Prepared Statement of William T. Fryer III
For Hearing on S 1543 - Process Patent Amendment of 1985
Before the Subcommittee of Patents, Copyrights, and Trademarks, Of the Committee on the Judiciary,
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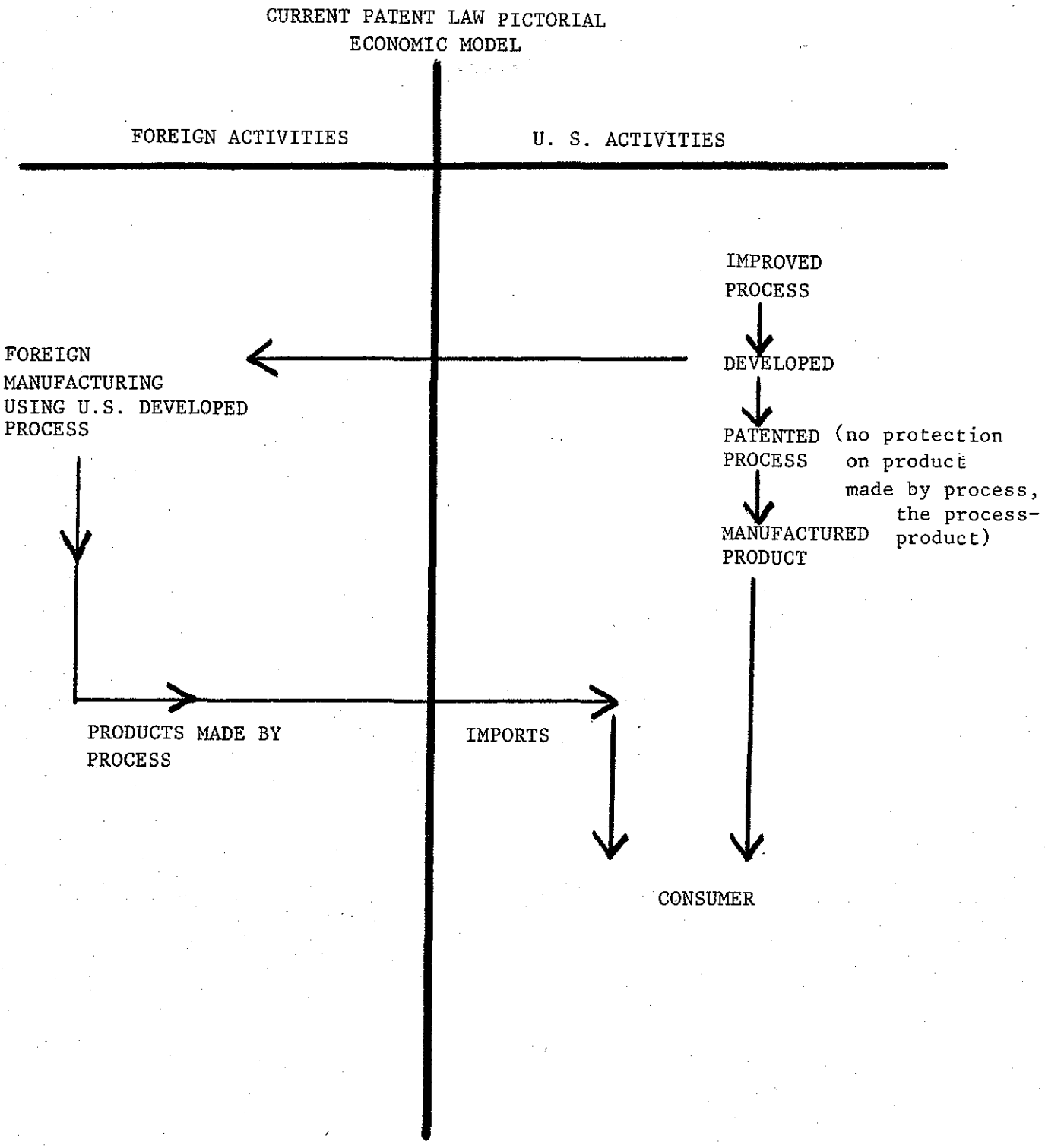
My name is William T. Fryer III, and I am a full-time law professor at the University of Baltimore School of Law in Baltimore, Maryland, where I have taught since 1980. Prior to 1980, I taught at the University of South Dakota School of Law, as a visiting professor at Pepperdine University Law School, and as an adjunct professor at Capital University School of Law in Columbus, Ohio. At each of these schools, except Pepperdine, I have taught antitrust and patent law courses and performed research in these fields and I continue to teach courses in these subjects at the Univeristy of Baltimore. I am an experienced patent attorney, having been a patent examiner, government attorney, corporate patent attorney and chief patent counsel, and law firm attorney. My active practice experience spans over 20 years, and thereafter I have served as a consultant and expert witness on several occasions. I give you this detailed introduction to show that I have a very broad and continuing interest as a teacher in the economic impact of the patent laws.

