangements are set forth in detail. The reader is cautioned at the outset and on appropriate occasion about the limitations of the main tools he uses, namely (1) semantics and (2) human intelligence.

The author sets the stage with sections on some premises and limitations; the opening part of the agreement; definitions; reservations and exceptions; and on nonexclusive and exclusive licenses. From these discussions he takes the reader in a logical series of steps through sections dealing with the general nature and particular provisions of the license agreement, such as those relating to the granting clause; licenses under improvements; royalties, reports and payments; special legal problems; more favorable terms provisions; transferability of rights and obligations; validity and construction of patents; representations and warranties; etc. Interspersed are cautionary observations with respect to possible misuse and antitrust problems. The reader is advised on the dynamic situation in the related antitrust and trade practice law and the advisability of consulting counsel on the latest developments in these subjects. After an enlightening consideration of the various provisions that might be incorporated in the patent agreement (with detailed examples), the author turns to the sale or other transfer of unpatented technology and concludes with a section on foreign patent licensing agreements. The text, examples in the text and examples in the appendices are cross-referenced. The appendix

also contains some fundamentals of U.S. patent law in outline form. A table of cases and a topical index completes the book.

Mr. Mayers has for many years been engaged in drafting and negotiating license agreements of a highly sophisticated nature, involving complex technology and large sums of money—that experience and the author's clear and cogent legal reasoning make this guidebook of special value to the profession.

L.J.H.

# Avoiding Fraud on the Patent Office

## An Institute Clinic

### CONTENTS

FRAUD ON PATENT OFFICE AS "ELEMENTAL" FRAUD 627

PRACTICE BEFORE THE PATENT OFFICE AND COURTS IN THE PAST 629;  
642; 664; 673; 680

SOURCES OF FRAUD 627; 632-636; 677

The Oath or Declaration of Inventorship 642-643; 656

Affidavits under Rules #131 and #132 643-644

Alterations in Application After Filing 643

Introducing References in Later Stages of Prosecution  
and After Issue 648-651; 667

Conflict of Interest 654-655

HOW, WHEN AND TO WHAT EXTENT DATA DISCLOSED 627-629; 631-  
632; 637; 639

Difficulty of Formulating a General Standard 629; 632; 657-659;  
676

Data That Should Be Included in Specification 631; 677

Prior Art References and Publication Precautions 635-637; 644;  
652-654; 656-663; 665-666; 676; 684-689; 692-693

Including Bad Experimental Results Along with Good 637-638;  
640-641; 644; 666-667; 675-677

When Questionable Statutory Bars Should Be Disclosed 638; 655-  
656; 677-678; 689; 692

Telephone Interview vs. Business Conducted in Writing 649

STANDARDS OF CONDUCT OF ATTORNEYS 645; 672

The Oath or Declaration of Inventorship 645

Claims Known or Should Be Known to Be Unpatentable 645;  
667; 671-672

Deliberately Claiming Broader Art 665; 669-670  
Disclosure of Prior Art 645; 690-695  
False or Misleading Representations of Fact or Law 645; 679-  
681; 683-684; 687-689  
Withdrawal from Case 646; 690

IF PATENT WOULD BE INVALID ANYWAY, WHY RAISE QUESTION OF FRAUD  
646

CHANGING INTERPRETATION ON REISSUES 663

DIFFICULTIES IN OBTAINING INFORMATION FROM RESEARCHERS 666

EX PARTE OPPOSITION 667-668

COMPUTER SEARCHING 668-669

FRAUD CHARGES AND PATENT LITIGATION 673-694

Only Government Could Attack for Fraud (Historical) 673

Defense of Fraud by Private Parties 673

Fraud Per Se an Element of Antitrust Violation 673; 694

Relation of Fraud Charge to Attorneys' Fees 673; 675

Prospect of Treble Damages 674-676

Fraudulent Securing of Foreign Patents Utilized As Obstacle  
to International Commerce 674

Unsubstantiated Charge of Fraud Generally Not Penalized 674-  
676; 680-681; 694

Demand for Jury Trial 675

Psychological Impact of Misrepresentation Charge 675-676

Discovery Procedure Likely to Uncover Misconduct 629; 633; 676-  
678; 684

Significance of Witnesses 677-678

Overly Defendant Oriented Litigation Situation 678; 694

Vulnerability to Charge of Conspiracy if Defendant Settles 679-  
680

Proposal for Validity Court to Handle Fraud 681

Proposal for Patent Office to Handle Fraud under  
Section 192 of New Bill 681-683

Testimony of Patent Office Examiners 683

Corporate "Awareness" of Fraud 687-688



# Avoiding Fraud on the Patent Office

## An Institute Clinic

### INTRODUCTION

A clinic on "Avoiding Fraud on the Patent Office" was held at the Institute's headquarters in Washington, D. C., on November 18, 1971.

Chairman of the Clinic was Frank Neuhauser of General Electric Company and the principle speakers, who represented four different points of view, were Paul A. Rose, Union Carbide Corporation, speaking as a soliciting attorney; Albert C. Johnston, Keith, Johnston and Isner, as a litigating lawyer; Jack Rabinow, Control Data Corporation, as inventor-research director; and P. J. Federico, Cushman, Darby and Cushman as a former member of the Patent Office staff. L. James Harris, Director of the Institute, welcomed the participants and presented the topic under discussion. As in the previous Institute clinics, the experts attended by invitation and represented a variety of disciplines.

Former clinics held by the Institute and reported in *IDEA* are Statutory Requirements of Companies for Protection of Intellectual Creations, Volume 8, Number 4; Computer Software Protection, Volume 13, Number 3; The Patent Cooperation Treaty: Views of Informed Innovators, Volume 14, Number 1; Trade Secrets, Volume 14, Number 2; Unfair Trade Practices Relating to Industrial-Intellectual Property, Volume 14, Number 3; International Trademark Protection: Private Interests and Public Programs, Volume 15, Number 1; and Joint Ventures Abroad: Industrial Property, Taxation, and Competition, Volume 15, Number 2.

**Clinic Participants**

Herbert L. Allen	—RCA Corporation, David Sarnoff Research Center
Andrew B. Beveridge	—Browne, Beveridge & DeGrandi
Brian G. Brunsvold	—Finnegan, Henderson & Farabow
Barry A. Bisson	—Sun Oil Company
Lawrence A. Chaletsky	—Cabot Corporation
Willard L. Cheesman	—The Upjohn Company
Ivan Christoffel	—A. H. Robins Company
Samuel Cohen	—RCA Corporation, David Sarnoff Research Center
Horace B. Cooke	—Special Consultant, The PTC Research Institute
Phillip A. Dalton	—Western Electric Company
Michael Davis	—Wenderoth, Lind & Ponack
Rufus S. Day, Jr.	—Squire, Sanders & Dempsey
H. Robinson Ertelt	—FMC Corporation, Chemical Group
P. J. Federico	—Cushman, Darby & Cushman
Charles E. Feeny	—Pennwalt Corporation
Marcus B. Finnegan	—Finnegan, Henderson & Farabow
R. D. Foltz	—Eaton Corporation
George E. Frost	—General Motors Corporation
John C. Green	—Project Leader, International Trade and Development Studies, The PTC Research Institute; Scientific Communications and Research Consultant
L. James Harris	—Director, The PTC Research Institute; Professor of Law, The National Law Center, The George Washington University
David C. Heckard	—Armco Steel Corporation
Dwight Holter	—Eastman Kodak Company
J. B. Hoofnagle	—Western Electric Company

Tipton D. Jennings	—Susquehanna Corporation
Maynard Johnson	—Dow Chemical Company
Albert C. Johnston	—Albert C. Johnston Law Offices
W. M. Kain	—Western Electric Company
Aaron B. Karas	—Standard Brands, Inc.
Maurice H. Klitzman	—IBM Corporation
C. Frederick Leydig	—Wolfe, Hubbard, Leydig, Voit & Osann, Ltd.
John R. Manning	—National Aeronautics and Space Ad- ministration
Luther A. Marsh	—Allied Chemical Corporation
John R. Moses	—Western Electric Company
David J. Mugford	—Bristol-Myers Company
Gerard E. Murphy	—Bell Telephone Laboratories
Stephen D. Murphy	—Celanese Corporation of America
Frank L. Neuhauser	—General Electric Company, Washing- ton Patent Operation
S. Chesterfield Oppenheim	—Adviser on Research, The PTC Re- search Institute; formerly Professor of Law, University of Michigan
Jack Rabinow	—Control Data Corporation
Allan R. Redrow	—Norton Company
Paul A. Rose	—Union Carbide Corporation
Richard W. Sternberg	—Monsanto Company
Herbert W. Taylor, Jr.	—Bristol Laboratories
David G. Thompson	—Western Electric Company
Joseph Tripoli	—RCA Corporation, David Sarnoff Re- search Center
Robert Uloth	—Mead, Johnson & Company
James W. Wright	—Lord Corporation
Louis G. Xiarhos	—Procter & Gamble Company
E. T. Yates	—Cities Service Research & Development Company
Robert J. Zellner	—Chemetron Corporation

## Proceedings of the Clinic

DIRECTOR L. JAMES HARRIS: Gentlemen, good morning. I want to welcome you on behalf of The PTC Research Institute of The George Washington University. The general purpose of our Clinics is to develop an effective instrument of communication and of professional education. What we want to do is to deal in depth with frontier problems. We want to surface generally inaccessible information. We want to explore new approaches to problems. We consider these approaches as part of our research program which is in the public interest and educational in nature.

To accomplish these Clinic objectives we invite a relatively small group of specialists, representing relevant disciplines. Specialists are selected on the basis of their experience and position. We carry on these deliberations in confidence under the aegis of the Institute. I want to emphasize that anything you say here today will be held in confidence. Before anything is published you will have an opportunity to edit your remarks.

The Clinic instrument that we are developing is intended to provide a means for diagnosing the problems, a method for instruction and, if possible, a means for supplying a remedy for the problems. First, of course, we've got to understand what's wrong. Like a doctor, we've got to find out where it hurts, what the disease is. And then, perhaps, we're in a position to work up some kind of remedy. To do this, and I must emphasize this point, it's very important for us to let our hair down. We don't want any company secrets, naturally, but we've got to tell ourselves the facts; we've got to have a maximum of trust among professionals. If we can get a frank and open professional discussion going, we can accomplish much. That is why, as I mentioned before, we conduct the Clinic under the aegis of the Institute, a research and educational organization.

We want to create an informal atmosphere, an uninhibited atmosphere, to get the maximum of give and take. We want to make this

give and take as creative as possible, sparking new ideas. Practically speaking, how can we accomplish this? What have we learned in developing these Clinics that you can benefit from—that all of us can now do to make this Clinic most effective? First, against the backdrop of your own ideas and experience, please try to listen to what's going on, evaluate what's being said by the other people in the Clinic. Second, if your own viewpoint seems to be unrepresented, by all means—and this is very important—contribute your input to the discussion. Third, we've got to keep our questions and our observations short. This is essential so that the benefit of the discussion will be maximized for everybody. Fourth, the Moderator will intrude as minimally as possible just to keep the trend of the discussion clear and to elucidate important points that might have gotten short shrift. In sum, the value of this exercise will depend entirely on the quality of the input of all of us. The key speakers will spark the discussion. These speakers are simply energizers, no more. They are experts, but we are all experienced in the field and we want to learn from each other. We've found that as a teaching and as a learning instrument the Clinic has proven unique to the past participants.

Why are we holding this Clinic today? As you were told in your invitations, since the *Walker Process Equipment* case in 1965, fraud on the Patent Office is being increasingly alleged in the courts and there is, accordingly, the increasing possibility that the courts will invalidate the patent or bar recovery. Also, there is the chance of a heavy antitrust damage award. And on top of all this are the ethical implications for the professional man of a charge of irresponsible conduct. The trend, as you know, has been toward placing more of the search burden on the applicant, and over all there is the changing legal climate for these property rights—particularly vulnerable because of their intangible nature—due to the challenge by consumer groups and other activists.

The format of the Clinic consists of the key speakers who will address themselves to three major problems. First is how should the applicant's own data be disclosed to the Patent Office; second, how should prior art be disclosed to the Patent Office; and third, what counsel can the litigating lawyer give on how such data should be disclosed. We commence the program with a presentation by Mr. Paul Rose of Union Carbide who will speak from the soliciting attorney's point of view. Then there will be a brief period for cross-questioning to clarify points. Such a period will follow each one of the presentations because you haven't had a chance to see the papers or remarks of the speakers before this meeting. This period will be very brief. The second paper will be

presented by Mr. Pat Federico of Cushman, Darby and Cushman from the point of view of a former member of the Patent Office staff. The remainder of the morning session will be devoted to open discussion. The third paper will be given after lunch by Mr. Jack Rabinow of Control Data from the inventor-research director's point of view. The final paper will be presented by Mr. Albert Johnston of Keith, Johnston and Isner who will speak as a litigating attorney. The remainder of the afternoon session will be devoted to open discussion. The Chairman is Mr. Frank Neuhauser of General Electric who has courageously assumed the chair for Mr. Harry Mayers, the scheduled chairman, who is ill.

Luncheon will be served at noon in the Adam's Rib restaurant on the ground floor of the Joseph Henry Building at 21st and Pennsylvania, which is two short blocks south. We will temporarily adjourn at 11:50 a.m., reconvene at 1:30 p.m. and carry on until 5:00 p.m. At the completion of the Clinic Mr. Neuhauser, on my left, will make some brief concluding observations. Please, before you speak, identify yourself. Speak loudly and clearly, so that we can make an accurate transcription. This is most important, introduce your comment, each time you speak, with your name. I know you will forget every once in a while, especially when you get into a heated discussion, but do mention your name even when the omission occurs to you at the end of your speech. I will now turn the meeting over to our Moderator, Mr. Neuhauser.

#### FRANK L. NEUHAUSER

Those of you who are in the mature group—and at my aged vantage point I'm not sure how many of you I'd classify there—but those of you in that category are well aware this is not a new subject. It goes back at least to the *Keystone Driller* case in 1933 which in effect set aside a long standing rule dating back to the *Goodyear* case in 1869 that fraud was not a defense in an infringement suit. Subsequently we had the *Hazel Atlas-Hartford Empire* case and then the much cited *Precision v. Automotive* case, the former in 1944 and the latter in 1945. But, as even those of you who are not mature know, what really started the present flood of fraud charges was the *Walker Process* case in the Supreme

Court in 1965. That case brought about, to use the current phrase, a whole new ball game. Instead of merely being a defensive weapon in an infringement suit, fraud became an offensive weapon potentially subjecting the patentee to antitrust charges, treble damages and assorted ancillary pains that are related thereto. About the same time and possibly related to this, courts began giving attorneys' fees with a little more frequency. In one case, the *Brand and Dow* case, something over a million dollars, if I recall, in attorneys' fees were awarded.

Now aside from the problems created for your clients I'm sure you are all aware that you have to be concerned, perhaps even more so. And not only from the civil aspect in your own practice but as the *Union Camp* case shows, even from the criminal side of the situation. And the most topical thing occurred here only a month ago when the Senate Patent, Trademark, and Copyright Subcommittee met and marked up, as they put it, the Patent Law Revision Bill S. 643, putting in a new Section 115 which provides that each of the agents and attorneys who participated in the preparation or prosecution of the application, the inventor, the applicant if he's not the inventor, all must make an oath that they have told the Patent Office everything that they know. I have paraphrased the last ten lines, as you are aware. Finally they modified Section 131 (c) to take out the protective clause that would have at least protected you and your client against inadvertent failure in a cite of reference. So you are now right in the forefront and quite vulnerable. Several phases of this subject as Mr. Harris has told you, will be covered by four eminently qualified experts who will be going on center stage in just a few minutes.

Just for your preliminary thinking and so that you will be prepared to enter into the discussion when we throw the subject open for floor discussion, you might just begin by running over in your mind some of the questions that presently occur to me to be involved—how do you handle the art that is available to you at the time of filing; how do you select, and with what permissible judgment what to submit to the Patent Office; what about information that comes to you later during prosecution; what about references cited against your foreign applications; how do you handle art that comes to your attention after the patent has issued? And suppose that the art is such that it may be better than that the Patent Office had but does not affect your claims? You are convinced that the claims without change are still valid. Suppose that it does affect the claims. Is there any limitation on what you could do by way of reissue to modify those claims in the face of less than completely candid conduct during the original prosecution? Are there reasonable

guidelines that can be prepared to guide you both ethically and from a business and professional standpoint? The National Council of Patent Law Associations tried to develop guidelines and came up with some suggested guidelines which, as far as I know, have not yet been adopted. The present guidelines in the Patent Office are the ABA Code. And what about good faith errors in judgment in selecting references? What about inadvertent failure to cite? I could catalog a few more and you could add to them and I hope you will during the discussion.

Let me just repeat some of the things that Jim Harris told you. Please, when we do get to the discussion period identify yourself so that the tape can pick it up. Speak clearly. If you can without embarrassment, give examples from your own experience; it puts a lot of meat on the bones if you can do that. And I hope that you won't refrain from speaking because you think that your ideas are far out or controversial, the whole subject is, and if you don't like your remarks when you see them in print you can edit them. You can cure your syntax or modify any other things that you think you would rather not see directly in print.

Now we have four people here that Jim referred to earlier as the energizers; they spark the discussion. Jim has already told you the areas that are going to be covered. Our first two speakers who will go on this morning—Paul Rose and Pat Federico—will discuss the first two aspects of the problem, that is, how, when and what do you cite, considering your own art or prior use or the art of a third party that you have uncovered. This afternoon we will get to the third part of that three-part program that Jim described, namely, discussion from the litigating attorney's viewpoint. First let's bring on Paul Rose who will look at this problem from the viewpoint of one engaged in soliciting patents before the Patent Office. Paul is head of the Washington Office of Union Carbide's Patent Section. He has been active for a long period in matters relating to Patent Office practice. I'm old enough to know that he was one of the drafters and moving forces behind the Patent Act of 1952. Finally, he is one of the most knowledgeable men I know concerning practice before the Patent Office.



PAUL A. ROSE

With that kind of introduction I guess I'd better go home while still ahead. Also, with all of this talent in front of me it's a little overwhelming at times to think that one can tell a group like this very much. But I thought that possibly first we might look into the background of this problem because from what has been held to be fraud on the Patent Office and in some cases what has not been held to be fraud on the Patent Office we can at least arrive at a jumping off point to decide what we might do in each individual case. Possibly the first thing to do, as the courts in many cases have done, is to remind ourselves of what fraud is. Fraud on the Patent Office is pretty much the elemental fraud that we learned in law school. There has to be a misrepresentation or concealment of a material fact with knowledge of its falsity and the intent that it will be acted on by another who is ignorant of the fact and who does act upon it in reliance on the misrepresentation to his detriment. In that context, the Patent Office relies on the representations of an applicant in promoting the grant of a patent, and a patent improvidently granted when such representations are false or misleading is detrimental to the public interest. So we have the basic element of fraud when there is a deliberate misrepresentation relied on by the examiner, and, as many cases have said, he allows the claim or patent that he otherwise would not have granted.

A review of the proliferation of recent decisions indicates that a charge of fraud on the Patent Office can stem as readily from a failure to disclose pertinent subject matter as from the actual falsification or misstatement of the facts. The immediate and I suppose shortest answer to both phases of the question—how, when and to what extent should data be disclosed to the Patent Office is, you might say, everything now, and in writing. Certainly, all noncumulative data relating to the alleged novel features of the claimed invention should be in writing in the record, either in the application itself or in discussions in amendments or other papers in the file. You cannot rely on verbal discussions with the examiner. There was one case in which the applicant, or the patentee, tried to avoid a charge of fraud on the Patent Office by saying that he had disclosed certain subject matter in an interview with the examiner. The court struck that down and said that that violated the rule that all business in the Patent Office had to be conducted in writing.

You can see the minutia the courts get into in holding one to the line

of disclosure in the Patent Office to the extent required. As I say, it should be at the earliest possible moment in point of time during the presentation in the Patent Office, and to the extent required to place the examiner in possession of all the facts necessary for him to make an informed judgment as to whether the patent should be granted. Paraphrasing a statement of one of my Washington colleagues, and also the courts in case after case, in view of the importance of the question to the public interest, that is the grant of a patent or not, patent attorneys are in a different position from advocates in other proceedings. They cannot willy-nilly make unilateral decisions as to what they will or will not disclose to the Patent Office or what they will omit from the disclosure.

You can see this theme developing in the cases more and more in the holding of the attorney and the applicant, of course, to a very strict rule of, you might say, nonadvocacy. He's got to tell it the way it is, and let the examiner be as fully informed of the situation then existing in relation to the invention or the development as he is and not simply select the best material, although we'll see when looking at some of the cases that some courts are willing to let you put your best foot forward. But the old idea that we deal at arm's length with the Patent Office and that the examiner can flounder around to the best of his ability in digging up the art and finding the flaws in our case is out the window today, as I see the trend in the decisions. Even though it hurts, you've got to tell the truth to the Patent Office and then either explain it away if it's harmful in some instances, or in some instances you just won't prevail in getting your patent.

Every time a patent attorney makes a selection of material available for inclusion in the disclosure of an application, or in an affidavit particularly, he lays the possible basis for a charge of fraud on the Patent Office. And then years later, on minute inspection as some courts have said, the patent may be held invalid if it is determined that knowledge omitted might have influenced the examiner to a different conclusion. And it's not surprising. Of course, we all know that when the court looks at something years later it focuses in on a fact that at the time in the whole context of the proceedings might have been a very small thing. But after everything calms down and this one thing is highlighted as being a reprehensible act, it is very often blown up into something that can put you down as far as maintaining the validity of the patent is concerned, whereas at the time you may not have given it much thought.

So we see that every step in the preparation, filing and the prosecution of an application is vulnerable to attack, that is, the disclosure in the application itself and affidavits and arguments as to the efficacy of the invention. Affidavits under rule 132 comparing data on the invention with the prior art are perhaps one of the most fruitful sources of fraud that we find; also, the facts relative to prior use or sale. If you make a unilateral decision that something that your client did with his invention before he filed the application was not a public use or sale in your mind, you are running a risk of a charge of fraud. I'm sure that in the past many of us have made decisions on our own that prior acts would not be construed as public use, so we filed the application and felt perfectly proper in asking the inventor to sign the oath as to no prior public use or sale. It seems to me looking at the decisions today that you can't make that decision—particularly in a close case. You've got to apprise the Patent Office of the facts and let the examiner make the determination as to whether or not in his judgment there has been a public use or sale. That sounds hard to oldtimers like me who remember the days when you were really dealing at arm's length with the examiner and left him to paddle his own canoe and didn't give him much help as to references that you might have known about, but on which you were willing to take the chances in court later.

Looking at some of the decisions, I picked up the *Xerox v. Dennison* case, 168 U.S.P.Q. 700, in which there was a motion for summary judgment on the ground of fraud as one in which the court gave what I thought was a rather good discussion of the principles and the problems we face today in prosecuting an application before the Patent Office. The court said we start with the principle that the applicant for the patent owes the highest degree of candor and good faith to the Patent Office, citing *Kingsland v. Dorsey*, 338 U.S. 318; 83 U.S.P.Q. 330, and the *Hartford Empire* case, which has been described in the oft-cited Supreme Court decision as "an uncompromising duty to report to the Patent Office all facts concerning possible fraud or inequity underlying the applications in issue." *Precision Instrument Mfg. Co. v. Automotive Maintenance Machinery Co.*, 324 U.S. 806; 65 U.S.P.Q. 133.

Although it's difficult to formulate a standard that will encompass all types of misconduct that would amount to inequity on the part of an applicant, the basic underlying theme is that there must be some element of wrongfulness, willfulness or bad faith that transgresses the basic concept of doing equity. Now Frank mentioned that there is a

section in the new Patent Act, which I hope doesn't get enacted in that form, which would make it improper, or you might say like collateral fraud on the Patent Office, not to cite a reference you don't even know about, on the grounds that you should have known about it. In fact, I was told recently about one case where that actually has been charged, and I don't know how it came out. The charge was, I believe, that having made a search, they should have found the reference patent, but they didn't and didn't cite it and therefore that was tantamount to fraud on the Patent Office. Well in a sense, the charge was that they should have had a better search made, therefore they didn't and therefore, there was fraud on the Patent Office.

So the trend is getting more and more to putting the applicant and the attorney in an almost impossible position so that you have to be more frank than you ever have been in the past. The court goes on to say it must be remembered that the purpose of the unclean hands doctrine in patent cases is to discourage an applicant from taking advantage of the fact that prosecution of a patent application is essentially *ex parte* rather than an adversary proceeding, and that the patent examiner accordingly must rely heavily upon the information furnished him by the applicant. (*Xerox v. Dennison*, 168 U.S.P.Q., page 700.)

I have the citations of all the cases that I've mentioned and I'll be glad to give them to anyone if I don't mention them during the course of the discussion. The whole point of this discussion—I'm not going to read all of this—but the court goes on to state that the applicant is under a very heavy burden of complete disclosure and not to retain anything that would prove of value to the examiner. The court does state that to deny enforcement as a matter of law merely because of an innocent or good faith nondisclosure would go beyond what is necessary to protect the public against the improvident granting of a monopoly. Such a standard could also have the harmful effect of forcing a patent solicitor to floor the Patent Office in each case with a mass of data of doubtful materiality rather than taking a risk that an inventor might later be denied the fruits of his monopoly because of failure to reveal some fact later magnified out of proportion by an infringer seeking to escape the reach of the patent by combing the inventor's files under the liberal pretrial discovery procedures and dredging up new found "facts." Of course, in the tetracycline case, you remember if you read it, there was a memorandum that was dug up on discovery that had written across the face of it, "All copies to be destroyed."

In your thinking about what you can and can't do, as far as excluding from the specification or other parts of the record any material in the fringe area is concerned, you can be sure I think that with the discovery procedures that are available today, the truth is going to come out, one way or another. As you read these cases you can see how digging on discovery has brought out the facts which have resulted in many patents being held invalid or unenforceable because of alleged fraud. The question of what data to include or exclude from the specifications arises in the preparation of many applications and, of course, can be very troublesome. There is a natural tendency to include that which is most favorable to the theory of the invention in the case and to exclude that which points away from it. You have a lot of experiments that have been run and some are not so good and some of them are much better. The tendency, of course, is to exclude anything that would indicate that maybe the development hadn't been an unqualified success.

In view of the ever closer scrutiny being given such selection, I believe that the best and most prudent course is to include all noncumulative data, certainly, which would give a complete picture to the examiner along with the inclusion of some data that might detract from the argument that you have an invention, such as one test in which the results were out of line. It's better, I think, to include some of those, if not all of them, and explain them at the time the application is filed rather than to have it come up later and be charged with fraud on the Patent Office. This may result in difficulties in the Patent Office but it fulfills the mandate of the majority view that the Patent Office must be given all relevant facts in the possession of the applicant so as to reach an intelligent and proper conclusion on whether or not the patent should be granted.

Now looking at a few cases on the matter of disclosure, in *Flick Reedy Corporation v. Hydro Line*, 144 U.S.P.Q. 566, the court held the patent unenforceable because the patentee kept its particular method of operation a secret and thus deliberately did not disclose the best mode of carrying out the invention. Of course, that's a case which we all could agree with because the best mode is written right into the statute, but the patent was held invalid for that reason. On the other hand, in *Union Carbide v. Stewart Laboratories*, 92 U.S.P.Q. 262, the patent covered the process of asterating synthetic sapphires and rubies, making the famous "LINDE" stars. Briefly the invention or the process involved reheating the boule which was made by the Verneuil process with a little titanium dioxide in it, to an elevated temperature to cause

precipitation of the titanium dioxide along the crystallographic planes of the crystal, so that when it was cut into gemstones you got the star effect. The defendant charged that the patentee had concealed the best mode by omitting from his specification that the crystal should be both seeded in order to obtain a proper orientation and subsequently annealed to prevent shattering when cut. That's an oversimplified statement of the charge, but that's the basic thing. Well, the court found that the need for both seeding and annealing was questioned and not established as the best mode of carrying out the invention at the time the application was filed. Therefore, it was held that there was no fraudulent intent in not including the seeding as well as the annealing as a two-step process. The patent was held valid and enforceable as enabling one skilled in the art to practice the invention.

A review of relatively recent decisions illustrates graphically not only the acts and omissions which have been found wanting, but also the difficulties which face the practitioner in everyday decisions. For instance, in the matter of candor in the preparation of affidavits, two courts recently reached opposite conclusions with respect to the self-same affidavit in the file of the same patent in suit in two separate jurisdictions. An affidavit was filed in procuring the patent to demonstrate unexpected herbicidal activity of the claimed compound over a closely related known compound. The applicant had available the results of 20 tests on different plants of the herbicide and from these he selected 11 for the affidavit. The attorney made a judicious selection, favorable, of course, to the applicant's contention that he had unexpected properties in the compound being claimed.

In *Monsanto v. Rohm & Haas*, 164 U.S.P.Q. 556, the District Court in the Eastern District of Pennsylvania held that withholding the disclosure of the results of some tests by omitting them from the affidavit was fraud on the Patent Office and that it invalidated the patent. Shortly thereafter, in *Monsanto v. Dawson Chemical Company*, 164 U.S.P.Q. 560, the District Court in the Southern District of Texas, having read the Pennsylvania case incidentally, held that the same affidavit was not proven to be a fraud on the Patent Office and that, "by the manner in which they went about this task, that is convincing the examiner of the unpredictable properties of 3,4-DCPA plaintiffs did nothing more than put their best foot forward." I think that court is looking back a long way to my time in prosecuting applications when we put our best foot forward without any thought that the act would be open to question. The court said that it had carefully considered the decision in the Pennsylvania case but decided it must and did reach its

own independent judgment. So it's rather startling that precisely the same facts with two different judges result in completely opposite conclusions, but I think it illustrates what we're up against in making a decision as to what to put in or omit from an affidavit or put in an application today. By far the majority, I think, of the fraud cases that allege misuse or withholding of pertinent data in the prosecution of the applications revolve around affidavits showing superior results or unexpected properties.

Probably the best known case involving affidavits in this context is the *Pfizer-Federal Trade Commission* case which you will find in 159 U.S.P.Q. 193. This was a very complex case, incidentally, in which there were several interferences which I won't go into, but at one point the examiner got the idea that some tetracycline, which was being claimed here, was probably produced in the practice of one of Cyanamid's patented processes for making aureomycin. He suggested that to the attorney for Pfizer who had been the winner by settlement of interferences with Cyanamid. So they filed an affidavit purporting to carry out one of the examples of the Cyanamid patent showing that no tetracycline was produced in the production of the aureomycin. However, facts were dug out on discovery later that they omitted from the affidavit a test based on another example in which 5 percent of tetracycline had been produced incident to the production of the aureomycin which would have substantiated the examiner's contention. They also failed to disclose that they ran the tests in which they got no tetracycline under conditions that were calculated not to produce any. In fact, it was calculated not even to make a good production of aureomycin, and they also failed to disclose that in samples of aureomycin which had been produced previously by Cyanamid there was a 6 percent content of tetracycline. Also the examiner asked Cyanamid's attorneys about the tetracycline production and contrary to a memorandum in Cyanamid's files that old samples of aureomycin contained 6 percent tetracycline they avowed that they had never produced any tetracycline in the production of aureomycin. That was the memorandum that I mentioned previously that had written on the face that all copies had been destroyed. The holdings in the tetracycline case cost the company a lot of money and licensing arrangements which I won't go into. But the court held that, because of the relationship between the companies, they were both under an obligation to make a full and accurate disclosure to the Patent Office.

In *Monolith-Portland Cement v. Kaiser Aluminum & Chemical Corp.*, 160 U.S.P.Q. 577, the patent was held unenforceable for a series of

breaches characterized by the court as calculated recklessness about the truth, amounting to less than fraud; but they considered it sufficiently serious to award attorneys' fees, which is one of the things you run into as the consequence of a finding of fraud on the Patent Office. The fraudulent representations in that case were concealment of its own prior public use by Monolith, but in defense of that charge, it only arose when they were denied the right to go back to an earlier application. So you can see there's another facet that you have to think about very carefully in filing continuation-in-part-applications: whether or not there's been an intervening bar due to your use or sale of the product either of which would bar the claimed subject matter in the CIP. That is what happened in this case. So they entertained a charge of fraud even though Monolith might have been perfectly reasonable in concluding that the second application should have had the benefit of the first. They also made misrepresentations in an affidavit with respect to unexpected results, which is the part of the case that is of interest to us at the moment, as well as false statements relative to the prior art. The misrepresentations in the affidavit were showing of unexpected results which they attributed to the invention being claimed, whereas it was shown in the testimony that three-fourths of the increased benefit attributed to the invention stemmed from using what they call short-shim bricks in the rotary kiln in which the process was carried out. They thereby misled the examiner into allowing the claims on the basis that the claimed invention was responsible for the improvement, whereas it was the nonpatentable improvement in the apparatus.

In *Armour & Company v. Wilson*, 119 U.S.P.Q. 365 and 124 U.S.P.Q. 115, the omission of material facts from an affidavit invalidated the patent. There the claimed invention was the addition of gelatin to an ACTH mixture which, they claimed in the affidavit and in the application, enhanced the activity over a saline ACTH mixture which was old. However, the affidavit failed to say that phenol had been added to the gelatin mixture which had been tested and shown to be superior, and the fact was that the phenol was responsible for the difference in activity rather than the gelatin. So there they threw in a little kicker in the experiment but failed to tell the Patent Office that it was the kicker and not the claimed invention that resulted in the improvement. That was held to be fraud on the Patent Office. In *SCM v. RCA*, 167 U.S.P.Q. 196, the patent was unenforceable because RCA maintained an unqualified assertion of a certain value assigned to a coating used in the process as the correct standard because the attorneys



feared that to do otherwise would impair the chance of obtaining a patent. The court held that the intentional nondisclosure of relevant facts to the contrary was fraud to the extent that while the court would not say that the examiner would not have allowed the claims if full and candid disclosure had been made—and this is rather significant to me—it refused to enforce the patent on the ground of unclean hands because of the willful failure to make a complete and candid disclosure.

Of course another and fruitful source of charge of fraud on the Patent Office is the failure to disclose references to the Patent Office which are known to the applicant. In *Strong v. General Electric*, 162 U.S.P.Q. 141, the court held that the applicant's failure to disclose to the Patent Office a prior publication known to him, disclosing the subject matter of some of the claims, invalidated the entire patent. In that case the unclean hands extended across the board to all the claims even though all of them were not affected by this reference. In the *Flick-Reedy* case, which I mentioned previously, the patent was held unenforceable by reason of inequitable conduct in misrepresenting the state of the prior art, so that statements relative to the prior art which mislead the examiner as to what the art teaches are also a source of error or danger. There is one case I don't have here, where the court held that the applicant or his attorney was guilty of fraud on the Patent Office because they buried a good reference in a bunch of references referred to in the case without pointing out the pertinence of this reference, thereby misleading the examiner into thinking that the generalized statement as to the group of references applied to all. It guided the examiner away from the reference and he ignored it and allowed the claims. In *Armour and Company v. Swift*, 168 U.S.P.Q. 269, the court held the patent invalid and awarded costs because the patentee withheld references known to it from the Patent Office and also made positive misstatements of facts regarding prior art practices.

In a great many of the cases, as I view them, what was practiced in the prior art as well as what was known in prior art references or publications seems to be coming to the fore as basis for a charge of fraud. If you mislead the Patent Office as to what the prior art is even though it isn't something you consciously decide on and it turns out to be a misstatement—willful misstatement—that can come back to haunt you also. On the other hand, it has been held that failure to call attention of the Patent Office to non-anticipating art or prior art no more pertinent than that cited by the Patent Office is not a fraud. (*Oglebay-Norton Company v. Universal Refractories Corporation*, 162

U.S.P.Q. 346, *Beckman Instruments v. Chemtronics*, 160 U.S.P.Q. 619.) However, in all these fraud cases the defense drags everything in that it can, and even though a reference is truly a cumulative reference and doesn't have to be cited even though you know about it, there again you run the risk of nondisclosure if a court five years later decides that that is a reference that might have influenced the examiner.

Now I guess I've been talking too long, really, to get this thing off the ground. As to the mechanics of when and how prior art should be brought to the attention of the Patent Office, of course one of the classical ways that you bring to the attention of the Patent Office the references which you really need to distinguish over from the very beginning, is to put it right in the specification—to set up a straw man, so to speak, and knock it down and write your case around such a prior art reference whether it be a patent or a publication. Thus, you build into the specification, by comparison and emphasis on distinctions which you consider important, the basis for a determination of nonobviousness. Probably by far in the greater number of cases today under the Commissioner's request for citing art to the Patent Office, the citation is contained in a separate communication, preferably filed before the first action, which calls attention to certain references of which the applicant is aware and which should be made a record. As a matter of fact, Section 707.05 (b) of the Manual of Patent Examining Procedure recommends that procedure and further provides that if no more than five references are cited and the applicant discusses them to distinguish the claimed subject matter over the disclosure of the references, they will be printed on the patent when it issues as references cited. The same is true with respect to references cited in "petitions to make special" under section 708.02 of the Manual.

In discussing this with various attorneys I find there is some reluctance by a number of attorneys to cite art before the examiner acts on the case. Or, if they do cite it before he acts on the case, they are reluctant to make any commitment as to what the art discloses vis à vis the claimed invention. Some take the position that they shouldn't put words in the examiner's mouth or ideas into the examiner's head as to a theory of rejection. Let him take his position first. Whether you agree with that or not it is an idea that some people have, and for those I would suggest the filing of a paper simply listing the references and furnishing copies. Incidentally, under that Manual section, you should also furnish copies of the references to the Patent Office. If you list the patents or other prior art and furnish copies in the record, I don't see

how anyone could charge you later with not having been candid with the Patent Office simply because you didn't argue the nonpertinence of the references at the time you filed it, leaving it up to the examiner. Others like to wait until after the first action and see what the examiner comes up with, and then if they have in their files references better than the examiner cites they set them up in the remarks of the first amendment preferably, or as soon as they are aware of the references. In that case, of course, it is necessary to differentiate the claims by argument from the references cited at that point after rejection of the case and also to supply copies. Otherwise the examiner probably wouldn't consider them.

In citing art to the Patent Office I think the best procedure is to be a little selective. You can't expect to give them a whole subclass of patents and have done your duty. Also, furnishing copies, I think, is very important. In conclusion, I would say in answer to both aspects of the question of disclosure of the applicant's data and of prior art that, to use a colloquial expression, the applicant in the light of recent cases is under a heavy burden "to tell it as it is," so to speak, and to err on the side of completeness rather than to tailor the disclosure to paint the best picture. This places the examiner in as good a position as the applicant in reaching the determination as to patentability. Otherwise, as soon as you begin to consciously withhold anything from the Patent Office that could have a bearing on patentability, you're treading on thin ice, and you can be sure if the patent gets into litigation that your opponent is going to dig out the facts and use them against you even though your action at the time and under the circumstances appeared perfectly proper.

**MODERATOR NEUHAUSER:** Thank you, Paul. Now the ground rules say that we will make available to you a few minutes, preferably not to exceed five, for you to ask at this time any questions of Paul as to matters you would like clarified, if you are not quite clear about what he said. The gentlemen back here, would you give your name, please?

**RICHARD W. STERNBERG:** I'm Dick Sternberg with Monsanto Company. In chemical practice we all realize that there is a real problem with disclosing data. It's not unusual for a chemist to run an experiment and fail in achieving his results; he won't know why he failed. Let's assume that he runs 15 experiments and 10 of them look good and 5 look bad, in essentially the same process. So he discloses all 15 experiments and

he would be hard pressed to say why these 5 failed. In organic chemistry particularly, this is not unusual, I would say. Yet the examiner can seize on this and say well, there must be something missing from these experiments because you get 10 good results and 5 bad results. You must be concealing something here. So you're faced with the situation that you've already shown your invention works and you believe that this is what the invention is. How do you overcome this problem?

MR. ROSE: That's the horns of the dilemma we are on, I think, in the present situation. I mentioned in the beginning that I think we're coming to the point where we're almost going to have to disclose those five unsatisfactory experiments, if the ingredients were there. Of course, every unsuccessful experiment does not have to be disclosed which does not involve the essence of the invention that's being claimed. I'm assuming as you are, I believe, that we've got 15 experiments and let's say all are putting in the same basic ingredients and going through essentially the same procedures to try to establish the parameters of the process and that five of them right in the middle were bad, and all around them we had ten which were good. The explanation could be that maybe some impurities are involved in some of them, something went wrong with the apparatus, the catalyst was not active in some of the cases, there was something there that altered the reaction, or something else unknown. I really don't know the final answer, but I do have a definite feeling from the way the case law is being developed, that you'd better put in the five and explain them away if you can, rather than have it come up later that you deliberately omitted those from the disclosure. Now that is the question I think that this Clinic is really here to discuss. It's a very practical problem and I think we can all have some input on it.

MR. STERNBERG: I think the same thing applies to the affidavit situation. I think in writing the application in the beginning you are often faced with the same problem.

MODERATOR NEUHAUSER: If we're going to have any more questions here, I'm going to ask Jim to brief me on the ground rules. My understanding was that this brief interlude was really to clarify something about Paul's talk, and not to get into a full-dress discussion. Now if you want to ask him particularly about something that wasn't clear in his talk, ask the question now; otherwise wait until later.

JAMES W. WRIGHT: Jim Wright, Lord Corporation. Mr. Rose commented quite extensively on the disclosure of prior art and data to the

Patent Office. I'd like to ask him to comment on what stage of the prosecution should we disclose questionable statutory bars from prior public uses or sales and what is their relation to the oath of the inventor.

MR. ROSE: Well, at the earliest possible time is the admonition of the court, as soon as they're known. In other words, you can't hold back until the case is allowed and then slip something in under Rule 132, so to speak, that the examiner wouldn't pay much attention to. However, if that's when you first do discover it, then that's when you should disclose it. And it should be in writing and in the record. That's the best answer I can give you.

MR. WRIGHT: My concern is with the oath which requires the inventor to state there has been no public use or sale more than one year prior to the date of the application. It seems as though he should take exception to the oath and put in some qualifying statement setting forth appropriate facts for the Patent Office to consider.

MR. ROSE: Pat has something on that in his talk—

MODERATOR NEUHAUSER: Wait until Pat's talk, and if it's not clear then, ask the question again.

C. FREDERICK LEYDIG: In a case where there are hundreds of experiments dealing with the invention in question, are you suggesting that all of them should be in the specification?

MR. ROSE: No. I think that would violate the rule on prolixity, which isn't really enforced very much in the Patent Office today, but I think that representative examples which are truly representative should be put in, but cumulative examples should not. Now in making the selection as to which you are going to omit from the disclosure, I think you have to use some care in not omitting some examples which might raise some question as to completeness of the disclosure—this is hard to generalize.

MR. LEYDIG: Given a highly sophisticated research laboratory it may be more readily ascertainable why things went wrong. Such a selection may be more easily made, although not necessarily. But what is the situation with someone who is not nearly so sophisticated, who is a poor laboratory worker, but nevertheless does a lot of work? Do you suggest either putting it all in the specification or providing the examiner separately with whatever is not in the specification?

MR. ROSE: I think your suggestion that you provide it separately from the original specifications might be a very good one because then you have a viable disclosure in your patent enabling one skilled in the art to practice the invention and yet you would have informed the

Patent Office that everything didn't work out correctly all the way down the line; but there's enough in there to prove that you did have a viable invention that can be duplicated. I'm going to take one more question over here and save the others until after Pat Federico.

ANONYMOUS: Excuse me, Paul. One thing you haven't commented on, and I wonder if it might be appropriate at this time, and that is the inventor's personality, which goes back to the previous question. Two things—first, many inventors are fiercely proud of their own professional stature, and I just recently had a drag-out fight with a man who is tops in his field to include one run that was bad. And it took me a day of argument with that inventor because he felt it reflected on his professional stature that he couldn't explain the run and that here were ten runs that were right. He just didn't feel that it was fitting to his stature—and I mean he is a top man in his field. That's one personality problem. The other problem is where there's a gap between the inventor and the attorney. The attorney just gets his material funneled to him through a filter, the inventor being the filter or perhaps a liaison. What do you suggest in these two situations where the inventor's personality may be really the problem and the attorney may have no awareness at all of the fact that the inventor is the one who holds back or has a bit of pride.

MR. ROSE: Well if the inventor holds out on the attorney and the attorney doesn't know about it, certainly he's not going to be charged with personal fraud on the Patent Office. On your reluctant inventor who wants to tailor his disclosure to make himself look good, the only thing I can suggest there is to tell him what the facts are, and what he might be getting into and of course, if you are the patent attorney for a company that has a laboratory and this is one of the workers there, I suppose you can insist that you make a complete disclosure. But I don't think you have a choice if you think that the complete disclosure is necessary to a fair presentation and he won't let you put it in or won't sign the case, then either put it in and have the company file under Rule 46 as assignee of an inventor who refuses to sign, or don't file at all. That's a pretty hard answer but it seems to me from the way the cases are going you've got to do it.

Now as to where you get the disclosure through the small end of the funnel, like the average attorney in general practice who deals with clients mostly through the mail, you may have to take what you get and live with it. I don't think offhand that an attorney is under an obligation to go out and dig for more disclosure unless he has some reason to believe that he is being shortchanged in the disclosure which he gets

from his client. In other words, you've got to have a Rule of Reason here as well as to strive for perfection, so to speak.

ANON. I don't see where that situation is concerned with filing a case. You satisfy yourself that an invention was made and the case is filed. But you're concerned with an affidavit filed later to substantiate some argument. I'm talking about preparing a case with an example I thought ought to go in and the man didn't want to put it in. This is in the draft stage of the application. It's a common problem.

