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FTC Offers Recommendations to Better Align Patent System and Competition Policy

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As part of its continuing efforts to better align the country's patent system with its competition policy, the Federal Trade Commission (FTC) recently released a 300-page report, *The Evolving IP Marketplace: Aligning Patent Notice and Remedies with Competition* (Report), which makes numerous recommendations to further that alignment. The Report notes that, while the patent system and competition policy both promote innovation and enhance consumer welfare, tensions can develop between the two as a result of the patent system conferring exclusivity on patent owners and the antitrust laws seeking to promote competition. The Report contends that those tensions can be better balanced by reforms in two areas: (1) improved notice, i.e., better informing the public of which technology is claimed by a patent; and (2) improved patent infringement remedies that would result from courts making a more consistent use of "an economically grounded approach to calculating patent damages."

The Report followed eight days of hearings that began in 2008 and a May 2010 workshop co-sponsored with the U.S. Patent and Trademark Office (PTO) and Department of Justice; the hearings and workshop involved more than 140 participants and more than 50 written submissions. This Report follows two others from the FTC—one issued in 2003 and the other issued in 2007—that have urged policies and legal rules to better harmonize the patent system and competition policy. *See* Fed. Trade Comm'n, *To Promote Innovation: The Proper Balance of Competition and Patent Law and Policy*, (Oct. 2003); Fed. Trade Comm'n and Dept. of Justice Antitrust Div., *Antitrust Enforcement and Intellectual Property Rights: Promoting Innovation and Competition* (April 2007).

IMPROVING NOTICE OF PATENTS TO THE PUBLIC

A principal recommendation of the new Report is clearer public notice of the precise technology claimed by patents. That reform, the Report asserts, would help spur innovation by increasing companies' confidence that the technologies they are developing do not infringe existing patents, when such is the case, and by helping companies identify and license patented technologies that they wish to use or develop. When the language used in patents is unclear or confusing, companies may choose not to pursue research and development of new products based on a misplaced fear that an existing patent is blocking or they may forgo use of a preferred technology and select a less desirable one because it is difficult to determine whether the preferred technology carries the cost of patent royalties. Accordingly, the Report recommends a number of improvements to public notice of patents that are designed to enhance companies' ability to (1) understand claims, (2) foresee claims emerging from patent applications, and (3) conduct patent searches:

1. **Improving the Ability to Understand Claims** – Uncertain or ambiguous terms used in patent claims can lead either to inadvertent infringement or the unnecessary abandonment of technology development. The Report offers a number of recommendations to improve the notice available in the patent clearance process, including the following:

    - Courts and the PTO should follow the lead of the PTO Board of Patent Appeals and Interferences and adopt a lower threshold for finding patent claims indefinite and thus invalid. The Report urges greater fidelity to the requirement of 35 U.S.C. § 112 that patent claims "particularly point[ ] out and distinctly claim[ ] the subject matter which the applicant regards as his invention."[1]
    - Lack of clear notice has been especially problematic in the area of computer-implemented means-plus-function claims. The Report, therefore, urges courts to consider the objectives of clear notice and definitiveness when determining whether a patent describes a sufficiently detailed structure to inform the public as to which means are claimed by the patent.
    - Courts should apply a standard for determining a "person having ordinary skill in the art" that is fact based, up to date, and appropriately tailored to the technology at issue. Whether a patent claim is sufficiently clear to satisfy the definitiveness requirement of 35 U.S.C. § 112 is to be determined based on a hypothetical "person having ordinary skill in the art." The Report says that, particularly in the IT context, courts are attributing too high a level of skill to that person of "ordinary skill in the art," and thus are allowing patent claims that are too broad and ambiguous. The Report also offered various recommendations calling for greater use of defined terms in patent applications and for using a patentee's prosecution history record as a source for claim interpretation.

2. **Improving the Ability to Foresee Evolving Claims** – Would-be patentees also need proper notice of (i) pending claims (i.e., applications that have been filed but that have not yet been published) and (ii) evolving claims (i.e., applications that have been amended to add new claims during prosecution). Accordingly, the Report made a number of recommendations to further those aims, including the following:

    - Legislation requiring that public notice of patent applications be issued within 18 months of filing
    - Legislation protecting from infringement actions parties that infringed only because of amendments to claims or the filing of new claims after a continuation, and that took substantial steps toward using the product or process before the amended or newly added claims were published

3. **Improving Patent Searches** – Given the sheer number of patents that inventors must search for and review, the FTC also made several recommendations to help inventors conduct searches in

1. The Report recommended that the PTO and courts adopt the holding of *Ex parte Miyazak*, 89 U.S.P.Q.2d 1207, 2008 WL 5105055, at *5–6 (B.P.A.I. Nov. 19, 2008) in which the PTO Board of Patent Appeals and Interferences held that if a claim is susceptible to two or more plausible claim constructions, it is too indefinite to be patented.

connection with developing new products. Those recommendations include the enactment of legislation requiring that the assignments of patents and patent applications be publicly recorded.

PATENT INFRINGEMENT REMEDIES

The Report made a number of recommendations for improving legal rules governing patent infringement remedies. The Report noted that both under- and overcompensation of patentees can hinder innovation, and therefore courts should award patent damages that "make the patent owner whole by placing it in the position it would have been but for the infringement"—no more or less.