I am not speaking on behalf of any of the parties involved in this legislation. I was solicited by the Subcommittee staff to present my independent, critical analysis of the economic factors involved in this legislation and to offer my opinion on its impact. I will have a few specific recommendations for your consideration that should help bring the impact of this legislation into acceptable balance.

The ecomonic situation surrounding this legislation is best illustrated by a simple picture of Figure 1 on the next page. The subject is protection of products made by a process, referred to in this paper as process-product. Other processes for creating the product are not the subject of this legislation. These other processes are freely utilized, unless they are subject of U.S. patent protection. As matters now stand, the outward flow of U.S. technology for use in foreign countries creates products that are imported into the U.S. These imports help to cause an unfavorable balance of payments between the U.S. and other countries. While the latest technological developments in this outward flow of technology are usually protected by U.S. product and process patents, helping U.S. industry recover some of its investment, the product patents usually expire earlier, as they are the first patents obtained. The improved processes create the same product in a cheaper and more efficient way, sometimes making the product manufacturing costs finally low enough for wide commercial availability of the product.

At the present time, these improved U.S. developed processes are being used overseas and the resultant products imported into the U.S. without any U.S. patent protection for the products created by these improved processes. U.S. patent law does not allow protection of a product made by a patented process unless there is a separate patent on the product. Since the product patent usually expires first, the improved process

FIGURE 1


CURRENT PATENT LAW PICTORIAL
ECONOMIC MODEL
FOREIGN ACTIVITIES
U. S. ACTIVITIES
IMPROVED
PROCESS
DEVELOPED
PATENTED
PROCESS
MANUFACTURED
PRODUCT
(no protection
on product
made by process,
the process-
product)
FOREIGN
MANUFACTURING
USING U.S. DEVELOPED
PROCESS
PRODUCTS MADE BY
PROCESS
IMPORTS
CONSUMER

creator is not able to stop importation of the product created by that improved process, even though its technology is being used to create products that compete with its own products in the U.S.

Competition from imports helps to give the U.S. consumer the highest product quality for the lowest price. Many U.S. and foreign companies are dependent on this unprotected technology and the U.S economic system recognizes this industry as a necessary part of the global competitive system. These industries wait for U.S. patents to expire and provide valuable competition with these patent owners. They challenge invalid patents and remove these undesired obstacles to the free flow of technology.

The U.S. patent system fits into this economic picture by increasing the incentive to create and manufacture new products and processes. Since tremendous investment is needed for new technology development, the absence of a reasonable return on that investment will discourage U.S. industry from creating new process-products. While these economic principles are well accepted, the application to the specific situation for this legislation requires a careful study of the economic impact. For this legislation to be effective it must create the needed investment incentive while not interfering with the necessary utilization of unpatented technology to maintain the competitive process.

With these facts and basic economic relations in hand, the stage is set to analyze the difficult question of whether S 1543, or a suitable amendment thereof, will benefit the U.S. economy. If this legislation becomes law it will stop the use of the patented process and the sale and use of processproducts in the U.S. A significant U.S. and foreign industry based on the use of this patented process technology will have to discontinue sales in the U.S. until the process patent expires. It will have to rely on unpatented technology to make the product. The cost of the process-product to the consumer for a limited period of time may be higher than if the technology was freely available for use overseas and importation and sale in the U.S. On the other hand, the process-product will have to be priced to encourage wide use for an adequate return on investment, tending to keep the price down. The same product made by processes that are freely available for use will be in competition, creating an even greater pressure on price of the process-product. After this limited period of product-process patent protection, the process and its product is available for use by all, and the price will be determined by the competitive system.

The U.S. process patent owner does have a procedure now for preventing imports of process-products, through the Internaltion Trade Commission (ITC). This procedure is much less important than the enforcement of the patent law in the federal courts, because the ITC can grant only an injunction, while the federal court can grant an injunction and assess damages. The patent law allows damages for a period of six years prior to the date of infringement suit. The ITC procedure is relative fast and has resulted in significant enforcement of U.S. process patents to stop process-product importation. While the ITC procedure offers an opportunity for the process patent owner to enforce its rights, there are negative aspects too. The ITC review is run on such a tight schedule, its enforcement effectiveness must be questioned. Another concern is the ITC staff controls the review process, a factor that leaves the outcome of a case in doubt, and in the end the procedure is a political decision. The President has the right to deny any order of the ITC, and it is always hard to tell what the White House advisors, and other administration officials will recommend to the President.

The federal court system enforcement of the patent rights added by S 1543 would not suffer from the same problems encountered with the ITC. The question that should be put to the proponents of this legislation is whether they would give up the present ITC procedure for process-product injunctive protection, if the patent laws were amended to add process-product protection. The willingness to make this exchange would support their argument that the present ITC system is inadequate in many respects. This change would focus the dispute in one arena and satisfy to some extent those who consider the patent process-product law amendment only serves to complicate the legal process and give the patent owner too much opportunity to obstruct the flow of technology.