MODERATOR NEUHAUSER: I suggest a postgraduate course in persuasion. I think we ought to discuss this problem in a little more detail later on, because it is a problem and I don't know of anybody who can give you a solution because it is a matter of human relationships. But feel free to bring it up later.

Our next energizer is Pat Federico who's going to talk about this subject from the standpoint of the Patent Office. Pat refers to himself as semiretired and not in the Patent Office but he was in there longer than any man I know personally. Pat is a truly respected and admired "Mr. Patent"—Pat Federico.

#### P. J. FEDERICO

I'm afraid I'm a little bit old fashioned—probably more old fashioned than Paul, and most of the things I'm going to say are from the standpoint of the experiences of an examiner in the Patent Office. But before starting I'd like to comment on the *Goodyear* case, because everybody who talks about fraud starts with saying that in 1869 the Supreme Court held that the question of fraud could not be raised in an infringement suit. In another case involving the same patent and raising the same question, the Supreme Court affirmed the dismissal of the suit on the ground that the patent had expired and the question was moot, which it really wasn't. The charge was that the extension of the patent had been obtained by fraud. The patent was granted in the days when the term was 14 years, but you could get an extension of seven years on conditions. The conditions were that you had an important invention and you had not received the compensation that an

invention of that importance merited, without any fault on your part. The petitioner for an extension had to show the value of his invention and that the compensation he received was inadequate, furnishing an accounting of his receipts and expenditures. I believe the charge related to a practice which had been approved by an early decision of the Commissioner of Patents. This practice was that a company was formed and the patentee sold his patent to it for shares of stock having a small par value. So the accounting showed only a small return from the patent. However, substantial amounts were received from the company, but this was from a wise investment in stock and not from the patent.

I'm going to talk a little bit from the standpoint of an examiner and what the Patent Office sees. I'll start with the filing of a case. There have been a few cases, some of which you may have run into, where the total case is fraud. The inventor is not the inventor. He swears he is, but he copied from somebody deliberately and you have a case that's fraud from the beginning. The *Precision Instruments* case has been mentioned. It involved that exact situation. The patent concerned had been obtained by somebody who was not the inventor; a former employee of Automotive left them and made some developments with somebody else and an application was filed in the name of a third party, alleging to be the inventor. The Patent Office normally has to take the oath or declaration of inventorship at its face value. They don't question the inventorship; the question actually cannot be examined. An oath or declaration has to be filed in which various allegations are made—the allegation of inventorship as I have just mentioned. All that the statute requires of an oath is an allegation of inventorship and a statement of citizenship. The statement of citizenship is a relic from the Act of 1836 when Britishers had to pay \$500 and other foreigners \$300 on filing an application and, strange as it may sound now, there was a requirement for working in our law that applied to foreigners only. These were eliminated in 1861 but the requirement for citizenship remained. That's all the statute requires.

The remaining allegations are Office requirements and you presumably get a filing date if any of these remaining allegations are missing, to be supplied later. Now that's where false statements can be made. Various statements, denying the existence of prior publications, public uses, etc., are required of the applicant "to the best of his knowledge and belief." If the examiner does find a printed publication that anticipates, early enough in date, of course the case is rejected, but no question of fraud can be raised by the examiner as he cannot show that



the applicant knew it. If an early enough publication by the applicant is found, and that rarely happens, the case gets rejected and the question of fraud isn't raised at that stage.

There was a case that went to the Court of Customs and Patent Appeals in which the inventor made the allegation but added a note calling attention to certain publications and argued that these printed publications did not constitute bars. The Office rejected on the publications and the CCPA reversed. I don't know that that's very common, but situations may arise in which there may be some doubts, and the facts could be set out either in the oath or a separate paper.

The next stage in the Patent Office where questions like this might arise is in connection with affidavits which are filed, either under Rule 131, or affidavits under Rule 132, which used to be called affidavits of merit. I did not mention alterations in an application after it had been filed. The rule is strict that alterations after execution cannot be made. According to Rule 56 the application may be stricken from the files.

There was a case in which the attorney added two claims after the case was executed. This came out in an interference and the Office struck the application from the files on the ground that it violated Rule 56. Reconsideration was requested on the ground that there was absolutely nothing in the claims that added to the disclosure, that is, the claims were completely supported in the disclosure and that they could have been added by amendment. The Assistant Commissioner said that that was beside the point, they were added after the execution, and he maintained his position. The Office, as I said, takes a pretty strict view of doing anything like that. Affidavits under Rule 131 are filed to show that the invention was made prior to the date of a reference, and the Office has a long standing practice of accepting as exhibits copies of original papers with parts blocked out. In my view that's wrong and should be totally abandoned. Dates are commonly blocked out. Quite often the affidavit alleges diligence and blocks out the dates. As far as the affidavit is concerned the experiments reported might have been made ten years before the date to be overcome, or they might have been made the day before, you don't know. I think the time has come to stop that practice, particularly in blocking out parts of the exhibits alleged to be irrelevant. My own personal feeling is that the time has come when the acceptance of bobtailed exhibits ought to be stopped. The argument in the old days was that you should not be required to make your dates public. We're not too much concerned nowadays about giving away dates, or about letting your dates be known. The other argument is that you might be revealing some

subject matter irrelevant to the question involved that you didn't want to reveal. That could be taken care of, if it were the actual fact, by petitioning the Commissioner, submitting a full copy, and asking leave to file the exhibit with certain parts deleted, and obtaining a ruling that you may or may not.

HERBERT W. TAYLOR, JR.: Would you apply that to preliminary statement exhibits? Blocking out text which is outside the count of the interference is what I had in mind.

MR. FEDERICO: Of course, the purpose of the preliminary statement is for the information of the other parties, and if a practice were established of petitioning to be permitted to file curtailed exhibits for ex parte cases, I don't see any reason why it wouldn't be run over into interference.

We have the affidavits under Rule 132. The question of reporting has been raised; I did have an experience once with a case where the bad experiment was included—this was in a 131 affidavit rather than a 132 affidavit—and the applicant wanted to show the experiments that antedated the reference. One of the experiments didn't work. The applicant gave the explanation that these were the earliest experiments run and when you do that in the first raw stages you sometimes get unexplainable results. The affidavit was accepted, but I think it would be pretty hard, particularly with some examiners, if half the experiments didn't work or gave the wrong results, and half of them did. Then, of course, questions of false statements may come up in interferences and the testimony in the interference may be false. There is one decision of Commissioner Ooms in which one of the parties had filed a false exhibit in the interference; this came to light and the application was stricken. A question arises in interferences of when to consider the question of fraud if raised. Presumably in view of the recent decision of the court the Office would have authority to consider it in the interference as part of the interference, rather than later. I think the procedure there is in a state of flux, to be further developed. Some of you may have had cases that illustrate the point.

ANON: The *Carter* case I have here covered that and the *TCPA* case.

MR. FEDERICO: I mentioned striking an application; this is what the Office could do when they discover fraud. The procedure is before the Commissioner and it must follow the Administrative Procedure Act. The result is that there is no longer any application.

On the question of submitting art, the Manual has been mentioned. That's the result of a notice, it's true. A long list of patent numbers are

given and it's seldom, if ever, that any of them are ever worth citing by the examiner; they give the examiner nothing but trouble. That's probably the reason for the notice which has been incorporated in the Manual. They can't forbid you from filing a list of 100 patent numbers, but they do give you advantages if you do it in a more cautious manner; according to the notice, if you limit the number of references to not more than five or have an explanation if you're going to have more than five, and if you give a discussion of the references and how the claims distinguish, with copies submitted, the references will be incorporated in the list of references cited in the printed copy, and so forth. This obviously is to discourage uncritical submission of mere lists and to encourage a real statement that points to the closest references and explains why the claims distinguish from them.

The question of standards of conduct of attorneys before the Office is now more real than it used to be 20, 30 or 40 years ago. Part of the effort has been to develop the set of proposed guidelines which have been mentioned. The guidelines were developed by a committee from the Patent Office and from the Bar and were distributed to the Council of Patent Law Associations about a year ago for comments. Some comments have been received, but they are in that status where they have not been adopted. Perhaps the need for adopting them may no longer exist in view of the changes in the rules. But I want to comment on some of these items.

The attorney or agent should not file an executed oath, affidavit or declaration in the Patent Office if he has reason to believe the applicant did not understand the nature and content thereof. In other words the attorney has a duty to see that the applicant who is signing the oath knows what he is signing. He should take steps to rectify the matter if he finds any oath, affidavit, declaration or other statement on file in the Patent Office contains a material omission or misstatement. He should not present or maintain in a patent application a claim which he actually knows to be unpatentable because of any statutory bar under the provisions of 35 U.S.C. 102, but this prohibition does not prevent him in good faith from advocating the patentability of the claim if he believes the reasons asserted for patentability are not frivolous. He should disclose to the Patent Office any prior art which has not been cited by the examiner, provided he then has actual knowledge of the prior art and he recognizes that it should be considered in determining whether the claim in a patent application which he is prosecuting meets the conditions of Section 103. He should not make false or misleading

representations of the fact or law to the Patent Office knowing them to be false or misleading. He should not omit material from communications to the Patent Office knowing that such omission could create a false impression or be misleading. He should refuse knowingly to participate in any possible fraud or inequitable conduct in dealing with the Patent Office.

In the event that a client refuses to permit a practitioner to comply with any of the foregoing guidelines in connection with the case in which a practitioner represents such client in a matter then pending before the Office, the practitioner must forthwith request release from the case; and if the client refuses he must withdraw. Failure to comply with any of the foregoing guidelines by reason of inadvertence or good faith exercise of judgment should not be deemed noncompliance with the spirit of these guidelines. Now in my view one reason why things have been slow on putting out any such paper is that most of it shouldn't be needed. Most of what's there goes without saying, and the vast majority of patent attorneys act before the Patent Office accordingly without even thinking twice about the matter. Perhaps the reason for not going further with the paper is the recent amendment of Rule 344 adopting the general code of professional conduct of attorneys. There is also Rule 346 relating to any paper filed by an attorney or agent or presented by an attorney or agent.

We are now concerned some of the time with questions that would not have been called fraud let's say 20 or 30 years ago; there is actually a different attitude in the prosecution of cases. It seems to me though that quite a few of the allegations and discussions take a view that the attorney knows everything and is smart, 100 percent smart, whereas the examiner knows nothing and is 100 percent dumb. Whereas attorneys do make inadvertent mistakes—now and then bad ones, decisions which do not seem to be taken into account—there are quite a few examiners who know what they are doing and attorneys would have a very hard time putting anything over on them if they tried. That sort of thing doesn't seem to be taken care of in some of the discussions.

In conclusion I would like to call attention to a decision not yet published (*Kearney Trecker Corp. v. Giddings*, 171 U.S.P.Q. 650) that involved the conduct of an examiner who had retired from the Office. The examiner was the chief of the division which had originally allowed the case; he had participated in the prosecution in the sense that he had to approve the examiner's actions, and he actually participated in interviews. After he left the Office he did not immediately

become registered. He was retained by the company to work on—I think he suggested it himself—getting a reissue of this patent with a broader claim, and also there was another competing patent involved which he was instrumental in having brought up and also reissued. Fraud was held. There was improper practice from the standpoint of conflict of interest even though the reissue itself was otherwise not necessarily improper. But the assignee, the patentee, suffered from it.

One point about this decision is that it brings out some distinctions concerning some questions which have been asked. It's quite often asked if a patent is invalid anyway, why bother with the question of fraud, because it isn't until the claim is actually invalid in the usual case that the question arises. Section 288 of the statute is a section which provides that you can sue and recover on a valid claim despite the fact that some of the claims may be invalid. This section was necessary in the statute because the common law rule was that if one claim in a patent was invalid the patent itself was unenforceable. The section abolishes the common law rule by providing that you can sue and recover on a valid claim despite the presence of an invalid claim, but it has the qualification that the invalid claim must have been there without deceptive intentions. So if there is fraud or deceptive intention as to one claim, the entire patent is unenforceable by reason of this Section 288. And there is also the question of disclaimer and reissue. If there is fraud in one claim, a reissue is barred that patent (Section 251); there might be a possibility of valid claims being presented, but that is immaterial. Likewise a disclaimer would be of no avail (Section 253). This decision has some comments on these matters which may clarify them.

MODERATOR NEUHAUSER: Thank you, Pat. Now I didn't let you get your question in a while ago, so you're the first one. And after that, Wally, you've got one that's hanging fire.

WILLARD L. CHEESMAN: I think Mr. Federico answered most of my questions. I wanted to pursue a little further again the presentation of evidence during the priority trial of an inventor where the opposing party is present and able to cross-examine. If an exhibit is presented that is blocked out it would seem to me that where it's an irrelevant matter that's blocked out, there's a different burden of responsibility here than where we have a strictly ex parte procedure. Is that correct?

MR. FEDERICO: I agree with you during the taking of testimony, because the opponents could call for production, but the question of interference was raised in connection with the preliminary statement which is filed before getting to trial.

W. M. KAIN: Will you comment on the best practice for bringing references to the attention of the Patent Office in late stages of prosecution, after allowance, after payment of the final fee, or even after issuance?

MR. FEDERICO: Assuming they are references which you think the examiner should have seen but which you believe are still avoided by the claims, as far as I can see the only thing you can do is to file a paper calling attention to them, with a statement of the reasons you consider the claims patentable. I doubt that there is any duty to withdraw the case and file a continuing case. Of course if the claim needs revision because of a new reference I think you've got to do something such as offering a proposed amendment.

MR. ROSE: That was covered in a case of the Court of Customs and Patent Appeals on the issue where the applicant tried to enter an amendment to avoid a reference discovered after he had paid his final fee. The Patent Office refused to withdraw the case from issue and the patent issued. The Patent Office refused to allow a reissue on the grounds there was no mistake, because he had let the patent issue. The court held that at that stage of the game it was beyond his control under Rule 313, I think it is, which says a case will not be withdrawn from issue after payment of the issue fee and therefore it was the kind of mistake that would sustain a reissue patent.

MR. FEDERICO: One might disagree with the court for the reason that the applicant still could have filed a continuing application.

MR. ROSE: That's a question of procedure, and at that point the Patent Office would have refused to enter an abandonment.

MODERATOR NEUHAUSER: Just to comment on that, Wally: We had a couple of instances that have come to my attention where patents came to the attention of the attorney after the patent had issued which in his judgment were at least as relevant and perhaps arguably more relevant than the art cited, but clearly in his judgment also required no changes in the claim. So he didn't think it was appropriate for reissue. What we did, in these cases was to send in a communication to the Patent Office asking them to place it in the file, giving the patents and the reasons why the claims, in our judgment, were still allowable. And as far as I know they were put in the file. They did not do that for a while but I understand that the Patent Office now will put a communication in the file after it issues.

ANON: We've had the same experience—they have put the papers in the file, for what good they do.

MR. FEDERICO: I ran into a situation which I suspect one of you was responsible for. Some time ago I was comparing some corresponding U.S. and German cases, in connection with the references cited in each office. The U.S. case was passed to issue without a certain reference having been cited. The German case, acted on later, had a certain reference cited which anticipated a claim in the U.S. case. Then in came a disclaimer, cancelling that claim from the U.S. patent.

MODERATOR NEUHAUSER: We're due to quit in one more minute and go to lunch. I did promise you. If you can do it within one minute, fine.

ANON: Okay, well maybe you can comment on it later on, but there's a practice that's an exception to the written document, written response rule in the Patent Office, that's quite prevalent today. I imagine it's prevalent with a lot of other people. That's the telephone interview, particularly before the first Action. I've had this happen in the past year maybe a dozen times all over the Patent Office. I get calls and the first question is, where's a good place to start searching? Yes—that's exactly it—can you give me something to give me a lead on where to search? It saves the examiner time—or do you know of any art that's come up since you filed the case, or do you have something referred to in the case that gives me a lead? Now this helps the examiner a lot but there's nothing in writing on it and, I don't know, it'd be interesting to get a comment on that aspect of the practice.

MODERATOR NEUHAUSER: Gentlemen, we will go to lunch. Now, I'm going to have Jim Harris tell you exactly how to get there. It's not very far but it's better if you go with his directions than with mine.

DIRECTOR HARRIS: It's two blocks south on 21st and Pennsylvania. It's the Joseph Henry Building, the ground floor, the Adam's Rib restaurant. We are scheduled for lunch at noon. We will resume the Clinic at 1:30 p.m. We stand temporarily adjourned.

## **Afternoon Session**

MODERATOR NEUHAUSER: Well I think we'll give you about a half-hour or so, if the two victims are willing, for discussing the subject matter and the questions that they may have raised in your mind and then about 2:00 we'll put the next two stars on. The gentleman in front.

ANON: I have a question for Mr. Federico or any other member of the panel. Suppose in the course of an application I have put my best foot forward and there were certain references I thought probably weren't very pertinent and I didn't give them to the Patent Office. Then the patent issues and, as I look back at the *Walker* case and things like that, I think that maybe the courts might not agree with my judgment in not having disclosed certain references to the Patent Office. Is there any procedure, whether by way of reissue or by another way, whereby I can go back to the Patent Office, put all my additional cards on the table, and if they agree with my judgment that they were not pertinent, I get a clean bill of health patent? (Laughter)

ANON: Mr. Chairman, may I comment on that?

MODERATOR NEUHAUSER: It's open season now, go ahead.

ANON: I think the question is an excellent one and it happens to fit something that, about two or three years ago, I spent some time drafting. It was a proposed revision of the reissue section which would have covered just exactly that situation and in contemplation that when issues of fraud and misrepresentation arose either from the applicant's own discovery of their existence or of some discovery of them in a litigation situation, that they might be cleared up by going back and having in effect a confirmation of the grant under the equivalency of a reissue. I don't recall that this thing ever took much root in anyone's thinking. I do remember discussing it with Tom Brennan, chairman of the Senate committee who seemed to think that the need was present but, of course, didn't commit himself. I understand that Pat has some ideas on this same subject, so maybe Pat could get into this.

MR. FEDERICO: Under the present statute, there's nothing you could do. If you applied for reissue to get narrower claims, you could call the examiner's attention to these references in the reissue prosecution, but you cannot apply for reissue with the same claims for the sole reason that you want the examiner to look at references. Now under the pending patent bill, anybody can call the Office's attention to references during the first six months after the patent is issued; this could be done by the patentee if he wants to. It isn't mentioned, but the language would permit it.

MODERATOR NEUHAUSER: Wally Kain may want to get in on this. He talked about it at lunch. He was contemplating filing a reissue in a similar situation in which he was going to use Paul Rose's technique of making the oath with an asterisk and right after that where it says "claimed less," you have an asterisk that says in the course of prosecu-



tion it may be less but right now you think you are entitled to the claim, if I'm not misquoting you. So you may have a test case.

MR. LEYDIG: For what it's worth, we have utilized the occasion of a reissue application to make of record all additional art. Now, whether that is a subterfuge may be a question in some cases. But I don't believe it is because in almost every situation you have some statutory reason for reissuing after the patent has been out a while. And to accompany that application for reissue with the prior art—that is being done. We've done it and many others are doing it. I think it certainly is a proper and prudent way to approach it.

MR. ROSE: You do that, though, by meeting the requirements of the present reissue statute, where your oath, in the reissue, must state either that the patent claims more or less than you are entitled to. Now you can take the patent that has, let's say, call it intermediate claims. You could file an oath saying that you think the patent covers less than you are entitled to, put in broader or otherwise modified claims, cite the reference, and I don't think you would be faulted for fraud. Or you could do as we were speaking a moment ago in talking about this before the meeting reopened, and that is put in some intermediate claim, or specific claims, that you might need as a safeguard and explain that in your oath and that, I think, would meet the reissue statute. If you keep precisely the same claim and say that you in effect want re-examination in the reissue you can't get it under the present statute.

MR. LEYDIG: Well, one of the reasons you may have claimed more than you are entitled to is the later recognition that there is prior art you did not know about.

MR. WRIGHT: In a recent California case where fraud on the Patent Office was found, the court enjoined the patentee from asserting any subsequent reissue. That was a case where deliberate fraud on the Patent Office was actually found. I can see that this case is compatible with what we're saying here. Where a deliberate fraud has been committed, the requirements for obtaining a reissue cannot be met.

MR. LEYDIG: I mentioned something to Mr. Federico on the way over to lunch and I would like to draw it out here. Several people today have discussed the question of sending in a large number of references, for example 18; somebody else mentioned 100. In a country where we have the search system, where it is assumed that the examiner will examine literally hundreds of references in the course of his search in order to find any that may be pertinent, what is wrong with sending in 18 or even 100, if, in fact, you find that you have that many pertinent references which the examiner has not found. You know that the

chances are extremely great that counsel for defendant in a heated litigation is going to accuse you of having improperly selected between one reference and another because it's certainly going to come out that you knew about the others. He will make the most of it. Why are you doing the Patent Office any disservice by laying before the Patent Office whatever references you may have?

MODERATOR NEUHAUSER: I think, Pat, that's your potato to handle.

MR. FEDERICO: I tried to give an answer before but I wasn't very successful. Theoretically there's nothing wrong with giving the examiner a thousand references and saying you ought to look at these. There would be a lot of grief if anybody ever did that; suppose these are a thousand that are in a subclass that has a thousand patents, the examiner would be perfectly justified in saying, I'm going to look through subclass anyway, I'm not going to look at these others.

MR. LEYDIG: Well there is the limitation of five though, at the moment, you see. That's the trouble.

MR. ROSE: There is a limitation of five only to the extent that if you limit it to five, furnish copies and discuss them, they will print them on the back of the patent. There is no limit to the number of references that you can cite to the Patent Office in a paper because they've got to enter the paper in the file. The onus of the thing is that if you cite too many everybody knows, as a matter of fact, that the examiner's not going to look them up. My solution to the problem where you have a lot is to furnish copies with the paper and, as I said in the introduction, no court is going to fault you if you furnish copies to the Patent Office, because the examiner will look at them, probably, if they're right in the file where he doesn't have to go out and dig them up.

MODERATOR NEUHAUSER: Could I ask Paul a question here on this: could I have two bites at the apple? Can I put in five and distinguish over them and get those five which I think are the most pertinent printed on the back of the patent, then to protect myself like Fred Leydig, send in a later paper with 45 patents listed. Or are they going to fault me on the ground that I listed 50 and distinguished only five?

MR. ROSE: I think that they would print the five that you put in before the first action and put the other paper in the file.

MODERATOR NEUHAUSER: There's a question over here.

ANON: Just an observation: An alternate to sending copies, and it helps the examiner a lot, is just to stick in the class and subclass printed on the patent. If you do this in your list, the examiner can just run through, he's looked, and if they're mostly from one sub he's probably looked in it and he can just pick up the ones he hasn't searched. As a

practical matter, I know in these phone calls that I frequently get, give the examiner the class and sub and he'll look at the patent, because it's easy then. The thing he doesn't like to do is take the time to look up the class and sub.

**JACK RABINOW:** I worked at the Patent Office as a member of a committee to study the information and paper problem. I quickly learned that in patent search too much is much worse than too little. If you give somebody a hundred patents, either the numbers or the patents themselves, you do him no favor at all. If you file for a patent, presumably you are going to file for a patent on something new and different and the only reason you should cite a patent is that it's so close that there's an argument possible in the mind of the examiner. But to say, here's the hundred patents of relevant art, doesn't help. Of course there is a lot of relevant art. There's usually a whole class of relevant art. He will never look at a large number of patents because he hasn't got time, he's working on a piece-work system in the Patent Office and Friday is a terrible day. What's more, I think you'll be accused of shady practice later in court because you cited 40 patents deliberately to obscure the issue because the 41st is the one you didn't cite. If you cited a hundred, someone will say, why didn't you cite the 101st? That's the particular reference of what was done in Germany, and so on.

So I believe that this type of citation doesn't help the examiner. It certainly wouldn't help me if I were the examiner. My feeling is that if you would cite two or three patents that give the examiners the closest art and if you can show that it doesn't really anticipate you, that's all you can do. Anything more than that will just confuse the issue.

**MR. WRIGHT:** It appears to me that a patent attorney is placed in a dilemma. If he cites too many patents, he's going to be accused of hiding a highly pertinent patent in a lot of patents. If he cites too few patents, then he's going to be accused of not disclosing a patent which later becomes pertinent because of the way references are combined. It's impossible to tell what reference might be important when combined with another reference.

**MR. RABINOW:** I think you should cite only those things that really have direct relation and I think it's perfectly proper if you don't cite any references at all. The question of fraud is based on whether you deliberately withheld something. That means that you wrote a claim that covers an old invention. If you don't do this I don't think you're under any obligation to God or country to cite all of the things that somebody might think have something to do with your invention. You're supposed to write a disclosure on something that was not

invented before, and no other patent has anything to do with this as far as the claims are concerned.

MR. LEYDIG: Mr. Rabinow, I think most of us agree with that principle, but the courts don't. That is the basic difficulty and it isn't a question of being helpful to the examiner. Surely it is that in part but that's not really what we're talking about. We're talking about how to avoid a charge of fraud on the Patent Office. That's our problem.

MODERATOR NEUHAUSER: I do want to add one thing, Fred. Jack carefully said you had no obligation to God or country; he didn't say anything about courts.

ANDREW B. BEVERIDGE: Commenting on what Fred Leydig just said: I think as attorneys we have to face up to the fact that there is no sure antidote to the problem. It's part of an occupational hazard, if you want to call it that. In other words, we can't solve the problem—let's face it. I think Mr. Rabinow has the better side of the argument. We should take the responsibility of trying to determine the most pertinent art and not take the subterfuge of flooding a given application with a hundred patents. This becomes meaningless.

ALBERT C. JOHNSTON: I'd like to add to what Andy says. It seems to me that this question really isn't a question of fraud on the Patent Office. This is a different question. It's a question of the fact that in any event counsel is going to cite against the patent in the courtroom something that wasn't cited and considered by the examiner; he does this because he is escaping thereby the presumption of validity. Now I don't care how many you cite, you can cite 100 or 1,000 and defense counsel is still going to find something that you didn't cite even if it's the foreign equivalent. And he will cite that and argue that there isn't the presumption of validity—I mean if he can make a reasonably sensible argument on that foundation. So it's pretty much in line with what Andy says. This is a procedural practical problem of bringing an interplay between the principals of law that vitiate the presumption of validity in the courtroom and the practical handling of the case in the Patent Office. I don't think that there's any practical solution to it, short of an entirely different system of litigating patents which is, in effect, that you build the whole question of validity back into a patent tribunal as distinguished from the federal court system.

MR. CHEESMAN: To comment on this of course you can simply ask the examiner to research the case, and thereby, presumably absolve yourself from all responsibility. But I agree with the comment from the panel here that if you are going to try to build up a case that is equivalent to

the original presumption of validity, you can't do it by inflating the record with a lot of things that you think the defense counsel might find. Why not have a look at them yourself before you give them to the examiner, and if you find paragraphs or sentences or parts of the drawings that are pertinent, point them out. And how can you be faulted if you happen to miss one or the other? Because there will always be one that you miss.

Now, may I switch subjects? Mr. Federico earlier in his talk mentioned a decision which relates to the *Kearney-Trecker* case of the reissue and the hiring of a primary examiner. Those two special facts are in that case. Now my question is this: The court found that the company in hiring the primary, as a retired examiner, for the purpose of, let's say, consulting in the preparation of the reissue, was guilty of a predatory act and, therefore, they found a Section 2 violation in the hiring of the examiner. Now my question is, is that finding specifically to be confined to the hiring of a primary examiner, or would any other examiner do?

MR. FEDERICO: I would say that applied to any examiner because the essence of the case was the contact with the application in the Patent Office; having dealt with exactly the same case before and then working on it afterward, makes a plain case of conflict.

MR. CHEESMAN: Is it likewise to be restricted to the special facts of a reissue? The decision does discuss to great length special facts of a reissue.

MR. FEDERICO: The decision would not be limited to reissue. Let's take two kinds of cases that might arise after an examiner leaves. The first kind of case is that after he has left he is retained in connection with one of the cases that was pending in the Office and on which he had worked. Now he isn't supposed to do that, and I have never heard of its having happened in recent decades. There would be practically the same situation as in the reissue—he had worked on the same case before. Now another situation that might arise, and again I haven't heard of its happening, is that after the examiner leaves he works on a new case that never was filed. He isn't supposed to do that for two years. But he does help on preparing a new case. Well, strictly speaking, there'd be no conflict of interest there unless he utilized information that he got while he was an examiner, such as if there was an interfering application and he helped prepare a new application, and knew about the interfering application and steered things the same way. Well there you'd have your same question, the same result ought to apply there.

MODERATOR NEUHAUSER: I think that from the corporate standpoint when we hire anybody from the Patent Office we carefully respect the fact that he doesn't work for that period of two years on any case in the art in which he was examiner.

J.R. MOSES: I'm beginning to get the feeling that the basic problem is fraud by defense counsel. In the beginning of your talk, Mr. Federico, you suggested where we do have questions about public use that we inform the Patent Office. I was just a little confused about that. In other words, where the attorney thinks that there might possibly be public use or a question of public use—should he notify the Patent Office?

MR. FEDERICO: I referred to several cases where an appendix had been attached to the ordinary oath, a footnote or additional paragraph, because there was a clear-cut question. Where various events have occurred and the attorney has come to the conclusion that there is no public use that would bar the patent, should that be put into the oath? I would say not, but when I said a statement, I was thinking mainly of a separate statement explaining the situation to the examiner, and it might or might not be under oath at that time.

MAURICE H. KLITZMAN: Coming back to the citing of 100 references versus 2 or 3, there are a couple of cases in which the judge commented on the good faith involved in which he said that it was evidence of good faith to have cited 2 or 3 and as to these other references that were not cited, the defendant would have to prove bad faith—some actual intent to withhold—which is very difficult to do. Therefore it is evidence of good faith to have cited some references.

MODERATOR NEUHAUSER: I do think we ought to observe one thing with respect to Jack Rabinow's comment—that you might cite 40 and then the 41st is the one that somebody says you should have cited. Also when you cite 40 you may well be accused by an alert counsel of camouflaging number 2 or number 3 by putting 39 around the one that's worthwhile.

LUTHER A. MARSH: I understand there's a recent survey that heretofore the Patent Office used to update their files quite often in the references and then the references disappear. Consequently the examiner doesn't have all the references theoretically that he ought to have. I understand this number now is something like up to 33 percent on some recent survey that I read. In this instance, if the counsel prosecuting the case also is unaware of this particular art, particularly where you are working in various arts, then how does this strike the panel?

The examiner hasn't found it, the outside counsel maybe doesn't even make a search, maybe he has no bearing to make a search on, he depends on the Patent Office to get into that art.

ANON: I didn't get the full import of the question—that no search was made by the attorney.

MODERATOR NEUHAUSER: Well, he questioned the integrity of the files, the fact that they were not 100 percent complete. Is that your point?

MR. MARSH: The Patent Office doesn't find it because it's missing from the files.

MR. FEDERICO: They did at one time, I don't know if they still keep it up—have a periodical survey of the files in which the copies were checked against lists and then filled up.

MR. MARSH: My point is that the outside counsel, in order to have this adequately done is going to spend some \$2500 to have a search made which is prohibitive just to get an actual search of that which ought to be in the files. Isn't it the duty of the Patent Office to update these?

MODERATOR NEUHAUSER: I think it's the duty of the Patent Office but I'm afraid that may be a little far from the broad question we have here. I hope they make the files a little more complete.

MR. ROSE: To answer the other party's questions, what you're asking is whether the applicant is under a duty to make a search in view of the poor condition of the examiner's files? The answer is no. However, if you know of pertinent art that he doesn't cite, then recent decisions hold in effect that you are under a duty to cite the best art known to you if it is not merely cumulative.

MR. MARSH: But there's no reason to make, say, a \$2500 search to check that art in and out.

MR. ROSE: Well, I'd go into business if I could get \$2500. (Laughter)

MR. WRIGHT: It seems to me that for patent attorneys to really know what to do in these situations, we need a clearer understanding of our duty and the acts on our part or on the inventor's part which will actually constitute fraud on the Patent Office. The standard has varied with time and appears to me to vary between courts. I think we need a clear decision from the Supreme Court setting forth the standard to be applied. Is complete candor or something less required?

MR. JOHNSTON: Let me comment on that. I think it might be useful to you in that regard if you wish to make a note that in the 1971 ABA

Patent Section Committee Report, the report of Committee 403 contains a list of litigated cases on the fraud issue broken down in categories of certain questions. And if you will take the time to read those cases I think you will get the answer to your question, which still wouldn't tell you what is going to happen to another case, but it would tell you what had happened in past cases.

MODERATOR NEUHAUSER: I'm not sure, Fred, I think I promised you and then this gentlemen here—

MR. LEYDIG: One quick comment on what we've been saying. I think we all feel that we'd better act this way. It has been said several times today that there is an absolute duty on us to cite all art. Now that apparently includes Section 102 and 103 prior art. There is nothing that I know of that says you have such an absolute duty to cite Section 103 art. Anybody care to comment on that?

MODERATOR NEUHAUSER: Anybody want to comment on Fred's statement?

MR. ROSE: I'll comment on that. You're absolutely right. In all these fraud cases that I have read and discussed this morning not one of them touched the 102-103 issue as such. What they say, and of course I don't think that the federal courts have the thing about 102 and 103 rejections that the Court of Customs and Patent Appeals has. They look at it from the old ground of what I was criticized recently for saying was invention. And if the court felt that the examiner would not have allowed the case if the reference had been cited, it found fraud or inequitable conduct in the failure to cite it. They begged the question of whether it was 102 or 103 and they tried to second-guess what the examiner would have done. Now that could be under either section. I don't remember a case that, in talking about fraud for failure to cite prior art, that's mentioned the applicable section of the statute. You may know of some, but I don't.

MR. JOHNSTON: Mr. Chairman, may I again use a report that I mentioned a moment ago. It breaks down the cases in this category. The first category, a duty to disclose only prior art that anticipates and cites seven decisions on that point. Then part 2, an uncompromising duty without classification. Two decisions, one of which is *Beckman Instruments*, another a *Monsanto* case. But in the *Beckman* case, I would remind you, the court held that it was no fraud.

MR. LEYDIG: I might say the *Monsanto* case didn't relate to prior art.

MR. JOHNSTON: Right. So that this is a rather vague area. The third category, a duty to disclose prior art more pertinent than that considered by the Office, citing two decisions. A fourth, a duty to disclose only



undisputed and obviously relevant prior art, cites one decision. Fifth, a duty to disclose everything that may affect patentability, it cites *Monolith* on that point. Next, no duty unless possible fraud or inequity, for which one case was cited. Next, does the duty extend only to anticipatory references or does it include those relating to obviousness? The comment is that *Monolith*, *Monsanto* and *Beckman* would appear to require disclosure of prior art relating to obviousness.

MR. FEDERICO: I think there is something illogical in the question in the first place, because I read 103 in a strict sense and take "not identically disclosed or described" in the prior art specified in 102 as meaning what it says. So if you have a situation of a plain 102 anticipation, you cannot have the situation where the attorney presented a claim and knows about a plain 102 anticipation; there is something false in the first place in presenting the claim. To me all cases that arise are 103-type cases, using my narrow viewpoint of anticipation; if there is a reference that actually is a 102 anticipation and the attorney knows about it, he's got a far greater duty than to merely call the Office's attention to it. He should take the claim out. The courts are however, apt to use anticipation in a looser sense.

RUFUS S. DAY, JR.: I think there's one distinction that we might mention here. We have a subcommittee in the Antitrust Section of the ABA that has been looking at these cases, and we reached a tentative conclusion that when the question is antitrust liability, the misrepresentation must be material in the sense that the patent wouldn't have issued without it. However, we don't find the same test applied when the question is whether the patent is unenforceable as a matter of patent law. On that question, there's been an insistence on full disclosure, full good faith, regardless of materiality in the sense that the patent wouldn't have issued without it. And this distinction between the test for antitrust liability and the test for unenforceability as a matter of patent law has been enunciated in several cases. The first one was the *Corning Glass* case, then *Beckman-Chemtronics* and most recently the *SCM-RCA* case.

BARRY A. BISSON: There's one type of prior art that hasn't been mentioned, which to me raises a real can of worms, especially within a large corporation. That is the earlier filed copending case by a different inventor. It is quite common to have different inventorship for one utility of a new composition than the inventorship of the composition per se.

For example, the inventor who is a chemist discovers a new compound. His sole utility for the compound is as a solvent. Somebody else

finds that the compound is good as a drug. So you have two copending applications, with the inventor of the compound being prior. The compound is not in the prior art because the application is still pending in the Patent Office. Is there a duty to disclose the copendency so that the examiner can cite that copending compound case against the later filed use case?

MR. ROSE: No. Well, I say that for this reason. You have two separate classes of invention here. You have a composition claimed in one application and a use or process of using it in another and the chances are that the examiner is aware of both. When I said no, I meant you didn't have to make the cross-reference to avoid fraud. I think as a practical matter you probably could or should make the acknowledgment in the use case if the examiner doesn't already know about the composition case, but the chances are he would in the same general art, but since you have two statutory classes of invention you're entitled to two patents. And one is not a reference against the other in the normal sense because the use case inherently admits the prior existence of the composition; one is not prior art unless you recklessly have overlapping claims in the second case. There have been cases where in the case of the second inventor, they came awfully close to the line of claiming the compound. There's a duty on the part of the attorney to maintain a line of distinction between the use case, where he takes somebody else's compound and uses it and the compound. It might be better practice to make the cross-reference in the second case but I don't think it would be fraud not to.

MR. BISSON: I lost a beauty in the CCPA, *In re. van Venrooy et al.*, 56 CCPA 1199, 162 U.S.P.Q. 37, 412 F 2d 250 (1969), where what was cited was a reference to an earlier filed abandoned application by a different inventor. In this case, there were two process inventions, not a compound and its utility. However, the case shows that if the Patent Office finds out about another related application they darn well are going to cite it.

MR. KLITZMAN: I don't agree with the view of Mr. Paul Rose. The 102 (e) question comes into play in his situation. It is prior art that is peculiarly within your knowledge and you can't rely on the examiner having the other case; he may or may not have it, and may be totally unaware of its existence. And if you have that kind of situation I think I'd feel safer in citing it because it is prior art under 102 (e).

MR. JOHNSTON: I'd like to agree with the last speaker and respectfully disagree with Paul. I think that it would be a serious mistake to fail to mention in the specification of the proposed application on the use of

the compound that a coworker had previously invented the compound. To fail to mention that that was his invention and was the subject of another application, I think, would be in error because in my view the coworkers work is very definitely prior art. If you filed claiming just the use and named the compound without having acknowledged that the compound was not your invention, where under ordinary circumstances the examiner would not be able to pick up a reference showing the compound, this, I think, would be very unwise and would properly give rise to the question of withholding knowledge of prior art.

MR. BISSON: Then you raise the other part of the can of worms— inventorship. If the contribution of the coworker, who was not mentioned as an inventor, is sufficiently important to be prior art, then the inventorship is probably wrong. The coworker was probably also a coinventor.

MR. JOHNSTON: I don't follow that, because it seems to me that by definition when you say you're filing in the name of Jones for a use of a compound that Smith had invented before Jones, it seems to me that by definition you've got two inventions

MODERATOR NEUHAUSER: I think I'd better cut this one off because we're getting afield from our subject and I have a man back here waiting.

MR. STERNBERG: I just have one comment on Pat Federico's analysis of three rejections because he has just picked a case where there's a single patent and you're trying to distinguish over that in the sense of there being no anticipation or obviousness as compared to a combination of references where the attorney may not at all realize the impact that one reference has on the other. Yet the Patent Office might or the courts might find, and I think this is where you have a distinction or possible distinction, that the applicant has not disclosed the most pertinent combination of references. How many combinations and permutations does an attorney have to go through to combine the art to make sure that he's disclosed everything that's significant to the Patent Office?

MODERATOR NEUHAUSER: Let me add to that before Pat and Paul pick it up. My interpretation of what you're required to do by way of distinction, assuming you cite five references, is distinguish individually over each of the five. You don't have to imagine all the combinations that the examiner can think of. But I'd like to get the answer to that too.

MR. FEDERICO: In my remarks on that point I merely wanted to bring

out that in my view all situations were 103 situations, because if you had a real 102 reference there was something more the matter, but I doubt very much whether an attorney has to build up all possible combinations. I wanted to comment on this other question of a use case where the inventor of the use did not make the compound but got it from somebody else. The case should be so presented that the only invention being asserted as an invention of the applicant is this use. That ought to be made clear. Going further, it ought to imply or state that the compound was not the applicant's invention.

MR. CHEESMAN: A very special case of what you've just been talking about, Mr. Federico, is where the compound is not old in the sense that it has been published, or in an issued patent. But it is, say, the subject of a private communication.

MR. FEDERICO: That's what I'm talking about—you told me about it.

MR. CHEESMAN: You suggested that the specification should be so written that that fact is either implied or expressed in it.

MR. FEDERICO: There should be no possible implications from the write-up of the specification that this inventor had anything to do with inventing the compound as a compound.

MR. CHEESMAN: Yes, I know it, but you haven't answered my question. I have the problem right now of writing the specifications on this very thing, a private communication. The new use invented by me. A compound privately disclosed to me. Now do I say so in my spec?

MR. FEDERICO: Not necessarily.

MR. CHEESMAN: That's what I wanted to know.

MODERATOR NEUHAUSER: Just don't claim it.

MR. JOHNSTON: Just say it's a known compound, or a compound of which you've acquired knowledge.

MR. FEDERICO: You just treat it as a known compound in your entire communications.

MODERATOR NEUHAUSER: We've got two questions, one man here and one back there. Mark you're first, and then I think we'd better interrupt. I hate to cut off any enthusiastic discussion, but the other two panelists present may bring another facet to this you might want to discuss.

MARCUS B. FINNEGAN: It seems to me we're talking about an almost insoluble problem here—the problem that Fred Leydig raised, where you've got, say, 20 patents cited against you as prior art. I can tell you a little story. About 10 years ago in my own practice we had a case in the Court of Claims, and there were 21 references cited against us. We had a settlement conference—this was very early in the case—and my

associate and I came down to Washington, perhaps not as well prepared as we should have been, and we started going over all these references. We'd been over what *we thought* were the key ones before, but we thought we'd better look at all 21 of them. We stayed up until about 3:00 a.m. going over these 21 references. There was one patent, the Leach patent, that was left. We took a quick look at the Leach patent and said, the defendant couldn't possibly rely on this reference; this patent is so obviously non-pertinent that we should forget it and go to bed.

The next morning we went into Hayward Brown's office and sat down. Henry Van Arsdale, who was an old timer, was assigned to defend the case for the government. We started talking about settling and the question of the pertinent prior art came up. Henry then picked up a copy of this Leach patent and said he thought it was a complete anticipation. He had a most ingenious way of reading the claims of our patent on the device that was illustrated in the Leach patent, but one that I venture would not have occurred to one out of 25 people.

So, that's what can happen when you get into court, and defendant's counsel uses the same ingenuity and may be able to convince the court that what you thought was an irrelevant reference is actually a very pertinent one. I just don't see any way out of the woods in that situation. You either cite the 40 or 50 patents or you make a selection based on your own subjective powers of reason, perhaps, and hope that those are the best references. But it seems to me that it's a tremendous dilemma.

MODERATOR NEUHAUSER: I have good news for you, Mark. It's now 2:20 and by 4:50 we will have solved your problem. Maury, if you have one that's very pertinent now, I'll let you have one last lick.

MR. KLITZMAN: One area that's changing a little bit in terms of obtaining a reissue is whether you claim more or less than you have a right to claim. There's the *State of Israel* case, 158 U.S.P.Q. 584, that let them claim foreign priority belatedly which technically had nothing to do with scope of claims. Then in the last few months, there was a Board of Appeals case, *Exporte Scudder*, 169 U.S.P.Q. 814, which permitted correction misjoinder by reissue. This case didn't have anything to do with claiming more or less than you have a right to claim in terms of the scope of the claims. And so they are permitting you to obtain a reissue on broader grounds by interpreting "more or less than he had a right to claim" broader than they had in the past, and I would suspect that this will enlarge as time goes on.

MR. ROSE: Rose will make one comment on the *State of Israel* case

and that is that the very basis of the case was that the thing claimed less than he had a right to claim, was priority. That was Holtzoff's decision.

**MODERATOR NEUHAUSER:** All right, let's shift over to our next two people. I've been so impressed by all the comments about candor and full disclosure and avoiding fraud that I think I ought to correct Jim Harris's initial statement about me. I'm not merely a substitute for Mayers, who is in a hospital and couldn't be here, but I'm a substitute for his substitute who couldn't be here. So let's turn to Jack Rabinow who is going to discuss this subject from the point of view of an inventor and a research director. Now Jack is everybody's favorite inventor and favorite entertainer. And if he didn't have one of the most creative minds I've ever encountered, he could have made it big in show biz. If you don't enjoy yourself in the next 20 minutes that he's going to talk, you've lost your sense of humor.

#### **JACK RABINOW**

Well, I'm not a modest guy, as you know, but I don't feel that I really belong in this crowd. You know, I'm the only inventor here; I guess some of you also invent sometimes. I hope you do. Just as I sometimes think of myself as an attorney. I suppose this is a great collection of patent attorneys; if it isn't a great collection your companies are being defrauded.

When I started working with the Patent Office and by "working" I mean fighting them, I found that their attitude was very strange in that they fought with me harder than I thought they should have. I thought they were supposed to protect my rights and it amazed me that they would try to cut me down as hard and as fast as they could. If they couldn't find art they'd reject my claims just to see if they could get some more time to find art. One examiner once actually told me that "the day was Friday so I rejected it on nonsense because I needed more time to look."

