Department of Justice

Testimony of

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Subcommittee on Courts, Civil Liberties
and the Administration of Justice
Committee on the Judiciary
United States House of Representatives

Concerning

Government Patent Policy
Provisions of H.R. 6933

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Mr. Chairman and Members of the Subcommittee:

I appreciate the opportunity to testify today on behalf of the Department of Justice in support of H.R. 6933, the omnibus Administration bill to provide for the re-examination of issued patents, a new fee system for the Patent and Trademark Office, and a uniform government policy for the allocation of rights in federally financed or supported contractor inventions. Section 6 of that bill would amend title 35 of the United States Code by adding a new Chapter 38 entitled "Government Patent Policy Act of 1980," which provides a sound approach for achieving greater uniformity in the allocation of patent rights in federally sponsored or supported research and development activities. In recognizing the need for a more prominent position for the private sector in the commercial development of funded inventions, section 6 appropriately balances the potentially conflicting interests to be achieved by this type of legislation -- interests that have been the subject of an intense debate for the past thirty years or more.

The Department of Justice and many others believe that government patent policy legislation is necessary not only to increase competition for government research and development contracts and to stimulate the best efforts of recipients of government research and development assistance, but also to improve the prospects for innovation nationally. The successful accomplishment of these goals will provide the American

economy with tangible benefits, including: additional competition in foreign and domestic markets; new and improved products; more jobs; a better competitive posture internationally; and a reduction in the public and private costs of the government's research programs.

The Department's interest in government patent policy legislation flows principally from our antitrust enforcement mission to make competition work in our economy. A primary objective of that mission is to foster innovation incentives. Innovation is as vital an element in the competitive process as the competitive process is in the success of this Nation's economy. Measures which will encourage greater innovation, such as the proposed Administration bill, H.R. 6933, will benefit consumers by creating additional competition in the introduction of new products and services.

Traditionally, the government has supplemented the innovation incentives provided by its antitrust enforcement activities in many ways; among them are the patent system and the sponsoring and supporting of research and development activities. The patent system tends to encourage investment in long-range, high-risk research and development projects by providing a limited and temporary respite from imitative competition while the innovator seeks to recover its innovation investment in the marketplace. However, the availability of

such protection does not always provide an adequate incentive for businesses to engage in particularly expensive and long-range research and development endeavors. This is especially true where imperfections in the market make it impossible for the potential efforts to justify the required investment. In such cases, the federal government improves upon the incentive structure by supporting all or part of the initial research effort. Since World War II the government's participation in research and development activities has increased substantially, so that it now sponsors or supports nearly one-half of the total national effort annually.

Patented inventions frequently result from such government research and development activities. As one might expect merely from the nature of the endeavors funded by the government, the vast majority of these inventions are not suitable for private commercial exploitation but, instead, are valuable only to the extent that they have contributed generally to the technology base of a particular industry or sector of the economy. Periodically, however, research does produce patentable inventions that have potential commercial value. The proposed legislation is concerned with providing an efficient and equitable means for assuring the commercial exploitation of these inventions.

Although this concern may be the paramount objective of section 6 of H.R. 6933, it is important to realize that other concerns must be adequately and credibly addressed by legislation in this area. Section 6 seeks to achieve at least five distinct goals: (1) adequate protection of the public's equitable interest in inventions resulting from federal funding; (2) encouragement of private contractors to exert their best efforts as well as encouragement of contractors to participate as widely as possible in government-sponsored research and development programs; (3) full disclosure to the sponsoring federal agency of all contractor inventions resulting from government funding; (4) the commercialization, under the most competitive circumstances possible, of inventions resulting from federal funding; and (5) the elimination of any unnecessary administrative costs incurred by the government or its contractors as a consequence of a federal agency's management of patent rights.

Because these goals tend to conflict in some ways, prior to the formulation of section 6 there has not been any broad consensus within the Government as to the appropriate manner in which to allocate rights in inventions made by government contractors. Presently, the federal agencies follow a variety of policies that accommodate these and other objectives in a number of different ways. There exists no comprehensive law

controlling the disposition of contractor inventions. Congress has enacted legislation only on a piece-by-piece basis, that is with respect to particular agencies or subject matter. Such laws generally provide that title to inventions resulting from the covered research and development normally will be retained by the government; none of the statutes provides that title should be given directly to the contractor. Nevertheless, some of the statutes permit the contracting agency to waive the government's title in an invention after it evaluates several factors, such as the invention's importance to the public health, welfare, and safety and the effect of the waiver on promoting the invention's commercialization. Such provisions are contained in the Federal Nonnuclear Energy Research and Development Act of 1974. 1/

In the absence of specific statutory authority, agencies allocate rights in inventions made by government contractors pursuant to guidelines contained in the 1971 Presidential Statement of Government Patent Policy. 2/ The Presidential Statement, which is implemented by the regulations of the various agencies, generally provides a flexible framework

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1/ 42 U.S.C. §§ 5908-5909.

2/ 36 Fed. Reg. 16887 (1971). This 1971 statement is a slightly modified version of the 1963 Statement of Government Patent Policy issued by President Kennedy. 28 Fed. Reg. 10943 (1963).

within which rights to inventions resulting from federal funding may be allocated. The Statement describes in general terms those conditions under which the government will take title to an invention and those conditions under which the contractor may acquire the title.