A second problem area created by this legislation is the burden placed on the defendant in the enforcement of a process-product patent in a federal court. Prior proposals for process-product protection have created a presumption that the patent process was being used when some level of proof was reached by the patent owner. Then the defendant had to come forward with proof that the process used was not the patented one. This disclosure, ultimately by the manufacturer, could force it to reveal its trade secrets. Whether the manufacturer is in the U.S. or overseas the problem is the same. Recent refusal by the Coke Cola Company to reveal its trade secret formula to a federal court is an example of an extreme situation, but it is a real problem for anyone with a trade secret. I see no reason to have a special presumption on burden of proof in process-product litigation. The courts have established rules of civil procedure and evidence to protect a manufacturer's secrets and require the patent owner to prove its case, and they should apply to all patent litigation. If the patent owner cannot find the evidence, it should not prevail.

My suggestion is to ask the industry representatives sponsoring this bill if they will accept in S 1543 a statement that the burden of proof used in other patent infringement litigation will be followed. If they agree to this point, a lot of the possible anti-competitive impact from this legislation is removed. Then, there is no supportable argument that this legislation is specifically designed or can be used unfairly to draw out the secrets of manufacturers, or to put retailers or wholesalers in the position of forcing the disclosure of the manufactuer's secrets to do business in the U.S. My understanding is that it is harder to prove a process is made a particular product, but companies under laws in other countries similar to the one proposed here have been able to meet that burden effectively. They should be willing to accept the same responsibility under the U.S. patent system.

The final area of economic impact that I will consider is the effect of this legislation on the U.S. industry component that sells or uses products made by a process-product patent under S 1543. These industry components will have to be concerned now over whether they are patent infringers and must stop selling or using the process-product and pay damages for past infringement. Under present U.S. patent law, only the manufacturer in the U.S. is liable, as the one who uses the patented process, since the process-product is not protected, without a separate product patent. The proposed legislation that protects also the process-product when the

process is protected could dampen economic activity, unless it is clear how the sellers, users, and manufacturers can operate with adequate notice that there is patent infringement.

In general the infringement notice provision under U.S. patent law is rather liberal. Damages for a product infringement start when actual notice is received by an infringer, or before when a patent notice is placed on the product. It is clear from S 1543 that there is no liability for damages due to notice on the process-product, and liability for damages starts when an infringer knows, or is notified of the infringement. There is a vague statement in the legislation about the effect of an infringement suit. This language needs to be clarified. Apparently, it means when an infringement suit is filed against a person, the damage period begins for that person.

The impact of the S 1543 damage provision on sellers and users, with liability going back to some informal communications of possible patent infringement, leaves the situation too unsettled for the economic system to function effectively. There are several simple ways to clear up this point, such as using the procedures now incorporated in H.R. 1900, the Industrial Design Protection Act of 1985. Another approach is to use the procedure found in the Semiconductor Chip Protection Act of 1984. I prefer the industrial design bill provision that in essence does not hold the sellers liable unless they know of the infringement and refuse to reveal the manufacturer of the goods, or if they are in collusion with the manufacturer in knowingly manufacturing and selling, or using, an infringing product. This method of concentrating on the root of the infringement problem, the manufacturer and its partners, avoids the scare tactics that can disrupt necessary competitive activity. I also favor written, registered or certified mail notice of infringement, before the seller or user is liable for damages prior to being sued.

In summary, I have presented three suggestions: (1) elimate the ITC action in favor of relying entirely on the federal court patent suit for protection of the patented process-product, (2) the use of the same burden of proof for all patent litigation, including process-product suits, and (3) clarification of who is liable and when. With these changes this legislation will effectively serve the U.S. economy. While I have focused on areas needing change, I want to emphasize that this legislation is needed to stimulate the U.S. economy. I am convinced from my experience and research that the U.S. industrial investment, jobs, and the consumer will all benefit by this change.

I have carefully studied the criticisms of this type of legislation presented in the previous hearings on S 1535 and S 1841, on April 3, 1984. You have noted that I accept with qualification some of these criticisms and offer simple solutions. Some of the prior objections were based on technical arguments that the U.S law should not be changed, because there is no working requirements here, as in some other countries, or there are limitations in 35 U.S.C. §102 concerning the geographic effect of prior art. As I understand these arguments, they are misguided and do not recognize the fundamental point that our patent system is carefully designed to serve the U.S ecomony. The courts, Congress, and practitioners recognize that in an capitalistic society useful technology will be developed and utilized. It has been so in the past and it is true now. This legislation is not for the purpose of restructuring the basic principles of the U.S. patent system. Our attention should be

directed and energy spent on how to fine tune a change in the U.S. patent system, where a clear need has been demonstrated. I trust my comments are useful in the further consideration of this important legislation. I welcome questions at any time and if I can be of further assistance, please let me know.

Summary

1. An analysis of the ecomonic situation surrounding S 1543 is presented.

2. Recommendations for improvement in this legislation are in the areas of eliminating the ITC action available now to obtain an injunction on a patented process-product in favor of relying solely on the federal court action with the added right to prevent use or sale of the process-product; clarification of the burden of proof for the defendant in a patent infringement suit; and clarification of when a seller or user of a process-product is liable as an infringer.

3. This legislation is verv important to the U.S. economy and in effective form it should be enacted promptly.