After I got to be friendly with them I asked one of the examiners (who is chief of the division now), "Is it your job to give me the best patent or the worst patent?" And he said, "Our job, under the Constitution, is to give you the maximum protection, but because the

lawyers always ask for too much, we try to cut them back knowing that they are asking too much with claims that are too broad and so, between us, somehow or other, justice prevails." I didn't like this position then but I think it's less true now. My attorney most of the time is Max Libman, but not always because Control Data has its own staff. We try not to claim more than we are entitled to. I find that the climate is changing, particularly during the last 20 years. The Patent Office does try to help the inventor now, much more than fight him.

I think that a great deal of the trouble that your discussion points up today is due to the attorneys. The attorneys are not always as scrupulous as they should be about the things they claim. They claim deliberately broader art than they should. And the Patent Office, knowing this, has traditionally fought you very hard. It seems to me that if the patent bar made a great effort to clean its own house, so that attorneys would never claim more than they are entitled to, it would be better than deciding whether or not to cite some art. It's much easier to draw a broad claim, then narrow it down in each subsequent action. So I think a lot of the fault lies with the attorneys who try to stretch the point a bit. The Patent Office knows this and then you get into court and there's a big fight.

I think that, in general, ethics are the result of laws, not the other way around. In other words, if the courts slap us down, the ethics will also change. I think patent attorneys will be much more careful after meetings like this. I myself will be more careful too. Yesterday I talked to Max Libman about this and told him I'd be speaking today and I really didn't know whether I should. Max said that this fraud accusation is tried very often. Everytime there's an infringement case and one side can't prove anything it claims the attorney for the other side was a liar. I think the patent bar should raise some holy hell about this. We know that there is clear fraud when a guy really falsifies records or doesn't state the things he should state or hides the records. It is quite another thing to say that I think this idea is obvious and you say it isn't. I should not be accused of fraud because of an opinion. As boss of my own small company and as an employee of Control Data, I always felt that we should write only such claims as we could sustain later in court. And I don't believe that one should cite every pertinent case because this may be silly.

For example, consider the watch regulator on which I have a dozen patents. After the first case we never had to cite any other references, because the record was pretty clear and we just applied for he

improvement patents. To repeat the same material would have been stupid. I think it's up to the attorney to decide when he should and when he shouldn't cite prior art. And I think the less the better. He should not hide a reference that he knows exists but he is under no obligation to tell the Patent Office their business, unless they ask him or unless he feels it would be helpful to bring in some remote art of which they may not be cognizant or a completely nonanalogous art which may be pertinent.

Someone raised the question that sometimes the researcher doesn't tell you, the attorney, everything he should. I can tell you as a boss of researchers that I also don't always get the information that I should. It's very hard to pull data out of my own employees. For example, I ask an engineer, what the hell is wrong with this machine? and he says I'll fix it, don't worry. I say, for God's sake will you please tell me, I'd like to know. After all I'm the boss, I'm paying you salary. And he says, you think that gives you all the rights in the world? So you think you have trouble? I can tell you that there are people who communicate and there are people who don't communicate, and sometimes you go crazy trying to figure out why. It's a basic problem of management.

Next item: I don't understand the business of citing those things which work and those things which don't work. All machines don't always work. We build reading machines at Control Data and, we may claim in the patent application for example, that this machine will read handwriting. That doesn't mean it will read everybody's handwriting. You can't do that. Usually, the writer himself can't read his own handwriting. You can only mean that there are average conditions when the machine can read handwriting, so if somebody later comes to you and says you're a liar because you claim to read handwriting and he has a case where it can't, I can only say that the facts are correct but that the conclusions are wrong.

No machine that cuts grass cuts all grass, or always will cut the same grass. It may be dull or the grass may be too low or too wet or God knows what. So if I were patenting a grass cutter, I'd be damned if I'd say that this grass cutter works 70 percent of the time and doesn't work 30 percent of the time. You have to draw a line someplace, and I don't think I'm under an obligation to say that I have ten experiments which work and five which didn't work. If the ten work you've got an invention. I think that the only time you should cite a failure is when it is very, very pertinent, when it illustrates something about the invention which is not obvious and when you would like to cite this failure. Suppose you have a chemical that kills germs all the time but one time



you missed a germ and the germ didn't get killed. Why should you cite that failure? That germ might be a special breed. If a car runs, do you have to say that sometimes it stalls?

I think it's time that the patent attorneys and the Patent Office should stop playing games. I think that you should tell them what you've invented and as briefly as possible. I think it's your duty not to write long claims and not to write 22 claims for an invention that really deserves two claims. I have known attorneys who are very proud of the fact that they had written 23 claims on a can opener. I think it's time to cut that trash out. The examiner gets properly mad when he sees this and the judge will get properly mad. I have 200 U.S. patents, the reason I know this is that my wife promised me a big cocktail party and last month I got my 200th—and this gives me the right to write my own disclosures and sometimes the claims. Like you, I use the word "means" all the time. I tried not to, it didn't work, everytime I try to write a claim in plain English, it comes out in the same God-damn language. If I had invented the telephone, I would have written means to send telephone messages by wire, period. I don't agree with the Patent Office and the Supreme Court about the prohibition of the single means claim. I'd like to invent something that could be described by a single means claim. I think I could get it allowed.

I think that *ex parte* opposition proceedings probably could eliminate many problems of so-called fraud. I always believed that after the patent is issued and before it becomes final everybody should have their say for six months or a year. This would eliminate the patenting of obvious things where the references were lost or missing. On the other hand, I don't believe the Patent Office should ever have the right to negate a patent when it's issued after this period. Let the courts do this. The idea of going into business and spending \$400,000 on an invention and then having the Patent Office decide that I don't have a patent (ten years after I got it ) would be too tragic. Let the guy who wants to say that I didn't get the patent fairly take me to court. I think there's much too much at stake after going into production, developing a lot of related art and opening a market for anything but a careful court review of the patent. I don't think it is fair for someone to wait ten years till the art and market are developed and then slug me with prior art that he had all the time. I think that either he should speak early or go to court and prove that I perpetrated a fraud.

I believe in *ex parte* opposition because I don't believe it's possible, much as I would like to see it, for the Patent Office to be so good that they can really find all of the art without outside help. I think the

Patent Office cannot be expected today to make a perfect search. The arts are too difficult, too subtle and the patents and publications are too numerous—so opposition proceedings would help and I think attorneys should help in every way they can.

I think that the present trend to do computer searching of patents could lead to a disaster for the American economy, or the world. If the Patent Office uses a computer to find pertinent patents and I use the same program to find the same patents, then nobody can accuse me of fraud, because both the Office and I will miss the same pertinent patents. One thing is sure about computer searching, an important patent is a difficult patent. If it is a simple invention you don't need a computer, you can go directly to the class and subclass and pick it up immediately. The first time I went to the Patent Office the examiner didn't even look into his "shoe." He simply reached in and said, like this? In the case of my particle clutch, the most pertinent art was in "coherers" and no computer would look in coherers for clutches. Neither did the examiner. But a friend who has read the article in the *Post* told him where to look; this kind of search will never be done by a computer. The Patent Office has spent considerable money on computer searching. I've opposed this before three committees.

I also don't believe for a moment that 30 percent of the patents are missing from the files. That's a million patents out of a file of three million. There are patents missing but I don't remember the figure. I don't know who steals them, apparently the searchers take them home or something. I just don't understand it. Well, against that I guess they'll set up a microfile system and a good bookkeeping system. This is where a computer could help. You could push a button and the computer would produce for you every patent that's mentioned in a particular reference. You could also update the records every week so that every week you have a complete file. Computers can print patent copies when you want them. But searching? Let it be done by intelligent people like the people in this room. Attorneys and examiners argue about subtle things that nobody in the world can resolve. And yet some people want a computer to do this, to settle what is old, what is new, what is obvious, what is not obvious. I hope the Patent Office drops most of this effort and uses the money for more intelligent examiners, which is the essence of the business.

After 200 patents and about 1,500 inventions, I do not know what an invention is. I mean I received patents for stuff that I would not allow, and I didn't get patents for stuff that I thought was brilliant. I think that the problems you raised are basically insoluble. One cannot ever

say that withholding information is a fraud unless he can prove by factual evidence that you had the information and deliberately withheld it. And I don't understand how any court could hold you responsible for not saying something unless somebody proved you did it knowingly and deliberately. I wouldn't worry about it. And I do tell my attorney to tell the examiner everything we can to help him. But I'll be damned if I'm going to do his job for him completely. I think they have to do something too. That's all I'm going to say.

MODERATOR NEUHAUSER: Thanks, Jack, and I'm sure you will agree that you were entertained in the last 20 minutes. I would like to comment on one thing before we get to your questions on Jack's statement, namely, an impression that at least a number of attorneys put in claims that are deliberately broader than they are entitled to. In fact, something that would read on art that they know of. You may want to make some comments about this. It ought to be extremely rare among attorneys for two reasons: one, I don't know how you can have the inventor make the oath if you put in a claim that it is not really his invention and you know it; two, I see no advantage to you in putting in a claim that you know you are going to have to amend or cancel later giving yourself a nice case of built-in file wrapper estoppel. My own personal practice for years has been to ask for as much as I thought I was entitled to. Admittedly I might later have to amend if the examiner is tougher than I am. My first claims are those I would argue through at least one response to the Patent Office if the examiner finds no better art than I knew about at the time I wrote the case.

MR. RABINOW: Let me ask the audience. Has anybody in this audience—you don't have to give your name—ever claimed more than he really thought he could get? A little broader coverage than he thought he could get? You mean none of you have ever asked for claims you knew you couldn't get? None of you ever did that?

MR. LEYDIG: That's an old wives' tale, Jack. It makes no sense to assert claims which you know are met by the prior art.

MR. RABINOW: Alright. All I can tell you is that without any doubt, attorneys working for big companies are more sophisticated than many of the private attorneys. A lot of attorneys tell me they do this.

MR. LEYDIG: Jack, in the same sense that a good attorney—and most of them are good attorneys—wouldn't do that, he wouldn't hold back a close piece of prior art. He knows very well that if he does so he has done his client and the patent a great disservice. That is something I haven't seen one court recognize—nor has it been discussed today.

MR. RABINOW: I agree with you. A good attorney simply cannot do

this because it's a waste of time and it doesn't help. In fact, the attorneys who do this, do this partly to please the customer. Also, I think it's different if an attorney is working for a large corporation and knows that he often has to end up in court. In the big leagues you don't hurt the quarterback if you can avoid it because you're going to get your ribs broken in the next play. So if you play big games you know that you need good, tight patent claims because you're going to be slapped down if you don't get them. But attorneys working for individuals often do claim more than they should to please the clients and then they settle for limited claims and I think they and the Patent Office understand each other. All I can tell you is that this group is not too representative of the patent bar of the United States.

MR. BISSON: There is one thing that happens and that is that you can claim more than you know the examiner will allow or than the Board will allow but you know that the court will give it to you. Along with the give and take that occurs in prosecution, you frequently decide that the invention isn't worth going to court so you settle for something less than what you feel the inventor is entitled to. I think this is done frequently in chemical cases, because there's a lot of argument as to how much you're entitled to claim under Section 112. You have to go to the court if you go past a certain point.

MR. RABINOW: Pat, when you were an examiner did you ever get claims that you thought the attorney knew he could not get?

MR. FEDERICO: Yes, one I remember clearly.

MR. RABINOW: He knew that you knew, didn't he?

MR. FEDERICO: And I knew that the attorney knew it. But I couldn't do anything about it.

MR. RABINOW: That's right. This is very interesting. You guys say you never did it, but here's an examiner who says he knew it, the attorney knew it and there was nothing subtle about this, right? He just claimed more and you cut him back and nothing ever happened. You just cut him back to where he should have been in the first place.

MODERATOR NEUHAUSER: Let me say, Jack, I don't want to insult anybody, but he wasn't a wise attorney when he did this. In the observation I made before he's dealing in trouble.

MR. RABINOW: There's no doubt about it, there's stupidity on both sides.

MR. JOHNSTON: I think that in many cases, and especially for small firms or individual inventors who are one-time clients, the attorney at the time he writes the case doesn't know the art. So he claims what he

can perceive in the disclosure, and it may be way off base as compared with what is actually needed.

MR. RABINOW: And you think it'll come out in the wash?

MR. JOHNSTON: You hope so.

MR. RABINOW: In this connection, just let me add one more item—I lectured at Berkeley last month and inventors from all over the San Francisco area came to see me. One man had an invention. He showed me the cover of his folder and says, would you like to criticize what is in the folder. So I read the cover and it said, “A Device to Guide You When You Drive a Car.” I said, I know what you did and what is in the folder. And he said, do you read minds? And I said yes, in my spare time. I said you obviously use a strip chart of some kind, it's moved by a speedometer or by hand so as you come to each check-point you'll know where to go next. He said, how did you know? I said, because I thought of it also, and there is a whole subclass of strip charts to tell you where to look next. And when I opened the folder, sure enough that was it.

The attorney in San Francisco told him to file it without making a search. I said what the hell was that done for? What did you pay him? He said, about \$600 or \$800 so far. I said did you have the first action? He said, not yet and I said you'll get it. The funny thing is that the attorney knew, or he should have known, that he should make a search. This idea is very old, as you know. The attorney should have known that this was old. He had put in all the claims as if it were a brand new idea. The attorney of course knows he's not going to get by the Patent Office so he figures why make a search? Let them reject it. In the meantime he'll get his first money.

ANON: He knew when he told the attorney.

MR. RABINOW: It doesn't make any difference. I don't give a damn what he told the attorney.

ANON: What if he told the attorney, you file, I don't care, I want it filed. No search.

MR. RABINOW: I think the attorney still shouldn't have done it.

MR. LEYDIG: Maybe the attorney didn't know—an attorney doesn't necessarily know all of the art. For example, I didn't know what you just told me.

MR. RABINOW: But you would have made a search.

MR. LEYDIG: Yes. But that's not the same point that I'm making. It's the same concept that results in a lot of these fraud decisions. This idea of assuming that somebody knew something. The true elements of fraud are a lot different from what a number of courts are now calling fraud on the Patent Office.

MR. RABINOW: I agree.

MODERATOR NEUHAUSER: Let me add one thing. Going back a number of years I remember an inventor coming in with a thing having to do with a weather strip and I said you ought to have a search made before you have an application written and he said I've been 40 years in the weather strip art and there's nothing like this. I wrote his application and the first action came back and it was an almost cold reference. In 40 years nobody had ever used this weather strip, but there it was patented.

Let us turn to our last energizer. This is Al Johnston. Al is a former president of the New York Patent Law Association and as you've observed already today, a real thinker about the patent system. From Dr. Harris's standpoint he is a strong supporter of this Institute and I know at least once before a Clinic participant and one who knows whereof he speaks where litigation and a lot of other things are concerned, including problems created by fraud, or maybe I should say the charges of fraud, and hopefully how to avoid them.

#### ALBERT C. JOHNSTON

I don't know about the x minutes; I hope they aren't too long! And I'm afraid I don't have many very helpful comments on how to avoid *the charges* of fraud. Maybe if I go back into some of the background and what I conceive is happening in the litigation arena today you will understand a little more why I make that general conclusion.

The ABA committee that has to do with this problem, in its report of this current year, stated as the view of the majority of the committee that the wave of decisions denying relief to patent owners and granting sanctions to reputed infringers as a consequence of improper Patent Office negotiations has come about from "a growing failure of patent solicitors to recognize their own professional responsibilities, both to their clients and to the Patent Office," and not from a failure of proper guidelines. In the view of the author of that report, a rigid application of the Code of Professional Responsibility of the American Bar Association would obviate the need for specific guidelines of the type recently

proposed. This is, I believe, something of the nature of what Jack was suggesting in his comments.

I feel that this is expressing an ideal that is rather wishful. It implies that the problem could be avoided if only patent solicitors would recognize their responsibilities to their clients and the Patent Office. But I think it isn't nearly so simple in many a situation. The courts, by their decisions in this whole area, have "added the fuel of interest to the fire of genius" as it relates to parties sued for patent infringement. They now have a tremendous interest in raising and litigating issues that have to do with bad faith and fraud. And patent solicitors, in my judgment, no matter how faithfully they try to abide by their ethical responsibilities, will in many cases overstate or misstate or fail to mention facts that, under the scrutiny given to them in litigation, will make the resulting patent at least open to the charge of fraud even if it isn't dangerously vulnerable to a finding of fraud.

Going back historically, in the days before I got into practice, fraud charges were not made in patent litigation, or when made they were typically thrown out; only the government could attack a patent for fraud. Then came *Keystone* and *Precision Instruments* and *Hazel-Atlas*. They changed the ground rules and let you bring in the defense of fraud and, more significantly on the litigation side of many situations, such a charge could now be a very potent factor if you had concerted conduct by a combination or a conspiracy involved in the patentee's action. Not yet was fraud per se an element of antitrust violation, but this came to be the rule as a result of the *Walker Process* case in 1965. *Walker Process* says, as I'm sure you all know, that proof of willful and intentional fraud, not merely so-called technical fraud such as what we've been concerned about here, where there wasn't any intent to be fraudulent; will constitute an unlawful attempt to monopolize under Section 2 of the Sherman Act if it is accompanied by sufficient monopoly power in the patent that resulted. So you have the two elements of monopoly power and intentional fraud. But even before *Walker Process*, in view of changes in the Patent Act that had developed, the roots of trouble existed in a fraud charge leveled against the patentee due to the provision for the award of attorney fees in exceptional cases.

I believe that the fraud charge is asserted frequently in patent litigation because its thrust goes not merely to the issue of validity but, more deeply, to put the patentee in a defensive posture and gain the effect that evidence of careless or inequitable conduct can have upon

the tribunal, at the same time enabling hope that it will support a claim for attorney's fees. Thus, the defendant may not only get rid of the patent but may also get himself recompense for having fought the case. *Walker Process* then came along and made the penalty of a wrongdoing patentee possibly a lot bigger. Treble damages became a prospect—and these might even be treble the attorneys' fees incurred in fighting the patent, under the conspiracy doctrine of *Dairy Foods* and some other cases, if that doctrine should be considered applicable. So now we have a large potential reward for the defendant who can prove both the requisite intentional fraud and the requisite market domination power. To pursue this reward becomes even a duty of defense counsel in a suit where his client is in competition with the plaintiff.

A possibly important outgrowth of *Walker Process* arises in a case between two competitors where the plaintiff not only has a United States patent but also has a foreign patent, as is often the case nowadays. I have seen no statistics on the subject, but it is not far-fetched to suppose that many of the foreign patents secured by American companies are secured under false representations of fact—made not under oath but by signing documents which state, in effect, that the invention wasn't in prior use anywhere in the world. An offshoot of *Walker Process* is that in litigations in this country antitrust liability is being asserted on the ground that the plaintiff fraudulently secured foreign patents which it utilized as an obstacle to international commerce in the subject matter of the American patents involved in the litigation.

One of the remarkable aspects of this whole situation of fraud charges is that the party who has made them and failed to sustain them has not, to my knowledge, thereby incurred any penalty. He can't even be assessed attorney fees if he brings insubstantial charges under the antitrust law. Whether he may be assessed fees under Section 285 of the Patent Act for having brought unsupported fraud charges has not been determined so far as I know. I don't recall seeing a case where attorney fees have been assessed on this ground. Thus, the party who claims fraud as the basis for influencing the judgment or as the basis for collecting attorney fees under Section 285 isn't likely to be penalized or assessed attorney fees. The result is that charges of misrepresentation to the Patent Office are commonly made in the defendant's pleading among the usual "boiler-plate" defenses asserted in answer to the complaint. And, even where the defendant's attorney is too conscientious to make an uninvestigated fraud charge, he will as one of his first



duties inspect every word in the file wrapper of the patent; and if he finds any statement in it that doesn't jibe with what he has learned to be the background of the case, or the actual facts, then he will make the charge of misrepresentation as a defense in the litigation. He probably has an obligation to do this.

One of the results is that the whole kit and caboodle of preparing for trial of patent litigation is getting to be outrageously protracted and costly, and outrageously unpredictable as to what the end result will be. And then, at the trial, you have a tremendous complication where the fraud charge gets into the evidence—especially because it reaches beyond just the question of patent validity into the issue of attorney fees, and maybe even to a question of treble damages under an antitrust claim. And bear in mind how difficult this problem can be if, as is occurring more and more, the party who levies the charge demands a jury trial. If there's any apparent merit in the evidence of misrepresentation it can be a potent factor influencing the judgment of the court or the jury on the more clearly substantive issues of validity or infringement. While most judges are reluctant to brand a litigant or his patent solicitor as one who perpetrated a fraud, a court will often consider evidence of concealment or trickery as an element inducing adverse findings that have less of a flavor of moral turpitude.

As an example of this last-mentioned effect: A suit some years ago involved a patent containing a table of test data which the solicitor had put into the specification. The data had been concocted, in that they didn't represent actual tests, and there was an error in them from which it could be deduced that they were not real. As I remember the situation, if there had been actual tests and they had been properly delineated, the point of the representation might have been established. At trial, the inventor on the witness stand was asked about the tests—did he perform those tests? The answer was no. Did they truthfully represent actual test conditions? The answer was hedged. Then, in an electrical moment of the trial, the judge turned to the witness and said, "Mr. X, isn't a person who applies for a patent supposed to tell the truth to the Patent Office?" The courtroom was quiet for an embarrassingly long time; you could feel the impact. In the decision which resulted, the court did not hold fraud. There were some other aspects of misrepresentation which in my judgment were more important to the patent. The judge did not find fraud; but he did find all the facts necessary to hold the patent invalid. And he did make a comment about the testimony of the inventor, based upon the incident,

which left little prospect of the Court of Appeals giving weight to the inventor's testimony.

Few litigants have actually collected damages under the *Walker Process* doctrine. I'm not aware of any case as yet where there has actually been an award of treble damages for fraud in patent procurement. But there are more and more cases where fraud becomes an element in what is charged to be a scheme or a conspiracy, thus giving it more danger and strength as an antitrust charge. It seems to me, as a general observation, that the prospective gains for a litigant to bring fraud charges are too many and too great, and the penalties for bringing them when they're brought without good cause are too few.

I submit that it is often more difficult for the patent solicitor to be "lily white" in all that he says than it is for the litigating party. What the solicitor said is viewed in retrospect with the benefit of discovery that has been explored through his client's files, and with the aid of advocacy spurred by a strong interest in making what he said be significant. Yet the solicitor has had a maze of negative conclusions to establish in his handling of the patent application—and, typically, a limited amount of time and a limited willingness of his client to explore all the masses of information that could bear upon the validity of these conclusions. I submit that no patent lawyer and no inventor ever knows all that is in the prior art; you can never know that there isn't something that you didn't find. So a patent is never perfectly protected against prior art until after it's been litigated beyond the last court. Or, it has expired.

A question was raised earlier today about filing a patent application for an invention represented by five examples that don't work and ten that do. It was suggested that all 15 examples be stated, maybe with some kind of explanation about the five. My judgment in that situation would be not to file the case until I knew the explanation. If the invention were a process or a composition that embraced the examples which didn't work, I surely wouldn't file a patent application showing inoperative examples. The inventor should be advised to go back and find out why five examples didn't work. Then the explanation might be made a part of the claim, to distinguish the ten working examples from the other five; or it might be that the five were erratic test work and that the records would show the error in them—in which case, the inventor ought to re-do the tests and then base his application on re-done tests that weren't erratic. If the application is filed with the five bad examples and the ten good ones and the solicitor tries to give the Patent Office an explanation of what happened, it seems to me that by

doing this he simply opens up more avenues for possible attack upon what he urged in the file of the patent. It is a rare person indeed who can take complicated documents having to do with complicated test work, write explanations *ex parte* under no stress of controversy, and not say something that isn't demonstrably too general or inaccurate or untrue. The facts some years later are what a court finds from what witnesses have said they were; and this is not necessarily at all what the solicitor believed they were!

I have much the same view in regard to bringing evidence on a question of prior use into a patent application for determination of that question by a patent examiner. This in my view cannot be done either safely nor soundly. I think you have to decide at your own risk: Was it a prior use or not? Was it experimental or not? I would make a record of all the evidence available and of how it led to the conclusions reached, and then would stand on that record. I think it is sheer wishfulness to submit that kind of issue to the examiner, for several reasons. One is the examiner isn't qualified to weigh the kind of evidence usually involved. Another is that most of the issues of prior use, particularly if they involve the problem of experimental versus public use, will hang on oral testimony. You're not likely even to reach all the witness. Furthermore, what the witnesses you do reach may say on the subject when interviewed in your office may be quite different from what they will testify when examined in the courtroom. I think you're only generating more problems and more areas for discovery in the course of litigation when you undertake submitting detailed evidence on a close question of prior use for consideration by the examiner. To do this seems to me to be utterly impracticable until a system is established to enable that type of determination with some continuing legal effect. Until then, all you're doing is setting up more representations, or even straw men, that may be knocked down in litigation; and they're certainly going to be explored from A to Z.

It seems to me that all the representations put before the Patent Office in a patent application will be considered self-serving and that the more one puts in the more trouble he may cause for the inventor. What was in the solicitor's mind at the time he stated something in the record of the application is a very difficult thing to know or prove. These are areas where the law still is that there's a burden on the defendant. The defendant of course goes back and collects all the records, and maybe finds some documents that nobody had in mind at the time the application was filed. Some of these documents may even be disastrous to the patent. If then it comes to the question of fraud,

you have either to get out of the law suit or to go into the courtroom and tell the judge or the jury that there was an honest mistake, requiring the defendant to prove otherwise. The outcome of this depends upon your witnesses. It simply is not feasible to anticipate all the possible problems and write statements about them to the Patent Office, where what the facts are depends upon what the witnesses will say.

It's a legitimate question to ask, why is there a double standard of consequences as to what a lawyer says about his client's case—the rigid standard as it relates to what you say in the Patent Office—and the relatively loose standard as to what defense counsel can say in the courtroom? The answer, of course, has its roots in what the Supreme Court has called “federal patent policy.” The patent applicant and his solicitor are seeking a monopoly over the public's use of something which, at the time the issue is before the court, is seemingly in the public domain. The declared public policy frowns severely, and penalizes, unless the patent really is “lily white.” That is the current state of affairs. The infringement defendant's lawyer, trying to win his client's case, seems to be fighting on the side of the free competition that the courts favor; this role, of course, he uses to the hilt.

While this may explain the difference, I don't think it quite justifies it. Isn't it true that the constitutional patent system has a broad public purpose too? If the products of this system are going to be stricken down as though it's unlawful to enforce them, or penalized severely, because something untrue was said at the Patent Office, doesn't the whole system become unwieldy and distorted? Where an untruth said at the Patent Office is, in fact, on a matter critical to patentability, why can't proof of that matter suffice to dispose of the validity issue? And where an utterance to the Patent Office is not of that critical nature, why should its occurrence distort so heavily as it often does today the validity or enforceability of the patent? Why should the fate of a public grant and of extremely costly discovery and trial proceedings on all the many issues in a patent litigation hang so heavily as it does today on the largely unpredictable effect to be given to something said or not said in the file of the patent? A poor witness on such a touchy issue as fraud can have tremendously destructive effects.

Can't we devise a system that suitably penalizes culpability where there is culpable falsification? And let the evidence on patentability govern validity without having the roots of the patent system get chopped up in the present overly defendant-oriented litigation situa-

tion? I think that such a system can be devised but I don't pretend to have the answer at this time.

MODERATOR NEUHAUSER: I suppose all of you are going to answer the questions. He finished that with about three or four questions and I'm sure you're going to answer them.

DIRECTOR HARRIS: Al, coming back to the present from what you hope might be accomplished in the future. You talked about the problems that can arise from a charge of fraud, including the problems of a counterclaim. Isn't there a unique kind of problem involved? If a defendant raises a charge of fraud and he subsequently wishes to settle, can he? Once having charged fraud do you not raise a serious question affecting public policy? Can you walk away from such a serious charge in order to mitigate your litigation expenses, and agree to settle for a nominal sum?

MR. JOHNSTON: That's a good question. Of course you're raising the question of whether or not there might be culpability or vulnerability to the charge of conspiracy in violation of the antitrust laws for having covered up a fraud.

DIRECTOR HARRIS: It seems to me a defendant has to think very carefully before he raises the question of fraud, particularly if he contemplates settlement.

MR. JOHNSTON: I think that that's a pertinent question, but on the other hand, I believe there are ways of settling these matters that do not involve any conspiratorial situation necessarily rendering the party vulnerable. Therefore, and as long as there are such ways, the possibility of some ensuing antitrust complication coming from the settlement isn't going to deter defense counsel from charging fraud. He's got to, really, if you take the view that a litigating lawyer has the duty to raise the points that he believes can support his client's cause—more or less the traditional notion of how the defense lawyer in a criminal case is supposed to comport himself. It seems to me he has to raise the issues unless he has concrete reason to believe that they shouldn't be raised. Certainly if he has plausible reason for raising them, they must be raised.

DIRECTOR HARRIS: I agree with you that he has to raise them, but I also think that once having raised the issue he has to be very careful about what he does subsequently.

MR. JOHNSTON: Well, certainly if you're talking about swapping licenses and that sort of thing you're absolutely right.

DIRECTOR HARRIS: If he introduces this issue into the litigation he's committed himself. I think he'd better go ahead with it. If he then indulges in certain other alternatives, I think he has a serious problem.

MR. JOHNSTON: Right. It works if his position is, I'm going to fight this plaintiff and fight this patent and I will settle for nothing less than a covenant not to sue or complete dismissal. He can do this.

MODERATOR NEUHAUSER: You are aware, and I suppose that's what you had in mind, that on a number of occasions, at least in speeches, the Department of Justice people have stated that you may not be able to settle; I don't know that they've ever taken any specification.

MR. JOHNSTON: My own view is that that situation only obtains if the settlement has resulted in a favorable position of these two parties and there is something to support the view that it was conspiratorial.

MR. DAY: I want to ask Mr. Johnston if he would agree that there is one little area of possible comfort here. If you have a case where validity in the ordinary sense is pretty clear, and the infringement is pretty clear, and the defendant as sometimes happens takes a potshot of ten fraud charges, and the court finds that none of them have merit, don't you have a pretty good case for either attorney's fees or punitive damages for the plaintiff just as in the case of other sham defenses?

MR. JOHNSTON: I think so, yes, but I don't think that those cases occur—but if it did occur, yes.

MODERATOR NEUHAUSER: In the back.

MR. STERNBERG: I was going to say if we turned the clock back to 1830 this situation wouldn't exist. Because at that time the Supreme Court's viewpoint on patents was that these things were designed to give the public the benefit of technologies that they didn't have before. There was a big point made of this by the Court in many cases, including the first reissue case which really preceded the 1870 act, where the Court said that this was a public policy, that somebody had pleaded a defective patent and he should be entitled to correct it and he should be entitled to enforce it. And yet we come around to 130 years later, after the antitrust law had been enacted, and the public policy on patents had completely changed in the opposite direction because the antitrust laws are now considered to have supremacy over the patent laws. I mean the philosophy of patents is, I think, changed to that extent that the courts are no longer willing to look at it from the standpoint of 130 years ago.

MR. JOHNSTON: I don't anticipate that we can in any respect turn back the clock, but I do feel that we need to look at the problem of litigation today with a very broad view of the inequity in it. I think in the fraud area we need to realize that since this is a charge essentially of fraud in procurement of a patent, which can't have real merit unless as a result of it the patent is issued when it would not otherwise have been issued, the question of fraud or not ought to go back for determination by a tribunal that has to do with patent law. I have the view which I have expressed to other groups that we need to give very serious consideration to changing the system of patent enforcement by establishing a patent court that will handle the validity issues of the patent litigation, if not the issues that have to do with infringement and misuse as validity issues,\* I would include issues having to do with questions of fraud on the Patent Office.

MR. FEDERICO: I promised Al that I would mention a suggestion, I may be a little bit naive but the problem he's been discussing is something that's been worrying me for some time because I've run into several situations where the defendant lawyer raised charges of fraud in situations that were so outrageously unfounded that I had the feeling something ought to be done. Now we do need a few decisions of the courts imposing some safeguards, such as assessing attorney's fees investigating the defense lawyers, and things like that; we don't have them yet and I doubt very much that there's much chance of getting them, or getting enough to do any good. Somebody in a meeting yesterday said that in half the patent suits filed, the defendant raises the question of fraud—he just throws it in, regardless. He was speaking figuratively, of course, but picking the 50 percent anyway, there are about 600 or more patent suits filed every year. So that means three hundred or more defense lawyers throw in charges of fraud when the majority of them haven't the slightest idea of whether there ever is any fraud there or not.

MR. JOHNSTON: Well Pat, I think that the practice in that regard with a lot of lawyers is that they just file a pro forma answer, and they include a fraud charge along with the usual defenses of alleged anticipation, without detailing it in any respect.

MR. FEDERICO: Right. And as you brought out there ought to be some obligations worked out the other way. Well my suggestion amounts to

---

\**Editor's Note:* Also see L. James Harris, "A Dual Patent Program: To Increase Patent Reliability and Decrease Litigation Costs," *IDEA*, Vol. 13, No. 1 (Spring 1969), p. 1; and *IDEA*, Vol. 13, Conference No. 1969, pp. 51-59, 93-94.

this: We have in the pending bill as it now stands in Section 192 something that's been changed from the original presentation and that is now a straightforward outright, revocation proceeding. At any time within one year after issuance of the patent any person may initiate proceedings on the grounds of public use, prior invention and obtaining the invention from somebody else. An *inter partes* proceeding is set up, as a result of which a decision by the Patent Office rejecting claims would be a revocation of the claims, a cancellation of the claims. The decision would be reviewable by the courts.

Now there is a gap in our law—there is no provision for revoking an invalid patent. This proposal is partial, it only relates to public use and prior inventorship. Why not go the whole hog and include all grounds and have this *inter partes* case of revoking claims, or cancelling claims of the patent during the first year, as it is here in the bill. But my suggestion on this point is a little different; in an infringement suit where the defendant raises the question of validity on any basis, which would include fraud, and references or what not, the court should be given the authority to require the defendant to initiate a proceeding in the Patent Office which would be provided for as an extra paragraph on this 192 section within a certain time limit. And the Patent Office would make a ruling on validity, fraud, etc. with teeth in it; it would be rejecting claims, holding them invalid, or what not; they would decide whether the failure to call references to the attention of the Office would have changed the picture.

MR. JOHNSTON: Pat, isn't that the German system essentially?

MR. FEDERICO: Not entirely. The court would have the authority to order the defendant to file such a proceeding, to initiate it, within a time limit; if the defendant did not do so within the time limit, the matter of validity would be out of the case. If the defendant started the proceeding, the decision of the Patent Office revoking certain claims or refusing to do so would be reviewable by the court having the infringement suit. There would have to be a petition for review of the Patent Office decision. I am not suggesting an advisory opinion but a decision holding certain claims are to be cancelled which would become effective if not brought up for review and if not reversed on review. If there is an adverse decision against the claims and the patentee does not petition for review, the case is over and the claims are out of the picture. When the case does go back to the court, the court would review the validity issues if brought up in connection with its consideration of the other issues; the court's decision then on the validity of those claims would be a revocation of those claims. This procedure



would have various effects but I mention it here as a suggestion on the problem of raising these unfounded defenses of fraud. These could all be sent back to the Patent Office to rule on.

The German system is different. They separate validity from infringement. If an infringement suit is filed, the court does not consider validity; it goes ahead and holds the patent infringed, if it is infringed according to their system of interpreting claims. If a defendant wants to challenge validity he files a separate suit in a separate court, formerly located in the Patent Office. The two suits have nothing at all to do with each other. The infringement court will not suspend action on the infringement suit unless there is a motion for cause with a good showing of probable success in the revocation suit. The infringement suit could go on to judgment, collection of damages, etc., without regard to validity, so the two are completely separated.

ALLAN R. REDROW: In connection with this fraud on the Patent Office business, we've talked a lot about what we should be doing but has anybody had occasion to call upon the examiner to say whether he was defrauded? I think there's been one case where the examiner was deposed, but what thought has been given to going to the Patent Office and getting them to say whether or not they were defrauded in this particular situation?

MR. FEDERICO: The usual cases are concerned with things that happened years ago when there was a big turnover among the examiners; an examiner might not be around or not remember anything at all about that case.

MODERATOR NEUHAUSER: There have been a couple of cases in Judge Lewis' court, though, in Northern Virginia, which, I think for the first time except for the tetracycline case, have brought the examiner in to testify. The Patent Office has successfully opposed over the years on various grounds, bringing the patent examiner in to testify in the court in the District of Columbia, but now they are in Arlington. Judge Lewis has held that the patent examiner could be examined, but I think he was examined only, if I recall the limitation, as to the facts, not as to his opinion.

MODERATOR NEUHAUSER: Any other questions?

MR. BISSON: Going back to one of your previous remarks. *In Magnetics* and *Chemical*, I think you said there was a table of data which had not actually been obtained. I'm in chemical practice and this has been done frequently and is probably still being done today. You run into the problem where the inventor says, "I know if you do this, you'll get this result, and it'll cost you \$50,000 to run the experiments to prove

it." So instead of running the experiments you file a patent with a paper example. What are your thoughts on this practice?

MR. JOHNSTON: Well, I think you're running the risk of exactly the same thing happening that happened in that litigation. The inventor is bound to be deposed. In that particular case, the inventor was deposed for two or three weeks before the trial and all his admissions concerning the data table were part of the deposition record; so when he was put up as a witness in the courtroom he didn't have any option—he had to admit that the data weren't real and it had a catastrophic effect on the case in that trial. Now, what to do; you don't concoct a table; you make a statement, but make it factual, that upon the basis of experience with actual examples it is evident that such and such would occur under some other conditions. This expresses a conclusion and not a test.

MR. BISSON: What would a patent examiner do when presented with an application in which it is clear that no actual example was run; it was just the inventor's opinion that such and such a chemical will be obtained if you do such and such?

MR. FEDERICO: There is absolutely nothing in the statute that requires these things to have been done in order to get a patent. Patents could be obtained on paper. They may be looked upon strictly, you might say, but that's as far as the law is concerned. An examiner might be rather skeptical and try to find flaws in the case, but if he can't why it just goes on.

MR. JOHNSTON: It seems to me a lot of these problems come down to the question of whether you are really telling the truth or whether you're trying to turn the truth, and the minute you try to turn it a little bit you generate a potential fraud charge. And even if it isn't a fraud case it may be a case where the court could be convinced that there was some bad faith representation and, therefore, you may get stuck almost as badly as if he found fraud.

MODERATOR NEUHAUSER: I don't want to inhibit this cross-conversation here because I think that's where you get some of the best points brought out, but try to remember as you interject yourself to give your name or the person transcribing this is going to be completely confused and you may get credit for lines you do or do not want.

MR. TAYLOR: Now a question with regard to references cited by a German examiner. If the U.S.-only solicitor has a number of cases all filed by somebody else in various countries, who is relatively unconnected and even in a different city, are you working up to saying that it would really be highly advisable for him to set up a system of obtaining and considering those references in order to discover any bad one?

MR. FEDERICO: If I might interject a fact on that last question, in connection with references cited by the German examiners. You know that we have a system of exchanging references that's been in operation for four or five years. In connection with U.S.-origin cases filed in Germany, the German office sends the U.S. Patent Office a certain sheet with identifying data of the two applications. For German cases filed in the U.S. the U.S. Office sends back to the German office a standard printed form identifying the cases. Then when the U.S. examiner has made a search the references he cites are entered on the sheet and it is returned to the German office. In the German office, when their examiners have made the search the references they cite are listed on the sheet and returned to the U.S. office. That has been going on for four or five years but of course with the new German system of deferred examination those reports do not come in on the majority of cases any more or the search might be too late.

MR. TAYLOR: Does that ever get into the U.S. file—the German search?

MR. FEDERICO: The sheet with the references listed is filed somewhere. I doubt that it is filed in the application file. Copies of the references are made and sent to the examiner so he is saved the trouble of trying to find them.

MR. ROSE: Further answering Mr. Taylor's question, if I understood it, it seems to me the question is double barreled. If you have a corresponding German or other foreign application to a U.S. application and you get references cited in that examining country, it's up to you, if they are any good or better than anything cited by the U.S. examiner and if the case is still pending in the U.S., to make those references known to the U.S. examiner. Now I think I may have gotten the tone of your question to be that if you have a whole series of cases abroad on more or less related subject matter are you supposed to examine all of those? And the answer to that would be roughly no. It would be too big a burden.

MR. TAYLOR: To comply with your first, we first have to get the references. I don't have them; somebody else has the German prosecution on their hands in another city.

MODERATOR NEUHAUSER: Judging by what I heard at lunch, particularly the large corporations have a separate foreign section, and you apparently do.

MR. TAYLOR: That's correct.

MODERATOR NEUHAUSER: I think it would be worthwhile to discuss what procedures may have been established in order to be sure that the

domestic attorney prosecuting the U.S. application is informed of any better art that comes to the attention of the attorney prosecuting the foreign application.

MR. LEYDIG: Paul, you say that when you learn about nonanticipatory prior art you have a duty to send it in. May I suggest that you darn well better—but there is no absolute duty. I think that is a large part of our problem here. We are now by the “can’t help it method” reaching a point where we are saying “we have a duty.” But I, for one, am not sure what that duty is. There’s nothing I know of, for example, that says you have a duty to cite every piece of prior art that’s cited in a foreign case. But it makes very good sense from the standpoint of the presumption and of avoiding a possible charge of fraud to do so. In answer to your other question, we deal with a British company who has subsidiaries all over the world. We have set it up so that every single reference that is cited in any country, in any equivalent case that we have, is brought to our attention. And we then bring it to the attention of the U.S. Patent Office. I agree with doing it. I am simply saying that there is possible harm and confusion in saying that you have an absolute duty and then holding back anything—even if you believe it is less pertinent.

MR. ROSE: On the question of duty, I think there’s no statutory requirement or no requirement of any rule in the Patent Office that requires you to do this. When I say you have a duty I mean that you have, let’s say, an obligation of candor generated by all these decisions that we’ve been talking about today. And in order to protect yourself or your client, you might say, you would have that sort of a duty, but not by rule or statute.

MR. LEYDIG: One thing that I don’t think we talked about, and I’ve noticed over and over again that in almost every case, *Monolith*, *Beckman*, *Monsanto*, right on down the list, when the judge gets ready to lower the boom he cites the *Precision* case which says in substance that there is a duty to bring to the attention of the Patent Office any knowledge of fraud. In the *Precision* case, it is important to keep in mind that there was an overt fraud and knowledge of such fraud that were being discussed. And, of course, one has a duty to bring fraud to the attention of the Patent Office. That has been extrapolated in *Monolith* and *Beckman*, however, to a duty to bring anything relating to patentability to the Patent Office and therein lies our problem, gentlemen. That’s why I say: why a limitation of five, why 18, why 100? If you are dealing with a product that has been the subject of laboratory testing, field testing, commercial testing, and there are literally thou-

sands of examples within a company's laboratory files of information on the utility of that particular compound, and you then get down to the point where you bring an affidavit to the Patent Office's attention—do you select or do you back up an Allied van and move it on down? Because patentees are being accused of fraud by reason of judgment calls by their attorneys—whether it be because of too few references cited or too many—I incline toward what I consider to be the lesser risk of citing too many. Obviously, one's professional judgment will dictate a cutoff at some point. I say—in view of the present climate—err on the side of possibly citing too many—be they references or examples.

MR. JOHNSTON: Actually the only authority that I can recall that talked about “uncompromising duty” is the *Beckman Instruments* in the court of appeals decision. My own view is that you cannot interpret this unqualified duty, uncompromising duty in any way that is realistic unless you say, well, he's really talking about good faith and not consciously suppressing things that are known to, or believed to have, a bearing. But if this rationale is correct, it seems to me to follow that you do not have a duty to go chasing around trying to find other pieces of paper that might be argued to be pertinent.

MODERATOR NEUHAUSER: Fred, let me add that if the pending patent bill passes in the form of the Subcommittee Print, Section 115 would require each of the attorneys who participated in preparation as prosecution to make an oath that he is aware of no prior art he reasonably believes to be more pertinent than that considered by the Patent Office and that he has made full disclosure to the Patent Office of all facts he reasonably believes pertinent to the prosecution of the case.

MR. JOHNSTON: The word is aware. And the other word is believe. Both of those words have to do with the frame of mind of the man at the time he makes the oath. It doesn't mean he has to go out looking all over the woods to try to find things that might be argued.

MR. KAIN: Concerning awareness, is a corporation “aware” of the knowledge in the minds of its agents, for example, of its international patent attorney in one city and its domestic patent attorney in another? I believe that some cautious lawyers would argue that the knowledge of both agents is imputed to the corporation. I am not concerned particularly with the provisions of the Subcommittee Print, but rather with the more general question of awareness necessary to sustain a charge of fraud.

MR. JOHNSTON: Of what is the corporation aware, is your question? What person of the corporation, is that your question?

MR. KAIN: My question is this. In the fraud on the Patent Office context, is the large corporation that we have spoken of, having an international patent attorney in one city and a domestic patent attorney in another, charged with the knowledge of both of its agents? Turning the question around, could this corporation defeat a charge of fraud in the procurement of its U.S. patent by arguing that it was "unaware" of information in the hands of its international patent attorney?

MR. JOHNSTON: I think I'll try to answer by saying that I believe most of the situations involve the awareness of the persons who were active in the patent application, namely the inventor and the attorney, and the question of corporate awareness as such gets into the act only to the extent that the evidence will create a sufficient inference that information in the possession of the corporation was also known to the persons who did the act. Incidentally, that very problem is involved in the *Acme* case in the 8th Circuit, where there was an issue of fraud and the district court held that knowledge of the matter underlying the fraud charge was not proved; but the court of appeals held to the contrary. I don't recall exactly the facts but it involved a corporation that had a related company and the inventor was in one company and the related company wasn't directly connected with him as I recall. The information was in the hands of the second company. The district court threw out the fraud charge on the grounds that it wasn't proved that there was awareness. But the court of appeals reversed on the grounds that the evidence showed sufficient knowledge and contact to generate the fact that there was awareness and required the district court to review the whole patent. So I think it comes down to the question of what did the evidence show in terms of awareness of the person who made the representation.