1. **Lost Profits** – The Report notes that when the patentee itself has commercialized its invention, its market reward is profits on the sale of the invention. Accordingly, when a competitor infringes, the patentee's proper measure of damages is lost profits owing to the infringement. The FTC recommends that courts accord patentees some flexibility in formulating a "but for" world in which infringement did not occur so that the patentee is not undercompensated for the infringement. By the same token, the FTC also said that legal rules governing lost profits damages claims should reckon with the possibility that the infringer might have developed a noninfringing technology to compete with the patented technology. The Report decries two current conventions—the "entire market value" rule and the practice of awarding patentees lost profits on some infringing sales and reasonable royalty damages on others. According to the FTC, those approaches do *not* take proper account of the possibility of noninfringing, competing technologies in calculating lost profits damages.

   The Report makes several other recommendations for changes to lost profits damages calculations, including the following:

   - Courts should take into account proof of any circumstances besides the infringement that would have diminished the patentee's profits in the "but for" world, and should consider the degree to which the patented invention was just one component of a larger product.
   - Courts should require proof of the degree of consumer preference for the patented invention over alternatives when awarding lost profits. A failure to account for weak consumer preference for the patented invention may lead to overcompensation of the patentee.

2. **Royalty Damages** – For patentees that license their products, the measure of damages upon a finding of infringement is the amount of royalty payments the patentee would have received from the infringer in an arm's-length negotiation conducted in the "but for" world. The Report recommends that courts award royalty damages consistent with a hypothetical negotiation between a willing licensor and a willing licensee (including for those patents subject to a reasonable and nondiscriminatory (RAND) commitment). The Report further recommends the following:

   - Courts should clarify for juries that the factors formulated in *Georgia-Pacific v. United States Plywood Corp.*, 318 F. Supp. 1116, 1120 (S.D.N.Y. 1970), *modified and aff'd*, 446 F.2d 295 (2d Cir. 1971) (affirming trial court's use of 15 factors for setting reasonable royalty damages after infringement) to determine a hypothetical royalty payment are not exhaustive. Courts also should not admit evidence solely because it happens to fall within one of the *Georgia-Pacific* factors if it is otherwise not germane to the particular circumstances at issue in the case.

- Courts should admit expert testimony based on payments for comparable licenses (as a yardstick for determining what the royalty payments would have been in the "but for" world) only upon a satisfactory showing of similarity between the infringed patent and the proffered comparables.
- Courts should not award damages that exceed the incremental value of the patented invention over its next-best alternative. That amount is presumably the maximum that a licensee would have been willing to pay in a negotiation conducted in the "but for" world.
- Further, patentees are overcompensated when they are awarded royalties based on the premise that the negotiation with the infringer would have taken place in the "but for" world *after* the infringer made large investments in the infringing technology. That premise yields an unjustifiably high royalty rate because it is based on a "hold up" of the infringer by the patentee. Courts should instead set the hypothetical negotiation at an early stage of the infringing item's development in order to avoid the inclusion of switching costs in the patentee's damages award.

3. **Permanent Injunctions** – Courts often grant permanent injunctions prohibiting future infringement in addition to awarding damages for past infringement. The Report made several recommendations for changes in legal rules governing the issuance of such injunctions, including the following:

- Courts should not presume irreparable harm based on patent infringement, but instead should consider whether the four factors articulated in *eBay v. MercExchange* have been satisfied before awarding injunctive relief.[2] Whether the patent owner made a RAND commitment should also factor into the determination of whether a permanent injunction is a proper remedy.
- Courts should consider the hardship that would be suffered by the infringer, except in those cases in which the infringer is copying a patented invention despite knowledge of the patent. Courts should also consider the public interest if the injunction were to result in a "hold up" on a patent for a minor component of a larger product.
- In the event that an injunction request is denied, courts should compensate patentees for their future expected losses based on a hypothetical royalty negotiation conducted in the "but for" world between a willing licensor and willing licensee.

Although many of the FTC's nonbinding recommended changes to the patent system are significant, particularly in respect to patent notice and infringement remedies, it remains to be seen which (if any) of the proposed reforms Congress, the PTO, and the courts will actually implement. Nevertheless, the FTC's voice is influential, and the report provides a thoughtful commentary on how to better harmonize the tension between certain of the rules and practices of the current patent system and the goals of national competition policy.

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2. In e*Bay vs. MercExchange, LLC*, 547 U.S. 388, 391 (2006), the Supreme Court said that a patentee must address the four factors traditionally articulated as the standard for obtaining equitable relief when trying to obtain an injunction based on an infringement: (i) the patentee would suffer irreparable harm absent an injunction, (ii) money damages would provide inadequate relief, (iii) equitable relief is warranted considering the balance of the hardships as between the parties, and (iv) the public interest would not be disserved by a permanent injunction.

If you have any questions or would like more information on the issues discussed in this LawFlash, please contact any of the following Morgan Lewis attorneys:

Chicago

David W. Clough	312.324.1772	dclough@morganlewis.com

Philadelphia

Mark P. Edwards	215.963.5769	medwards@morganlewis.com

Washington, D.C.

David R. Brenneman	202.739.5056	dbrenneman@morganlewis.com
J. Clayton Everett, Jr.	202.739.5860	jeverett@morganlewis.com
Scott A. Stempel	202.739.5211	sstempel@morganlewis.com

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