MR. CHEESMAN: Well, I've sort of been passed by but I wanted to comment on a comment, mainly that as I recall *Precision* did not restrict the uncompromising duty to fraud. I think it also mentions inequitable conduct or fraud. Now to me, the duty or whatever he is talking about, goes further than simple fraud. You just don't try to fit the facts into the rigid legal definition of fraud and if you don't find one element, forget it. If you've got inequitable conduct, whatever that is, you have an uncompromising duty. That's the way I read it.

MR. LEYDIG: I'm not distinguishing between the two. My point is simply this. The court was saying if you know of some improper dealings, you've got to tell about it. But that has been extrapolated to: if you know of anything that is relevant to patentability you must tell about it. That's a great difference. That's the point I'm making.

MR. CHEESMAN: I must have misunderstood your point.

MR. ROSE: The afterthought of that, though, of what Mr. Leydig says is that if *Precision* says you know of fraud you have an uncompromising duty to disclose it. On the other hand, if I know of a very pertinent reference and I don't disclose it to the Patent Office then I know that I'm committing a fraud and I've got a duty to tell the Patent Office about it, you might say. At least I should tell them about the reference, otherwise I generate a situation fraught with danger of a charge of fraud if the patent gets into litigation. Thereby evolves the duty to disclose a reference. I know that many people don't like the word "duty" but I use it not in the sense of a statutory requirement, but in the context of what the courts have demanded.

MODERATOR NEUHAUSER: I believe Mr. Johnston has to leave and I'd like to ask him a quick question. In the course of his presentation he said, if I understood correctly, that he felt you could not safely bring before the examiner the issue of prior use, that the examiner wasn't really qualified to consider it. Now what concerns me, however, as I read the case: It seems to me the courts become more concerned about something that is not brought to the attention of the Patent Office where it is something that the Patent Office would not normally be able to learn about through its own resources—as for example prior use—than they do about failure to cite a patent where presumably the Patent Office could find it. Now I find trouble if I don't bring in the prior use if it's a questionable one, at least put the facts on the Patent Office's record. I'd like to have your comments on that.

MR. JOHNSTON: I agree that it is a dilemma. You may also recall that I suggested that we need a system whereby that could be done, and have some legal effect. But the reason I feel that it isn't wise to do it is if we're thinking of a situation that requires the collection of a lot of evidence involving not only documentary things but also oral testimony as to intent. I think that the examiner isn't qualified to handle it in terms of judging evidence of that nature—number one. Number two, I feel that the situation of the litigating patent counsel trying to collect that type of evidence under a condition of *ex parte* prosecution is likely to be an imperfect job, and it's a dangerous job because of the inadequacy of his presentation. Therefore, faced with this dilemma, I would much prefer to make a record of all the evidence that I could collect at the time, have that as a record, reach a judgment based upon an objective appraisal, as objective as I could make it, and if I felt doubtful about it, consult somebody else and get an opinion, make a

record of it and then simply act in the Patent Office according to my conclusion. And this would be the way I would handle it.

MODERATOR NEUHAUSER: Thank you Al. If there are no questions I'd like to pose one that troubles me a little. The Patent Office, as I understand it, has opted for the ABA Code of Professional Responsibility. I don't know the section specifically, you probably do, but there's one in there that has troubled some lawyers in respect to the fact that if your client is doing something wrong, let's say committing a fraud, you are not only compelled to urge him not to do so and, if he insists, to withdraw from the case, but you have to tell the court about it. If your client brings some things to your attention that you think ought to go to the Patent Office at the risk of fraud and he refuses to let you do this, and you withdraw from the case, do you have to tell the Patent Office?

ANON: Let me have the floor a second, please. You make a great big issue about the difference between the *Precision* case and the *Beckman* type of case. But let's not forget, in each case there was something that the Patent Office should have known, or at least the Court thought it should have known, and there was proven in the *Precision* case and at least three-quarters proven in the *Beckman* case, a deliberate refusal, with knowledge, to give it to the Patent Office, so it just slipped aside. When you look at it that way, it doesn't matter whether it's interference, or if it's a piece of prior art you have in your hands in your ex parte.

MR. LEYDIG: I'd like to respond. I'm not really making a big difference there. What I'm trying to do, because it is essential is to make whoever is alleging fraud really prove fraud. Now, if a patent happens to be held unenforceable because of some improper dealing, such as knowledge of a piece of prior art or a prior use that nine people out of ten would say was anticipatory—and, indeed, in *Beckman* it was held to be an anticipatory reference—that's one thing. But if it's not Section 102 art, indeed not even close to being a 102 reference, although clearly pertinent, that's another thing.

Let's remember that in 1963, David Ladd as Commissioner, sought to institute a provision—Mr. Federico can correct me if I'm wrong—a provision which in effect says, if you know of any prior art, bring it to the attention of the Patent Office. Now that was put before the patent bar, there were hearings held on it, and it ultimately was dropped. It was not done. Now at that point it must be assumed, both because Ladd wanted to institute it and because it was argued down, that there was no such duty as to Section 103 references. I'm being rather technical here because once you get out of the anticipatory situation and get into



the 103 situation, it clearly becomes a question of judgment. And while in retrospect a court may say, well you darn well should have known, that may well not have been the case at the time. Destroying the presumption is one thing but calling questionable judgment of a professional “fraud” is quite another.

I’m saying that when many of the patents that are now being litigated were prosecuted, before courts were calling fraud what they are now calling fraud, the attorneys in question were doing things that at least 99 percent of them thought were ethical—even if as a matter of judgment a lot of those 99 percent would have cited the reference to protect the presumption. Now that means that in their judgment if they thought a piece of prior art should not be brought to the attention of the Patent Office because it was not anticipatory and they were foolish enough not to cite it when they knew that it would ultimately strengthen their patent if they did—that may be poor lawyer’s work but that doesn’t make it fraud. Now ten years, 15 years later, you have the situation where somebody is saying that was fraud. I submit it is not fraud. The reason I point to *Precision* is that when a court relies on *Precision* and quotes that language which says, if you know of fraud tell the Patent Office, I agree completely. But if it’s really a question of good or bad judgment, that’s something else again. Render the patent invalid if you will—under Section 102 or 103—but let’s stop calling errors in judgment fraud.

MODERATOR NEUHAUSER: The gentleman back here.

MR. STERNBERG: I just wanted to mention in connection with the *Precision* case that when they went to other counsel he advised them really that the Patent Office wouldn’t do anything about it.

MR. LEYDIG: That’s a different thing, isn’t it?

MR. STERNBERG: That’s right. In other words, they had a real problem as to what could be done to rectify the situation, and his advice was that the Patent Office wouldn’t do anything about it. And this was dropped for that reason. No one really knew what to do, how to handle it.

ANON: I’ve got a specific problem I was involved in not too long ago that touches on the edges of some of this. That is, the question of what on earth would the Patent Office do. We copied claims for interference, and then when the time came for the 204-C affidavit, as we were gathering our evidence, which we already had to some extent, but polishing it, we realized there was a way of interpreting the claims that would bring in a whole new area of art. Half of the claims, let’s say, brought in a new art area. So the question then came, well, I guess we

better run a search. So we ran a search, and, if you interpret the claims one way, as covering a particular type of operation, you then bring about half a dozen—really 102 type of references, Chinese copies we were within the response period, but we didn't even have enough time to complete the search, so what we did was refile, put in what art we had, and what we'll do is actually put in the rest of the art later. But you run into a question. You copied the claims for interference purposes. You want to maintain the interference. So what do you do? In our case, we just took and presented the art and said, we don't know; if you interpret the claims this way, this art is going to be pertinent. If you interpret them another way, it's not. And we left it there. But the Patent Office—what can they do, since the interpretation—if they take the interpretation as adverse to the patentee, they are attacking the validity of an issued patent. It's sort of a dilemma. What do you do in that nasty situation? And I think it can come up a little more.

ANON: I'm still a little bothered by Mr. Johnston's comment that if it's prior use I'm better off not to disclose it to the Patent Office. I believe that's my judgment, that it's experimental use and therefore not prior art. If there's some question there I just can't believe that I can convince the court that the Patent Office is not qualified to determine a question of this nature and therefore that's why I didn't disclose it to the Patent Office. It seems to me they are just as qualified to examine and find out whether those things were applicable as other prior art. I just find difficulty with it. I would be afraid to use that as a guide myself.

MODERATOR NEUHAUSER: I would too. I think you can have two facets to this, however. There are things which, I am sure, you have to determine in connection with filing the application in the first place as to whether something is or is not experimental use, and you make a clear determination under the law that this is experimental use. I don't know that it is necessary that you then spread it on the record and make the Patent Office go through with it. But if there was any doubt, I would personally supply the information to the Patent Office whether or not they are qualified to consider it. I'd have it on record for them to consider.

Any other questions? I'm just going to comment very briefly, not by way of summary, but touching maybe a few of the highlights and perhaps some of my own observations. I think we can probably summarize Paul Rose's approach here and, Paul, you may dispute, even interrupt if I quote you incorrectly—by saying that he would bend over backwards to disclose all noncumulative facts that could be of interest

to the Patent Office, and particularly in affidavits. He emphasized—and I think most of us, if not all of us would agree—that the standards are becoming steadily higher in terms of conduct for the Patent Office. We will not apologize for not solving the problems for you. You have still with you problems ranging from at least embarrassment all the way through potential disbarment or malpractice suits or even criminal charges; for your client, problems ranging from nonenforcement through antitrust charges and treble damages. Paul said—I think this has come out in several cases in our discussion—that what is practiced in the prior art—and particularly what was done in the public use and things of this sort as opposed to what was published in patents—is becoming increasingly important. The mechanics of bringing things to the Patent Office were discussed, including putting them into specifications or in a separate communication, preferably before the first Patent Office action, to help the Patent Office. As I understand some presentations, some attorneys would prefer to do it after the examiner has stated his art. They feel that they have a backdrop of what the examiner is proposing before they determine what they should do.

Now, I think that attorneys just have to face the problem that they are going to have to make a judgment as to what references to cite. I don't think that it gets you off the hook to put 50 references in and say, I've got everything in there now that he can possibly think of, and now I can't possibly be charged with fraud. If you miss something that somebody can bring in, you may be accused of camouflaging. You have to make a judgment, as you have done for years, in determining whether to file or not. My own view is that you have to disclose anything that you reasonably believe with good judgment might have a bearing on the examiner's conclusion as to allowability of the claim. I think, Fred, there maybe you and I depart, at least as I understand you, because I don't think this is limited to Section 102. If I find something that could be an arguable point on Section 103, and I think my invention is distinguishable, the examiner might take another position. If he has not indicated an awareness of that reference, I think I have to bring it to his attention.

MR. LEYDIG: I would agree with you 100 percent. All I'm questioning is, whether the law says you have an absolute duty and if you fail in such duty you are guilty of fraud.

MODERATOR NEUHAUSER: Well, I think that the courts say you have a requirement, duty, or obligation, or whatever you call it, of candor. Now, I understood Mr. Rabinow—between entertainment value that he

provided—wants attorneys to ask only for what they are entitled to. I think most people I'm acquainted with do this. He would have you cite only a limited number of patents. I think there my own view would be somewhat in accord. You have to make a judgment. Sometimes this may not be a limited number. Really it's a matter of judgment in the individual case. He would have attorneys quit making, if I paraphrase his statement correctly, frivolous charges of fraud, and I think this is certainly a valid observation. And he wouldn't want you to play games with the Patent Office. I have a feeling he thinks we play more games than we do.

Al Johnston commented, I think pertinently, in his remarks that the benefits to be gained from the fraud charges as far as the defendant is concerned are presently too great and the penalties for bringing a groundless fraud charge are too small, and maybe there ought to be a little better balance in that matter. Now, again, I can't help but mention one case, which I think is a clear aberration, to add to all the ones that Al Johnston cited.

I'm sure most of you are aware of the *Winters v. Koratron* case, where the judge said, you don't even have a matter of judgment. Everything your client gives you, you have to provide to the Patent Office without even a filter, if I understand that case. That one I don't think will be duplicated.

I'm sure we didn't provide any solutions because there are no clean-cut easy solutions short of judgment. I would say it can best be handled by: (1) good faith exercise of the best possible judgment on the part of the patentee's attorney and (2) responsibility on the part of the defendant's attorney in bringing the charge of fraud. There was an observation, I believe by Rufus Day about the difference in standards that were applied with respect to antitrust questions and nonenforcement questions. And another observation that the difference between the standard which is very strict for disclosing to the Patent Office at least as we now observe it, compared to what he feels is a loose standard with respect to what the defendant's lawyer can charge. This is merely repeating what I said earlier when we talked about two aspects of this problem.

That's about all I have to say, Jim, except my thanks as a substitute for a substitute, to the four panelists for doing such a superb job so that all I had to do was intrude occasionally. And thanks to you all for participating so well.

DIRECTOR HARRIS: Thank you, Frank. I just want to say that I, too, have had a difficult time not to intrude more often. As I said at the outset, the object of the Clinic is to get the maximum input from all participants. This has really been a splendid meeting. I think we did a lot of diagnosing, and some constructive remedies should come out of this cogitation. The ideas expressed here will surely challenge the decision-makers. You will have an opportunity, of course, to edit your remarks before publication. Naturally, we haven't come up with all the answers, but some excellent ideas and sentiments have been exchanged. If the decision-makers take account of what was offered here, it should result in redressing some of the imbalance presently prevailing in favor of defendants who raise the question of fraud. I want to thank the Moderator and all the participants for a very interesting and provocative session. The Clinic stands adjourned.



## INDEX\* TO VOLUME 15, 1971-72

### A

- Acoustics  
and noise abatement, patent statistics relating to R&D expenditures on 564
- Advertising, false (See Unfair Competition)
- "American Patent Utilization in Canada"  
article by O. J. Firestone 376
- Andean Group Agreement 276
- "Another View of the Antitrust Status of Territorial Limitations in International Licensing"  
article by Howard I. Forman 27
- Anten, Lewis 405
- Antitrust (See also Consumerism; Joint ventures; Licensing; Patent; Unfair Competition)  
competition policy in new R&D setting and 488-499  
consumer protection and 45; 85  
defense in patent litigation 532  
government policy in 85, 88  
license limitations and 1  
international 27  
patent conflict 1; 27; 19; 31  
patent law trend and 1; 27; 489-499; 502-513; 515-517
- "Antitrust and Competition Policy in New R&D Setting"  
special conference session 488-499
- "Antitrust and Consumer Protection in Tandem: What Should

We Expect of Section 5"

- annual conference paper by John C. Bodner, Jr. 85
- "Antitrust Policy in a Technological Society: The Distinction Between Practices and Structure"  
annual conference paper by Allen C. Holmes 88
- "Aspin Bill" 386
- Australia

Commonwealth Scientific and Industrial Research Organization 281

computer program protection 310

Author abstracts

priority assertion and early disclosure through 268

### B

- Bennett, James T. 564
- "Billy M. Horton Receives Inventor of Year Award"  
note on 176
- Blair, Homer O. 202
- Bodner, John C. Jr. 85
- Browne, Francis C. 88

### C

Canada

- American patent utilization in 376
- patent system and policy 381
- recoupment of defense R&D costs 301

---

\* Italicized numbers in the index refer to pages in the 1971 Conference number of *IDEA*.

## IDEA

- computer program protection 310
- Carter, Sydney 460
- CATV  
Sports broadcasts protection 385
- Chuppe, Terry M. 523
- Cohen, Jerry 595
- Colclough, O. S. 232; 479
- Coles, James Stacy 437
- "Commercial Value of Patented Inventions"  
article by Richard L. Sandor 557
- Commonwealth Scientific and Industrial Research Organization (Australian) 281
- "Computer Program Protection in Three British Commonwealth Countries: What Can U.S. Learn?"  
article by Laurence R. Letson 304
- Consumerism (See also Antitrust; Federal Trade Commission; Unfair Competition)  
antitrust and 45; 85; 88  
benefits from patent system 31  
Class Action Act of 1971 48; 72  
class actions 51  
commercial honesty and 45; 93  
foreign legislation 48-50; 62  
Fraud Prevention Act of 1971 47; 64
- "Consumerism and 'Old-Fashioned Commercial Honesty'"  
annual conference Kettering Award Address by Walter J. Derenberg 45
- "Contexts for Research"  
conference paper by Henry David 7
- Copyright (See also Consumerism; Unfair Competition)  
challenges in field of 472-473  
protection for  
phonograph records 57; 58; 79  
sports broadcasts 385  
Revision Bill 386
- "Copyright Protection for Sports Broadcasts and the Public's Right of Access"  
article by Paul E. Kritzer 385
- Cost factors in patent litigation 523
- ## D
- David, Henry 439; 7
- Day, Richard E. 488
- Defense, Department of 300
- Derenberg, Walter J. 45
- DeSimone, Anthony R. 97
- "Development and Management of University-Derived Inventions, The"  
article by John L. Gray 49
- Disclosure  
early, through author abstracts 268
- Discovery proceedings  
in patent litigation 523
- ## E
- East-West trade 542
- Ecology  
legislation on 361  
organizations 375  
programs on environmental problems 358, 14  
role of trademarks in 357  
symbols 365
- Edwards, Corwin D. 19
- "Emerging Needs in Tax Policy



- Concerning Research and Education"  
 special conference session 500-517
- "Emerging Restrictions on Transfer of Technology"  
 report by John C. Green 274
- "Empirical Study of Cost Factors in Patent Litigation, An"  
 report by L. James Harris, Terry M. Chuppe, and Le Manh Tri 523
- "Enterprise Under Stress: Changing Premises and New Responses"  
 annual conference proceedings 1-116
- "Experience Aspects of USSR Industrial Property Rights Protection"  
 report by PTC Research Institute team 542

**F**

- Federal Trade Commission (See also Consumerism; Unfair Competition)  
 Act, Section 5 85; 109  
 practice under 45, 85, 93  
 new legal developments at 94-96  
 corrective advertising 94  
 trade regulation rules program 95-96
- Federico, P. J. 232
- Firestone, O. J. 376
- Forman, Howard I. 27
- France  
 recoument of defense R&D costs 297
- Fraud on the Patent Office clinic on 617

- defense in patent litigation 532
- Freed, Joel M. 57
- "Functions, Costs and Fees of the U.S. Patent Office"  
 article by Jerry Cohen 595

**G**

- Gapcynski, William G. 293
- Goldsmith, S. Delvalle 31
- "Government Patent Policy Revisited: Reflections Occasioned by President's 1971 Memorandum"  
 article by Martin G. Raskin 340
- Gray, John L. 49
- Green, John C. 274; 282; 523

**H**

- Hanson, Arthur B. 500
- Harris, L. James 84; 187; 435; 523; 615; 1
- Harter, Franklin C. 575
- Hartman, Lawton M. 443
- Hilinski, Chester C. 242
- Hoffmann, Paul 131
- Holman, Mary A. 564
- Holmes, Allen C. 88
- Horton, Billy M. 176; 480

**I**

- Indonesia  
 Academy of Sciences 281
- Industrial property (See also Antitrust; Copyright; Joint ventures; Licensing; Patent; Technological transfer; Trademarks; Unfair competition)  
 R&D, technological education and, policy correlations 429  
 rights, USSR protection of 542

Innovation (See also Invention)  
 rewards for 575

International (See also Antitrust;  
 Industrial property; Joint ven-  
 tures; Licensing; Patent; R&D)  
 computer program protection  
 304  
 consumer protection 45  
 licensing, antitrust status of  
 territorial limitations in 27  
 problems in the "knowledge  
 industry" 439-459  
 property rights protection 542  
 recoupment of defense R&D  
 costs 293  
 Soviet analysis of U.S. patent  
 system and expenditures for  
 R&D 322  
 technology transfer, programs  
 482-487  
 trademark protection, clinic 79;  
 62-63  
 U.S. antitrust policy 88

"International Trademark Protec-  
 tion: Private Interests and Public  
 Programs"  
 Institute clinic 79

Invention  
 changing conditions of 21-24  
 complex identity of 25-26  
 historical setting of 20-21  
 incentives for 575; 24; 35  
 patented  
     commercial value of 557;  
     567  
     legal rights of employee  
     and employer to 575  
     to measure R&D expendi-  
     tures for antipollution  
     techniques 567  
 proprietary rights to 22-25

Inventors  
 changing role of 19  
 rights of and rewards to 575;  
 19; 31

Inventors' certificates 542

**J**

Joint ventures (See also Antitrust;  
 Licensing; Technological trans-  
 fer; Unfair competition)  
 abroad: industrial property,  
 taxation, and competition  
 182-267  
 antitrust, unfair competition  
 laws and 235-241  
 business organization of 191-  
 194  
 government antitrust policy in  
 88  
 patent, trademark, know-how  
 laws and 202-232  
 pollution control and, 493-498;  
 515-517; 31  
 tax laws and 242-249

"Joint Ventures Abroad: Industrial  
 Property, Taxation, and Compe-  
 tition"  
 clinic on, 182-267

Jones, Stacy 179

**K**

Kettering Award Address, The 45  
 Klass, Felix 191  
 Know-How (See Licensing)  
 Kritzer, Paul E. 385

**L**

Ladas, Stephen P. 140  
 Lanham Trademark Act  
 Section 43 (a) 78

Le Manh Tri 523  
 Letson, Laurence R. 304  
 Licensing (See also Antitrust; Joint ventures; Patent; Unfair Competition)  
     book review note on agreements drafting 615  
     compulsory, government policy on 492-493  
     foreign  
         Australia 289  
         Canada 380  
         USSR 542  
     limitations, patent and know-how 1; 27-29; 34-37  
         territorial, antitrust status in international 27  
 Lightman, Joseph M. 87, 357, 542

**M**

Moss bill 575

**N**

Nader, Ralph 32, 46, 85  
 National Academy of Sciences 281  
 NATO  
     countries, recoument of defense R&D costs 293  
     “New Book Note on *Drafting Patent License Agreement*” 615  
     “New Challenges to Patent, Know-How, and Other Industrial-Intellectual Property Rights”  
         special conference session 460-478  
     “New Circumstances for Industrial Property”  
         annual conference session 19-84  
     “New Conditions and Problems of the ‘Knowledge Industry,’ Na-

    tional and International”  
         special conference session 439-459  
     “New Context for Research”  
         annual conference session 7-18  
     “New Film on ‘The Way of Invention’ Available”  
         note on 520  
     “New Setting for Antitrust and Unfair Competition”  
         annual conference session 85-97  
 Noise abatement  
     patent statistics relating to R&D expenditures on 564  
 Novelty  
     legislation 405

**O**

“Observations on the Role of Trademarks in Ecology”  
     report by Joseph M. Lightman 357  
 Oppenheim, S. Chesterfield 1

**P**

Patent (See also Antitrust; Consumerism; Industrial property; International; Joint ventures; Licensing; Unfair competition)  
     antitrust conflict 1; 27; 19; 31; 85; 88  
     disclosure  
         by abstract 272  
     Employee-employer rights to ownership of 576  
     laws  
         technological progress and 19  
     license limitations 1, 27  
     litigation, cost factors in 523

- policy, government 340  
 protection in USSR 542  
 statistics, use in estimating  
   R&D expenditures for noise  
   abatement 564  
 system  
   as stimulus to invention  
   576  
   consumer benefits from 31  
   criticism of 19  
   defense of 31  
   goals of 578  
   Soviet analysis of U.S. 322  
   value of 597  
 utilization of 557, 565  
   in Canada 376  
 "Patent-Antitrust Spectrum of Patent and Know-How License Limitations: Accommodation? Conflict? or Antitrust Supremacy?, The"  
   report by S. Chesterfield Openheim 1  
 Patent Office, U.S.  
   financial structure 602  
   functions, costs and fees of 595  
   problems under present system  
   602; 27-30; 41-42  
   role of, present and future 597  
   Soviet analysis of 322  
 "Patent Statistics As a Surrogate for Spending: A Case Study of Patents Relating to Acoustics and Noise Abatement"  
   article by Mary A. Holman and James T. Bennett 564  
 "Patents: A Force for Competition and the Consumers' Best Friend"  
   annual conference paper by S. Delvalle Goldsmith 31  
 "Paul E. Kritzer Wins 1971 Patent Office Society Award"  
   note on 522  
 Pitofsky, Robert 93  
 Pollution control (See also Ecology, Joint Ventures; Noise abatement)  
   antitrust policy and joint ventures in 493-498; 515-517; 32  
   government regulation 15-18  
   industry responsibility 14  
 Pre-trial Conference  
   in patent litigation 523  
 "Programs in Department of Commerce to Enhance Technology and Facilitate Its Transfer"  
   special conference paper by James H. Wakelin 482  
 "Priority Assertion and Early Disclosure Through Author Abstracts"  
   report by Irving H. Siegel 268

## R

- Raskin, Martin G. 340  
 "Recoupment of Defense R&D Costs in NATO Countries"  
   article by William G. Gapcynski 293  
 Research and education  
   contexts, plurality of 7-13  
   new conditions and problems  
   439-459  
   public character of 9-10  
   relation to government 10-13  
   tax policy concerning 500-517  
   values in 10-13  
 R&D (see also Industrial property)  
   expenditures for noise abatement 564  
   inventions, employee-employer rights to 575

proprietary rights to 22-25; 40  
 recoupment of defense costs in  
 NATO countries 293  
 Soviet comparative analysis of  
 U.S. expenditures for 322  
 technological education, indus-  
 trial property and, policy cor-  
 relations 429  
 utilization of patented inven-  
 tions 557  
 "R&D, Technological Education,  
 and Industrial Property: Policy  
 Correlations for the 1970's"  
 special conference 429-519

## S

"Sandman Bill" 386  
 Sandor, Richard L. 557  
 "Scientific and Technical Develop-  
 ment, the Monopolies, and the  
 Patent System"  
 article by Yu. A. Sergeev and  
 N. Yu. Strugatskaya 322  
 Scott Amendments 41; 511; 3; 19;  
 33; 40; 98  
 "Selected Papers from the Insti-  
 tute's Fifteenth Annual Confer-  
 ence to be Published"  
 note on 521  
 Separation of Issues  
 in patent litigation 524  
 Sergeev, Yu. A. 322  
 "Shapiro, Bernstein & Co. v. Goody  
 Revisited: Judicially Sanctioned  
 Restraint on Alienation and Dou-  
 ble Satisfaction"  
 article by Joel M. Freed 57  
 Shelton, John P. 281  
 Siegel, Irving H. 268  
 "Some New Legal Developments at  
 the Federal Trade Commission"

annual conference paper by  
 Robert Pitofsky 93  
 "Special Problems of Innovation  
 and Technology Transfer"  
 article by John P. Shelton 281  
 Sports broadcasts  
 copyright protection for 385  
 "Stacy Jones Authors New Book"  
 note on 179  
 "Statutorily Decreed Awards for  
 Employed Inventors: Will They  
 Spur Advancement of the Useful  
 Arts?"  
 article by Franklin C. Harter  
 575  
 Stern, Richard H. 11, 27  
 Strugatskaya, N. Yu. 322  
 Summary Judgment Motions  
 in patent litigation 524, 531  
 Summers, George D. 449

## T

Tax  
 laws relating to joint ventures  
 242-249  
 policy concerning research and  
 education needs in 500-517  
 Technological education  
 R&D, industrial property and,  
 policy correlations 429  
 Technological Progress and the Pat-  
 ent Laws"  
 annual conference paper by  
 Corwin D. Edwards 19  
 Technological transfer  
 government  
 antitrust policy 88  
 programs 482-487  
 in joint ventures 199, 207  
 problems of innovation and  
 281

restrictions on 274  
 Timberg, Sigmund 235  
 Trademark (See also Consumerism; Ecology; Unfair competition)  
 PTC Research Institute's research program 87  
 protection  
   in USSR 542  
   international 62  
   clinic papers on 79  
     "Multiple-Country Filing: Madrid and Its Alternatives," Anthony R. DeSimone 97  
     "National Laws and International Treaties: Implications and Interaction," Francis C. Browne 88  
     ". . . Protection and Enforcement Abroad," Paul Hoffmann 131  
     "Unfair Competition in Trademarks Abroad," Stephen P. Ladas 140  
 role in ecology 357

## U

Unfair competition (See also Antitrust; Consumerism; Federal

Trade Commission; Joint Ventures; Licensing)  
 Act of 1971 59; 81  
 in false advertising 45, 93  
 in trademarks abroad 140  
 "Union Carbide and the Environment"  
   conference paper by Joseph S. Whitaker 14  
 United Kingdom  
   computer program protection 305  
   recoupment of defense R&D costs 296  
 University-derived inventions  
   development and management of 49  
 USSR  
   trademark protection 542

## W

Wakelin, James H., Jr. 482  
 Weiser, Gerard J. 190  
 West Germany  
   consumer class actions in 49  
   employed inventor legislation 582  
   illegal copying of phonograph records 57  
   recoupment of defense R&D costs 295  
 "What's New With Novelty: Section 102 of S. 643"  
   article by Lewis Anten 405  
 Whitaker, Joseph S. 14

Proceedings  
Fifteenth  
Annual Conference

October 20, 1971  
Washington, D. C.

The PTC Research Institute of  
The George Washington University





*Enterprise Under Stress:*

*Changing Premises and New Responses*



# The Conference

The Fifteenth Annual Conference of The PTC Research Institute focused on the theme, "Enterprise Under Stress: Changing Premises and New Responses." Three main topics were discussed: (1) New Context for Research; (2) New Circumstances for Industrial Property; and (3) New Setting for Antitrust and Unfair Competition.

At the Luncheon Session in his honor, Walter J. Derenberg, the Charles F. Kettering Award recipient for 1970, delivered the Award address on "Consumerism and 'Old-Fashioned Commercial Honesty.'"

The research work of The PTC Research Institute represents the first university attempt at a comprehensive study of the patent, trademark, copyright and related systems in the United States. This study is systematically planned and coordinated, inter-disciplinary in nature and utilizes a combination of specialities such as economics, statistics, psychology, sociology, and law; and empirical, that is, based on the facts gathered by the staff on the actual operation of the systems.

Invited to the Conference were key representatives from different fields of activity throughout the nation: commerce, education, science, industry, finance and government.

This presentation of the proceedings of the Institute's Annual Conference this year comprises the principal contributions. These contributions, submitted for publication by the participants, are set forth in this Journal as separate papers and are published in this Conference Number in the order in which they appeared on the Conference program. Although it is our custom to print the edited version of the verbatim presentation, several of the participants upon their request substituted more complete papers or reports. In view of the time constraint, these authors were not able to make complete presentations at the Conference. Robert Kramer, Dean of The National Law Center of The George Washington University, welcomed the participants to

the Conference, and Director L. James Harris provided the keynote for the meeting.

Chairman of the morning session was Robert W. Cairns, Deputy Assistant Secretary of Commerce for Science and Technology; and the afternoon session was chaired by John C. Bodner, Jr., of Howrey, Simon, Baker and Murchison. Speakers in order of their appearance were Henry David, Executive Secretary, Division of Behavioral Sciences, National Academy of Sciences; Jeremiah J. Kenney, Jr., Washington Representative of Union Carbide Corporation (who represented and delivered the paper of Joseph S. Whitaker, Union Carbide's Coordinator of Environmental Affairs); Corwin D. Edwards, formerly Head of Bureau of Economics, Federal Trade Commission; S. Delvalle Goldsmith, Ladas, Parry, Von Gehr, Goldsmith and Deschamps; Allen C. Holmes, Jones, Day, Cockley and Reavis; and Robert Pitofsky, Director of the Bureau of Consumer Protection, Federal Trade Commission.

## INTRODUCTORY REMARKS: A KEYNOTE

L. JAMES HARRIS\*

ENTERPRISE UNDER STRESS: CHANGING PREMISES AND NEW RESPONSES, the theme of this Conference, dramatizes the broad interests of The PTC Research Institute. All creativity is not included in those inventions that go through the Patent Office route. One has to see in a broad context where the need for creativity is and then activate the machinery to produce it.

Society must look outward. It has always to go back to the technological invention base, the motor, or at least one of the major motors, for the individual drive to innovate. One is deeply interested in what makes the motor tick, such as the patent right. But there is a need to become more aware of the broad technological and economic scene in which the motor must function.

The general atmosphere for creativity is not as good as some like to believe. It is difficult, for example, for new ideas to filter up in a

---

\* Director, The PTC Research Institute; Professor of Law, The National Law Center, The George Washington University.

company—particularly one whose executives feel complacent about a company's industrial position. Not only does creativity not get free play, but it may, sometimes quite unintentionally, be used as a word of advertising rather than of actual progress. You are all familiar with another symptom of company bureaucratization—the “not invented here” syndrome. How does one break through this type of crust?

Business is now being asked to respond not only to the marketplace, but to a growing number of demands that come from government regulation, ecology, consumerism, et cetera—a whole new relatively amorphous aggregation of demands. Creativity in terms of product wants of the public has increased substantially and many of the environmental costs the public seeks will not be easily covered. To survive, enterprise must actively seek a new balance among all the pressures, some of which conflict. Can management be equipped to communicate well with the general public while dealing effectively with, for example, its patent-antitrust-unfair competition problems? Experience with the proposed Scott Amendments to S. 643 (Appendix A) relating to adjustments in the patent-antitrust relationship and to the threat to the common law of trade secrets are examples of the complex problems involved in communication and how much has to be learned about the mechanics of the complex.

How can companies used to listening to the voice of former markets now pay heed to other constituencies—from Washington, from activists, from workers, from students, et cetera? Can they be effectively integrated into company strategy and at what cost?

First, one should recognize that at this time the problem of creativity in terms of technological invention is relatively trivial compared with the problem of the development and marketing of these inventions in the new environment. The problem is systemic. There is a total creativity problem. The real question is with the tree itself. This is the reason for the broad scope of this Conference. It seems increasingly clear that creativity is required at all levels in order to accommodate creativity in the technological boiler room. A flexible creativity is needed throughout.

Therefore, in addition to an awareness of the broad problem, the second need is how to break the “crust” to encourage creativity at every level, not just the creativity of the individual inventor pursuing his own idea. This of course is not an easy task under present conditions. For example, hired management that may be around for only a short while will be reluctant to take on really new ideas. Moreover, there may be a lack of management talent; the skill to do what is needed may be in

short supply. And of course in bad times people are more interested in making a quick profit so they operate with a short-term horizon on a short fuze—even going through the patent system route may be shunted. Thus there seems to be a need for the adoption of a new total approach to break the crusted attitudes of companies and other relevant organizations, including governmental institutions.

The third point is that the challenge is both domestic and international. Our society must not only meet the new costs of consumerism but, at the same time, the new challenges to our productivity from world competition. It is well known that the Japanese, for example, visit the U.S. to see what they can pick up and market. Do we fail to see such opportunities for ourselves? Or is it a failure on our part to drive through? Or is it the challenge from abroad at all levels that we do not yet entirely appreciate? For example, are our laws, such as antitrust, too restrictive on American business in the international arena?

In the 1800's there were British Parliamentary inquiries as to why American inventiveness appeared to be better than theirs. Now it's our turn to examine ourselves. It doesn't do any good for us to say, anytime the Japanese or the Germans win out, that they are "dumping."

Perhaps there is room for creativity in international diplomacy. Perhaps—and though I jest, this may spark some thinking—there is a need to appoint a labor leader as ambassador abroad and have him spread some of the labor and other benefits we have accepted in the U.S.—such as higher wages, depollution and consumerism. Here can be seen the inability in our top echelon to take advantage of ideas and spread them. If these ideas are so good for the U.S., they may be equally good for other countries.

The fourth point is that the challenge of the Japanese is not really to the attic inventor. We are not suffering primarily from a lack of technology, although the base can't do the job unless there is creativity at all levels—and this could result in a running out of basic fat. The point is that technology doesn't market; it doesn't sell. If the fellows out in front don't broaden our markets or our laws are too restrictive, we become unbalanced and our technological contributions die. Thus if we are a society out of balance, we must take constructive steps to remedy the situation.

Constructive business operations are not routine. You can run any business routinely as long as the orders come in. But now companies are cutting back on R&D. Are they not good enough to use the research because there is too little of everything else to go along with it? Which brings us to a fifth and final point. Talking about creativity isn't

## 6 IDEA

enough. Perhaps a total approach is needed (1) that is geared to meeting the problems posed to management by the new demands outside the marketplace and by outside competition, especially from abroad, (2) that is innovative at all levels in business and in government and (3) that is innovative on psychological levels as well as in making goods.

Problem solving occurs at all levels. Often human leadership attitudes are involved. People committed to a way of life have to reexamine themselves. Recently President Nixon made a dramatic change in his approach to domestic and foreign problems. Our society continues to have strong latent possibilities for change. We don't have to be locked in—there is always the opportunity for the intangible creativeness. For example, President Nixon seized on a law that ostensibly was intended to embarrass him and used it most dramatically against inflation.

Thus, there is need to balance innovation and invention. Engineers and chemists have not generally been laid off because of their poor work, but rather because of other factors such as inadequate marketing, programming, projecting, leadership, et cetera. Technical competence is therefore not sufficient. It is not a question of R&D and patent people being wrong. It is rather a need for everybody else also to be right—a need for everybody to be in step. To do this it is desirable to transform values rather than abandon them. We must eat crow—but with dignity. Organizations, institutions, and nations all have such problems. You can give up or you can transform the agenda. Let me rein in my personal enthusiasm and be content to sound a keynote rather than explore too fully. We all want to hear what the speakers have to say.



## A. NEW CONTEXT FOR RESEARCH

### Contexts for Research

HENRY DAVID\*

THE MORE I REFLECTED upon the subject upon which I was invited to speak, the "New Context for Research," the more I understood the opening sentence of an inaugural lecture delivered by a distinguished French scholar, Michel Foucault, on "Orders of Discourse." It reads: "I would really like to have slipped imperceptibly into this lecture, as into all the others I shall be delivering, perhaps over the years ahead."

I understand, in short, how much more difficult it is to establish with persuasiveness the point of departure for my remarks than it is to give shape to the substance of the message I wish to convey. Consequently, I will, in a sense, bypass the considerations that lead me to substitute for the announced title one that is more consonant with their content—namely, "Contexts for Research." Note, first, that I have eliminated the critical modifier "new" from the title, and, second, that I am suggesting that today's research enterprise may be variously—and differently—

---

\* Executive Secretary, Division of Behavioral Sciences, National Academy of Sciences.

examined and assessed in the light of the several contexts within which it is located and perceived. If there is validity in this notion of a plurality of contexts, there is also at least a surface validity that attaches to the central proposition that I wish to present.

That proposition, in brief, is that the theme of this PTC Research Institute Conference—"Enterprise Under Stress: Changing Premises and New Responses"—invites careful examination before it is accepted at face value. In this setting, I would expect a certain sympathy with the cautionary notice, "caveat emptor."

Of the numerous contexts within which that complex *social* enterprise that we label research may be perceived and assessed, I propose to call attention to four.

## I

One context is defined by styles of scientific inquiry and the historical development and, therefore, by the specific internal logic of each of the scientific disciplines. These define the context of research in the sense that the methods and internal logic of each discipline identify the intellectual challenges to which research scientists are responsive. This responsiveness appears in the recognition by researchers of those "scientific" problems that are susceptible to solution, and thus serves to identify what I will call the opportunity structure for research activity and the consequent allocation of resources for research by scientists.

Within this context, what may be labelled as "new" are not the values that govern and regulate research activity or the behavior of the various communities of scientists. It is the promise of future advances in scientific knowledge. Here, it may be suggested that one way of looking at these future advances that induces a certain sense of humility is to bear in mind that we do not quite know how far human brains can go with the business of forming what have been called "fictions"—that is, "internal assumptions about the state of what is assumed to be the external real world."

## II

A second context for the perception and assessment of the research enterprise are the several different institutional settings within which research activities are conducted. From this vantage point, I see little evidence that compels the conclusion that the institutional patterning of research activity that has emerged since World War II is being subjected to radical—that is, strikingly new—alterations over the shorter run. Academic institutions are still the primary loci for free basic research. Government-sponsored research institutions that have enjoyed

some measure of independence may be having difficulties. However, as a class of facilities they are not threatened by extinction. Other non-profit, not-for-profit, and for-profit research organizations are all undergoing the discomforts of operating in a sellers' market. But they still perform needed functions and remain important institutional capabilities for research. Industrial corporations, in spite of the current acute depression of research afflicting activities in a few fields, loom larger as institutional capabilities for research than they did a decade ago.

Since the late 1960's, industrial firms have been the performers of about 70 percent of all research and development in the United States. More important, by the close of the decade, they were supporting more than half of their research and development work with their own funds. Between 1956 and 1968, by contrast, federal funds financed more than half of industrial research and development. Since 1966, the industrial sector has been the only one in which significant increases in research and development support have occurred.

### III

A third context for the appreciation of research as a social enterprise is its *public* character. The importance of this context is self-evident. The source of most of the funding for research—in some fields virtually the sole source—is governmental. The critical policies, as I have remarked elsewhere, “that bear upon the purposes, conditions, volume, and forms of scientific activity, the education, training, and utilization of scientific manpower, and the effects of science upon human affairs, including the uses to which scientific knowledge is put,”<sup>1</sup> are *public* policies. They are the products of political processes.

As the public bill for research and development and the education and training of scientific and related manpower has grown larger during the past decade, it has been increasingly subjected to better informed and sharper scrutiny and to widening public debate. As both the end purposes of the public investment in research and development and the utilization of their results came to be questioned in the light of public-policy alternatives that represent different social priorities, the allocation of public resources to science has emerged as a subject of broadly based, rather than élitist, concern. To a greater extent than ever before, both the status and the purposes of research activities enjoy—or suffer from—public visibility. And this in turn renders them

---

<sup>1</sup> Henry David, “Behavioral Sciences and the Federal Government,” *American Psychologist*, Vol. 24, No. 10 (October 1969), p. 917.

more vulnerable to the play of forces not only external to but also sometimes quite remote from the intellectual factors that shape advances in the sciences. Both science and research are experiencing, in consequence, the effects of a growing politicization.

## IV

What I call the public context of research is intimately linked with the last of the four different contexts in which it may, as I have said, be assessed and examined. This is the cultural or intellectual climate that *appears* to threaten both the values of science and the future vitality of the research enterprise. Here I cannot do more than suggest some features of this climate, the manifestations of which can be recorded in Europe as well as in the United States, with a handful of quotations.

The last annual meeting of the British Association for the Advancement of Science prompted the following observations in the lead editorial of the *New Statesman* of September 10, 1971:<sup>2</sup>

Science is too important to be left to the scientists: if there is one message to emerge from the annual meeting of the British Association for the Advancement of Science, this is it. Scientists are unfitted to the task of shepherding the creature they serve. That creature is today's Leviathan, its coils winding into every corner of our lives. Who is to control it? During the past week eminent members of the scientific establishment have expressed wildly divergent views on the relevance of science and technology to society. But in the end the decisions—or some of them at any rate—have to be taken by politicians. They, in the name of the public, must therefore learn that the position of science in our society has changed—that it now occupies the centre of the stage. How do we find the right place for science in politics, and put it there?

J. Bronowski has recently presented a case for the “disestablishment of science”<sup>3</sup> that also engages the problem of the relationship between science and government. He speaks of “the favorite daydream of the bewildered citizen: to call a moratorium on science,” and notes that “scientists also feel helpless in the rush of events, which unseen hands seem constantly to direct toward more and more massive and unpleasant forms of death.” But, he states, “to buy time” through “a moratorium on science” for the needed assessment of and reflection on, so to speak, the course of human history, for which so many seem to yearn, is both impractical and self-defeating.

In fact no scientist [Bronowski declares], and I hope no one who cares for knowledge, would accept a moratorium even if it were

---

<sup>2</sup> P. 317.

<sup>3</sup> *New York Times* (October 18, 19, 1971).

practical. The tradition of free inquiry and publication has been essential in setting the standard of absolute truth in science: it is already eroded by secrecy in government and industry, and we need to resist any extension of that . . . a literal standstill in science is wrong-headed. . . .

The counterthrust to the deployment of so large a proportion of scientific and technical talent to the creation of "more and more massive and unpleasant forms of death," Bronowski argues, "must come spontaneously out of the community of scientists." They must express the "conscience" of science, if science is to have a conscience, and do so by cutting the "entanglement" of "government in science and science in government" through which both "the integrity of all science" and "the public trust in science" are so gravely endangered. The surgical operation that Bronowski recommends, with recognition of the uncertainty of its success, has, of course, been disputed on several grounds.<sup>4</sup> It is best represented by his own words:

The time has come to consider how we might bring about a separation, as complete as possible, between science and government in all countries. I call this the Disestablishment of Science, in the same sense in which the churches have been disestablished and have become independent of the state.

Evidently the choice of priorities in research should not be left in the hands of governments. This is a view that government departments will not like, so that scientists who hold it will need to be singleminded if they are to make it heard. They may have to refuse to apply for grants and contracts that are allocated directly by departments. Again, this would be a hardship for many scientists, who now have nowhere else to go for money and who would be forced to suspend their research. But they must be willing to face the hardship for a time if they are serious and united in the will to put science into the hands of scientists.

In the long run, the aim should be to get a single and over-all fund or grant for research, to be divided by all the scientists in a country. This would be an effective form of disestablishment, and no doubt governments would accept it rather than watch research become moribund.

The Disestablishment of Science will compel the body of scientists to assign its own priorities on behalf of the community and with it, and divide the over-all grant at its disposal accordingly.

The scientific community, through its own and other communal representatives, will have to judge and balance the importance of the different branches of science at any time and of the new lines of research in each. It will have to guess the time and the chance of success in each line. And then it will have to combine the judgments

---

<sup>4</sup> See, for example, the comments by Sir Peter B. Medawar, Gerard Piel, Anthony Wedgwood Benn, and Eugene Rabinowitch in *Encounter* (September 1971), pp. 91-95.

of importance with the guesses at success in order to arrive at a scale of priorities—a scale of claims, as it were—in accordance with which it must divide its over-all grant.

Both candidates for the presidency of the American Association for the Advancement of Science in 1971, Carl Pfaffman and Leonard Reiser, registered their sensitivity to the many current manifestations of doubt about, if not rejection of, the worth of science, of the heavy dependence of the research enterprise upon governmental support, and of the growing pressures to make science more directly and immediately “relevant” to obvious human needs. From interviews<sup>5</sup> conducted with both candidates, I quote the following remarks:

[Carl Pfaffman] It is true that the high state of science in this country is a result of government support. Many fields came of age that earlier had only amateur standing. But whether we have gone overboard on federal support of science, I'm not sure. With government support you do lose some control of your destiny, but that is a part of any government endeavor, since many other people, with different motivations, come into the decision process. . . .

To support science for immediate practical advantage is unwise. Research—as a fundamental part of intellectual life—and utility are the two essential aspects of science. Utility is important, but if science is to be supported for that alone, there will be disappointments.

Anti-science, anti-intellectual feeling is not new, and science is also getting harder. It has always been difficult, but many are now asking, Is it worth the effort?

A clearer perception of what science achieves in the long run is needed: it is not just practical payoff, but understanding of nature and of man as part of the natural and social world. . . .

Also, much of the hostility is really directed against institutions of science and the uses to which science is put, and this is tied in to the broader question of how institutions operate. It is not science itself that is being questioned.

[Leonard Reiser] We have paid a price for basing our support of science primarily on its technological promise. As technological expansion was curtailed, support for science has also been curtailed.

The question is: how can science as an intellectual endeavor, as well as a technological endeavor, maintain society's support? How does one convince the Congress and the people of the country that activity which can be fully understood by only a few should be supported by all; that the advancement of science and the improvement of our society are not independent?

For several years there has been an indifference to competence, coupled with the feeling that one could solve problems by shouting.

Now, however, there seems to be a new sense of realism about what it takes to solve society's problems.

I cannot believe that a generation of young people will rule out

---

<sup>5</sup> *AAAS Bulletin*, Vol. 16, No. 3 (September 1971).

the study of science, which ranks as one of mankind's greatest achievements, unless we present science badly; or unless the application of science is perceived as detrimental.

Of the many evidences that scientists are being castigated as self-centered and élitist—a characteristic feature of the present climate—it will be sufficient to quote from a letter received by the editor of *Science*:<sup>6</sup>

It would certainly seem from the record to date, that basic research scientists are so preoccupied with the exquisiteness of their protocols and the refinements of their research approaches that they have missed entirely the objective and intent of we taxpayers who are funding their "ivory tower isolationism." . . . We as taxpayers expect something more in return than scientific dialogue between the scientists at seminars and in medical journals.

It is also worth quoting the observation by the editor of *Science*, Philip H. Abelson, that recognizes the extent to which today's intellectual climate has powerful implications for the conduct and direction of the research enterprise as a whole:

To serve the public most effectively, scientists, engineers, and physicians need a friendly, sympathetic environment and one in which their limitations are understood. Until recently such an environment prevailed, but the last few years have brought changes in the public's attitudes. Many adverse changes are involved, but one of the most important is the public's inaccurate estimate of what can be achieved. The public has come to expect miracles from engineering and medicine.

## V

To some the current cultural climate offers an opportunity to alter the pattern of utilization of and the ends served by the nation's scientific resources developed since the close of World War II. In others, it inspires a search for the operational expressions of the notion of the "social responsibility" of science. For still others, it raises the question, "Can Science Survive in the Modern Age?"<sup>7</sup> This is the title of the thoughtful and balanced C. P. Snow lecture delivered by Harvey Brooks at Ithaca College in January of 1971, which deserves wide and careful reading. This is not the occasion to offer my own answer to the question that Dean Brooks poses. However, the prospect that it raises serves to reinforce the point that I made in my opening remarks—namely, that the particular context within which one perceives and assesses the research enterprise makes an enormous difference.

---

<sup>6</sup> *Science*, Vol. 172, No. 3987 (4 June 1971).

<sup>7</sup> See *Science*, Vol. 174, No. 4004 (1 October 1971).

## Union Carbide and the Environment

JOSEPH S. WHITAKER\*

POLLUTION IS ONE OF THE MOST PERVASIVE and complex problems of our times. All of us are very aware of its existence, its varying degrees of severity, and we have begun the battle to control it. Technological advancements, improved abatement procedures and more effective government regulations are bringing some relief. But we are also in the midst of increasing demands for goods and services—which translate into greater wastes and add to the burden of the battle.

Mankind finally became aware of his total environment because his survival seemed to be in doubt. Initially, the fear translated into hysteria in some quarters. Fortunately for all of us, cooler heads now seem to prevail and the hysteria has been tempered to a great degree. "Time" has become the prime factor in our universal fight to abate pollution—time, and a much deeper understanding of the goals we seek.

There is an ever-increasing tendency to have the country believe that industry is refusing to do its part to clean up the environment. This is

---

\* Coordinator of Environmental Affairs, Union Carbide Corporation. Dr. Whitaker's paper was presented at the Conference by Jeremiah J. Kenney, Jr., Washington Representative of Union Carbide.



really not the case, and particularly as far as Union Carbide is concerned. I believe our intent is well documented in our corporate policy and practice statement on environmental health, which was prepared for internal use as a firm guideline to be followed by all.

One of the fundamental principles of Union Carbide is to conduct all of its operations with responsive regard for the environment in which our products are manufactured, distributed and used—for the health, safety and well-being of our employees, customers and the general public. We have taken an active role in seeking equitable and realistic control regulations, proper and safe use of our products and processes, and the identification of problem areas not yet under full control. The responsibility for administering and operating under this environmental health policy is placed with each division, area company or subsidiary—to examine carefully all actual and potential environmental health problems, and to develop specific programs for control or elimination.

The question certainly arises among the cynics whether Union Carbide has ever bothered to implement its environmental policy. I can assure you that environmental quality or pollution control—whatever you wish to call it—has become an integral part of every business decision.

I think it is important that all of us realize the relationship between our desire and our ability to control our pollutants. Much of Union Carbide's pollution abatement work—particularly that needed for steam power stations and the ferroalloy smelting operations—is on-site developmental work. The "hardware," if it is available, must be engineered to do jobs it wasn't really built to do. This problem is recognized by the various regulatory agencies which have established variable time schedules—ranging from two to four years—for the installation of abatement equipment.

Our ferroalloy facility at Marietta, Ohio has been the subject of much criticism. Among other things, we have been accused of arrogance and economic blackmail and, in my opinion, we have been wrongly accused. The facts, without going into great detail, are that at Marietta we have two problems. The first is our process furnace emissions—those coming from the furnaces which produce the various ferroalloys which are used in stainless steel and other high performance metals. These emission levels are in compliance—as a matter of fact we were ahead of schedule during 1970. The second and more troublesome emission source occurs at our power plant which is used to produce steam and the large quantities of electrical power used to produce the alloys. We have been required to achieve major reductions in our sulfur oxide and

fly ash emissions. This corporation offered reasonable, positive proposals to abate Marietta's pollution at the earliest feasible date. In fact, we are moving ahead with a program which is acceptable to the federal regulatory agency.

In March and April of 1970, pollution abatement recommendations for Marietta were issued. One of these specified a 40 percent reduction in sulfur oxide emissions at the power station by October 1970.

The only way to meet this reduction would have been through the substitution of low-sulfur coal. As you may recall, there was a nationwide fuel crisis during the summer and fall of 1970 which occasioned the creation of Cabinet-level committees to devise means of meeting the nation's most urgent needs. Because of that situation, Union Carbide was unable then to secure supplies of low-sulfur coal.

In January 1971, the Federal Environmental Protection Agency requested that we make specific commitments to meet the recommendation for a 40 percent reduction in sulfur oxides. Fortunately, low-sulfur coal had become available, principally because the economic recession created a slight easing in the coal market. Therefore, we were able to achieve the sulfur reduction, as recommended, by March 1971, and the Marietta power plant is currently operating in accordance with the government timetable.

In September of this year, we had to achieve an additional 25 percent reduction in fly ash emissions at the Marietta power station. Our initial reaction to this recommendation, in view of the coal shortage, was that we knew of no way to accomplish this reduction other than shutting down a portion of the power plant, with the consequent layoff of employees. This was not a matter of defying the government or of economic blackmail. It was simply a statement of fact. Again, because of the easing coal situation, we were able to meet the September requirement.

Contrary to impressions that seem to have been created by the news media, this corporation certainly has accomplished something toward pollution abatement. Alloy and Anmoore, West Virginia, have become quite well known in the press. Yet we are vigorously following schedules and programs for pollution control which have been approved by the state of West Virginia.

Achievements at the Alloy plant include installation of electrostatic precipitators on the power station stacks to collect in excess of 99 percent of the fly ash emissions. Construction of the largest dust collector ever placed on a ferroalloy furnace has been completed, and by the end of this year we will have achieved an 80 percent reduction in

combined emissions from the ferroalloy furnaces and the power plant at Alloy. At Anmoore, we are in the midst of a rebuilding program, also approved by the state of West Virginia, to abate particulate emissions from our carbon electrode manufacturing facility.

At Union Carbide facilities where regulations have not yet been placed on the books, we have established pollution control programs which we anticipate will satisfy future standards. New plants, of course, have abatement equipment designed into their construction.

The extent of our contributions to a better environment are far from all-encompassing, but they are of some significance. Our scientists created a break-through in sewage treatment with the invention of the "UNOX" system, which substitutes 95 percent pure oxygen in place of air to treat municipal and industrial wastewater. Compared with conventional sewage treatment plants, the "UNOX" system offers capital savings of 30 to 50 percent, and operating savings of 10 to 25 percent. In a similar vein, we have devised a method by which the dissolved oxygen content of rivers can be increased to help upgrade the quality of the water. In the pursuit of our own problems, we have designed equipment to monitor the quality of both air and water. We now use these instruments successfully, and they are also being used by others. We have received an award for constructing the only licensed chemical waste landfill operation in the state of West Virginia.

I feel that one of the main problems facing everyone of us is a "clear" determination of the "rate" at which existing pollution is to be abated. The answer, depending upon the particular pollutant, may range from "now" to "we don't know when." Taking the positive approach to the time factor, we must also give equal attention to the "how." Some of industry's more outspoken detractors will say "right now"—whether or not it is reasonable. The only alternative for meeting "right now" may be curtailed production.

Shutting down a facility is certainly not the most acceptable route toward pollution abatement. It puts people out of work, affects the economics of the community, and is the most costly course of action for the company—assuming the product is needed. However, we should not lose sight of the possibility that for the good of everyone we could reach the point where curtailed production of a particular product may be the only alternative to a relatively clean environment.

Sometime in the near future, we all may well be called upon to implement and elaborate on the decisions being made today to abate pollution. Hopefully, the time factor will be less critical. But we can also hope that the concern for quality environment will not diminish

beyond all logic. Today's answers will not erase tomorrow's questions. These are complex times. We are all living and operating under a set of criteria, both regulated and moral, which many of us do not fully comprehend. Regulations which had been written into the statutes are being revised; pollution control standards are neither constant nor nationwide. Scientists are divided on the seriousness of the problems confronting us. Are we going to lower the temperature to a point where we bring on a new ice age—or raise it to a point where Denver will be our leading seaport? And, as most of us know first hand, today's technology for pollution abatement leaves much to be desired.

I keep saying that Union Carbide, for its own part, cannot remedy "yesterday," and it needs a reasonable time to fix "tomorrow." This is not the kind of statement that leads to what the publicists call "good press"—only because it is too blunt. Given a sufficient amount of time and dollars, we can reach compliance with most of today's requirements—with the emphasis on today. But when we accomplish that goal, it is already tomorrow, and by some measures we are too late.

A very prevalent evaluation about "tomorrow's" pollution control is that we will come face to face with some requirements that we simply will not have the technology to accomplish. It seems likely that the problem won't be how to get the pollutants out but how to prevent them from getting in in the first place. My guess is that recycling will be the wave of the future: Using the same cooling water over and over; a closed cycle heat exchange; a method to remove sulfur from the fuel rather than taking sulfur oxide from the stacks; or atomic fission and then fusion as the major source of energy for power.

There is also a school of thought which says that we are going to have to learn to use less—or even go without some of those things we now find useful. It seems to me that the probability of the entire population changing to this degree is rather slight unless—or until—some great environmental catastrophe leaves the public almost no other alternative, which brings us back to my original supposition that increasing demand for goods and services adds to the burden of our problem. This demand comes of course from the desires and needs of people. A finite world with finite resources cannot—I think—support an infinite population over an infinite number of years. We must make changes.

## B. NEW CIRCUMSTANCES FOR INDUSTRIAL PROPERTY

### Technological Progress and the Patent Laws

CORWIN D. EDWARDS\*

DISCUSSION OF PATENT LAWS BY AN ECONOMIST—particularly one who, like myself, has been identified with antitrust agencies and with support for antitrust policies—usually takes the form of attack upon certain features of patent law or practice as inconsistent with antitrust policy. It includes accounts of the strategies by which certain large companies have perverted patent arrangements for monopolistic purposes; expressions of concern about the massing of thousands of patents in a few corporate hands; and support for proceedings in which the Antitrust Division is trying to shrink current abuses of patents and licenses. It expresses the attitude that a central problem as to patent policy is to make that policy more consistent with competition.

To speak along these traditional lines would be attractive to me today, not only because I accept the views that I have briefly summa-

---

\* Formerly Head of the Bureau of Economics, Federal Trade Commission.

rized, but also because such a speech would be timely. The competition problem raised by government patent policy has grown and is growing. Within the last year or two the Administration has enlarged the opportunity for private firms to acquire exclusive patent rights over government-financed inventions; and this has been done in a situation in which most federal funds for research and development go to fewer than 50 companies.<sup>1</sup> Currently the Scott Amendments (Appendix A) are proposing for patents what the Chairman of the Senate Judiciary Committee's Antitrust Subcommittee recently called the most substantial antitrust exemption since that for the insurance industry, though I understand that some of the bill's worst features have been deleted from its latest version. It is tempting to use my time for a sustained attack upon these amendments.

Nevertheless, what I shall say will have a different focus. It will be concerned not with antitrust but with technological progress, and will raise the question whether the patent laws are consistent, not with competition, but with effectiveness as means to promote the progress of the industrial arts.

In the setting in which the patent laws were enacted, their contribution to technical progress was relatively clear. Invention, like most economic activity, was individual. Inventors were scarce, and inventions scarce also. Few people had enough resources, curiosity, and skill to invent. Even the ablest inventor could produce inventions only sporadically—a few in a lifetime, focused upon the limited technical field that one man could master. The likelihood that a second inventor might independently duplicate the same invention was too remote to be important. Thus an inventor might safely keep his invention a secret. If he disclosed it, he might expect to be imitated; but only at a pace adapted to the gradual processes of diffusing knowledge and changing habits in a slow moving society. Even the speediest imitations were not likely to transform a technology in less than 17 years.

In such a world, invention served a social purpose like that of organized science today: It was a major means of aerating society with change. There was need to encourage invention and to induce disclosure of its results. To assure inventors monopoly of their inventions for a limited period of time could do both, at little or no cost to the economy. Each disclosed invention, a discrete event, was a net contribution to technology, likely to be missed or long delayed if the inventor

---

<sup>1</sup> According to the National Science Foundation, in 1967 the first 40 research and development programs privately operated received 88% of all federal funds for such programs.

did not make and disclose it. There was no likelihood that an inventor's monopoly of his invention would enable him, within the patent period, to acquire monopoly not only of his invention but also of the field of activity in which it was used. It was improbable that a single inventor could attain enduring control of a technology by dovetailing inventions end to end. Thus the progress of the arts under the stimulus of patent incentives to invent and disclose was likely to be greater than without the patent system; and the danger of monopoly was not likely to appear. What the patent system appeared to do was merely to encourage invention and foster disclosure by protecting the inventor from imitators who, but for the patent, could duplicate his idea without incurring the delays and costs incident to the development of it.

Changes in underlying conditions have destroyed the plausibility of these common-sense appraisals. True, some inventing continues to be done and some inventions applied in the old individual way; and this fact complicates the problem of public policy, as do residues of an older culture in any changing situation. But the main stream of activity in achieving and applying inventions has become science-based and systematic rather than sporadic; collective rather than individual; publicly financed as well as privately financed; and subject to control by relatively few large corporate organizations so far as it is not controlled by governments.

If the term *invention* had not been already established in the law of intellectual property, it would not have gained currency as a suitable description of the process by which opportunities to innovate now arise. The appropriate term today is *research and development*. R&D as a process is science-based. Its key ideas are formulated along a moving frontier of scientific knowledge. These ideas, or scientific principles, are achieved, for the most part, in organizations not operated for profit. Yet in 1970 industry did more than \$750 million of basic research, of which it provided the funds for more than \$500 million.

The exploratory activity of science, whether in a non-profit institution or an industrial laboratory, minimizes secrecy. Each new step is promptly disclosed to the public and subjected to criticism by the scientific community. A scientific principle is not patentable. Yet we continue somehow to believe simultaneously (1) that scientific research is adequately encouraged and its results adequately disseminated without allowing scientists or scientific organizations to acquire proprietary rights in its product; and (2) that without proprietary rights for inventors the processes of invention and innovation would wither away.

As science develops new insights into relationships among phenom-

ena, new technological developments often come to be reasonably predictable as applications of the new principles. The new technology is not, of course, self-evident. Somebody must find answers to numerous problems before a scientific principle can be applied and before that application can be cheap enough and reliable enough for commercial use. But the general lines along which such work should proceed are often so obvious that parallel efforts to convert a scientific discovery into a useful result are common, and success is often achieved independently and almost simultaneously. Nevertheless, the patent principle that developed when inventions were discrete and sporadic has continued. The first to succeed gets not only the benefit of his own achievement but also a legal right to prevent others who succeed later from using the same achievement, even if they attain it independently.

This right to exclude others from using the results of their own ideas and efforts is unique among the concepts of property. When applied to R&D it has various strange effects: (1) It induces firms to explore technological possibilities that they have no present desire to use, lest somebody else patent these possibilities and thus fence them in. (2) It induces firms to explore technological possibilities that may be important to their competitors, in the hope of patenting these and thus blocking the development of more effective competition. (3) It induces rivals that are exploring the same technological possibilities to do so at a feverish pace in an effort to finish first; and it sometimes induces them to claim invention when the results of their experiments are not yet capable of use. By leaving to the patentee, without curb, the entire decision about the pace at which a patent shall be put to use, it strengthens the incentives that he may have to delay or even suppress innovations that might have unfortunate effects upon his existing business—that might, for example, so lengthen the life of his product as to reduce his replacement sales, or might necessitate drastic write-offs in the value of his existing equipment.

Whether, when such matters are considered, the right to exclude creates, on balance, more technological progress than it prevents is anybody's guess. It certainly confronts the Patent Office from time to time with the obligation to award an enduring monopoly to a selected one of two or more rival inventors who have made similar inventions quasi-simultaneously; and the harshness of the deprivation that might be incurred by the inventor not found to be first provides incentives for negotiation of various kinds of unofficial contracts by which the results of invention are shared in ways not contemplated in the patent laws.

The process of making science useful, from the original idea to the



eventual industrial process or product, is properly described as a two-part activity, research and development. Research is recurrently needed for discovery or refinement of scientific principles by work focused upon an unsolved problem that arises from a projected application of known science. The major part of the work, however, consists of solving practical problems by use of knowledge already available to the technically skilled community. It consists, that is, of new applications of what is evident to persons skilled in the art. But throughout the R&D process, there is difficulty in applying the pre-scientific term *invention*. A discovery of a scientific principle is too broad to be considered an invention; an application of existing knowledge is too narrow. But for the pre-existence of the legal concept of invention, such discoveries and applications probably would have been considered to exhaust the entire intellectual field of R&D. *Invention* would not have been considered a suitable description of what goes on in a large corporate laboratory. But since the concept of invention had to be accommodated, room has been made for it. What is clearly too scientific to be patentable has come to be called *basic research*; what is clearly mere recombination of knowledge has come to be called *development*; and a third category, *applied research*, has been devised to describe intermediate activity from which patents may conceivably flow. With R&D thus divided, less than 22 percent of the total of such activity in 1970 consisted in applied research, and less than 13 percent of it consisted in applied research by industry.<sup>2</sup> Of industry's own R&D expenditures, 71 percent were for development, over 5 percent for basic research, and slightly more than 23 percent for applied research. Industry did nearly 60 percent of all applied research, but paid for less than 70 percent of this with its own funds.

In this setting, change has (1) greatly altered the incentives to invent and disclose; (2) so beclouded the concept of invention that inventions can no longer be readily identified and distinguished from one another; (3) thwarted the Congressional purpose to base patent monopoly on full disclosure; (4) converted the exclusivity of patent rights into an obstacle to technical progress; and (5) enhanced the risks that patents may be used to impair technical progress. In other words, apart from whatever change may have taken place in the relation of the patent system to free competitive enterprise, the system is perverse in its impact upon incentives for technical progress. We retain it, not because it is any longer appropriate to its setting, but for the dual reason that it

---

<sup>2</sup> Figures from the National Science Foundation, National Patterns of R & D Resources.

buttresses major vested interests and that there are problems about the management of R&D for which no alternative consensus has yet developed.

#### THE PATENT SYSTEM AND INCENTIVES

Decisions to explore possibilities for industrial innovation are not made in corporate laboratories by prospective inventors. They consist of plans for R&D, responsibly formulated by research executives, given appropriate degrees of priority in a budgetary process, and then executed by research personnel who perform their assigned parts of the exploratory plan. As a source of personal incentives, patents are almost irrelevant in industrial laboratories. They may be tokens of success, like medals or certificates of merit; they may be, as Charles Kettering thought, sources of personal ambition that can interfere with effective teamwork. They are not the principle incentives of inventors that invent on salary.

Whether or not large companies today need special incentives to engage in R&D is uncertain. They cannot count upon technological stability—could not do so even if each of them tried to maintain it. Basic research, largely undertaken in or financed by governments, private foundations, and educational institutions, contributes a large flow of new scientific knowledge that is available for adaptation to business use. The enterprise that does not seek to adapt it runs serious risks that other enterprises will do so, and that in consequence it will find its own products no longer acceptable or its own productive methods becoming obsolete. The enterprise faces new social problems, such as concerns about pollution; if it does not try to meet these problems it risks coercion. In a large part of the spectrum of business, firms must invent to reduce the risk of their own elimination; and industrial change in this part of the spectrum confronts enterprises elsewhere with new opportunities and necessities.

But apart from this consideration, incentives have changed. The basic corporate decision about R&D is to spend a stated amount of money on an R&D program. So far as a corporate laboratory undertakes such expenditure in anticipation of gain from patent monopolies, the incentive is not, as in the case of last century's individual inventor, a long-shot gambling risk. The risks involved in translating new achievements in basic science into technological accomplishments are seldom formidable particularly in the later stages of activity that require most of the expense. Moreover, the financial decision about an R&D pro-

gram, like the decisions of an insurance company, contemplate reduction of the risks of single projects by grouping them with others. Interesting questions can be raised about the nature of corporate research under this type of incentive, whether, for example, there will be a socially desirable balance between experiments with different degrees of risk. But these questions need not be explored here.

The overshadowing change since World War II has been the fact that most funds for R&D are no longer provided by industry. In 1970, according to the National Science Foundation, industry supplied less than 40 percent of all funds for R&D, as compared with nearly 57 percent by government. Indeed, industry provided not quite 56 percent of the total funds that it itself expended for R&D and received the rest from government. Even these figures overstate the financial stake that industry has in the research process. With the corporate income tax over 50 percent and with R&D expenditures fully deductible from profits for tax purposes, about half of industry's own expenditures for R&D probably would have been added to tax expenditures if they had not been spent for research. As a crude approximation, slightly more than one dollar out of four in industry's R&D budget is spent under the ordinary incentives of profit and loss. Today the possibility of patent monopoly increases the attractiveness of benefits that may be obtained by industry from organized research conducted chiefly at government expense.

### *Identification of Inventions*

Change has also obscured the capacity of those concerned with invention to identify inventions and to distinguish them from one another. Industry has had incentives to win rewards for innovative activity by stretching the concept of invention, introducing tenuous conceptual distinctions between this activity and the rest of research and development; and since most industrial R&D expense is for development, these incentives have been greatest in extending the idea of invention to include much that looks to a layman like trivial application of existing knowledge. By patents upon minutia, the quality of patents has been degraded. The courts have acquired a countervailing function—to look skeptically at such tenuous distinctions in order to withhold awards of patent monopoly from those whose work is pure science or is mere workmanlike recombination of existing knowledge. The survival of a patent that has been subjected to challenge before a high court has become highly problematical.

But apart from the degradation of patents, it has become practically impossible to divide the continuous flow of a changing and tightly correlated technology into a series of self-consistent separately owned properties, each so defined that its boundaries and ownership are clear. Since each patentee has incentives to define his patent broadly, using language as expansible as he can get accepted, this fact alone creates confusion. And apart from such verbal imperialism, the process of defining claims is inherently too crude to be practicable where technology is complicated, tightly interconnected, and rapidly changing. The confusion is inherent in the concept of invention. Individual contributions are not so distinct, the aggregative accumulation of ideas is not so clearly delimited and stratified, and the meaning of descriptive terms is not so precise as to permit the construction of accurate maps of intellectual property. In the words of Richard Buxbaum, "A clutch of patents belonging to an enterprise in a modern field like petrochemicals or electronics cannot efficiently be disentangled to ascertain which of the exact processes (and to a lesser extent products or apparatus) used or manufactured by competitors are covered by the claims. Conversely, it is often impossible to ascertain, with any reasonable expenditure of time and money, the exact extent to which a given process is covered by a multitude of patent claims in various hands."<sup>8</sup> In the simpler language of an inventor friend of mine, "The idea had been patented four or five times, but he (the employer) wanted it patented; so I used some algebra to make the application look complicated and patented it again."

From this indeterminate complexity flow several of the conspicuous defects of the patent system—the unreliability of patent grants as indicators of the validity of patents; the recurrent disagreements as to validity or patent boundary between the Patent Office and the courts or between two or more courts; the importance of willingness and ability to litigate as indicators of the actual strength of patent claims; the ingenuity with which contracts that acknowledge validity are used to by-pass judicial decisions about the strength of patents; and the importance that attaches to possession of a large number of patents, whatever the probable validity of each when separately appraised. All of these peculiarities are symptoms of a central defect—that those who own or must cope with patents are trying to adjust claims to intangibles in a field in which the exact nature of property rights is largely unknown

---

<sup>8</sup> Richard M. Buxbaum, "Restrictions Inherent in the Patent Monopoly: a Comparative Critique," *University of Pennsylvania Law Review*, Vol. 113, p. 638.

and unknowable. A terrain of interconnected patent rights is as chancey as suburban real estate would be if all property lines were described as vaguely as the boundaries of an 18th century New England farm, without reference to generally known baselines from which the surveys can be run.

The precarious nature of property rights to patents has considerable though unmeasurable retarding impact upon the ability of patentees to convert patents into innovations. It is impossible to say to what extent economic growth may be slowed by negotiation and litigation incident to conflicts over the validity of patents and over licenses and pools. In particular instances it is clear that companies have maneuvered for an appreciable period for better terms, while lack of agreement deferred adequate use of the patented technology. In particular instances it is clear that negotiations broke down and technology was, for the time being, withheld from would-be users. In particular instances it is clear that long-drawn-out litigation involved risks that retarded development by some or all of the parties to the conflict. The underlying nature of the patent right—complete monopoly for the patentee, discretionary complete exclusion of others by him—probably fostered more negotiation, litigation, and delay than was inevitable in the adjustment of conflicting claims. The main point, however, is that the nature of the patent right invited both multiplicity and uncertainty in the claims themselves, and thus invited conflict.

### *Inadequate Disclosure*

The patent system notoriously fails to elicit from patentees the disclosures by which anybody skilled in the art could use the invention. Instead, two distinct types of patent licenses have appeared—one in which the patent alone is licensed; another, in which the license conveys not only patent rights but also the relevant know-how. So far as the latter type of license has become necessary, the patentee eats his cake and has it too. He has been granted a monopoly conditioned upon disclosure; but his disclosure has been so limited that use of his invention remains a trade secret, capable of being sold as an addition to the patent. The public does not get the information that the patent purports to give. Thus the patent system is weak as a means to add what has been invented to the body of generally available technical knowledge.

Though such inadequacies may be partly due to insufficient policing of the disclosure requirement by the Patent Office, some such failure is

a natural result of the interconnected nature of technology that has already been discussed. Where there is an array of patents, the knowledge relevant to each patent in the array cannot be segregated from that relevant to the others, like a series of packages in which each has a separate content. The knowledge overlaps, not only from patent to patent, but also between that relevant to the patents already issued and that relevant to patents that may be issued in the future. From the point of view of the patentee, disclosure of what is relevant to a patent often would include a great deal of developmental information that cannot be patented and that is the result of the most costly part of the R&D process underlying numerous other patents, present and future. If permitted to do so, therefore, a patentee makes his disclosures minimal. To cope with the voluminous detail that constitutes the know-how of many processes and appliances is beyond the capacity of the Patent Office. (In one case with which I had contact, the know-how for a machine covered about 300,000 sheets of microfilm.) The Patent Office, therefore, acquiesces in the perversion of patents from their intended function of conveying to society full knowledge about the nature of the patented technological frontier.

#### *Cross Licenses and Technical Progress*

As technology has become complex and interconnected, the chance becomes remote that any one patentee will make inventions comprehensive enough to cover all of the best devices of a particular technology or field of activity. Where there are numerous patents, mostly owned by companies with industrial laboratories, the lesser patentees possess such meager patent rights that they usually sell the rights they have to one of the larger companies; but if there is more than one large company in the technological field, none of the big firms, even after numerous acquisitions, can be technologically self-sufficient except by being, in various respects, technologically retarded. Some of the most desirable technology will have been invented or acquired by the others. Each patentee will possess, at best, only a substantial fragment of the most efficient technology.

Under such conditions, cross-licensing of patents is indispensable to the progress of the industrial arts. If each patentee were to exercise his legal right to use his own patents exclusively, the patent system would become a means of blocking the arts instead of advancing them. The crucial questions as to the impact of a patent system upon technology (and upon industrial structure) are, therefore, the breadth of cross-licensing and the conditions under which it takes place. Yet at this

crucial point we have no clear public policy. The patent laws say that each patentee has an absolute right to refrain from licensing. The antitrust laws say that, although monopoly of a patent by a single patentee is not a forbidden restraint of trade and although many restrictions are permissible in licenses granted by a single patentee, patent pools involving interaction by two or more patentees are subject to antitrust action if they involve restrictions. In this country (unlike many others) no law or policy has formulated the conditions of public or private interest under which licenses should be available as a matter of right. None has codified the degree of patent privilege that should continue to be enjoyed by patentees who pool their patents for sound technological reasons. Very gradual developments of case law have set certain limits upon the rights of patentees to impose restrictions upon their licensees. We continue to apply the patent system as though its essence were monopoly of patents, whereas its essence has become exercise of some degree of privilege in the sharing of technology.

The significance of this distinction is enhanced by two facts: First, that a few great patent holders hold most of the patents; and second, that their dominance often endures much longer than 17 years. Cross-licenses and pools become harder to create without serious antitrust risks as firms become larger and fewer. Once a big firm has attained a substantial patent position, the likelihood is considerable that this firm can buttress that position by a flow of new patents derived from its own inventions and acquisitions; and by dovetailing these end to end it may hold its patent position for a time much longer than the duration of a patent. Under these conditions, the technology of the large patent holder benefits from the fact that the fraction of total technology under a single control is large. But the disadvantage from the obstacles to ready cross-licensing is an enduring one.

#### RISKS THAT PROGRESS MAY BE IMPAIRED

What has been said leads to the conclusion that in various ways the patent system is used in a manner that impedes technological progress, and that in the aggregate these impeding effects may constitute an important off-set to any stimulating effects that it may have. (1) Firms can patent not only inventions that they intend to use but also inventions that they intend to keep out of use by themselves or others. They can withhold from use innovations that might impair the profitability of their current operations and can use patents to block and fence the activities of their competitors. (2) Numerous patents are issued upon trivia—patents many of which are invalid, but few of which

actually reach the courts for invalidation. These patents then prevent the rest of the business community from adopting trivial improvements that properly belong in the public domain. In the aggregate, the effect of withholding numerous trivia may not be trivial. (3) So far as firms exercise their legal right to be sole users of their patents, refusing to issue licenses, the technology available to the rest of the community is kept thinner than it need be until the patents have expired—a period that, in these days of rapid change, is often longer than that of the usefulness of the invention. Where firms reciprocally refuse to license, the best combination of technology is available to nobody. (4) Where cross-licensing is avoided or limited in order to conserve patent monopolies from antitrust attack, there is a similar shrinkage in the opportunity to achieve the best technological combinations. (5) When introduction of potential technology is delayed by negotiation or litigation about the validity of patents or about priority of invention or about the terms of license, the delay impairs technical progress; and the inherent uncertainty of patent boundaries and patent claims tends to enhance the occasions for such delays. (6) When licenses obligate licensees to refrain from using patents in particular types of activity or in particular territories, or when they impose restrictions upon use of other technology to accompany the licensed technology, these restrictive provisions prevent licensees from using the best available technology in as large a field as might otherwise be occupied by it. (7) When a firm makes insufficient disclosure of the know-how that is necessary to exploit a patent, it impedes use of that patent even by its licensees, except in instances in which the license includes supplementary know-how. Moreover, by thus restricting access to the knowledge that is the foundation of existing patents, the nondisclosure constitutes an obstacle to further invention and innovation by all other firms in the community.

Thus the process of seeking and then exploiting monopolistic patent rights includes, necessarily, types of activity that tend to retard technological progress. If the patent system is indispensable to R&D, and if it can rest upon no other type of incentive than the inducement of absolute monopoly rights, then these retardations are inevitable, and one can only hope that the stimulus exceeds their aggregate effect. But the purpose of this paper has been to raise questions about the validity of these *ifs*. If, in a world of large corporate laboratories and much subsidized research and development, we were to rethink the problem of incentives for initiation of such activities and conditions for the dissemination of the results, could we not evolve a system in which the anomalies and defects were less glaring?



# Patents: A Force for Competition and the Consumers' Best Friend

S. DELVALLE GOLDSMITH\*

THE TITLE OF THE CONFERENCE, "Enterprise Under Stress," is particularly apt. Everybody and everything seem to be under stress today: enterprise, entrepreneurs, producers and consumers, our economic system in general and our patent system in particular. Therefore our subtitle, "New Circumstances for Industrial Property," is also apt: stress causes strain and strain usually involves change. We must accordingly examine our industrial property system and see what changes are being made or should be made to meet the stresses of our time. By "industrial property" (now sometimes called "intellectual property") is meant patents, trademarks and copyrights but the present discussion will be confined chiefly to patents.

Our patent system is under attack. This is nothing new. Although patents are specifically provided for in the Constitution to "promote the progress of science and useful arts," their method of accomplishing this is by the grant of limited monopolies, and antimonopolists look upon any monopoly as something bad.

---

\* Partner, Ladas, Parry, Von Gehr, Goldsmith and Deschamps.

As a matter of fact, there were antimonopolists in England in the 1600's when our patent system was born. They secured passage of the famous "Statute of Monopolies" of 1628 which prohibited monopolies giving the King's favorites control over staple articles of commerce but excepted patent monopolies in these words:

. . . shall not extend to any letters patent . . . of the sole working or making of any manner of new manufacture within this realm. . .

In what ways can antimonopolists attack a patent system? There are basically three:

- (1) Eliminate patents.
- (2) Retain patents but eliminate their effect of stimulating innovation (and getting innovations to the consumer) by providing for compulsory licensing of all patents.
- (3) Reduce the value of patents by restricting the ways in which they can be used.

Route 1 is not often suggested these days. It was tried many years ago in Holland and Switzerland but patents are now granted in these countries as in nearly all others. Even the Communist countries have patent systems.

Route 2 would require licensing of all patents. The patentee would get a royalty (set by the Patent Office or courts and probably small) but any one who wanted to could use the invention. This would deal innovation a severe blow—almost as much as elimination of patents. At first, some research and development would continue at the usual expense. The rest of the business community would wait and see (without expense) what inventions were made and then take licenses for the ones they wished to use. Ultimately the first group would see the economic error of their spendthrift ways, and most practical research and development would then stop.

Route 2 has not been openly advocated by the antimonopolists—at least on a wide scale—presumably for the reasons just indicated. But in isolated instances (for instance in the Clean Air Amendments Act of 1970), it has been introduced. It is true that there are compulsory licensing provisions in the laws of foreign countries but these are particularly where there has been abuse of the patent monopoly by non-working of the invention within three years from the patent grant.

Route 3 (restricting patent rights) seems to be the favorite attack. Therefore it would seem useful to pass from the general to the specific at this point and consider this attack. In this connection we can refer to the statements of two prestigious attackers: Federal Trade Commissioner Mary Gardiner Jones and Ralph Nader and his "Public Interest

Research Group." (The U.S. Department of Justice is another attacker of patents granted by its sister Department of Commerce). The focus of their attack, at present, is directed against the so-called "Scott Amendments" (Appendix A) to the Patent Revision Bill (McClellan S. 643) now pending before Congress.

There are two Scott Amendments. The principal one (Amendment No. 24) is concerned with the restrictions which may be included in a patent license and what a licensee must do if he wants to attack the validity of the patent under which he is licensed, as now permitted by the *Lear v. Adkins* decision of the Supreme Court. The other one (Amendment 23) is concerned with preemption by the federal patent law of state laws and other federal laws relating to the protection of unpatented ideas.

The first thing to be noted in an analysis of the arguments against the Scott Amendments (based on Commissioner Jones' speech in Boston and a letter from Nader to Senator Scott) is that the Commissioner recognizes the value to the consumer of "the scientific and technological development of this country which is the primary goal to be served by the patent laws of this country" and recognizes that a persuasively advanced justification for the patent monopoly "is that only by such a protection can the requisite stimulus be provided for the heavy investment of time and resources which is required in creating the original invention and translating it into basic know-how and specific products and services available to the public and the nation." Nader does not say anything about this but, on the contrary, sees no good in anything about the patent system or patent lawyers. His arguments often descend to a series of aspersions on the Patent Bar, such as:

. . . overt attempt of the Patent Bar and the industry it services to consolidate economic power in the hands of patent owners at the expense of the American consumer.

The amendments . . . represent the interest of industry which seeks to consolidate more economic power in its hands and the Patent Bar who wishes to enhance their own status by making patents more desirable as a profitmaking device.

Nader does not seek to clarify or improve the amendments but demands that Senator Scott "repudiate" and "withdraw" them.

Let us begin with a consideration of Commissioner Jones' more substantive points, the chief of which seems to be that the amendments would adversely affect the present "delicate balance" between the patent and antitrust laws.

One of Commissioner Jones' principal objections to Amendment 24 is that it makes it clear that "field of use" and territorially restricted patent licenses are proper. In other words, if a patent covers an invention capable of being used for A or B, the patentee may have one licensee restricted to use A and another licensee restricted to use B. Or he may grant a license only for use A and keep use B for himself. Also, as a patent covers the entire country, the patentee may have one licensee for part of the country and another licensee for another part of the country. Or he may grant a license only for part of the territory and keep the remainder for himself.

It is hard to see how this type of license restriction can be bad as it merely subdivides the patent right but does not extend it. It is difficult to understand why advocates of "consumerism" oppose licensing of this type which is obviously favorable to the small inventor or small business man (the latter being more closely related to the consumer than a large corporation is). As owner of a patent, a large corporation with relatively unlimited resources can exploit it itself throughout the country or in restricted areas and fields as it desires. The "little" patentee on the other hand usually has not and cannot raise the capital for exploiting the invention himself. He is often dependent on licensing (assuming he has a valuable invention at all), and a prospective licensee may be able to pay him only enough for use of the invention in a limited field or area.

The above is not to say that all license restrictions are good. Thus, if I offer to grant a license only on the condition that my licensee stops supporting his wife, or on the condition that he does not sell to minority groups, or, to take the classical example, on the condition that he purchases unpatented material from me, I am obviously extending my patent control to something which has nothing to do with my invention. Such restrictions will be struck down under our antitrust laws regardless of the Patent Revision Bill and the Scott Amendments. Even in the 1628 Statute of Monopolies the exception in favor of patents was not absolute but only permitted patent grants

so as also they be not contrary to law or mischievous to the State, by raising prices of commodities at home, or hurt of trade, or generally inconvenient.

Certainly, almost 350 years later, we are capable of controlling "mischievous" use of patents without eliminating helpful and reasonable licensing practices.

Commissioner Jones also objects to patents as being adapted to perpetuate a monopoly, presumably through the patenting of improve-

ments when an original patent is about to expire. The answer to this is that the *patenting* of improvements is the result of the *inventing* of improvements. Thus the patent law does exactly what it is supposed to do—stimulate further invention. If the improvement is a minor one, the original invention will be used—free of royalty—after expiration of the patent which covered it. If the improvement is a major one, a licensee may wish to continue paying royalties so that he can use the improvement. The consumer will then have the improved product available to him. This is not perpetuation of the original patent monopoly but the grant of a new limited patent monopoly for a new product. As always, the patent system is *self-adjusting*—a large reward for an important invention and no reward, or a small one, for a minor invention. And all this without a proliferation of government evaluation and award agencies such as would be necessary for a system of individual awards instead of a patent system!

Nader's chief substantive argument seems to be against Section (f) (2) of Amendment 24 which states that a patent owner will not be guilty of misuse "because he has entered an arrangement granting rights under the patent that 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 and patent grant." Certainly this Section is concerned only with the licensing of rights "under the patent" and is not intended to legalize rights not coming under the patent monopoly. The language is rather broad, as recognized in a further amendment proposed by the Patent Bar which would insert the word "merely" before "because" so that the Section would not make such restrictions legal but only not make them *per se* illegal; the further amendment would also require the restriction to be "related to the disclosure and claims" of the patent. If Nader's objection to Section (f) (2) is breadth or unclearness of language, an effort should be made to change the language, as is being done by the Patent Bar as just noted.

The basic principle that a patent system properly administered exists for the benefit of the consumer and not to his detriment must be recognized. To improve the standard of living of the consumer, new and improved products must be available to him. Patents are granted as an incentive for inventors and manufacturers to establish new industries which will provide such products.

There is an inclination to stress the role of patents in rewarding the inventor and giving him an incentive to invent—but this is really not the most important function of a patent system. It has been said that

some inventors would invent anyway—without any special incentive. What a patent system does most importantly is to “bring new manufacture to the realm.” Because of the patent monopoly, the inventor or his assignee or licensee is willing to put money into development and commercialization of an invention in the belief that he will be able to recoup his investment and make a profit due to the exclusivity given by the patent grant. It is only in this way that the benefits of the invention get down to the consumer.

Another way in which a patent system (without compulsory licensing) stimulates innovation and competition is that a business man, seeing his competitor with a new patented product not available for license, must “invent around” the patent monopoly in order to stay in business. In other words he must create and commercialize a different product at least as good as and preferably better than his competitor’s product but not coming within his competitor’s patent monopoly. Thus patents which provide *exclusivity* promote *competition*. If, however, the second manufacturer could get a compulsory license under his competitor’s patent, he would have no incentive to “invent around” the patent; he could take a license and the consumer would have only one product at his disposal.

The second aspect of Amendment 24 concerns the right of a licensee to attack the patent under which he is licensed. The Amendment does not seek to overturn the rule of *Lear v. Adkins* giving the licensee this right but provides that, before he attacks the patent, he must renounce future benefit from the license. This does not seem unfair. Otherwise the licensee can play a game at which he can never lose: if he succeeds in destroying the patent he can use the invention without payment; if he fails, he can continue on the basis of the license he previously negotiated.

Amendment 23 involves a rather complicated legal situation and does not require discussion here especially as it does not change what is already in the Patent Revision Bill but only the wording.

It is interesting to note that Nader has recently taken a position against an antitrust exemption to automobile manufacturers to permit them to cooperate in the development of a pollution-free automobile. His reason for this is apparently that the Clean Air Bill (mentioned above) provides for compulsory licensing. This is consistent with his general position favoring compulsory licenses but hardly consistent with his position as a consumer advocate. Although he presumably wants a pollution-free automobile as soon as possible, he says, in effect, let one or a few firms engage in research and development in this field and

then the other firms can get compulsory licenses. This shuts out the consumer, first from the benefit of many programs of research and development and, second, from the benefit to be derived from other firms cooperating with the primary researches so as to provide the desired innovations in the best form and at the earliest possible moment.

Another recent position taken by Nader gives a good indication of a basic deficiency of compulsory licensing. While apparently in favor of compulsory licensing generally, Nader has opposed a proposal of the Department of Agriculture to grant exclusive royalty-free licenses under government-owned patents. This is consistent because compulsory licenses are usually nonexclusive. But here again the consumer should rear up against his alleged protector. If the development and merchandising of a patented idea will take a large amount of capital, a manufacturer will want the protection of exclusivity to justify his investment. If he is denied this, how will the products of the patent ever reach the consumer?

In connection with Nader's attack on the Patent Bar, it must be obvious to him as a lawyer that, in infringement litigation, just as many patent lawyers representing defendant infringers seek to destroy patents as patent lawyers representing plaintiff patentees seek to preserve them. This they must do as advocates of their clients' interests. On the other hand Nader is correct that, when it comes to patent law revision, patent lawyers are generally in agreement as to the need for legislative expression of a Rule of Reason in matters such as license restrictions. A patent lawyer wants to be able to give his client definite advice on fundamental principles of patent and antitrust law so that his client's agreements will be proper, thus reducing litigation time and expense. For this reason he tries to provide definiteness in patent law. If the patent lawyer was as anxious for litigation fees as Nader seems to think he is, he would fall right in line with Nader and leave these aspects of patent law so nebulous as to ensure a multiplicity of court actions at which the lawyer could appear on behalf of his client.

Patent lawyers are not opposed to progress and change as Nader seems to think (although it is true that lawyers are generally conservative as regards change as they are not able to give their clients definite advice as to the result of changes until there have been court decisions). Thus the present McClellan Bill, *which has the support of the Patent Bar*, would bring many important changes to the U.S. patent system such as the following:

- (1) Possibility of filing patent applications either by the inventor or owner of the invention, thus establishing harmonization with the rule in nearly every other country.
- (2) Application may be filed by an agent, thus making it possible to preserve the rights of the inventor or owner in urgent situations.
- (3) In the case of joint inventors, each inventor does not have to be involved in the invention of every claim. This simplifies the problem of when to designate a sole inventor or joint inventors and permits combination and simplification of applications and consequent saving of expense.
- (4) Change of the patent term so that it runs from the filing date (or the first of a series of filing dates) rather than from the grant date. This means that the term cannot be lengthened by slowness in prosecuting the application or by filing a series of applications.
- (5) Reexamination after grant. This gives anyone who thinks he may be prejudiced by the patent an inexpensive way to raise objections to the patent grant.
- (6) Grant of a patent to the first applicant where there are conflicting applications. This would simplify and reduce the expense of "interference" proceedings.

In addition to changes such as these, the parties in interest—namely the inventors, invention-owners, manufacturers and consumers, and the members of the Bar who represent all of these—should continue a study of our patent system in an effort to improve it, particularly in its fundamental aspects. Thus, standard of invention, Patent Office procedure (including possible "adversary" procedure in the Patent Office as suggested by former Supreme Court Justice Abe Fortas\*), early publication of patents, and reduction in the time and cost of patent litigation (including the possibility of specialized patent courts) are topics that should receive continuous and careful consideration. The real danger is that, because of imperfections which are inherent in any human system, those who are against patents may be able to destroy our patent system or modify it in such a way that it will no longer stimulate innovation.

As a specific example of attacks on patents, the remarks of the

---

\* Abe Fortas, "The Patent System in Distress," *IDEA*, Vol. 14, No. 4 (Winter 1970-71), p. 571.



distinguished economist, Dr. Corwin Edwards, should receive careful consideration.

Dr. Edwards' views are at first rather frightening since they are not merely that certain features of patent law or practice are objectionable but that fundamentally, patent laws are not effective as means to promote the progress of the industrial arts. However it is submitted that the facts and assumptions contained in Dr. Edwards' remarks do not support the latter conclusion.

Thus Dr. Edwards seems to be a supporter of patents for individual inventions and individual inventors even though he is violently against patents when invention is "science-based and systematic rather than sporadic" and "subject to control by relatively few large corporate organizations so far as it is not controlled by governments." It seems to the writer that this dichotomy disregards the continuing individual (and "sporadic," if you will) nature of some invention and, more importantly, disregards the realistic relativity of the present economy in which invention sponsored by small companies is just as individual and sporadic relatively to large corporate research as the sporadic invention of individuals (in Dr. Edwards' "good old days" of patents) was relatively to the smaller corporate enterprises of the time.

Dr. Edwards, in condemning the modern effectiveness of a patent system, also disregards the function of patents in stimulating competition among large corporate competitors. He really does not disregard this but, whenever he speaks of corporations "dove-tailing inventions end to end" to achieve control of an area of technology (more euphemistically, "building up a patent picture"), his remarks are always about *one* corporation engaged in this nefarious practice. What about the other corporations trying to do the same thing with *their* research and patent—either in a different direction of development or just "inventing around" their competitor's patents? Surely such competition, particularly among giant corporations, must be beneficial for the consumer.

Of course, if one corporate entity becomes so large and powerful and controls so many patents that it completely dominates an industry, this will generally be bad for the consumer. But we have our antitrust laws to take care of this. It has been said that some supporters of patents think they should not be subject to antitrust laws. It is not believed that this is the case: if it is, it is wrong. Patent laws and antitrust laws coexist—the only outcry by the Patent Bar regarding antitrust laws where they affect patent rights is for it to be made clear by legislation where the legitimate exercise of the patent right ends and a violation of

the antitrust laws begins. The latter was the purpose of most of the "Scott Amendments" to the current patent revision bill.

Dr. Edwards goes on to say that, if the term "invention" had not already been established in the law of intellectual property, the appropriate term "research and development" would now be used instead. Then he goes on to divide R&D into the following:

- (1) Basic Research—"too scientific to be patentable."
- (2) Development—"merely recombination of knowledge."
- (3) Applied Research—"devised to describe intermediate activity from which patents may conceivably flow."

While this subdivision has been made by Dr. Edwards in derogation of patents, it seems to the writer that this very subdivision is a pithy description of, and justification for, a patent system. Certainly patents should not (and are not) granted for scientific principles, permitting a patentee to control any development based on a scientific principle he has discovered. At the other end of the spectrum, patents should not be granted for what Dr. Edwards calls "recombination of knowledge" and what is called in "patentesque" (the peculiar language invented—but not patented—by the patent practitioner) "obvious to the skilled workman in the art." The intervening area (which Dr. Edwards and many others correctly call "applied research") is, it is submitted, the proper field for patents.

Dr. Edwards is not entirely consistent because, on the one hand he denigrates as patentable subject matter (as he should) "mere recombination of knowledge" but, on the other hand, seems to criticize the function of the courts "to look skeptically at such tenuous distinctions in order to withhold awards of patent monopoly from those whose work is pure science or is mere workmanlike recombination of existing knowledge." Here again, I think, Dr. Edwards has given us a description of how a patent system, such as we have in the United States, works—a patent is granted by an administrative body (the Patent Office) on the basis of a careful examination but without the test of *inter partes* action. However, when the patentee wants to enforce his patent, a court in an *inter partes* proceedings reaches its own conclusion as to whether the subject matter of the granted patent comes in Dr. Edwards' Category 3. If it comes in Dr. Edwards' Category 1 or 2, the patent is declared invalid.

Another argument advanced by Dr. Edwards against patents is that there is often inadequate disclosure of an invention in the patent application whereas an important consideration for the patent grant is

full disclosure of the invention so that other researchers will know what has already been done and so that industry can practice the invention when the patent is no longer in force. Apparently the reason for Dr. Edwards' conclusions is that some patent licenses are "bare" licenses of the patent right while others also include "know-how." Dr. Edwards says "So far as the latter type of license has become necessary, the patentee eats his cake and has it too."

It is difficult to see what is wrong in charging a licensee X if he only wants to operate within the scope of a patent, and X + Y if the licensee also wishes to have the benefit of the patentee's experience in carrying out the invention. Obviously, the patentee may never have put his invention into commercial use in which event it would certainly be more equitable to charge the licensee X rather than X + Y. On the other hand the licensee may wish to have the use of working drawings, manufacturing short-cuts, and engineering assistance from a manufacturing patentee and be willing to pay extra for this. He might even want to pay an additional Z if he could also use the patentee's trademark.

It would seem therefore that Dr. Edwards' objections in this respect relate to business practices rather than the patent system. As far as concerns actual "inadequate disclosure," i.e. withholding of essential information for carrying out the invention, this is carefully watched by the Patent Office where the patent application is studied by an examiner who is skilled in the art to which the invention relates. And, of course, even if an inadequate disclosure gets by the Patent Office it (and the patent) can be struck down by the court.

Certainly, Dr. Edwards would not suggest swamping the Patent Office with all available knowledge relating to an invention. He himself gives an example of an invention where "the know-how for a machine covered about 300,000 sheets [frames?] of microfilm."

It is interesting to note that the United States Patent Office requires a much fuller description of an invention than most foreign Patent Offices. This is one of the complaints of foreigners who seek patent protection here. Also, the United States patent law is one of the few requiring disclosure of the "best mode" known to the inventor for carrying out his invention. Most foreign laws are satisfied by a disclosure sufficient to enable someone skilled in the art to carry out the invention.

Dr. Edwards does not stress, as much as some previous critics of the patent system have, the "bogey" of unused or withheld patents. However he suggests that a patent system "induces firms to explore technologi-

cal possibilities that they have no present desire to use"—presumably then to employ the patents for blocking purposes only. Apart from the fact that there may be some per se desirability in exploring new technological possibilities, utilization studies conducted by The PTC Research Institute indicate that 55-65 percent of assigned patents are used commercially. It is interesting to note that the same studies show that only 40-50 percent of unassigned patents (presumably these are the "individual" inventions looked upon with favor by Dr. Edwards) are so used.

Dr. Edwards puts his finger on a problem of our patent system or any patent system in deciding to whom to award a patent in the case of simultaneous or nearly simultaneous independent inventions of the same inventions by different inventors. Under United States patent law, an effort (sometimes rather complicated and expensive) is made to grant the patent to the *first inventor*. In most other countries, the patent is granted to the *first to file his application in the Patent Office*. Moreover many countries (contrary to U.S. practice) permit an independent inventor to continue use of an invention in his possession before the other inventor's filing date. Admittedly, none of these solutions is a perfect one but Dr. Edwards does not offer a different solution except, perhaps, to abolish patents entirely. It is submitted that, while this might be an easy way out of a difficult problem, it would not be advantageous for inventors, the public, or the economy generally.

A final criticism by Dr. Edwards seems to be that, even if a patentable invention is invented by the "applied research" of a corporation, they really don't deserve to own the patent right (1) because some of the research cost may have been paid for by the government, and (2) because the cost of the research is tax-deductible as a business expense. It is submitted with respect that, on this point as well as many others in his paper, Dr. Edwards does not seem to be antipatent at all but rather antibusiness. If a corporation is not allowed to designate research costs as a business expense, why should any overhead—rent, clerical salaries, desks, advertising, et cetera—be deductible? As far as government contribution to research is concerned, certainly this can be (and is) controlled by laws other than the patent laws.

Where there is abuse of patents or business practices, this can be controlled by law; it is not necessary to throw out the babies (patents and business) with the bath water of abuse.

The Kettering Award  
Address

The Kettering Award Address was given by Walter J. Derenberg, Professor of the New York University School of Law and partner in the law firm of Von Maltitz, Derenberg, Kunin, & Janssen, New York. Dr. Derenberg was presented the Award at a luncheon in his honor at the Fifteenth Annual Conference of The PTC Research Institute held on October 20, 1971, at the Shoreham Hotel in Washington, D.C. Dr. Derenberg received the Institute's 1970 Charles F. Kettering Award in recognition of his outstanding contributions in research, education and public service relating to the field of industrial and intellectual property.

# Consumerism and "Old-Fashioned Commercial Honesty"

WALTER J. DERENBERG\*

AS THE TITLE OF MY PAPER SUGGESTS, it will be concerned not only with the current tremendous surge for all kinds of consumer protection both here and abroad, but it will consider the sometimes conflicting role which consumer protection plays or should play within the much more neglected law of unfair competition in the narrower sense of the word, i.e., the rules of fair play and fair competition which our courts should enforce as between one or more competitors or associations of competitors, regardless of their ultimate financial effect on the consumer.

It has become a matter of great concern to most of us that, particularly since the Supreme Court's decisions in the *Sears, Roebuck* and *Compco* cases,<sup>1</sup> the private law of unfair competition has become emasculated and that little room has been left for the principles of "old fashioned commercial honesty" which the lower court in the two

---

\* Professor of Law, New York University School of Law; partner, Von Maltitz, Derenberg, Kunin & Janssen.

<sup>1</sup> *Sears, Roebuck & Co. v. Stiffel Company*, 376 U.S. 225; *Compco Corp. v. Day-Brite Lighting, Inc.*, 376 U.S. 234 (1964).

quoted decisions had sought to enforce in product simulation cases in which the plaintiff's patents had been held invalid.<sup>2</sup> It will be recalled that in sweeping dicta, the late Mr. Justice Black observed that not only in patent cases but in copyright cases as well, the federal law had preempted the field to such an extent that our state courts could not (except with regard to the protection of labeling and "distinctive dress") grant protection against imitations or simulations even where a competitor imitated "nonfunctional" elements, and that regardless of the defendant's motives and of the secondary meaning and celebrity which the plaintiff's product may have acquired. Only in a footnote reference to Section 2 of the Copyright Act of 1909 did Mr. Justice Black refer to the fact that the copyright act itself preserved the common law copyright in "unpublished" works.

The main purpose of my paper today then is not to join the already massive efforts toward better protection of the consumer against fraudulent advertising and other forms of deception, but to inquire what has become, both nationally and internationally, of that branch of our law which traces its origin to the famous *Associated Press* case<sup>3</sup> in 1918 and which applied principles of commercial honesty in granting protection against misappropriation and other newly developed private law concepts in controversies primarily involving competitive interests rather than only the ultimate benefit to the consuming public.

With regard to present and future trends of consumerism, we are all aware from day to day of a multitude of efforts, both prospectively and under existing law, to enhance and strengthen consumer protection. Indeed, the need for more effective government protection of consumers is almost unanimously recognized and the question before us—and particularly before the Congress—is only which form of Congressional action might most adequately and expeditiously further such needed protection. Since the advent of "Naderism" and since the report of the American Bar Association Commission to study the Federal Trade Commission of September 15, 1969,<sup>4</sup> little doubt has been left

---

<sup>2</sup> *Stiffel Company v. Sears, Roebuck and Co.*, 313 F.2d 115 (7th Cir. 1963); *Day-Brite Lighting, Inc. v. Compco Corp.*, 311 F.2d 26 (7th Cir. 1962). It was in the second lower court decision that Judge Knoch quoted Judge Duffy's statement in *Radio Shack Corp. v. Radio Shack*, 180 F.2d 200, 206 (7th Cir. 1950) that the essence of "unfair competition" is that it be unfair, and that "in all cases of unfair competition, it is principles of old-fashioned honesty which are controlling."

<sup>3</sup> *International News Service v. Associated Press*, 248 U.S. 215 (1918).

<sup>4</sup> Published by the American Bar Association, Chicago, Illinois (1969), 119 pages. The report was requested by President Nixon and was rendered by a 16-man commission, under the chairmanship of Miles W. Kirkpatrick, with Prof. Robert Pitofsky acting as counsel to the commission.



that traditional methods of Federal Trade Commission practice under section 5 of its act have proven much too time-consuming, too uncoordinated and lacking in teeth in connection with the suppression of false advertising. The chairman of the highly critical report of the ABA Commission and its counsel presently hold the high offices of Chairman of the Commission and Chief of its Consumer Protection Division, respectively, and we are all aware that an entirely new wind is blowing in recent months toward more effective enforcement by "corrective" advertising and other methods. No longer is it likely that it may take several decades before a misleading advertisement of "Carter's Little Liver Pills" may be publicly corrected by eliminating any reference to the word "liver," nor would it seem likely under present policies that such a case may reach the United States Supreme Court on two separate occasions.<sup>5</sup>

It is not known at the present time which of the currently pending consumer protection bills will ultimately become the law and, if so, in what form. As of the present moment, there are at least four bills<sup>6</sup> pending in the 92nd Congress, under at least three of which consumer class actions are contemplated. Only the so-called Administration Bill S. 1222 entitled "The Consumer Fraud Prevention Act of 1971" (Appendix (C)) would not provide for the almost unlimited type of consumer class action which is contemplated under the three other previously mentioned bills. Without going into detail at this point, suffice it to say that, as of June 28, 1971, a majority report of the Consumer Protection Committee of the Antitrust Section of the American Bar Association reiterated its earlier view that the type of consumer class action proposed by these three bills, H.R. 5630, S. 984 and S. 1378 (Appendix D), should not be favored. In referring to its earlier report, the majority states:

Moreover, the several legislative proposals do not accomplish their intended remedial and deterrent purposes on the national level, but instead espouse a time-consuming, unwieldy and inefficient mechanism to confront all wrongs—class actions—which may be more likely to hinder rather than foster optimum consumer protection. In effect these proposals may provide but a shadow remedy.

The majority then added that in its opinion:

Additional local consumer agencies or a system of small claims courts, masters or arbitrators can quickly and easily be woven into

---

<sup>5</sup> *Carter Products, Inc. v. FTC*, 268 F.2d 461 (9th Cir.) *cert. denied*, 361 U.S. 884 (1959).

<sup>6</sup> See Report of the Consumer Protection Committee, American Bar Association, Antitrust Section, Concerning Proposed Consumer Class Action Legislation, June 28, 1971, prepared by Alfred W. Cortese, Jr.

the fabric of a federal consumer protection program and established under the administrative aegis of the Justice Department, the Federal Trade Commission or a new agency such as the Federal Trade Practices Agency as suggested in the report of the President's Advisory Council on Executive Organization [the "Ash Report"]. Coordinating such local agencies at the national level through a federal agency such as Justice or FTC should ensure treatment of both national and local problems.<sup>7</sup>

However, in a much more detailed Minority Report of June 6, 1971,<sup>8</sup> a contrary view has been expressed. In the Minority Report it is stated, *inter alia*:

The class action simply requires the court at an early stage to conduct proceedings leading to a determination of the validity of the class action. Apart from that, pretrial discovery and basic proof of liability at trial are no more complicated by having a class action than by having only an individual action.<sup>9</sup>

This minority statement is, of course, in accord with the view expressed by Senator Tydings on two occasions when he introduced S. 1980, the Class Action Jurisdiction Act, in the Senate in 1969.<sup>10</sup> Personally, and based upon recent experience in foreign countries, I share the Majority Report's point of view that it would not further the ultimate interest of the American consumer if our courts were overburdened with the type of class action presently contemplated in the three above-mentioned bills, and that these may well lead to considerable misuse of the types which have already occurred in foreign countries.

It may be of interest to note in this regard that since the German law by recent amendment<sup>10a</sup> permitted suit for unfair competition not only on behalf of trade associations in the involved competitive area

<sup>7</sup> *Ibid.*, at pp. 2-3.

<sup>8</sup> Minority Report of the Consumer Protection Committee, American Bar Association, Antitrust Section, Concerning H.R. 5630, S.984 and S.1378—"The Consumer Class Action Act of 1971" and S. 1222—The Consumer Fraud Prevention Act of 1971 (92nd Congress, 1st Session), July 6, 1971, prepared by Herbert B. Newberg.

<sup>9</sup> *Ibid.* p. 45.

<sup>10</sup> 115 Cong. Rec. S4163-4164, No. 67, April 25, 1969, and 115 Cong. Rec. S11411-S11412, No. 156, Sept. 26, 1969.

<sup>10a</sup> Law of July 21, 1965, 1965BGB1.I, 625. According to the act, the right of complaint was given those associations "whose chartered purposes include the protection of the interests of the consumer through information and advice, provided that the associations are empowered to file complaints in civil law disputes." This was subsequently amended by an act of June 26, 1969, which provides for injunctive relief on behalf of consumer groups "provided that the complaint concerns deceptive assertions about goods or commercial services or some other transaction for purposes of competition through which the essential interests of the consumer are affected." However, no right to recover damages is provided.

(this had always been permitted) but also on behalf of consumer groups generally, numerous instances have occurred where, for instance, a lawyer husband formed an association with his wife or secretary, then picked up some alleged unfair methods of advertising or other form of unfair competition and brought suit on behalf of such newly established "group" in the expectation of at least receiving a fee for his action on behalf of the "consumer group."

Professor Schricker, in his profound recent study of this problem, states:

The introduction of the consumer association right of complaint did not bring entirely gratifying results in Germany. In more than a few cases, the proceedings have followed this pattern: A young attorney joins together with his wife, office personnel, and a few friends to form a consumer association, and he assumes permanent legal representation of the group. Then begins an industrious search for competition violations, particularly in middle class shops, where, for example, a forbidden premature start of an end-of-season sale, a violation which is apparently commonplace among such merchants, may be found. After each inspection run, a flood of warning letters and threatened court orders flows to the management of the now disconcerted enterprises, which, if they surrender or lose before the court, must bear the attorney's costs. It may be assumed that the association was formed in order to increase the lawyer's intake of fees.<sup>11</sup>

Professor Schricker recognizes, however, at the same time, that not only in Germany but elsewhere in Europe genuine consumer interests in what Senator Magnuson referred to in his book as *The Dark Side of the Market Place*,<sup>12</sup> have found increasing protection as a rather novel branch of law closely interwoven with the law of unfair competition, if not indeed a part thereof.

Among recent "consumer developments," Professor Schricker refers, for instance, to the Final Report of the Committee on Consumer Protection in England of 1962 which resulted in the enactment of the Trade Descriptions Act of 1968 providing criminal and administrative machinery for the suppression of deceptive advertising.<sup>13</sup> He also refers to the recent conference on "Fair Trade and the Consumer in Western European Law" which met in Cambridge in 1969, a subject thoroughly discussed in the monumental study on the law of unfair competition in the member states of the European Common Market authored by

---

<sup>11</sup> Gerhard Schricker, "Unfair Competition and Consumer Protection in Western Europe," 1 ICC (*International Review of Industrial Property and Copyright Law*) 415, No. 4, 1970, at p. 430.

<sup>12</sup> Magnuson-Carper, *The Dark Side of the Market Place* (1968).

<sup>13</sup> The so-called "Malony Report" (London: Board of Trade, 1962).

Professor Ulmer and his Staff at the Max-Planck-Institut in Munich.<sup>14</sup> Nor are these efforts limited to continental Europe. As recently as October 4, 1971, the Chairman of the Canadian Consumer Council stated, with regard to the proposed Competition Act in Canada, that the act is intended to put an end to the hypothetical "credulous man" and that the usual "puffery" which is thought to be disbelieved by any "reasonable" man would no longer be permitted. He is quoted as having said: "The consumer will be able to sue advertisers for what amounts to breach of contract if the product does not perform as the ads claimed it would."<sup>15</sup> A small-claims type of court would be created for this purpose.

In the meantime, a Congressional controversy continues with regard to the setting up of a Special Consumer Protection Agency and its proposed role. As of September 28, 1971, the House Government Operations Committee approved a bill to establish an independent federal agency, to advocate and protect consumer interests with authority to intervene on behalf of consumers in proceedings before regulatory agencies.<sup>16</sup> The establishment of such an agency was criticized by some members of Congress, by Mr. Nader, and others, as not going far enough in having independent investigative and subpoena powers.<sup>17</sup> This is in sharp contrast to the view of the Administration, which (correctly, in my opinion) had opposed the concept of an independent consumer protection agency on the ground that it would unnecessarily add new machinery to the federal bureaucracy.<sup>18</sup> Despite Administration opposition, it seemed fairly certain as of September 25, 1971, that a consumer agency stronger than that favored by the Administration might ultimately come into being.<sup>19</sup>

Most recently it has become known that as of the end of September 1971, Senator Hart introduced S. 1823, an amendment to the Federal Trade Commission Act, which would read in part:

---

<sup>14</sup> Ulmer, *Das Recht des Unlauteren Wettbewerbs in den Mitgliedstaaten der EWG* (Munich: C. H. Beck'sche Verlag, 1965).

<sup>15</sup> *Advertising Age* (Oct. 4, 1971), at p. 77.

<sup>16</sup> According to the *New York Times*, the House passed this bill on October 14, 1971, and hearings are now expected to be held in the Senate by a Government Operations Subcommittee headed by Senator Ribicoff on a similar "landmark" bill. The Senate will also consider the House bill. *New York Times* (Oct. 14, 1971), at p. 1.

<sup>17</sup> *New York Times* (Sept. 28, 1971), p. 27.

<sup>18</sup> *New York Times* (Sept. 13, 1971), p. 19.

<sup>19</sup> "A Strong Consumer Agency Takes Shape," *Business Week* (Sept. 25, 1971), p. 45.

Any person, partnership, or corporation who shall be injured in his business or property by any other person, partnership, or corporation by reason of any unfair method of competition in commerce, or unfair or deceptive acts or practices in commerce forbidden or declared to be unlawful by this section, may sue therefore in any district court of the United States in the district in which the defendant resides or is found, or has an agent, without respect to the amount in controversy; and shall recover threefold the damages by him sustained; and the costs of suit, including a reasonable attorney's fee.

The bill further provides that an order to cease and desist of the Commission which has become final shall be prima facie evidence against such defendant and that such suits for damages shall be brought within three years from the Commission of the unfair methods of competition or unfair or deceptive acts or practices.<sup>20</sup>

In the meantime, some rather bizarre efforts have been made on behalf of groups of individual consumers to seek relief in certain instances of alleged consumer fraud by private causes of action based on allegedly existing principles of the law of unfair competition and, more specifically, Section 5 of the Federal Trade Commission Act (Appendix B). These have been quite unsuccessful thus far and, in my opinion, rightly so. I refer particularly to the case of *Holloway v. Bristol-Myers Corporation*,<sup>21</sup> in which an action for injunctive relief, compensatory and punitive damages was brought by two women, one of whom claimed to have been damaged by the purchase of six bottles of "Excedrin" which, in her opinion, did not live up to the advertising for that product. The other individual plaintiff based her claim on a theory of "public nuisance" as a result of having been subjected to reading these advertising claims or having had to listen to them on television. Joined as plaintiffs in this adventurous private action was a Federation of Homemakers, as well as a consumer association of the District of Columbia. Judge Jones dismissed the action on the ground—decided before many times—that Section 5 of the Federal Trade Commission Act does not furnish a basis for a private cause of action, either directly or under the "doctrine of implication." It was held that the plaintiffs neither stated a cause of action under the FTC Act nor a common law cause of action which could even remotely approach the necessary jurisdictional minimum amount of \$10,000 damage. With regard to the common law action and the alleged claim of "public nuisance," the court said:

---

<sup>20</sup> The bill was referred to the Senate Commerce Committee.

<sup>21</sup> 327 F.Supp. 17 (D.C. D.C. 1971).

Moreover, this Court has considered such factors as the probable extent of the plaintiffs' discomfort, the lack of physical damage to any property, the plaintiffs' ability to avoid some of the discomfort, and the nature of the interferences with property rights for which the law has traditionally granted relief and finds the plaintiffs' novel theory of a tort nuisance of advertising to be insubstantial.<sup>22</sup>

Alleged damage claims under Section 5 of the FTC Act had been previously rejected, *inter alia*, in *Frederick Chusid & Co. v. Marshall Leeman & Co., Inc.*<sup>23</sup> in the following words:

The sixth claim is for money damages and an injunction for alleged violation of the antitrust laws, said to be Section 5 of the Federal Trade Commission Act (15 U.S.C. §45). This claim is plainly without merit because there is no private action for damages under the "antitrust laws" for violation of the Federal Trade Commission Act. That Act is not one of the "antitrust laws" as defined in the Clayton Act (15 U.S.C. §12). *Cf. Nashville Milk Co. v. Carnation Co.*, 355 U.S. 373, 375 (1958). There is no private right of action under Section 5 of the Federal Trade Commission Act. *Carlson v. Coca-Cola Co.*, 318 F. Supp. 785 (N.D. Calif. 1970).<sup>24</sup>

In the *Carlson* case, a private individual had sued on his own behalf and that of innumerable others on the ground of incorrect and misleading allegations in connection with a contest entitled "Big Name Bingo." The court held that the federal district court lacked jurisdiction since no private cause of action or any form of private class action could arise under Section 5 of the FTC Act. The same result was reached in the still more recent case of *State of Florida v. Eli Lilly & Co.*,<sup>25</sup> in which it was held that no private right of action for damages could be alleged under the Federal Food, Drug, and Cosmetic Act.

Equally unsuccessful—and, in my opinion, quite rightly so—have been recent efforts to place ordinary consumer complaints, which, in most instances, would give rise to private actions of breach of contract or warranty, under the mantle of Section 43 (a) of the Lanham Trademark Act (Appendix E), where, historically speaking, they do not belong. As I have pointed out elsewhere,<sup>26</sup> this section was a somewhat improved provision based on Section 3 of the amendatory Trademark Act of 1920, which had sought, in a rather inadequate way, to codify this country's international obligation under the Paris Convention to

<sup>22</sup> *Ibid.* at 24.

<sup>23</sup> 168 U.S.P.Q. 755 (S.D. N.Y. 1971).

<sup>24</sup> *Ibid.* at 769-770.

<sup>25</sup> 329 F.Supp. 364 (S.D. Fla. 1971).

<sup>26</sup> Derenberg, "Federal Unfair Competition Law at the End of the First Decade of the Lanham Act: Prologue or Epilogue?" *New York University Law Review*, Vol. 32 (June 1957), pp. 1029-1065.

give protection against false designations of origin by those who were located in the geographic locality involved and against the use of false descriptions by competitors. It may be recalled that in the first case ever brought under Section 43 (a), a person, whose claim under the Federal Employers' Liability Act had been barred by the statute of limitations, conceived the idea that in a malpractice suit he could now allege a "false description" (or, should we rather say, a false *prescription*?) under the Lanham Act.<sup>27</sup> His suit was, of course, dismissed, but it remained true that in 1956, almost ten years after the act was passed, Judge Clark of the Second Circuit could still say: "[T]here is indication here and elsewhere that the bar has not yet realized the potential impact of this statutory provision."<sup>28</sup>

How times have changed! Apparently the section is now again sought to be invoked as part of the consumer movement in situations for which it was obviously not intended. In the recent celebration ceremony in this very hotel of the 25th anniversary of the enactment of the Lanham Act,<sup>29</sup> Mrs. Virginia Knauer, the President's Special Assistant for Consumer Affairs, said "[The] Lanham Act has obvious consumer aspects." Then she asked the following rhetorical question:

[Do you think that] the very broad language of the Lanham Act, permitting suits by "any person who is or believes he is likely to be damaged" by any "false designation of origin or any false description or representation" will forever go unnoticed? I doubt it. We may very well see repeated tests of consumers' standing under this provision, notwithstanding any prior interpretations of the law.<sup>30</sup>

That Mrs. Knauer was somewhat misinformed or, at least, overoptimistic has recently been demonstrated by the significant case of *Colligan et al v. Activities Club of New York, Ltd.*,<sup>31</sup> in which a class action was brought under Section 43 (a) by a group of students who allegedly had been deceived by misrepresentations of a travel agent who had advertised a ski tour under all kinds of promises which failed to materialize. In observing that the issue of consumer standing to sue under Section 43 (a) was one of first impression in the Second Circuit,

<sup>27</sup> *Carpenter v. Erie R. R.*, 132 F.2d 362 (3d Cir. 1942), *cert. denied*, 318 U.S. 788 (1943).

<sup>28</sup> *Maternally Yours, Inc. v. Your Maternity Shop, Inc.*, 234 F.2d 538 at 546 (concurring opinion) (2d Cir. 1956).

<sup>29</sup> National Briefing Conference on the Twenty-Fifth Anniversary of the Lanham Act, June 17-18, 1971, Washington, D.C., reported in *BNA's Patent, Trademark & Copyright Journal, News & Comment*, No. 33 (June 24, 1971), at p. A-1 *et seq.*

<sup>30</sup> *Ibid.* at p. A-2 and A-3.

<sup>31</sup> 442 F.2d 686 (2d Cir. 1970).

the court, in a lengthy opinion by Judge Moore, unanimously came to the conclusion, based on legislative history, that Section 43 (a) of the trademark registration act had been intended to create both a special and limited unfair competition remedy "without regard for the interests of consumers generally and almost certainly without any consideration of consumer rights of action in particular. The Act's purpose, as defined in Section 45, is exclusively to protect the interests of a purely commercial class against unscrupulous commercial conduct."<sup>32</sup>

This interpretation I must endorse, despite my sympathy with the victims in this ill-fated adventure. It is understood that the unsuccessful plaintiffs in this class action recently filed a petition for certiorari in the Supreme Court on the issue of consumer standing under the Lanham Act, which is reported at some length in BNA's *Patent, Trademark & Copyright Journal*.<sup>33</sup> According to the petitioner's attorney in his scholarly brief:

The exercise of federal jurisdiction affords the only solution to these problems. The federal courts alone are authorized to issue nationwide injunctions. Unlike state courts, the district courts can entertain as part of a class action claims arising among parties and regarding transactions entirely outside their districts. Efficient national enforcement of federally awarded damages can be obtained by merely registering the original judgment in any federal court.<sup>34</sup>

The brief then quoted President Nixon's message on consumer protection as follows:

The damage suffered by any one consumer would not ordinarily be great enough to warrant costly, individual litigation. One would probably not go through a lengthy court proceeding, for example, merely to recover the cost of a household appliance.<sup>35</sup>

Personally, I doubt whether the Supreme Court, as it may soon be newly constituted, will be any more sympathetic to this type of private action than was a pre-Lanham Act court (consisting of three judges who subsequently became justices of the Supreme Court) in the famous *American Washboard* case,<sup>36</sup> although that case had involved a *competitive* situation which today would squarely come within the scope of Section 43 (a). It may be recalled that in the *Washboard* case, the court had said:

---

<sup>32</sup> *Ibid.* at 692.

<sup>33</sup> *News & Comment*, No. 39 (August 4, 1971), at p. A-7 *et seq.*

<sup>34</sup> *Ibid.* at p. A-8.

<sup>35</sup> *Ibid.* at p. A-11.

<sup>36</sup> *American Washboard Co. v. Saginaw Mfg. Co.*, 103 Fed. 281 (6th Cir. 1900). (The judges were Taft, Lurton and Day.)



It is doubtless morally wrong and improper to impose upon the public by the sale of spurious goods, but this does not give a private right of action, unless the property rights of plaintiff are invaded. There are many wrongs which can only be righted through public prosecution and for which the legislature and not the courts must provide a remedy.<sup>37</sup>

The court remarked that, otherwise, a veritable "Pandora's box" of litigation would be opened.<sup>37a</sup>

This, then, brings us back to the basic and original theme of my present address: In all the storm—political and otherwise—about consumer protection, we should not lose sight of the fact that here and in almost all other countries the law of unfair competition is and should continue to be a code of ethics and fair conduct directed to the protection of "old-fashioned commercial honesty" and legitimate interests of competitors, even if such body of law may in some instances appear in superficial conflict with the financial interests of the ultimate consumer. In other words, the fact that as a result of price-cutting, price wars, price discrimination, design or record piracy, or any other form of unfair conduct the consumer may be able to obtain a product at a cheaper price should not blind us to the fact that an equity court should decide such cases not by judging them on the basis of a windfall or "loss-leader" to the consumer but bearing in mind that small business and small competitors also are members of the general public and that an important "public interest" does exist in all countries to insure fair competition as between competitive organizations. If it had not been in recognition of this basic principle, the entire law of unfair competition, both in its national and international aspects, would never have come into existence. It was this idea which pervaded the Supreme Court's landmark decision in the *Associated Press* case<sup>38</sup> where the Court said for the first time:

The fault in the reasoning lies in applying as a test the right of the complainant as against the public, instead of considering the rights of complainant and defendant, competitors in business, as between themselves. . . . Stripped of all disguises, the process amounts to an unauthorized interference with the normal operation of complainant's legitimate business precisely at the point where the profit is to be reaped, in order to divert a material portion of the profit

---

<sup>37</sup> *Ibid.* at p. 285.

<sup>37a</sup> It is interesting to note that until recently trade associations as distinctive from "consumer groups," which are still excluded, were not even permitted to file opposition proceedings in this country; this has been changed as a result of *Tanners' Council of America, Inc. v. Gary Industries, Inc.*, 169 U.S.P.Q. 608 (CCPA 1971).

<sup>38</sup> *International News Service v. Associated Press*, 248 U.S. 215 (1918).

from those who have earned it to those who have not; with special advantage to defendant in the competition because of the fact that it is not burdened with any part of the expense of gathering the news. The transaction speaks for itself, and a court of equity ought not to hesitate long in characterizing it as unfair competition in business.<sup>39</sup>

It was the same philosophy which led the late Judge Jerome Frank, in his concurring opinion in a dispute involving the use by the plaintiff of the trademark "V-8" for vegetable juice as against defendant's use of practically the same trademark for a vitamin product, to observe:

... usually where the economic interest of consumers conflicted with the economic interest of the competitor, only the consumer interest was judicially considered. Yet, in intervening in the "unfair competition" cases, the courts at first seemed to have directed their attention primarily to the adverse effects of unethical business activities on business competitors and to have paid relatively little heed to the interest of consumers. For it does not follow that because conduct is unfair to a business rival it will harm consumers: By practices which are unethical when viewed from the angle of his competitors, a businessman is frequently able to undersell them; the resultant lowered prices ease the strain on his customers' pocketbooks fully as much as if he had acted "fairly."<sup>40</sup>

I do not believe that the Supreme Court in recent years, particularly in the *Sears* and *Compco* decisions,<sup>41</sup> intended to set aside this principle, which is the foundation of the law of unfair competition in every civilized country in the world. It is noteworthy that in denying protection against slavish imitation of unpatented (and, by dictum, uncopyrighted) material, the Court never once mentioned the *Associated Press* case and that no indication is found in either *Sears* or *Compco* that the Court intended to overrule its earlier decision. In only one federal case since *Sears* and *Compco* has a court of appeals (in what I consider to be an ill-considered opinion) expressed the view that the *Associated Press* case was no longer the law. I here refer to the *Paladin* litigation<sup>42</sup> in which the Court of Appeals for the First Circuit set aside a jury verdict awarding the creator of the "Paladin" character a substantial amount of money on the basis that a large network had, without doubt, imitated the plaintiff's style, name and visiting card and practically every other element of his personality. Although admitting that the network was a "pirate," the court felt bound to deny the

---

<sup>39</sup> *Ibid.* at 239-240.

<sup>40</sup> *Standard Brands, Inc. v. Smidler*, 151 F.2d 34, at 40 (2d Cir. 1945).

<sup>41</sup> *Sears, Roebuck & Co. v. Stiffel Company*, 376 U.S. 225; *Compco Corp. v. Day-Brite Lighting, Inc.*, 376 U.S. 234 (1964).

<sup>42</sup> *Columbia Broadcasting System, Inc. v. De Costa*, 153 U.S.P.Q. 649 (1st Cir. 1967).

plaintiff any legal protection, amplifying its ruling with the rather grotesque observation that the result might have been different if the plaintiff had used the symbol © on the chess piece that appeared on his visiting card.

More decisions of this sort would seem to invite the Bar to attempt to claim copyright protection even where it is obviously not appropriate because the failure to do so would eliminate any hope of protection against pirates and unfair competitors *ab initio*.<sup>43</sup> It is gratifying to say that while immeasurable damage has already been done in a number of unfair competition cases where the courts felt duty bound to follow *Sears* and *Compco*,<sup>44</sup> there are at least an equal number of cases involving title protection, trade secret cases, and, most importantly, cases involving direct and complete copying, rather than imitation, as well as some common law copyright infringement cases, in which lower courts, both state and federal, have refused to consider themselves bound by *Sears* and *Compco*.<sup>45</sup>

However, I submit that more than such piecemeal judicial action is needed. For instance, in recent months—and, indeed, at this very moment—the dubbing and counterfeiting of phonograph records has

<sup>43</sup> Derenberg, "Product Simulation: A Right or a Wrong?" *Columbia Law Review*, Vol. 64 (1964), p. 1192.

<sup>44</sup> For the latest such case, see *Press Publishing Co. v. Atlantic County Advertiser, Inc.*, 108 N.J. Super. 75, 260 A.2d 6 (1969), where the court rejected plaintiff's argument that the *International News* case and recent cases following it were controlling, and found *Sears* and *Compco* to relate more closely to the case at Bar.

<sup>45</sup> See, for instance, *Downey v. General Foods Corporation*, 323 N.Y. Supp. 2d 578 (App. Div. 1971). In *Beconta, Inc. v. Larson Industries, Inc.*, 350 F.Supp. 116 (N.D. Ill. 1971), Judge McGarr, in distinguishing *Sears* and *Compco*, said: "It is difficult to assume that the United States Supreme Court intended by these decisions to remove from the states and their courts all power to deal equitably with traditional concepts of unfair competition, and equally difficult to assume that the decisions were intended to deprive the Federal Courts of the power to apply time-honored principles of the law of unfair competition to litigants before the Federal Court by virtue of diversity of citizenship." (330 F.Supp. at 120.) See also discussion and cases cited in Bricker, "Thirty Months After *Sears* and *Compco*," *Bulletin of the Copyright Society*, Vol. 14 (1967), p. 293; Latman, "Fifteen Years After *Mazer v. Stein*: A Brief Perspective," *Bulletin of the Copyright Society*, Vol. 16 (1969), p. 278; Gamboni, "Unfair Competition Protection After *Sears* and *Compco*," *New York University Law Review*, Vol. 40 (1965), p. 101; Ahrens, "The Misappropriation Doctrine After *Sears-Compco*," *University of San Francisco Law Review*, Vol. 2 (1968), p. 292; Treece, "Patent Policy and Preemption: The *Stiffel* and *Compco* Cases," *University of Chicago Law Review*, Vol. 32 (1964) p. 80; and Derenberg, "Copyright Law," *Annual Survey of American Law 1969/1970* at p. 722; 1970/1971 at p. 524. See also the Annual Reports of the Register of Copyrights for the fiscal years ending June 30, 1968, June 30, 1969, and June 30, 1970.

reached such alarming proportions that not only have some states outlawed this practice, but it has become obvious that only a national law, even if it should antedate the much needed general copyright law revision, would put a halt to this grossly unfair and unethical practice no matter if a consumer should be able to buy what may well be an inferior recording at a cheaper price.

As recently as September 22, 1971, the House Subcommittee of the Committee on the Judiciary, through its chairman, Congressman Kastenmeier, reported out favorably S. 646 (Appendix F),<sup>46</sup> which will recognize a limited copyright in sound recordings and which has the support of even the Department of Justice, the Department of Commerce and the Librarian of Congress. S. 646 has passed both Houses of Congress as of the middle of October 1971 and now awaits the President's signature.<sup>47</sup> While it recognizes no performing right in phonograph records, the act will at least substitute a more effective *national* law for the efforts of various state legislatures to outlaw this practice. Such federal action was forcefully recommended by a distinguished expert in this field before this Institute as long as four years ago.<sup>48</sup> The new act will certainly put an end to the outrageous practice in some states in which record dubbers had the audacity openly to state on piratical tapes:

No relationship of any kind exists between [the pirate] and the original recording company, nor between this recording and the original recording artist. This tape is not produced under a license of any kind from the original recording company nor the recording artist (s) and neither the original recording company nor artist (s) receives a fee or royalty of any kind from [the pirate]. Permission to produce this tape has not been sought nor obtained from any party whatsoever.<sup>49</sup>

It is certainly most significant that record piracy has taken on such enormous proportions nationally and internationally that at this very moment, with the participation of the United States, a separate international treaty is proposed for the purpose of suppression of this practice. It may be interesting to note in this regard that, according to *Billboard* magazine of October 9th, even Europe is now infested with black

---

<sup>46</sup> 92nd Cong., 1st Sess.; see also H. Rept. 92-487, Sept. 22, 1971 entitled "Prohibiting Piracy of Sound Recordings."

<sup>47</sup> President Nixon signed the bill on October 15, 1971. The act will expire on Jan. 1, 1975, because by that time Congress expects that the Copyright Revision Bill will have been enacted into law. For a sum-up of S.646 and its effect on the pirates, see *Billboard* (Oct. 23, 1971), pps. 1 and 8.

<sup>48</sup> Sidney A. Diamond, *IDEA* Vol. 11, Conference Number (1967), p. 197.

<sup>49</sup> *Columbia Broadcasting System, Inc. v. Spies*, 167 U.S.P.Q. 492, at 494 (Ill. Cir. Ct. 1970).

market products, a factor which is causing grave concern, and that illegal copying of recordings in, for instance, West Germany, is estimated to constitute between 20 and 25 percent of the entire music market.<sup>50</sup>

However, it is my submission that it is not sufficient from either a domestic or an international point of view to concentrate on that form of piracy or unfair competition which at the present time appears to be most rampant. Similar problems exist in connection with design piracy in the fashion industry,<sup>51</sup> in connection with disparagement of competitors and their products, in the wide area of problems falling within the area of "degeneration of trademarks,"<sup>52</sup> and numerous other practices.<sup>53</sup> In my opinion, as well as in that of the vast majority of our profession, with the possible exception of reservations on the part of some members of the staff of the Antitrust Division of the Department of Justice, there exists only one overall remedy which, in the last analysis, would be of lasting benefit both to honest competitors and the consuming public: I refer to a general federal law of unfair competition modelled after certain European precedents which we have been trying to get enacted since the days when then Congressman John V. Lindsay introduced H. R. 4651 before the House, and which in slightly different form is at present once more before the Senate, introduced by Senator McClellan as S. 647 (Appendix G).<sup>54</sup>

Although the proposed act is referred to as "The Unfair Competition Act of 1971," it was thought expedient to propose it as an amendment to Section 43 (a) of the Lanham Act. It does, however, include, in addition to a catalog of outlawed individual unfair trade practices, a so-called "catch-all" provision in Section 43 (a) (4), which would provide a civil action in case of any instance of unfair competition "by misrepresentation or misappropriation." As presently worded, according to Section 43 (b), the remedies provided in the McClellan Act shall be available "to any person whose business or vocational activity, or the goodwill thereof, is or is likely to be damaged, to prevent and to

---

<sup>50</sup> See, "Piracy Increases in Greece and Germany," *Billboard* (Oct. 9, 1971), at p. 21. In Greece, it is stated, tape piracy accounts for at least 40% of all sales of recorded music.

<sup>51</sup> See Latman, "Fifteen Years After *Mazer v. Stein*, A Brief Perspective," *Bulletin of the Copyright Society*, Vol. 16 (1969), p. 278.

<sup>52</sup> For a recent comparative study (in English), see Lars Holmqvist, *Degeneration of Trade Marks* (Malmo, Sweden: Beson-Tryck AB 1971).

<sup>53</sup> As is well known, there have been attempts for many years to pass specific legislation protecting designs. The Design Bill has now been incorporated, as Part III, of S.644, the Copyright Revision Bill.

<sup>54</sup> 92nd Cong., 1st Sess., introduced Feb. 8, 1971.

recover for the forms of unfair competition enumerated in paragraph (a) hereof." No allegation of competition between the parties, no allegation of confusion, mistake or deception, or intent to injure the business or vocational activities of any other person or the goodwill thereof, is required. Nor will the McClellan bill under Section 7 (c) take the place of any remedy under common law or pursuant to the statutes of any state of the United States (including patent and copyright statutes), nor shall it be construed to preempt the jurisdiction of any state to grant relief in cases of unfair competition.

As long ago as 1967 I urged, in a paper before this Institute,<sup>55</sup> that every effort should be made, not only on behalf of business but on behalf of the consumer as well, to have such a federal unfair competition law enacted, if only to overcome the debilitating effect of the *Sears* and *Compco* Supreme Court decisions, which in their dicta went even beyond the limitations which the representatives of the Department of Justice had urged in their brief *amicus curiae*. Permit me to repeat here a quotation from Mr. Justice Brandeis' opinion in *Federal Trade Commission v. Gratz*,<sup>56</sup> in which he said:

Instead of undertaking to define what practices should be deemed unfair, as had been done in earlier legislation, the act left the determination to the commission. Experience with existing laws had taught that definition, being necessarily rigid, would prove embarrassing and, if rigorously applied, might involve great hardship. Methods of competition which would be unfair in one industry, under certain circumstances, might, when adopted in another industry, or even in the same industry under different circumstances, be entirely unobjectionable. *Furthermore, an enumeration, however comprehensive, of existing methods of unfair competition must necessarily soon prove incomplete, as with new conditions constantly arising novel unfair methods would be devised and developed.* (Emphasis added.)<sup>57</sup>

The late Edward S. Rogers, who had first suggested the enactment of a federal unfair competition law after the Supreme Court's decision in *Erie R.R. v. Tompkins*,<sup>58</sup> expressed it even more admirably:

. . . the courts are dealing with shrewd and ingenious defendants—with calculating competitors—who would like nothing better than to be told "this is as far as this court will go. You are safe so long as you refrain from these specific practices."

Experience shows that by the time the judicial machinery reaches a place where the pirate was yesterday, and is ready to deal with

<sup>55</sup> Derenberg, *IDEA*, Vol. 11, Conference Number (1967), p. 197.

<sup>56</sup> 253 U.S. 421 (1920).

<sup>57</sup> *Ibid.* at 429.

<sup>58</sup> 304 U.S. 64 (1938).

him, that elusive person has moved forward and is still a little ahead—at a place where the courts will not reach until tomorrow—and is there engaged in doing something which will enable him to advantage himself at someone else's expense in some manner hitherto unthought of<sup>59</sup>.

As has been persuasively pointed out as lately as June 1971 in a scholarly article in the *Harvard Law Review*,<sup>60</sup> a law of this type if accompanied by effective and readily obtainable enforcement provisions, will go a long way toward eradicating exaggerated and untrue forms of advertising which the present revitalized Federal Trade Commission is trying to cope with through the remedy of "public correction" and in other ways. It is quite encouraging to learn that as of this very date, the Commission has commenced a most comprehensive series of hearings reviewing the entire method of present day advertising from the consumer's point of view,<sup>60a</sup> so that stricter advertising controls both with regard to unfair competition and trademarks may be applied than those suggested by some recent writers<sup>61</sup> and by the Ninth Circuit Court of Appeals in its astonishingly permissive decision in *Smith v. Chanel*.<sup>62</sup>

Perhaps most significant in this regard is the recent determination by the Antitrust Division of the Department of Justice to prosecute violators of FTC Orders for criminal contempt in cases in which businessmen are found to have repeatedly disregarded the orders. According to *Business Week*,<sup>63</sup> a federal court in a little noticed decision in Topeka, Kansas recently imposed suspended jail terms and five years probation on the president and vice-president of an aircraft mechanics school who had been found in violation of a cease and desist order. In less drastic cases, the Department will, of course, resort to civil penalty actions rather than criminal proceedings against violators of regulatory orders.

One final word with regard to efforts toward more effective protec-

<sup>59</sup> 38 T.M.R. 259, 269-270.

<sup>60</sup> Warren S. Grimes, "Control of Advertising in the United States and Germany: Volkswagen Has a Better Idea," *Harvard Law Review*, Vol. 84 (June 1971), p. 1769.

<sup>60a</sup> See "F.T.C. Plans Major Report on Truth in U.S. Advertising," *New York Law Journal*, Vol. 166 (Oct. 15, 1971), at p. 1.

<sup>61</sup> See, for instance, Livermore, "On Uses of a Competitor's Trademark," *Stanford Law Review*, Vol. 20 (1968) p. 448; Alexander, "Honesty and Competition: Some Competitive Virtues in the False Naming of Goods," *Southern California Law Review*, Vol. 39 (1960), p. 1.

<sup>62</sup> 402 F.2d 562 (9th Cir. 1968). See Derenberg, "The Twenty-Second Year of Administration of the Lanham Trademark Act of 1946," 162 U.S.P.Q. Part II, No. 6 (August 11, 1969) at p. 34.

<sup>63</sup> "Justice Dusts Off a Sharp Weapon," *Business Week* (Oct. 9, 1971), at p. 30.

tion in the international field: Only a few days ago Congress passed S. 1253 (Appendix H), under which funds will be made available to the Commerce Department, Patent Office, the State Department and other agencies and groups to institute studies for closer cooperation concerning patents, trademarks and related matters so that our "acutely embarrassing position internationally" may be relieved.<sup>64</sup> I submit that in addition to studying such treaties as the Madrid Agreement Concerning the International Registration of Trademarks, the European patent treaty and other treaties, some attention should at last be given to certain areas in the international field in which we have been particularly delinquent. I refer, for instance, to the problems of so-called "delocalization" of appellations of origin (*appellations d'origine*) in connection with which European countries have entered into special agreements in recent years to correct what has been aptly called "sins of the past";<sup>64a</sup> most of these agreements we may not even be aware of in this country. It should not be possible, for instance, to claim in a court of law, as was recently done in *Wurzbürger Hofbrau Aktiengesellschaft v. Schoenling Brewing Co., Inc.*,<sup>65</sup> that the term "Old Wurzbürger," even if approved by the Alcohol Tax Unit, could be used as a type designation for an inferior local beer produced in the United States, and that the original brewer's efforts to protect the world famous German trademark were an "antitrust" violation. Perhaps only when we shall come across a German or Swiss "Bourbon" will we become finally aware of a greater need for protection of appellations of origin of this sort than we recognize at the present time.<sup>66</sup>

Moreover, the time has come when the relationship between trademarks and antitrust should be considered on an international basis so

---

<sup>64</sup> *News & Comment*, No. 46, (Sept. 29, 1971), p. A-1.

<sup>64a</sup> See Moser von Filseck, "Der Schutz geographischer Herkunftsbezeichnungen als internationale Aufgabe," MA 1955, p. 191, cited in Beier, *Geographische Herkunftsangaben und Ursprungsbezeichnungen* ("Soll Deutschland dem Lissaboner Ursprungsabkommen beitreten?"), *GRUR Int.* (1968), p. 69, at note 33. Cf. also Krieger, "Möglichkeiten für eine Verstärkung des Schutzes deutscher Herkunftsangaben im Ausland," *GRUR* (August-September 1960) at p. 400 *et seq.*

<sup>65</sup> 169 U.S.P.Q. 714 (S.D. Ohio 1971).

<sup>66</sup> It may be noted that at the Diplomatic Conference at Lisbon in 1958 a proposal for more effective protection of appellations of origin was vetoed by the delegation of the United States. See Ladas, "The Lisbon Conference for Revision of the International Convention for the Protection of Industrial Property," *The Trademark Reporter*, Vol. 48 (1958), p. 1291. See also with regard to bourbon whiskey, the report prepared by William J. Marshall, U.S.N. (retired) as President of The Bourbon Institute, March 15, 1968; also the remarks of M. Jolin before the Council of Europe, Group of Experts on Spirits, and Council of Europe document in relation to "Bourbon," GR/Sp (67) 3.



that some uniform answer may be found to such difficult problems as, for instance, that of so-called "parallel imports of genuine goods,"<sup>67</sup> a problem which has come to the fore again in the United States as a result of proposed new regulations by the Bureau of Customs which would deny protection to the American trademark owner in all cases in which some form of "common ownership or control" exists between foreign manufacturers and American distributors or vice versa.<sup>68</sup> Only if the relationship between antitrust, trademarks and unfair competition will be more clearly defined than has thus far been the case, both nationally<sup>69</sup> and internationally, will the antitrust defense to this type of litigation cease to be referred to as a "kneejerk" response.<sup>70</sup>

In conclusion, permit me to reiterate the main theme of my paper which was well expressed exactly 40 years ago by a Harvard professor of economics, in the following words:

Most persons who interest themselves in problems of Business Ethics take the view that the incidence of unfair business methods is largely on the purchaser or consumer. Although this may be a matter of major public interest, in view of the fact that everyone is a consumer, *such an analysis is not adequate. Indeed, most views of Business Ethics, and of remedial legislation and adjudication, are deficient because they take into account this single interest only.* As also appears in problems concerning the broader business relationships, the interests of the competitor and of the trade should also be considered, for the values generated by a vigorous and economically sound trade group contribute to economic and social welfare. (Emphasis added.)<sup>71</sup>

---

<sup>67</sup> Cf. Vandenberg, "The Problem of Importation of Genuinely Marked Goods Is Not a Trademark Problem," *The Trademark Reporter*, Vol. 49 (1959), p. 707; Derenberg, "Current Trademark Problems in Foreign Travel and the Import Trade," *The Trademark Reporter*, Vol. 49 (1959), p. 674; and most recently, Atwood, "Import Restrictions on Trademarked Merchandise—The Role of the United States Bureau of Customs," *The Trademark Reporter*, Vol. 59 (1969), p. 301. See also, Beier, "Territoriality of Trademark Law and International Trade," *IIC*, Vol. 1 (1970), p. 48.

<sup>68</sup> See "Notice of Proposed Rule Making," *CFR* Parts 11, 24, (Dec. 19, 1970), p. 133. See *News & Comment*, No. 8 (Dec. 24, 1970), at p. G-1 *et seq.*

<sup>69</sup> Cf. the franchising problem and the "Chicken Delight" case, *Harvey Siegel v. Chicken Delight, Inc.* reported in *News & Comment*, No. 48 (Sept. 23, 1971), Text, p. E-1.

<sup>70</sup> *News & Comment*, "Trademark Owner Defeats Antitrust Counterclaims," No. 46 (Sept. 30, 1971), at p. A-7, *et seq.*

<sup>71</sup> Carl F. Taesch, in *Policy and Ethics in Business* (1931), at p. 374.

## APPENDIX C

92<sup>D</sup> CONGRESS  
1<sup>ST</sup> SESSION

S. 1222

---

IN THE SENATE OF THE UNITED STATES

MARCH 12, 1971

MR. MAGNUSON (by request) introduced the following bill; which was read twice and referred to the Committee on Commerce

---

### A BILL

To provide increased protection for consumers, prevent consumer fraud, and for other purposes.

*Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That this Act may be cited as the "Consumer Fraud Prevention Act of 1971".*

### DEFINITIONS

SEC. 2. As used in this Act—

(a) "unfair consumer practice" means any of the following acts or practices committed by a supplier—

(1) offering goods or services intending not to sell them as offered for the purpose of inducing sales of other or different goods or services;

(2) advertising goods or services intending not to supply reasonably expectable public demand, unless the advertisement discloses a limitation;

(3) knowingly making false or misleading statements concerning the need for, or necessity of, any goods, services, replacements, or repairs;

(4) representing that the consumer will obtain any rights, privileges, or remedies knowing that the consumer will not;

(5) representing that goods are new knowing that they are not;

(6) representing that goods are of a particular standard, grade, quality, style, age, or model, knowing they are not, except that the conduct described in this paragraph shall not be an unfair consumer practice if the supplier shows that an affirmation merely of the value of the goods or services, or a statement of his opinion of the goods or services, or similar statements, did not take unfair advantage of the level of knowledge, ability, experience, or capacity of the consumer;

(7) knowingly making false or misleading statements concerning (i) the reason for, existence of, duration of, or amounts of price reductions, or (ii) savings in comparison to prices of competitors or one's own price;

(8) representing that goods or services are those of another, knowing they are not;

(9) failing to return or refund a deposit or advance payments for goods not delivered or services not rendered, when no default or further obligation of the person making such deposit or advance payment exists;

(10) knowingly representing that goods or services have sponsorship, approval, origin, characteristics of safety or performance, ingredients, uses, benefits, or quantities that they do not have, or that a person has a sponsorship, approval, status, affiliation, or connection that he does not have, except that the conduct described in this paragraph shall not be an unfair consumer practice if the supplier shows that an affirmation merely of the value of the goods or services, or a statement of his opinion of the goods or services, or similar statements, did not take unfair advantage of the level of knowledge, ability, experience, or capacity of the consumer;

(11) taking consideration for goods or services intending not to deliver such goods or perform such services, or intending to deliver goods or provide services which are materially different;

(12) offering gifts, prizes, free items, or other gratuities, in connection with a sale of goods or services to a consumer, intending not to provide them as offered;

(13) knowingly making false or misleading statements concerning the existence, terms, or probability of any rebate, additional goods or services, commission, or discount offered as an inducement for the sale of goods or services to a consumer in return for giving the supplier the names of prospective con-

sumers or otherwise helping the supplier to enter into any other consumer transaction;

(14) using physical force, threat of physical force, or undue harassment in dealing with a consumer;

(b) "knowing", "knowingly", and "knowledge" refer to actual knowledge, knowledge presumed where objective circumstances indicate that the supplier acted with knowledge, or knowledge presumed where circumstances indicate that the supplier acted in disregard of reasonable safeguards or care in ascertaining the truth of representations made;

(c) "consumer" means any natural person who is offered or supplied goods or services for personal, family, or household purposes;

(d) "supplier" means any person in the business of making goods or services available to consumers either directly or indirectly;

(e) "goods" means tangible personal property but does not include securities, or interests in securities, or aircraft to the extent regulated in design and construction; "goods" includes personal property intended to be attached to or installed in any real property without regard to whether it is so attached or installed;

(f) "services" includes the provision of intangibles, other than—

(i) insurance services;

(ii) credit services and services by common carriers and public utilities, to the extent that unfair consumer practices are prohibited with respect to these services under other Federal law regulations; and

(g) "statement" means any representation in advertising, any oral or visual presentation, or any other conduct intended to communicate to consumers.

### UNFAIR CONSUMER PRACTICES UNLAWFUL

SEC. 3. (a) It is unlawful for any supplier to commit any unfair consumer practice.

(b) An unfair consumer practice under this Act is an unfair or deceptive practice under section 5 of the Federal Trade Commission Act.

### CIVIL PENALTIES

SEC. 4. A supplier who willfully commits an unfair consumer practice shall be subject to a civil penalty of not more than \$10,000 for

each such act. The civil penalty may be assessed in an action instituted by the Attorney General under section 5 of this Act.

### RESTRAINING VIOLATIONS

SEC. 5. The United States district courts, the District Court of Guam, and the District Court of the Virgin Islands shall have jurisdiction to restrain violations of this Act in actions brought by the Attorney General. The court may at any time grant such injunctive relief as it deems appropriate. Whenever it appears to the court that the ends of justice require that other persons should be parties in the action, the court may cause them to be summoned whether or not they reside in the district in which the court is held, and to that end process may be served in any district.

### SUITS BY CONSUMERS ADVERSELY AFFECTED

SEC. 6. (a) When a supplier (i) in an action brought by the Attorney General under section 5 of this Act, has been enjoined from committing any unfair consumer practice, whether after final adjudication or by consent decree, or (ii) in a proceeding brought by the Federal Trade Commission under section 5 of the Federal Trade Commission Act with respect to acts or practices alleged to be unfair consumer practices within the meaning of section 2 of this Act, has been ordered to cease and desist from such unfair consumer practice, and the order has become final within the meaning of section 5, either after adjudication or by consent decree—any consumer claiming to have been adversely affected by the act or practice may bring suit against the supplier in a United States district court, the District Court of Guam, or the District Court of the Virgin Islands, and may recover actual damages, and the costs of suit, including reasonable attorneys' fees, and, when appropriate, restitution, reformation, rescission, and other equitable relief.

(b) Irrespective of whether an attorney's fee is assessed against the supplier, the court may inquire into the reasonableness of the fee agreed upon between the consumer and his counsel, and revise that fee as the circumstances warrant.

(c) In any action brought under this section, a supplier may, before trial or within thirty days after a judgment of liability in the case of a separate trial on the issues of liability and relief, submit to the district court a plan for relief for consumers injured by the unfair consumer practice and on whose behalf the action is properly maintained. Such a plan may be approved by the district court if the court

finds that such plan will reasonably assure that—

(1) it will be administered in a fair and impartial manner and adequate funds will be made available to pay for the costs and expenses of maintaining and administering the plan;

(2) reasonable notice will be provided to consumers who may have been damaged by unfair consumer practices;

(3) aggrieved consumers will be afforded an opportunity to apply for relief within a reasonable time, not in excess of one year from the date of approval of the plan; and

(4) adequate funds will be available, or other adequate arrangements will be made, for relief through the plan, and for this purpose a bond may be required.

Promptly upon the filing of a plan the supplier shall cause to be issued public notice as approved by the court advising of the submission of the plan. Within twenty days from the publication of such notice persons who may be financially interested in the proceeding may submit written comments on the adequacy of the plan to the court. Any party to the action may request a hearing on the adequacy of the plan. Upon approval, such plan shall be entered as part of a final judgment and decree and the court shall retain jurisdiction to the extent necessary to supervise its operation. In the course of supervising the plan, the court may hold hearings and issue orders and opinions.

#### JUDGMENT IN FAVOR OF THE UNITED STATES AS EVIDENCE

SEC. 7. A final judgment or decree rendered in any proceeding by the United States under section 5 of this Act to the effect that a supplier has engaged in an unfair consumer practice within the meaning of this Act shall be prima facie evidence against that supplier in any action or proceeding brought by any consumer against the supplier under section 6 of this Act, as to all matters respecting which said judgment or decree would be an estoppel as between the supplier and the United States: *Provided, however,* That this subsection shall not apply to consent judgments or decrees entered before any testimony has been taken.

#### VENUE

SEC. 8. An action under this Act may be brought in any district in which the claim arose or in which the supplier resides, is found, has an agent, is licensed to do business, or is doing business.

## LIMITATIONS OF ACTIONS

SEC. 9. Any action under section 6 of this Act shall be brought within one year after the termination of the proceeding under section 5 of this Act or under section 5 of the Federal Trade Commission Act on which it is predicated.

## CIVIL INVESTIGATIVE DEMANDS

SEC. 10. (a) Whenever the Attorney General has reason to believe that any person under investigation for any violation of the provisions of this Act may be in possession, custody, or control of any documentary material, or may have knowledge of any fact, relevant to an unfair consumer practice within the meaning of this Act, he may, prior to the institution of a civil proceeding under section 5, issue in writing, and cause to be served upon such person, a civil investigative demand, requiring such person to produce the documentary material for examination or to answer in writing written interrogatories pertaining to such knowledge.

(b) Each such demand shall—

(1) state the nature of the conduct alleged to constitute the unfair consumer practice which is under investigation;

(2) describe the class or classes of documentary material to be produced thereunder with such definiteness and certainty as to permit such material to be fairly identified;

(3) propound with definiteness and certainty the written interrogatories to be answered;

(4) prescribe a return date which will provide a reasonable period of time within which the material so demanded may be assembled and made available for inspection and copying or reproduction or within which the interrogatories propounded may be answered; and

(5) identify the custodian to whom such material shall be furnished, or the person to whom such answers shall be made.

(c) No demand shall—

(1) contain any requirement which would be unreasonable if contained in a subpoena duces tecum issued by a court of the United States in a proceeding brought under section 5 of this Act or if propounded in an interrogatory directed to a supplier in any such proceedings; or

(2) require the production of any documentary evidence, or the disclosure of any information, which would be privileged from

disclosure if demanded by a subpoena duces tecum issued by a court of the United States, or by an interrogatory propounded, in any proceeding under section 5 of this Act.

(d) Demand may be served at any place within the territorial jurisdiction of any court of the United States.

(e) Service of any such demand or of any petition filed under subsection (f) of this section may be made upon a partnership, corporation, association, or other legal entity by—

(1) delivering a duly executed copy thereof to any partner, executive officer, managing agent, or general agent thereof, or to any agent thereof authorized by appointment or by law to receive service of process on behalf of such partnership, corporation, association, or entity;

(2) delivering a duly executed copy thereof to the principal office or place of business of the partnership, corporation, association, or entity to be served; or

(3) depositing such a copy in the United States mails, by registered or certified mail duly addressed to such partnership, corporation, association, or entity at its principal office or place of business.

(f) A verified return by the individual serving any such demand or petition setting forth the manner of such service shall be proof of such service. In the case of service by registered or certified mail, such return shall be accompanied by the return post office receipt of delivery of such demand.

(g) The provisions of sections 4 and 5 of the Antitrust Civil Process Act (15 U.S.C. 1313, 1314) shall apply to custodians of material produced pursuant to any demand and to judicial proceedings for the enforcement of any such demand made pursuant to this section: *Provided, however,* That documents and other information obtained pursuant to any civil investigative demand issued hereunder and in the possession of the Department of Justice may be made available to duly authorized representatives of the Federal Trade Commission for the purpose of investigations and proceedings under the Federal Trade Commission Act.

#### REPORTS OF THE ATTORNEY GENERAL

SEC. 11. The Attorney General shall annually report to the President and to the Congress on the effectiveness of this Act.



OTHER LAWS NOT AFFECTED

SEC. 12. This Act shall not annul, alter, or affect in any manner the meaning, scope, or applicability of any Federal or State law, including but not limited to laws concerning the provisions of goods and services to consumers and the Public Health Cigarette Smoking Act of 1969.

SEPARABILITY

SEC. 13. If any provision of this Act is declared unconstitutional, or the applicability thereof to any person or circumstance is held invalid, the constitutionality of the remainder of the Act and the applicability thereof to other persons and circumstances shall not be affected thereby.

## APPENDIX D

92D CONGRESS  
1ST SESSION

S. 1378

---

IN THE SENATE OF THE UNITED STATES

MARCH 24 (legislative day, MARCH 23), 1971

MR. BAYH introduced the following bill; which was read twice and referred to the Committee on Commerce

---

### A BILL

To provide implementation of the Federal Trade Commission Act, to give increased protection to consumers, and for other purposes.

*Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That this Act may be cited as the "Consumer Class Action Act of 1971".*

SEC. 2. FINDINGS AND PURPOSE.—The Congress finds that there is a Federal interest in curbing unfair and deceptive practices which affect commerce. Congress finds that it promotes the free flow of goods in commerce and promotes the public welfare to provide an adequate process for class actions on behalf of similarly situated consumers.

SEC. 3. DEFINITIONS.—As used in this title—

- (a) "Unfair consumer practice" means any of the following:
- (1) any material statement, whether oral, written, or by visual description or other representation of any kind, or by half-truth or intentional omission, in connection with the sale, lease, rental or loan or the offering for sale, lease, rental, or loan of goods or services to consumers, or the extension of credit to consumers, or the collection of debts from consumers, which has the capacity, tendency or effect of misleading or deceiving consumers. Such statements include, but are not limited to—
    - (A) offering goods or services intending not to sell them as offered;
    - (B) advertising goods or services intending not to supply reasonably expectable public demand, unless the advertisement accurately discloses the limitation;

(C) making misleading statements concerning the need for any goods, services, or repairs;

(D) making misleading statements concerning the rights, obligations, liabilities, privileges or remedies of the consumer;

(E) representing that goods are new when they are not;

(F) representing that goods are of a particular standard, grade, quality, style, or model when they are not;

(G) making misleading statements concerning the reasons for, existence of, or amounts of price reductions or comparative price or value;

(H) representing that goods or services are those of another, when they are not;

(I) representing that goods or services have sponsorship, approval, origin, characteristics of safety, performance or non-pollution, ingredients, uses, benefits, or quantities that they do not have, or that a person has a sponsorship, approval, status, affiliation or connection that he does not have;

(J) taking consideration for goods or services without delivering the goods, performing the services or refunding the consideration within a reasonable period of time;

(K) making misleading statements concerning the profitability, risk, or any other material respect of any business opportunity or venture, or preparation or course of study for same, intended to be embarked upon by a natural person;

(L) offering gifts, prizes, free items or other gratuities without providing them as offered;

(M) making misleading statements concerning the existence, terms or probability of any rebate, additional goods or services, commission or discount offered as an inducement for the sale of goods or services to a consumer in return for giving the supplier the names of prospective consumers or otherwise helping the offerer to enter into any other consumer transaction;

(N) threatening that a creditor will take action that he does not actually take in the regular course of business;

(2) the use or threat of physical force against consumers or the undue harassment or coercion of consumers;

(3) failure to return deposits or advance payments for goods not delivered or services not rendered, when no default or further obligation of persons making such deposits or advance payments exists;

(4) violations which give rise to civil liability under state statutory or decisional law for the benefit of consumers;

(5) any other action prohibited by rule of the Federal Trade Commission, in accordance with the provisions of section 6 (g) of the Federal Trade Commission Act (15 USC 46 (g)), as amended, provided that such rule—

(A) became effective prior to the time of the action complained of, and

(B) was expressly designated by the Federal Trade Commission as a rule intended to constitute the basis of civil liability under this Act.

(b) “Intentional”, and “intending” refer to actual intent, intent presumed where objective circumstances indicate that the person acted with intent, or intent presumed where circumstances indicate that the supplier acted in disregard of reasonable safeguards or care;

(c) “Consumer” means any natural person who is offered or supplied goods or services for personal, family, or household purposes, or who is offered a personal business or money-making opportunity;

(d) “Goods” includes real property but does not include securities or interests in securities or aircraft to the extent regulated in design or construction;

(e) “Services” includes insurance services.

SEC. 4. It shall be unlawful for a person to commit any unfair consumer practice as defined in this Act if—

(a) his business affects commerce; or

(b) the violation or violations affect commerce.

SEC. 5. The district courts of the United States shall have original jurisdiction of civil class actions brought by a consumer or group of consumers under this act on behalf of himself or themselves and all consumers similarly situated. The jurisdiction of district courts of the United States under this section shall be concurrent with that of the courts of the several States. If an action under this Act is brought in a court of a State, the provisions of rule 23 of the Federal Rules of Civil Procedure shall apply to such action to the same extent that such provisions apply in the case of an action brought in a United States District Court.

SEC. 6. (a) In order for an action to be entertained under this Act, the court must find that the action is of such nature as to be entertainable under rule 23 of the Federal Rules of Civil Procedure.

(b) If the court finds that the case is entertainable under rule

23 of the Federal Rules of Civil Procedure, it may nevertheless decide, in its discretion, whether or not the controversy should be entertained or dismissed without prejudice to refile the same in a court of competent jurisdiction of the State. In so determining the court shall consider—

- (1) the nature and importance of the case;
- (2) the condition of its docket and the likelihood that the matter would unduly delay other cases;
- (3) the multidistrict or multistate nature of the matter; and
- (4) the relative procedural advantages of trying the case in the Federal or in the State court.

(c) In order for an action to be entertained under this Act in a district court of the United States the court shall make a determination of whether or not the amount which can reasonably be expected to be the amount in controversy exceeds \$25,000. If such amount cannot reasonably be expected to exceed \$25,000, then the court shall not entertain the action. For the purposes of this paragraph, the aggregate claims for all members of the class shall be taken into account to make up such requisite amount, and, if injunctive relief is sought and may reasonably be expected to be appropriate, the court shall consider the probable damages to the class of injunctive relief were not granted as an item in making up such requisite amount.

SEC. 7. No person shall be a member of a class in an action under this Act unless the amount of his loss or claim exceeds ten dollars.

SEC. 8. In any action under this Act, the court shall only award—

- (a) injunctive and declaratory relief;
- (b) restitution and actual damages;
- (c) relief or penalties specifically provided for under any statute giving rise to a right within the jurisdiction of the court in a case arising under this Act; and
- (d) costs of court as provided in section 14; and in no event shall award damages for personal injury or exemplary damages.

SEC. 9. In an action in a United States District Court under this Act based upon violations of State law, the law of the States shall be applied as if jurisdiction were based upon diversity of citizenship.

SEC. 10. Section 1441 of title 28, United States Code, shall not apply with respect to any action of which the district courts have jurisdiction solely by reason of the fact that the act complained of is alleged to be a violation of State statutory or decisional law for the benefit of consumers.

SEC. 11. At least thirty-five days prior to instituting an action under this Act, the prospective plaintiff or plaintiffs shall mail notice to the prospective defendant or defendants informing them, in general terms, of the nature of the alleged unfair consumer practice or practices. No action for monetary relief may be maintained if, within thirty days after the mailing of the notice, the prospective defendant or defendants—

(a) identify from business records all consumers similarly situated and notify them that appropriate refunds, credits, adjustments, replacements, or repairs will be made within thirty additional days; provided that where sales, leases, rentals or loans were effected through misleading statements, the defendants must notify the affected consumers that their money will be refunded upon their tender of the merchandise or any unused portion of the services, and where consumer debts were collected through misleading statements, the defendants must notify the affected consumers that the money will be refunded upon request; and

(b) cease the alleged unfair consumer practice or practices. Evidence of compliance or attempted compliance with this section shall not be construed as an admission of engaging in an unlawful practice.

SEC. 12. Actions pursuant to this Act shall be administered, so far as feasible within the discretion of the court, to avoid a multiplicity of suits, to avoid duplicating or overlapping class actions, and to avoid expenses of litigation which unduly repress obtaining justice under the Act. Such administration shall include, but shall not be limited to, assessing the costs of any required notice of the action as justice requires and providing for the use of facilities of the court, including mailing privileges, in such manner as justice requires.

SEC. 13. Actions pursuant to this section for redress of consumer injury shall be administered, so far as practicable, to facilitate voluntary settlements. The court shall have authority, upon the tender of a reasonable settlement offer by the defendant or defendants to the entire class, to supervise the submission of such settlement offer to the class. The court may take reasonable steps to insure that the consumers in the class are afforded, so far as feasible as determined by the court, the opportunity to exercise an individual choice with respect to accepting or rejecting any settlement offer. The court shall insure that equal space for the presentation of views as to the merits of the offer shall be tendered to plaintiffs and defendants in the notice of the offer to the members of the class. The cost of communicat-

ing the offer, or subsequent offers, tendered under the provisions of this section to the members of the class, shall be borne by the defendants. Such settlement offers shall be completed as expeditiously as possible.

SEC. 14. Whenever a consumer shall prevail in an action brought pursuant to this section, he shall be allowed to recover, in addition to damages, the costs of suit, including attorneys' fees. Such costs may be awarded from money damages which the defendant owes to members of the class who cannot be located with due diligence. Upon termination of a class action under this Act, whether by judgment, settlement or compromise, the court shall inquire into the reasonableness of attorneys' fees charged and revise such fees where necessary to assure that they are reasonable, taking into consideration, among other factors, the contingency of success, the actual time spent by attorneys in preparation and prosecution of the action, the difficulty of the case, the experience of plaintiffs' counsel, the amount recovered in the action, and the benefits to the public of the litigation.

SEC. 15. An action to enforce any claim under this section shall be forever barred unless commenced within three years after the claim arose, except that in the case of an action dismissed without prejudice to be filed in a State court under section 9 this limitation shall be tolled between the time that the action is commenced in Federal court and one month after the Federal court dismisses the action without prejudice to refile.

SEC. 16. An action under this title may be brought in any district in which the claim arose or in which the defendant resides, is found, has an agent, is licensed to do business, or is doing business.

SEC. 17. This Act shall not annul, alter, or affect in any manner the meaning, scope, or applicability of any Federal or State law except as specifically provided herein (as, for instance, in the case of application of Federal Rule 23 in cases brought upon a claim under this Act in State court), including but not limited to laws concerning the provision of goods and services to consumers and Public Law 91-222 (84 Stat. 87), or limit in any way the availability of rights or remedies under such law.

SEC. 18. If any provision of this Act is declared unconstitutional, or the applicability thereof to any person or circumstance is held invalid, the constitutionality of the remainder of the Act and the applicability thereof to other persons and circumstances shall not be affected thereby.

## APPENDIX E

### TRADEMARK ACT OF 1946,

#### AS AMENDED

Public Law 489, 79th Congress, Chapter 540, approved July 5, 1946;  
60 Stat. 427

**Sec. 43(a) (15 U.S.C. 1125a). False designations of origin and false descriptions forbidden**

Any person who shall affix, apply, or annex, or use in connection with any goods or services, or any container or containers for goods, a false designation of origin, or any false description or representation, including words or other symbols tending falsely to describe or represent the same, and shall cause such goods or services to enter into commerce, and any person who shall with knowledge of the falsity of such designation of origin or description or representation cause or procure the same to be transported or used in commerce or deliver the same to any carrier to be transported or used, shall be liable to a civil action by any person doing business in the locality falsely indicated as that of origin or the region in which said locality is situated, or by any person who believes that he is or is likely to be damaged by the use of any such false description or representation.



## APPENDIX F

92D CONGRESS  
1ST SESSION

S. 646

---

IN THE SENATE OF THE UNITED STATES

FEBRUARY 8 (legislative day, JANUARY 26), 1971

MR. McCLELLAN (for himself and Mr. SCOTT) introduced the following bill; which was read twice and referred to the Committee on the Judiciary

---

### A BILL

To amend title 17 of the United States Code to provide for the creation of a limited copyright in sound recordings for the purpose of protecting against unauthorized duplication and piracy of sound recording, and for other purposes.

*Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,* That title 17 of the United States Code is amended in the following respects:

(a) In section 1, title 17, of the United States Code, add a subsection (f) to read:

“To reproduce and distribute to the public by sale or other transfer of ownership, or by rental, lease, or lending, reproductions of the copyrighted work if it be a sound recording: *Provided*, That the exclusive right of the owner of a copyright in a sound recording to reproduce it is limited to the right to duplicate the sound recording in a tangible form that directly or indirectly recaptures the actual sounds fixed in the recording: *Provided further*, That this right does not extend to the making or duplication of another sound recording that is an independent fixation of other sounds, even though such sounds imitate or simulate those in the copyrighted sound recording; or to single ephemeral recordings made by transmitting organizations for their own use.

(b) In section 5, title 17, of the United States Code, add a subsection (n) to read:

“Sound recordings other than fixations of sound accompanying a motion picture.”

(c) In section 19, title 17, of the United States Code, add the following at the end of the section: “In the case of reproductions of works specified in subsection (n) of section 5 of this title, the notice shall consist of the symbol P (the letter P in a circle), the year of first publication of the sound recording, and the name of the owner of copyright in the sound recording, or an abbreviation by which the name can be recognized, or a generally known alternative designation of the owner: *Provided*, That if the producer of the sound recording is named on the labels or containers of the reproduction, and if no other name appears in conjunction with the notice, his name shall be considered a part of the notice.”

(d) In section 20, title 17, of the United States Code, amend the first sentence to read: “The notice of copyright shall be applied, in the case of a book or other printed publication, upon its title page or the page immediately following, or if a periodical either upon the title page or upon the first page of text of each separate number or under the title heading, or if a musical work either upon its title page or the first page of music, or if a sound recording on the surface thereof or on the label or container in such manner and location as to give reasonable notice of the claim of copyright.”

(e) In section 26, title 17, of the United States Code, add the following at the end of the section: “For the purposes of this section and sections 10, 11, 13, 14, 21, 101, 106, 109, 209, 215, but not for any other purpose, a reproduction of a work described in subsection 5 (n) shall be considered to be a copy thereof.

\*SEC. 2.. This Act shall take effect three months after its enactment. The provisions of title 17 of the United States Code shall apply only to sound recordings fixed, published, and copyrighted on and after the effective date of this Act and nothing in title 17 of the United States Code shall be applied retroactively or be construed as affecting in any way any rights with respect to sound recordings fixed before that date.

## APPENDIX G

92D CONGRESS  
1ST SESSION

S. 647

---

IN THE SENATE OF THE UNITED STATES

FEBRUARY 8 (legislative day, JANUARY 26), 1971

MR. MCCLELLAN (for himself and Mr. SCOTT) introduced the following bill; which was read twice and referred to the Committee on the Judiciary

---

### A BILL

To amend the Act to provide for the registration and protection of trademarks used in commerce, to carry out the provisions of certain international conventions, and for other purposes.

*Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That this Act be cited as the "Unfair Competition Act of 1971".*

SEC. 2. The title of the Act entitled "An Act to provide for the registration and protection of trademarks used in commerce, to carry out the provisions of certain international conventions, and for other purposes", approved July 5, 1946 (60 Stat. 427), is amended by inserting after "commerce," the words "to protect persons against unfair competition".

SEC. 3. Section 32(2) (15 U.S.C. 1114(2)) of said Act is amended by deleting its present introduction and paragraph (a) and substituting therefor: "Notwithstanding any other provision of this Act, the remedies given under this Act for the infringement of any right shall be limited as follows:

"(a) where an infringer is engaged solely in the business of printing for others and establishes that he was an innocent infringer, the owner of the right infringed shall be entitled as against such infringer only to an injunction against future printing;"

SEC. 4. Section 34 (15 U.S.C. 1116) of said Act is amended by deleting from the end of the first sentence thereof "of the registrant of a mark registered in the Patent Office" and substituting therefor

“protected under this Act”, and by inserting in the third paragraph after the word “proceeding” (first occurrence) the words “involving a registered trademark and.”

SEC. 5. Section 35 (15 U.S.C. 1117) of said Act is amended by deleting the first sentence thereof and substituting therefor: “When a violation of any right protected under this Act shall have been established in any civil action arising under this Act, the plaintiff shall be entitled, subject to the provisions of sections 29 and 32 and subject to the principles of equity, to recover (1) defendant’s profits, (2) any damages sustained by the plaintiff, and (3) the costs of the action.” and by inserting a new sentence as the last sentence of said section to read: “The court in exceptional cases may award reasonable attorneys’ fees to the prevailing party.”

SEC. 6. Section 36 (15 U.S.C. 1118) of said Act is amended to read: “In any action arising under this Act, the court may order that labels, signs, prints, packages, wrappers, receptacles, and advertisements in the possession of the defendant, the use or intended use of which is in violation of any right protected under this Act, and all plates, molds, matrices, and other means of making the same, shall be delivered up and destroyed.”

SEC. 7. Section 43 (15 U.S.C. 1125) of said Act is amended by deleting subsections (a) and (b) and substituting therefor:

“SEC. 43. (a) Any person who shall engage in any act, trade practice, or course of conduct, in commerce, which—

“(1) cause or is likely to cause confusion, mistake, or deception as to the affiliation, connection, or association of such person, or as to the origin, sponsorship, or approval of his goods, services, or vocational activities, or results or is likely to result in passing off the goods, services, or vocational activities which he offers as or for those of any other person, or

“(2) by a false or misleading representation or omission of material information, either misrepresents his goods, services, vocational activities, or their geographic origin, or misrepresents or disparages another person’s goods, services, vocational activities, or their geographic origin, or

“(3) results or is likely to result in the wrongful disclosure or appropriation of a trade secret or confidential information, or

“(4) without being limited to or by the foregoing subsections (1) through (3), otherwise constitutes unfair competition by misrepresentation or misappropriation,

shall be liable in a civil action for unfair competition.

“(b) The remedies provided in this Act shall be available to any person whose business or vocational activity, or the goodwill thereof, is or is likely to be damaged, to prevent and to recover for the forms of unfair competition enumerated in paragraph (a) hereof: *Provided*, That it shall not be necessary to prove competition between the parties, actual confusion, mistake, or deception, or intent to injure the business or vocational activity of any other person or the goodwill thereof.

“(c) The relief provided for by this section shall be in addition to and shall not affect those remedies otherwise available under this Act, under the common law, or pursuant to the statutes of any State or of the United States (including patent and copyright statutes). Nothing in this section shall be construed so as to preempt the jurisdiction of any State to grant relief in cases of unfair competition.”

SEC. 8. Section 44 (h) (15 U.S.C. 1126h) of said Act is amended to read: “Any person designated in paragraph (b) of this section shall be entitled to the remedies provided in this Act for unfair competition and infringement of marks.”

SEC. 9. The provided clause of section 46 (a) is amended by deleting “in force on the effective date of this Act” and inserting after “which does not relate to trademarks” the phrase “or unfair competition.”

SEC. 10. Section 1338 (a) of title 28, United States Code, the first sentence is amended by inserting “, unfair competition” after “copyrights.”

SEC. 11. Section 1338 (b) of title 28, United States Code, is amended to read:

“(b) The district courts shall have original jurisdiction of any civil action asserting a claim of unfair competition under the law of any state, when joined with a substantial and related claim under any Act of Congress relating to patents, copyrights, unfair competition, or trademarks.”

SEC. 12. This Act shall become effective upon enactment, but except as otherwise herein specifically provided it shall not affect any suit, proceeding, or appeal then pending.

## APPENDIX H

92D CONGRESS  
1ST SESSION

S. 1253

---

IN THE SENATE OF THE UNITED STATES  
MARCH 16, 1971

MR. McCLELLAN (by request) introduced the following bill; which was read twice and referred to the Committee on the Judiciary

---

### A BILL

To amend section 6 of title 35, United States Code, "Patents", to authorize domestic and international studies and programs relating to patents and trademarks.

*Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,* That section 6 of title 35, United States Code, is amended to read as follows:

**§ 6. Duties of Commissioner**

"(a) The Commissioner, under the direction of the Secretary of Commerce, shall superintend or perform all duties required by law respecting the granting and issuing of patents and the registration of trademarks; shall have the authority to carry on studies and programs regarding domestic and international patent and trademark law; and shall have charge of property belonging to the Patent Office. He may, subject to the approval of the Secretary of Commerce, establish regulations, not inconsistent with law, for the conduct of proceedings in the Patent Office.

"(b) The Commissioner, under the direction of the Secretary of Commerce, may, in coordination with the Department of State, carry on programs and studies cooperatively with foreign patent offices and international intergovernmental organizations, or may authorize such programs and studies to be carried on, in connection with the performance of duties stated in subsection (a) of this section.

"(c) The Commissioner, under the direction of the Secretary of Commerce, may, with the concurrence of the Secretary of State, transfer funds appropriated to the Patent Office, not to exceed \$100,000 in any year, to the Department of State for the purpose of making special payments to international intergovernmental organizations for studies and programs for advancing international cooperation concerning patents, trademarks, and related matters. These special payments may be in addition to any other payments or contributions to the international organization and shall not be subject to any limitations imposed by law on the amounts of such other payments or contributions by the Government of the United States."

## C. NEW SETTING FOR ANTITRUST AND UNFAIR COMPETITION

### Antitrust and Consumer Protection in Tandem: What Should We Expect of Section 5

JOHN C. BODNER, JR.\*

THE FEDERAL TRADE COMMISSION HAS BEEN, of late, the center of a great storm of controversy. The Nader Report denounced the agency in angry tones for failing to live up to its basic statutory responsibilities. The report of the ABA committee echoed, if less stridently, many of the same criticisms and added helpful insights of its own, concluding that "the case for change is plain" and "if change does not occur, there will be no substantial purpose to be served by the Commission's continued existence." The Ash Council Report pronounced decisively that no such purpose was to be served in any event and that the Commission should therefore be abolished.

---

\* Partner, Howrey, Simon, Baker & Murchison, Washington, D.C.

The Commission is, however, still very much with us. The criticisms seem to have had a healthy effect. Many changes have come about and undoubtedly many more are in the wind. They will be needed if the Commission is to keep abreast of the rising tide of consumer discontent and competitor dissatisfaction. It is to these new and vigorous demands and responding changes in enforcement and administration of regulatory legislation that this panel discussion is addressed.

As we know, under its basic statute (Section 5 of the Federal Trade Commission Act, Appendix B), the Commission is charged not only with eradicating "unfair methods of competition" but also with putting a stop to "unfair or deceptive acts and practices in commerce." The breadth and duality of this responsibility is symbolized by the fact that under recent reorganizations, the Commission has both a Bureau of Competition and a Bureau of Consumer Protection. It is precisely this fact of dual responsibility that poses one of the Commission's most important future challenges.

Policymakers in the past had a tendency to view these two functions as separate and anything but coequal in importance. There was a basic and pervasive belief that vigorous application of the competitor oriented antitrust laws would provide a cure for the problems of both the producer and the consumer. This view held that the function of the antitrust laws was to deconcentrate markets and eradicate artificial restraints on the flow of trade. If this regulation of the production function was successfully accomplished, it was thought, the consumer would automatically be provided with a wide array of ever improving goods at the lowest possible price.

We now have some idea in this age of mass media that that model was grossly oversimplified. Its basic flaw was that it put the cart before the horse. The competitive strictures of the antitrust laws are needed, but in order for them to have optimal effect, the consumer must perform his critical allocative function in a rational informed way. We are reminded constantly that considerations of price and quality do not alone govern today's marketplace. The modern consumer faces far more obstacles in making an informed choice than any of his predecessors did. Goods and services are far more numerous and complex. Even more significantly the means of communication employed in representing or misrepresenting their properties have become increasingly sophisticated. The marketplace itself, with the modern supermarket or department store as the paradigm, has taken on a highly impersonal character. The Commission stands astride this situation as the only



government instrumentality with a broad statutory mandate to deal with both interrelated segments of the problem.

Consumerism itself has become a political movement. Consumers no longer complain and entreat; they demand information adequate to the making of informed choices. The strength of their collective voices needn't surprise anyone. The unparalleled rise in disposable personal income and consumer credit in the United States has given us an economy where consumer expenditures are responsible for nearly two-thirds of the total goods and services produced each year in the United States.

At the same time the Commission is being subjected to incredible pressure at the consumer level, it also faces renewed challenges from producers. Concentration in major industries is a source of both economic and political disquiet. Other areas of trade restraint badly need its attention. It is becoming increasingly apparent that the Commission cannot effectively promote competition without also attending to the interests of consumers and vice versa. It must not only effectively stimulate competition at the producer level; it must see to it that the consumer has the means to evaluate the end product of the producer's efforts. A few dramatic gestures in one area to the exclusion of attention to the other would be disastrous. There are those who say that the present tools of government are no longer adequate to this dual task; that what is needed is government intervention in the marketplace in a massive way, reminiscent of public utility regulation. This view has not prevailed but it does accentuate the challenge which the present system must meet. How well it is met may depend on the sort of job the Commission, with its limited resources, does in melding its two functions. Means of carrying on this task will now be suggested by our two panelists.

# Antitrust Policy in a Technological Society: The Distinction Between Practices and Structure

ALLEN C. HOLMES\*

IT IS INDEED APPROPRIATE that a conference sponsored by this Research Institute and dealing with "Enterprise Under Stress" should devote a portion of its time to antitrust and unfair competition.

A truism accepted by all is that the antitrust activities of the federal government, and to a lesser extent of private complainants and state governments, have played a major role in preserving the free market economy which has been essential to the development of our present industrial society. Now, however, we are faced with the need to reexamine the premises of that antitrust policy in the light of the rapidity, breadth and depth of the development of new technologies which has taken place during the past quarter century.

I don't propose to undertake a recapitulation of the development of our antitrust law, or to dwell upon the significant antitrust decisions. I would, however, like to point out that traditionally antitrust concerned itself primarily with the control or eradication of various anticompetitive *practices*. It did not, until very recently, focus primarily upon the

---

\* Partner, Jones, Day, Cockley and Reavis, Cleveland.

*structure* of our economy. In saying this, I am not unaware of the landmark decisions under Section 2 of the Sherman Act involving tobacco, oil, railroads and steel. Further, I am acutely conscious of the enormous impact of the *Alcoa* decision upon modern enforcement activities. Nonetheless, I think it fair to say that until the last 15 years the thrust of antitrust enforcement, with respect to both so-called "hard core" violations and so-called "rule of reason" activities, was to challenge specific joint or unilateral *practices*.

For reasons which I shall discuss subsequently, this approach has continuing validity today. On the other hand, the challenge to the *structure* of American industry is based upon doubtful or nonexistent premises. The concern about the very existence of oligopoly, irrespective of its consequences, is predicated upon economic thinking and empirical studies conducted in the 1930's and 1940's, before our economy felt the recent enormous surge of creative innovation.

What have been the consequences of the commercial development of these new technologies? First, we have moved from an economy which was to a large extent labor-consuming to one that has become capital-consuming. This has radically changed the burden of shifts in demand. Much of our industry was historically a large consumer of labor. The high ratio of labor cost to capital cost made it possible to reduce costs rapidly as demand shifted or fell by laying off or reassigning employees. Today, with many fewer employees and much greater investment in capital goods, costs cannot be so easily controlled. The market pressure to reduce prices to the point where incremental costs plus any substantial portion of fixed costs are covered is great.

Second, the need for enormous capital investment in developing and marketing the new products of our multifaceted research activities has in many instances greatly reduced the number of potential entrants. Third, the distinctions between markets for various products has been greatly blurred. Innovation has replaced individual products with systems which provide goods and services meeting the demand formerly satisfied by the individual products, but completely unlike the replaced product. Further, the affluence of our society is such that the range of consumer purchases has been enormously expanded, with a concomitant increase in interproduct competition.

Inevitably, this rapid technological change has enormously increased the risks that are attendant upon the operation of any enterprise. In fact, even the largest companies cannot in many instances take the great risks required to launch a new business. Joint ventures have become an absolute necessity in connection with both domestic and foreign enter-

prises. The demand for ever increasing quantities of energy and the need for exotic metals have induced companies to invest large sums in remote and politically unstable countries. In many instances wisdom has dictated that such undertakings be on a joint basis. The calamitous situation in Chile emphasizes the dangers of unilaterally pursued investments.

Notwithstanding these basic changes in the pattern of our economy, we are still seeking to apply traditional standards and analysis to these modern economic enterprises. In view of the impact of innovation and the development of these new technologies, it seems appropriate at least to ask the question whether the antitrust agencies should not pause in their efforts to restructure American industry. Until new economic analysis based upon *current* empirical data has been undertaken, and until priorities as between antitrust and non-antitrust policies have been determined, it would seem inappropriate to attempt to push the modern industrial structures into the molds of the past. The rapid development of the technologies of Japan and Western Europe and the extraordinary size of capital investments therein require us to evaluate very carefully whether we can continue the luxury of policies which inhibit rationalization of capital investment in this country.

Today, concern about the limitations of our resources, ecology, the need to improve the position of minority groups, and other socially desirable objectives such as improving health care has made all of us aware that we can no longer put achievement of these objectives on a lower level of priority than the effort to preserve a free market economy through the application of our antitrust laws. One reason given for establishing antitrust policy as the highest priority has been that we must at all cost avoid injection of government controls into business activity. While all of us regard with considerable concern the indiscriminate interjection of government into the private sector of the economy, we have in fact come to live with a great deal of participation by government in private business. The farming industry has long since abandoned the free market. While I do not advocate that for other aspects of our economy, it is clear that it would be hard to establish that innovation has not been occurring on the farm, or that the farm has become less efficient, or that the public is poorly served by its agricultural industry.

The most recent actions of the federal government with respect to prices and wages emphasizes again that the efforts of antitrust enforcement cannot produce a stable and healthy economy in which inflation can be controlled, employment expanded, and consumers afforded a

wide range of choice. Under these circumstances antitrust cannot be afforded a kind of veto over other policy objectives which might in any degree impinge upon antitrust policies.

On the other hand, our new technologies have brought us a vast number of new products, highly complex in character, performing sophisticated functions and requiring constant and difficult maintenance. The recently expanded efforts of the Federal Trade Commission to deal with the unfair practices that have, or have threatened to, develop in the manufacture and marketing of such products and services seem to be an appropriate recognition of the needs of our society.

The need for factual disclosures increases as the ability of the buyer to make individual judgments about a product based upon his own knowledge decreases. Likewise, warranty obligations become increasingly important as the consumable product becomes more complex. The identification of health and safety factors, particularly with respect to new products that have just been offered to the public, is imperative in our technological society. Even the terms and conditions of purchase, including financing, are appropriately the subject of scrutiny when the transactions become so complex that the ordinary person cannot understand them without extensive and very explicit guidance.

No doubt there has been in various agencies some excess of zeal in dealing with these matters. No doubt there also has been a lack of zeal in other instances. It would appear, however, that an economy dedicated to the useful exploitation of invention and the appropriate utilization of innovation should welcome measures that will increase the confidence of the consumer in the effectiveness of our market system in providing safe, healthful, operative and satisfying products. This emphasis upon consumer protection seems to me to be in the tradition of dealing with *practices* that are anticompetitive and therefore destructive of our free market system.

Now a brief word about the relationship between patent and antitrust policy. We are all conscious of the intensity of the debate over the pending legislation designed to deal with this problem. Here again the important point is to recognize that the issues may have changed from what they were in the past. The need to increase the rate of utilization of new technologies in order to reduce costs and place our economy in a more competitive position vis-à-vis the other developed countries is far more pressing than it has ever been. A great many patentable inventions are now technologically superseded long before the statutory monopoly theoretically expires. We must enhance, not inhibit, the

development of new processes during their period of maximum utility. The problem is not to work out a nice conceptual rubric which places the patent monopoly appropriately in the antitrust framework; rather, the focus should be upon the encouragement of conduct which will most effectively utilize the creativeness of our industrial society. The per se rule should have limited scope; actual and substantial anticompetitive consequences should be demonstrated before we extend antitrust limitations in the licensing field.

Furthermore, there is no justification for developing doctrines of trade secret law which, by threatening forfeiture of property rights, prevent limited dissemination of innovative knowledge. Once again, a rational policy would encourage maximum use of new information unless substantial anticompetitive effects were shown.

This Institute has established an enviable reputation for its pioneering research into the practical operations of the patent, trademark and copyright systems of the United States. This Institute, or another equally dedicated, needs to extend this investigation into the even broader field of our evolving industrial structure—a structure reflecting in large measure the impact of the ventures and innovations covered by these patents, trademarks and copyrights.

## Some New Legal Developments at the Federal Trade Commission

ROBERT PITOFSKY\*

I WOULD LIKE TO DISCUSS WITH YOU TODAY, briefly and informally, two general areas marked by increasing activity at the Federal Trade Commission: (1) the regulation of false and deceptive national advertising, and (2) the promulgation of trade regulation rules.

I suppose it's obvious to all who observe enforcement policy at the FTC that the agency has selected for priority treatment the regulation of false and misleading advertising claims, particularly those appearing on national TV. A series of cases have been brought in the last year. We have inaugurated a new policy of demanding substantiation for advertising claims (of which I will have more to say a bit later), and we are now embarked on a series of hearings attempting to discover more about the way in which advertising strategies are selected, implemented and measured.

I believe we have filed about 20 or 25 cases in the last year or so challenging various advertising claims. Interestingly, I think few of these cases raise novel questions of substantive law. Perhaps the "toy

---

\* Director, Bureau of Consumer Protection, Federal Trade Commission.

cases" against Mattel and Topper were an exception, in that the complaint contended that the definition of truth and relevance in television advertising directed toward children was different from that with respect to TV advertising directed to an adult audience. I would have thought the point was almost self-evident, but it may not have been made clearly in prior cases. For the rest, I would suggest that most of the cases filed could have been brought on the basis of established law 20 or 25 years ago.

On the other hand it is certainly true that these cases have dramatically changed the ground rules with respect to remedy. In the past the Commission won most false advertising cases it elected to bring, but then settled for a simple cease and desist order. The result I'm afraid is that the Commission won the case but the consumer interest was not really advanced. If you were a potential advertiser and knew that the likelihood of being challenged legally was about 1 in 10,000, and further knew that if you litigated vigorously the case could be dragged out for a decade or more, and that at the end of that long process the only remedy to be imposed would be to direct you to stop advertising in the way you had been—you might be inclined to go ahead with questionable advertising and let the chips fall where they may. Certainly there would be a great temptation—if a dramatic and potentially successful advertising theme were involved—to go along with the suggested advertising campaign even if it played fast and loose with the facts.

The simple cease and desist order was also deficient as a remedy because it failed to deal with the continuing residual effect of deceptive advertising. For example, if an advertising theme were particularly vivid and compelling and much money was spent over many years to press the theme home with the public, it's quite possible that people would continue to buy the product on the basis of false impressions long after the cease and desist order had gone into effect.

It was for these reasons that the Commission began a year or so ago to experiment with different remedies in false advertising cases. We have attempted a kind of restitution or specific performance remedy against one advertiser, increasingly resorted to affirmative disclosure remedies against others, and most important, have introduced the notion of corrective advertising. Corrective advertising is a remedy which requires an advertiser found to have violated the provisions of Section 5 of the Federal Trade Commission Act (Appendix B) to go back to the public, in the same media in which he approached the public in the first place, and disclose the truth about its product.



I am convinced that that remedy is within the arsenal of the FTC's equitable powers. Not only is it consistent with the traditional antitrust notion that a court of equity is authorized to deprive a wrongdoer of the unlawful fruits of its law violations, but it is also consistent with the whole notion of free market regulation of our economic process. False advertising undermines the free competitive process because it gives consumers misinformation which denies them a full opportunity to make sensible and rational choices among competing products. Corrective advertising can cure that situation and allow products once again to meet in the marketplace on the basis of price, quality and other relevant characteristics.

Incidentally, the ad substantiation program, whereby companies upon demand are required to submit to the FTC tests or other evidence to back up advertising claims, is based on similar considerations. Hopefully, if companies know that they will have to substantiate their claims on a public record, they will be a trifle more cautious in the first place and insure that the claims they make are valid since it follows that if they are not, consumers will have an opportunity to review the substantiating data and reject the false impressions created. Conversely, the seller with a high quality product offered at a competitive price cannot help but profit when consumers are fully advised about its virtues. It is often the seller who does not have a quality product or has grossly overpriced its product who depends upon bigger and better (and occasionally untruthful) advertising campaigns.

I said at the outset that I wanted to say a few words about our trade regulation rules program. In a general way, the rules that have been published can be divided into two categories: those that tend to declare illegal under Section 5 some existing marketing practice, and those that require under Section 5 that sellers make relevant information available to consumers so that they can protect themselves against costly purchasing errors.

In the first category, I would include as examples the proposed rule abolishing the holder-in-due-course doctrine and the rule that requires that sellers who advertise food specials have the product marked at the right price and sufficiently stocked to satisfy reasonably anticipated demand during the period of the sale. The great virtue of these rules is that they apply equally to all businessmen in like circumstances. The situation that so often arose in the past—and was the subject of legitimate criticism by the companies subject to FTC regulation—was one in which a single seller was picked out and subjected to an order among many engaged in much the same practice. Given the limited

resources of the FTC and the inherent difficulties of proceeding industry-wide in every important matter, it often turned out that the hapless victim was subjected to a tough and competitively significant order, while his closest competitors were free so far as the government was concerned to continue the very practice that was the subject of the original suit.

The other category of rules has to do with required disclosure of information. I would list as examples the rule requiring posting of octane ratings in gasoline marketing and the proposed rule requiring care labels in certain categories of textile products. I think of these rules as the affirmative side of marketing regulation. Instead of simply telling advertisers what they may not claim (because deceptive or unfair), the agency directs them to disclose certain information in circumstances where silence itself would be misleading. Taking the octane rule as an example, under present circumstances one could easily find a series of gasoline stations along a given highway all charging 39.9 cents for regular gasoline. The truth of the matter is that one of those gasolines may be 90 octane, the second 91 and the third 92 and yet all sell under the generalized "regular" octane rating.

A free market system of course is premised on informed buyers "voting" their dollars for the product which combines the highest quality and most reasonable price. With full octane disclosure, one would expect that pressure would mount on companies offering the lesser octane to cut price to bring it more in line with a true evaluation of the qualities of the product. Once prices are reduced, they would not be raised unless and until the seller had managed an improvement in quality. This is all a matter of hornbook marketing, and yet in the absence of relevant information, a consumer is simply not in the position to bring the kind of pressure necessary to make the free market system work. And on the sellers' side, there is little pressure to cut price and great pressure to come up with better advertising themes to sell what the public regards as essentially like-priced products of uniform quality. Hopefully, required disclosures—such as that involved in the "octane rule"—can restore the basic conditions upon which a competitive system can operate.

I have selected today only two areas of Commission activity, and I am sure you will appreciate that much more is going on. Advertising, and related marketing, is of course not the only problem area in consumer protection, and I suspect that priorities will change and new cases and new trade practice rules will be initiated. But whatever the specific problem areas singled out for priority treatment, it seems clear that the

“consumer movement”—backed by a concerned and vocal constituency—is here to stay. I hope and expect that an active and vigilant FTC, deeply committed to effective consumer protection, is here to stay as well.

## APPENDIX A

For the convenience of our readers we are reprinting below, along with Amendments 23 and 24, an excerpt from the remarks of Senator Scott (including material he asked to be printed at the conclusion of his remarks in the *Congressional Record* Re Sections 261 and 271, 301, and the section of the Report of the President's Commission on the Patent System Re Recommendation XXII) made on May 11, 1971 before the Subcommittee on Patents, Trademarks, and Copyrights, of the Senate Committee on the Judiciary.

---

“During the last Congress, I introduced two amendments to the then-pending patent revision bill. I reintroduced these amendments, the so-called Scott amendments, on March 19 of this year.

“I noted during the last Congress that I was introducing these amendments so that they might appropriately be the subject of wide discussion and debate by all interested parties. I was not wed then, nor am I wed now, to the specific language set out in my amendments. I am, however, in full accord with the general thrust and purpose of these amendments. I, therefore, reintroduced these two amendments with the hope that a chance for full congressional consideration and action will be enhanced by the early date of their reintroduction. I am, therefore, very pleased that Senator McClellan is holding these hearings.

“Although I will submit substantial exploratory and supporting data at the conclusion of my remarks for the hearing record, I am taking this opportunity to briefly explain the purpose of my amendments.

“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) proposed to sections 261 and 271 deals with patent license provisions and is intended primarily to implement recommendation XXII of the report of the President's Commission on the Patent System.

“I believe these amendments address themselves to extremely important questions in the patent law field. There is merit to their underlying principles. It is for this reason that I proposed them to S. 643. However, I harbor no pride of authorship in the specific language and stand ready to examine alternative approaches to meet the needs

to which my amendments are addressed. It is my hope, however, that these amendments will serve to further stimulate thought and discussion on the action needed in these important areas.

"For purposes of background and clarification, it should be noted that the General Patent Revision bill introduced in the 91st Congress was S. 2756 and is identical to the current bill, S. 643, in all areas affected by the Scott amendments. My amendment No. 23 to S. 643 is identical to my amendment No. 579 to S. 2756. My amendment No. 24 to S. 643 is identical to my amendment No. 578 to S. 2756."

[From the Congressional Record]

RE SECTIONS 261 AND 271 (RECOMMENDATION XXII)

The amendments proposed to Sections 261 and 271 of S. 2756 are intended primarily to implement Recommendation XXII of the Report of the President's Commission on the Patent System. The net effect of those amendments, with regard to patents or applications for patent, would be to:

A. Re-arrange Section 261 (b) to make clear, in the first paragraph, a patent (or a patent application) owner's right to assign or license his patent (or application) exclusively, and in the second paragraph to limit the license to: (1) specified fields of use covered by the patent or application), (2) specified geographical territories, (3) exclusive or non-exclusive practice of the invention, and/or (4) any desired number of licenses as he may please.

B. Add new subparagraph 261 (e) so as to specify that an assignor cannot challenge the validity of the patent he has assigned unless he first returns the price paid and bases his attack on grounds not available at the time of the assignment.

C. Add a new subparagraph 261 (f) to stipulate that no party to a license can contest validity of a licensed patent unless he (1) first surrenders all future benefits and (2) then or thereafter settles all past obligations due under the license.

D. Add new Section 271 (f) and 271 (g) to provide a statutory basis for the following licensing practices, as follows:

(f) (1) the granting or prohibiting of certain fields of use of the (patented) invention, and permitting or prohibiting one or more of the primary functions of the patent, namely the right to exclude others from making, using or selling the (patented) invention.

(2) the granting of a license which contains a provision excluding or restricting any conduct reasonable under the circumstances.

(g) (1) the granting of non-exclusive cross licenses and the granting of a license containing a provision requiring the grant back of a non-exclusive license under improvements on the licensed invention.

(2) the granting of a license which requires a royalty fee or price:

(i) of any amount, however paid, on any desired royalty base;

(ii) computed on any basis convenient to the parties;

(iii) covers a single patent or a single package consisting of a multiple number of patents; or

(iv) which differs from that agreed to with other parties.

Section 271 (f) (1) would make it just as legal to license less than all of the right to exclude others from making, using and selling the subject matter patented (35 USC 154) as it is to license the entirety of the right. It would assure continued freedom of the patent owner to license for a term less than the remaining term of the patent, license to make and use without licensing sale, license to make use and sell in specified sizes or for specified purposes or fields, etc.

The Supreme Court sustained a limited field license in *General Talking Pictures v. Western Electric Co., Inc.*, 305 U.S. 124 (1938). Other decisions on the subject are collected in Oppenheim, *Federal Antitrust Laws* (1968), pp. 706-8. In *Atlas Imperial Diesel Engine Co. v. Lanova Corporation*, 79 Fed. Supp. 1002 (D. Del., 1948), the court sustained a license to a patent to engines which was limited to a specified maximum size.

Limited licenses have, at least until recently, been considered legal in the same respect as unlimited licenses. They are useful in many situations. For example, the Government takes at least a license to make, have made, and use for Government purposes in connection with inventions made during the course of Government financed research. Many antitrust decrees provide for compulsory licenses under all the patents of the defendant for certain limited purposes such as "to make use and vend lamps, lamp parts or lamp machinery". *U.S. v. General Electric Co.*, 115 F.Supp. 835, 848 (D. N.J., 1953).

Under the proposed statute there would be no inquiry as to the "reasonableness" of the particular portion of the total patent right to exclude that is offered for license or is licensed—any more than there is inquiry as to the "reasonableness" of the price a patent owner proposes to charge or charges for a license or whether a refusal to license at all is "reasonable".

The proposed language would not make legal those contracts or combinations that go beyond the grant of a limited license and restrain trade. Conduct such as occurred in *Hartford-Empire Co. v. U.S.*, 323

U.S. 386 (1945), where limited licenses were part of an overall combination to restrain trade, would continue to be illegal.

Section 271 (f) (2) would continue the right of the patentee to include in licenses such reasonable terms as are necessary to secure the full benefit of the invention and patent grant. For example, 35 USC 287 provides for a limitation on recoverable damages for patent infringement unless certain notice is on the patented articles. Under the proposed language a license requirement to this end would be legal. Similarly, a common form of license royalty is a percentage of the sales price. To secure the full benefit of the invention and patent grant with such license arrangement, the patentee should be entitled to receive necessary data as to what is sold by the licensee so as to determine that the royalties are correctly paid. The proposed language would assure that such provisions are free from challenge under the antitrust or any other laws.

The proposed language would not legalize agreement provisions that are not reasonable to secure the patent owner the full benefit of the invention and patent grant. For example, it would still be improper for a license to require that the licensee abstain from making or selling products that compete with the patented product. See *National Lockwasher Co. v. George K. Garrett Co.*, 137 F(2d) 255 (3d Cir., 1943). Also, limitations on the patentee, such as occurred in *United States v. Besser*, 96 Fed. Supp. 304 (E.D. Mich., 1951) (Aff'd. 343 U.S. 444 (1952)) and *United States v. Krasnov*, 143 Fed. Supp. 184 (E.D. Pa., 1956) (aff'd. 355 U.S. 5 (1957)), do not secure to the patent owner the full benefit of his invention and patent right in a reasonable manner and would continue to be invalid.

Section 271 (g) deals with a number of common arrangements that up to now have been considered generally legal but have been recently questioned to at least some degree.

Paragraph (g) (2) (i) continues the present law that the amount of royalties a nonexclusive license back. If the patentee is to grant a license it is only equitable that the licensee be prepared to reciprocate. This consideration had led the courts to approve nonexclusive grant-backs even in antitrust decrees rendered after proven violations of the Sherman Act. See, e.g., *United States v. National Lead*, 332 U.S. 319, 359 (1947).

Paragraph (g) (2) (i) continues the present law that the amount of royalties is purely a matter of private bargaining. In *American Photocopy v. Rovico, Inc.*, 359 F(2d) 745 (7th Cir., 19), the court held, in overruling a preliminary injunction, that excessive royalties were a

patent misuse and antitrust violation. After trial on the merits it was concluded that there was no misuse. 257 Fed. Supp. 192 (N.D. Ill., 1966) and 384 F (2d) 812 (7th Cir., 1967.) While the effects of this decision are now largely dissipated, it is believed appropriate to have a statutory provision that will avoid future such holdings.

Paragraph (g) (2) (ii) continues the present law that consideration need not be measured by the extent of use of the patented invention. Minimum royalties, for example, are a proper and very useful way to handle license fees. Although such royalties were specifically held valid in *Automatic Radio Mfg. Co. v. Hazeltine Research*, 339 U.S. 827 (1950), questions have been raised and the matter is believed best clarified by statute.

Paragraph (g) (2) (iii) makes it clear that the principle of paragraph (g) (2) (ii) applies to the analogous case where an arrangement involves a plurality of patents or patent claims and the royalty charge is not segregated as to any particular patent or patent claim.

Paragraph (g) (2) (iv) deals with differing royalty fees or purchase price figures. In *LaPeyre v. FTC*, 366 F (2d) 117 (5th Cir., 1966), and a number of other cases involving the same facts, dissimilar royalty rates were found to offend Section 5 of the Federal Trade Commission Act or the Sherman Act. These cases rest on an exceptional fact situation not likely to be repeated. Paragraph (g) (2) (iv) would make certain that the *LaPeyre* and companion cases are limited to their particular facts. A patent owner is not and should not be in the position of a public utility. The Congress has consistently and properly refused to enact compulsory licensing statutes. An endless number of considerations affect the royalty rate or purchase price to be arrived at as a matter of private bargaining, including the particular field of use by the licensee, the licensee's sales volume, the extent the licensee grants a license back, and many others. Paragraph (g) (2) (iv) assures that this bargaining can continue.

---

#### RE SECTION 301

There is at present in S. 2756 a Section 301 which sets forth the traditional provisions that the Federal patent laws do not preempt contractual or other rights or obligations not in the nature of patent rights, imposed by State or Federal law on particular parties in connection with inventions or discoveries, whether or not subject to the Federal patent statutes. In view of recent judicial decisions which cast a shadow of doubt on the propriety of entering into contracts for the



protection of trade secrets, technical know-how, and the like, and which suggest that such private contracts are preempted by the patent laws, it is recommended that this point be legislatively clarified by rewording Section 301 along the following lines:

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, or trade secrets, of unfair competition or of other nature.

In the absence of such a provision in the statutes it may be presumed that any body of technical knowledge, which by its very nature normally would constitute patentable subject matter, would be subject to application of the federal patent laws. But this would be unfair and unreasonable if the subject matter consisted 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 (e.g. a literature study to determine from the prior art the best process route to a certain item of manufacture, and a plant design based thereon; a computer program based upon pre-existing know-how; exact product simulation of form, color, size, etc.). In the absence of protection for such subject matter in the patent laws there is, nonetheless, a critical need for protection that should be available through the private law of contracts or the law of torts. Section 301 will fulfill that need and assure that the patent laws are not improperly applied so as to exclude such protection in situations where contract or tort law is indicated.

The need for Section 301 is important to the independent or relatively small researcher or developer of technical know-how and to large companies as well. At any level of operations the property rights which may be affected by that provision are of tremendous importance in the development and use of American technology. For example, a common occurrence are agreements entered into between domestic and foreign entities which involve, among other things, the transfer of technological information—important details of a process or product for which the recipient is willing to pay substantial sums of money. In 1968 the United States' technological balance of payments for agreements to exchange such technical information credited our country with 1½ billion dollars. In the absence of a law such as Section 301 provides such technical agreements might be outlawed as being preempted by the patent statutes. But the patent laws would afford insufficient protection for the subjects of those agreements as they may consist almost exclu-

sively of non-patentable technical know-how. Thus, the net effect would be to put an end to the exchange of information and payments therefor now represented by those agreements, for in the absence of adequate protection few persons or companies would want to chance disclosing their know-how and few would want to pay for acquiring know-how that anyone may duplicate with impunity.

---

REPORT OF THE PRESIDENT'S COMMISSION ON THE PATENT SYSTEM

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.

There is no doubt, in the opinion of the Commission, of importance to the U.S. economy of both the U.S. patent system and the antitrust laws. Each is essential and each serves its own purpose within the framework of our economic structure. However, conflicts between the two have arisen. But this does not mean that the two systems are mutually exclusive, that a strong patent system is a threat to the antitrust laws, or that the latter cannot be effectively enforced so long as a patent system grants limited monopolies.

On the contrary, the two systems are fully compatible, one checking and preventing undesirable monopolistic power and the other encouraging and promoting certain limited beneficial monopolies. In this way, each may easily achieve its objectives in a strong economy.

The Commission, therefore, does not favor any proposal which would weaken the enforcement of the antitrust laws or which would curtail in any way the power of the courts to deny relief to a patent owner misusing the patent he seeks to enforce. 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.

No useful purpose would be served by codifying the many decisions dealing with patent misuse into a set of rules or definitions permitting or denying enforceability of patents in given circumstances. The risk of unenforceability is too great and such a codification is wholly unnecessary. All that the Commission believes to be required is explicit statutory language defining, for the purpose of assignments and licenses, the nature of the patent grant heretofore recognized under the patent statute or by decisional law. This is, the right to exclude others from making, using and selling the patented invention.

The mere exercise, conveyance or license of these conferred rights should not in itself constitute misuse of a patent. A patent owner should not be denied relief against infringers because he either refused to grant a license or because he has exercised, transferred or licensed any of the conferred patent rights himself. This should not include immunity of even these conferred patent rights from the antitrust laws when the patent owner becomes involved in a conspiracy to restrain or monopolize commerce, or when the patent is itself used as an instrument for unreasonably restraining trade.

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. 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 direction relation to the machine claims in his patent. By the same standards, the patent owner could not control commerce in one of the unpatented elements of his combination invention where his claims are to the whole combination.

92D CONGRESS  
1ST SESSION

S. 643

---

IN THE SENATE OF THE UNITED STATES

MARCH 19, 1971

Referred to the Committee on the Judiciary and ordered to be printed

---

**AMENDMENT**

Intended to be proposed 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, viz: Beginning with line 17, page 44, strike out all to and including line 22, page 44, and insert in lieu thereof the following:

**“§ 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 or contracts, of confidential or proprietary information, of trade secrets, of unfair competition, or of other nature.”

**Amdt. No. 23**

92D CONGRESS  
1ST SESSION

S. 643

---

IN THE SENATE OF THE UNITED STATES

MARCH 19, 1971

Referred to the Committee on the Judiciary and ordered to be printed

---

**AMENDMENTS**

Intended to be proposed 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, viz:

On page 37, strike out line 32 and insert in lieu thereof the following:

“§ 261. Transferable and licensable nature of patent rights”

On page 37, beginning with line 35, strike out all to and including line 2, page 38, and insert in lieu thereof the following:

“(b) (1) Applications for patent, patents, or any interest therein shall be assignable in law by an instrument in writing, and in like manner exclusive rights under applications for patent and patents may be conveyed for the whole or any part of the United States.

“(2) 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 under a patent or patent application and for the whole or any part of the United States, by exclusive or non-exclusive arrangement with a party or parties of his selection.”

On page 38, between lines 15 and 16, insert the following new subsections:

“(e) No assignor of a patent shall contest, directly or indirectly, the validity of the patent, when asserted against him by his assignee or any owner of the patent deriving title through the assignee, unless (1) the consideration involved has been restored to, or for the benefit of, the first assignee, and (2) such assignor asserts a ground for invalidity not reasonably available to him when the assignment was made.

“(f) No party to a license, immunity, or other express waiver under a patent shall, unless consented to by all other parties thereto, contest the validity of the patent, provided that any party who gives written notice that he unconditionally renounces all future benefit from the license, immunity, or other waiver may

Amdt. No. 24

then and thereafter contest the validity regardless of any contract to the contrary, but such renunciation shall not operate to relieve the renouncing party from any performance due prior to the renunciation.”<sup>3</sup>

On page 39, between lines 19 and 20, insert the following new subsections:

“(f) No patent owner shall be guilty of misuse or illegal extension of patent rights because he has entered into, or will enter only into—

“(1) an arrangement granting some rights under the patent but excluding specified conduct, if the conduct excluded would be actionable under this title, or

“(2) an arrangement granting rights under the patent that 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 and patent grant.

“(g) No patent applicant or patent owner shall be guilty of misuse or illegal extension of patent rights because he has entered into, or will enter only into, an arrangement of assignment, license, or waiver of some or all of his rights under this title for a consideration which includes—

“(1) a nonexclusive license or waiver of patent rights; or

“(2) a royalty, fee, or purchase price:

“(A) in any amount, however paid or measured, provided that any amount paid after the expiration of a patent is based solely upon activities prior to such expiration;

“(B) not measured by the subject matter of the patent or by extent of use by the other party of the rights assigned, licensed, or waived;

“(C) not computed in a manner that segregates the charge for any particular patent, or for any particular claim or claims of one or more patents; or

“(D) differing from that provided in some other arrangement.”.

## APPENDIX B

UNFAIR METHODS OF COMPETITION AND UNFAIR OR DECEPTIVE ACTS OR PRACTICES UNLAWFUL. COMPLAINTS, FINDINGS, AND ORDERS OF COMMISSION. APPEALS. PENALTIES (38 Stat. 719; 52 Stat. 111; 64 Stat. 21; 66 Stat. 631; 72 Stat. 942; 15 U.S.C. 45).

Sec. 5.<sup>8</sup> (a) (1) Unfair methods of competition in commerce, and unfair or deceptive acts or practices in commerce, are hereby declared unlawful.

Unfair methods of competition.

(2) Nothing contained in this Act or in any of the Antitrust Acts shall render unlawful any contracts or agreements prescribing minimum or stipulated prices, or requiring a vendee to enter into contracts or agreements prescribing minimum or stipulated prices, for the resale of a commodity which bears, or the label or container of which bears, the trade-mark, brand, or name of the producer or distributor of such commodity and which is in free and open competition with commodities of the same general class produced or distributed by others, when contracts or agreements of that description are lawful as applied to intrastate transactions under any statute, law, or public policy now or hereafter in effect in any State, Territory, or the District of Columbia in which such resale is to be made, or to which the commodity is to be transported for such resale.

Unfair or deceptive acts, etc., added.

(3) Nothing contained in this Act or in any of the Antitrust Acts shall render unlawful the exercise or the enforcement of any right or right of action created by any statute, law, or public policy now or hereafter in effect in any State, Territory, or the District of Columbia, which in substance provides that willfully and knowingly advertising, offering for sale, or selling any commodity at less than the price or prices prescribed in such contracts or agreements whether the person so advertising, offering for sale, or selling is or is not a

State Fair Trade Laws.

---

<sup>8</sup> This section, as set forth above, includes therein the McGuire Act amendments of July 14, 1952 (see footnote 1), 66 Stat. 631.

party to such a contract or agreement, is unfair competition and is actionable at the suit of any person damaged thereby.

(4) Neither the making of contracts or agreements as described in paragraph (2) of this subsection, nor the exercise or enforcement of any right or right of action as described in paragraph (3) of this subsection shall constitute an unlawful burden or restraint upon, or interference with, commerce.

(5) Nothing contained in paragraph (2) of this subsection shall make lawful contracts or agreements providing for the establishment or maintenance of minimum or stipulated resale prices on any commodity referred to in paragraph (2) of this subsection, between manufacturers, or between producers, or between wholesalers, or between brokers, or between factors, or between retailers, or between persons, firms, or corporations in competition with each other.

Prevention by  
Commission.

(6) The Commission is hereby empowered and directed to prevent persons, partnerships, or corporations, except banks, common carriers subject to the Acts to regulate commerce, air carriers, and foreign air carriers subject to the Federal Aviation Act of 1958, and persons, partnerships, or corporations insofar as they are subject to the Packers and Stockyards Act, 1921, as amended, except as provided in section 406 (b) of said Act, from using unfair methods of competition in commerce and unfair or deceptive acts or practices in commerce.<sup>9</sup>

---

<sup>9</sup> Subsection (f) of Section 1107 of the "Civil Aeronautics Act of 1938," approved June 23, 1938, Public No. 706, 75th Congress, 52 Stat. 1028, amended former Sec. 5 (a) by inserting following the words "to regulate commerce," the words "air carriers and foreign air carriers subject to the Civil Aeronautics Act of 1938," as set out in Sec. 5 (a) (6); by Act of Aug. 23, 1958, (72 Stat. 809, Public Law 85-726), "Federal Aviation Act of 1958," was substituted in lieu of "Civil Aeronautics Act of 1938".

Public No. 85-909, 85th Cong., approved Sept. 2, 1958, amended the Packers and Stockyards Act, 1921, as amended (7 U.S.C. 226, 227, and 72 Stat. 1749, 1750) by striking out subsec. (b) of sec. 406 and inserting in lieu thereof the following:

"(b) The Federal Trade Commission shall have power and jurisdiction over any matter involving meat, meat food products, livestock products in unmanufactured form, or poultry products, which by this Act is made subject to the power or jurisdiction of the Secretary, as follows:

"(1) When the Secretary in the exercise of his duties requests of the Commission that it make investigations and reports in any case.





Testimony. or in person. The testimony in any such proceeding shall be reduced to writing and filed in the office of the Commission. If upon such hearing the Commission shall be of the opinion that the method of competition or the act or practice in question is prohibited by this Act, it shall make a report in writing in which it shall state its findings as to the facts and shall issue and cause to be served on such person, partnership, or corporation an order requiring such person, partnership, or corporation to cease and desist from using such method of competition or such act or practice. Until the expiration of the time allowed for filing a petition for review, if no such petition has been duly filed within such time, or, if a petition for review has been filed within such time then until the record<sup>10</sup> in the proceeding has been filed in a court of appeals<sup>11</sup> of the United States, as hereinafter provided, the Commission may at any time, upon such notice and in such manner as it shall deem proper, modify or set aside, in whole or in part, any report or any order made or issued by it under this section. After the expiration of the time allowed for filing a petition for review, if no such petition has been duly filed within such time, the Commission may at any time, after notice and opportunity for hearing, reopen and alter, modify, or set aside, in whole or in part, any report or order made or issued by it under this section, whenever in the opinion of the Commission conditions of fact or of law have so changed as to require such action or if the public interest shall so require: *Provided, however,* That the said person, partnership, or corporation may, within sixty days after service upon him or it of said report or order entered after such a reopening, obtain a review thereof in the appropriate court of appeals of the United States, in the manner provided in subsection (c) of this section.

(c) Any person, partnership, or corporation required by an order of the Commission to cease and desist from

Report of findings.

Issuance of cease and desist order.

Modification, etc.

Reopening, altering, etc. of order.

Proviso. Right of appeal.

<sup>10</sup> The Act of August 28, 1958, Public Law 85-791, 72 Stat. 942, amended Section 5 (b) by deleting the phrase "transcript of the" appearing before the word "record."

<sup>11</sup> The Act of May 24, 1949, 63 Stat. 107, amended all laws in force on September 1, 1948, in which reference was made to "circuit court of appeals" by substituting therefor the words "court of appeals."

using any method of competition or act or practice may obtain a review of such order in the court of appeals of the United States, within any circuit where the method of competition or the act or practice in question was used or where such person, partnership, or corporation resides or carries on business, by filing in the court, within sixty days from the date of the service of such order, a written petition praying that the order of the Commission be set aside. A copy of such petition shall be forthwith transmitted by the clerk of the court to the Commission, and thereupon the Commission shall file in the court the record in the proceeding, as provided in Section 2112 of Title 28, United States Code. Upon such filing of the petition the court shall have jurisdiction of the proceeding and of the question determined therein concurrently with the Commission until the filing of the record and shall have power to make and enter a decree affirming, modifying, or setting aside the order of the Commission, and enforcing the same to the extent that such order is affirmed, and to issue such writs as are ancillary to its jurisdiction or are necessary in its judgment to prevent injury to the public or to competitors *pendente lite*.<sup>12</sup> The finding of the Commission as to the facts, if supported by evidence, shall be conclusive. To the extent that the order of the Commission is affirmed, the court shall thereupon issue its own order commanding obedience to the terms of such order of the Commission. If either party shall apply to the court for leave to adduce additional evidence, and shall show to the satisfaction of the court that such additional evidence is material and that there were reasonable grounds for the failure to adduce such evidence in the proceeding before the Commission, the court may order such additional evidence to be taken before the Commission and to be adduced upon the hearing in such manner and upon such terms and conditions as to the court may seem proper. The Commission may modify its findings as to the facts, or make new findings, by reason of the additional evidence so taken, and it shall

Review by appropriate court of appeals.

Jurisdiction.

Findings as to facts conclusive.

Modifications, etc., by Commission of findings as to fact.

<sup>12</sup> The Act of August 28, 1958, Public Law 85-791, Sec. 3 (b), 72 Stat. 942, amended the second and third sentences of Sec. 5 (c) to read as set forth above.

file such modified or new findings, which, if supported by evidence, shall be conclusive, and its recommendation, if any, for the modification or setting aside of its original order, with the return of such additional evidence. The judgment and decree of the court shall be final, except that the same shall be subjected to review by the Supreme Court upon certiorari, as provided in section 240 of the Judicial Code.

Judgment and decree final; review by Supreme Court.

(d) Upon the filing of the record with it the jurisdiction of the court of appeals of the United States to affirm, enforce, modify, or set aside orders of the Commission shall be exclusive.<sup>13</sup>

Exclusive jurisdiction of the court of appeals.

(e) Such proceedings in the court of appeals shall be given precedence over other cases pending therein, and shall be in every way expedited. No order of the Commission or judgment of court to enforce the same shall in anywise relieve or absolve any person, partnership, or corporation from any liability under the Antitrust Acts.

Proceedings given precedence.

(f) Complaints, orders, and other processes of the Commission under this section may be served by anyone duly authorized by the Commission, either (a) by delivering a copy thereof to the person to be served, or to a member of the partnership to be served, or the president, secretary, or other executive officer or a director of the corporation to be served; or (b) by leaving a copy thereof at the residence or principal office or place of business of such person, partnership, or corporation; or (c) by mailing a copy thereof by registered mail or by certified mail addressed to such person, partnership, or corporation at his or its residence or principal office or place of business. The verified return by the person so serving said complaint, order, or other process setting forth the manner of said service shall be proof of the same, and the return post office receipt for said complaint, order, or other process mailed by registered mail or by certified mail as aforesaid shall be proof of the service of the same.<sup>14</sup>

Service of processes.

Verified return; proof of service.

---

<sup>13</sup> The section reflects the amendment by Public Law 85-791 to read as set forth above.

<sup>14</sup> This section was amended by Public Law 86-507, 86th Cong., approved June 11, 1960 (74 Stat. 200), reading as set forth above.

(g) An order of the Commission to cease and desist shall become final—

Commission's order final.

(1) Upon the expiration of the time allowed for filing a petition for review, if no such petition has been duly filed within such time; but the Commission may thereafter modify or set aside its order to the extent provided in the last sentence of subsection (b); or

Upon expiration of time for filing petition for review.

(2) Upon the expiration of the time allowed for filing a petition for certiorari, if the order of the Commission has been affirmed, or the petition for review dismissed by the court of appeals,<sup>15</sup> and no petition for certiorari has been duly filed; or

Upon expiration of time for filing petition for certiorari.

(3) Upon the denial of a petition for certiorari, if the order of the Commission has been affirmed or the petition for review dismissed by the court of appeals;<sup>16</sup> or

Upon denial of petition for certiorari.

(4) Upon the expiration of thirty days from the date of issuance of the mandate of the Supreme Court, if such Court directs that the order of the Commission be affirmed or the petition for review dismissed.

Supreme Court mandate affirming Commission order.

(h) If the Supreme Court directs that the order of the Commission be modified or set aside, the order of the Commission rendered in accordance with the mandate of the Supreme Court shall become final upon the expiration of thirty days from the time it was rendered, unless within such thirty days either party has instituted proceedings to have such order corrected to accord with the mandate, in which event the order of the Commission shall become final when so corrected.

Order modified or set aside by Supreme Court.

(i) If the order of the Commission is modified or set aside by the court of appeals,<sup>16</sup> and if (1) the time allowed for filing a petition for certiorari has expired and no such petition has been duly filed, or (2) the petition for certiorari has been denied, or (3) the decision of the court has been affirmed by the Supreme Court, then the order of the Commission rendered in accordance with the mandate of the court of appeals,<sup>16</sup> shall become final

By court of appeals; when final.

---

<sup>15</sup> See footnote 11, p. 1458.

<sup>16</sup> See footnote 11, p. 1458.

on the expiration of thirty days from the time such order of the Commission was rendered, unless within such thirty days either party has instituted proceedings to have such order corrected so that it will accord with the mandate, in which event the order of the Commission shall become final when so corrected.

Rehearing.

(j) If the Supreme Court orders a rehearing; or if the case is remanded by the court of appeals<sup>17</sup> to the Commission for a rehearing, and if (1) time allowed for filing a petition for certiorari has expired, and no such petition has been duly filed, or (2) the petition for certiorari has been denied, or (3) the decision of the court has been affirmed by the Supreme Court, then the order of the Commission rendered upon such rehearing shall become final in the same manner as though no prior order of the Commission had been rendered.

"Mandate."

(k) As used in this section the term "mandate," in case a mandate has been recalled prior to the expiration of thirty days from the date of issuance thereof, means the final mandate.

Penalty for violation.

(l) Any person, partnership, or corporation who violates an order of the Commission to cease and desist after it has become final, and while such order is in effect, shall forfeit and pay to the United States a civil penalty of not more than \$5,000 for each violation, which shall accrue to the United States and may be recovered in a civil action brought by the United States. Each separate violation of such an order shall be a separate offense, except that in the case of a violation through continuing failure or neglect to obey a final order of the Commission each day of continuance of such failure or neglect shall be deemed a separate offense.<sup>18</sup>

---

<sup>17</sup> See footnote 11, p. 1458.

<sup>18</sup> Public Law 459, 81st Congress, approved March 16, 1950, 64 Stat. 21, amended Sec. 5 (1) by adding the second sentence to said section.