As a consequence of the vast array of statutes and regulatory authorities directing the allocation of patent rights in inventions made by government contractors, the agencies have adopted a wide variety of non-uniform and sometimes inconsistent policies governing the disposition of such rights. Some agencies grant title in inventions to the contractor in a majority of instances; others generally retain title for the government. Unless prohibited by statute, nearly all agencies waive title to the contractor under certain circumstances. Moreover, some agencies that are subject to more than one statutory or regulatory scheme have adopted patent rights allocation policies that vary according to the particular research and development program in which the contractor is participating.

This lack of uniformity has created considerable confusion among contractors who perform research and development activities for several agencies or programs. As President Carter observed with respect to federally funded invention rights in his Industrial Innovation Message to the Congress of

October 31, 1979: "This confusion has seriously inhibited the use of those patents in industry." Section 6 of H.R. 6933 embodies the President's proposal for a uniform government patent allocation system and would replace the numerous conflicting patent allocation policies presently in force with a single government patent policy.

The Administration's bill differs somewhat from the Department of Justice's historical position in the government patent policy debate. We have previously stressed two goals: (1) that the government retain the principal rights in inventions resulting from government sponsored or supported research and development, in order to ensure that contractors could not use inventions paid for by taxpayer's funds to exact supracompetitive profits or to increase significantly their economic power in particular markets; and (2) that, as a general principle, the public interest requires that a contractor not receive exclusive rights in an invention until after the government has been given a reasonable opportunity to evaluate the identified invention and its potential market impact.

While varying to some extent from the Department's former position, the Administration's bill continues to reflect the importance of the basis for our concerns. It seeks to accommodate these considerations, however, through enactment of a novel statutory scheme. Although it permits some deviation,

the bill generally provides for the government to take title to inventions resulting from federal funding. Contractors receive exclusive licenses in fields of use that they specify, and in which they agree to commercialize the inventions, so long as the receipt of these rights is not inconsistent with the public's interest in those inventions. The government retains the right to license the invention or otherwise make it available to the public in fields of use not selected by the contractor. Research and development contracts with small businesses and nonprofit organizations are treated somewhat differently. Such contractors generally would receive title to any resulting patents rather than licenses.

Regardless of whether the contractor performing the research is a large business, a small business, a nonprofit organization, or other entity, the government receives a royalty-free, nonexclusive right to practice the invention; it also retains "march-in rights" that permit it to terminate a contractor's exclusive rights when necessary to commercialize the invention, to protect the national security, to meet requirements for public use specified by government regulation, or to correct situations inconsistent with the antitrust laws.

The Department's support for the Administration's bill is based upon a thorough re-examination of the rationale behind

our historical position. Important inputs into this re-examination included our consultations with government agencies that fund research and development and the experience we achieved through our participation on interagency committees analyzing the relevant issues. We conclude that the novel provisions in H.R. 6933 serve adequately to safeguard the public's equitable interest in funded inventions and to assure that the grant of exclusive rights under the patents will not have substantial anticompetitive effects. We therefore urge adoption of this innovative proposal for allocating relevant patent rights.

The Administration's bill seeks to maximize the prospects for achievement of the five government patent policy goals. The experience of government agencies funding research and development indicates that certain of these goals are best achieved through the offer of some degree of exclusivity to the contractor. First, well-qualified businesses with strong proprietary positions in particular fields are sometimes reluctant to bid for government research and development contracts unless they can be assured that their independently-acquired proprietary positions will not be compromised as a result of their participation in the government program. Providing such a business with the opportunity to receive exclusive rights will induce it to participate at competitive

rates and to exert its best efforts in the program. The grant of exclusive rights thereby will help to achieve the goal of encouraging the widest possible participation in government funded programs.

Moreover, with respect to the goal of commercialization of inventions, the majority of those inventions that are commercially valuable require substantial development before they may be marketed. Exclusive rights in these inventions are most often necessary to provide the contractors with sufficent incentives to make commercialization investments.

Finally, H.R. 6933 generally will promote efficiencies by limiting administrative costs. It establishes the presumption that contractors normally should receive exclusive rights in inventions resulting from federal funding. The bill therefore eliminates the necessity for agencies to conduct inquiries into the most appropriate allocation of those invention rights, except where, at the time of contracting, it would appear on the basis of reasonably foreseeable facts that a contractor's acquisition of exclusive rights would be contrary to the agency's mission or the public interest. Consequently, the agency's limited review after an invention has been identified would focus only on those events that were not foreseeable at the time of contracting.

While offering exclusive rights to encourage contractor participation, reporting, and commercialization, the Administration's bill also contains safeguards to assure achievement of the other government patent policy goals; it protects the public's equitable interest in inventions resulting from federal funding and ensures that the acquisition of exclusive rights by contractors does not result in a substantial impairment of competition.

The Administration's bill protects the public's equitable interest in inventions resulting from federal funding in various ways. First, it allows the government to extend licenses in all fields not claimed by the contractor or in which no commercialization occurs. Pursuant to this authority, the government can attempt to bring to the public the benefits of an invention's full commercialization.

Next, at the time of contracting, an agency may deviate from the general patent rights allocation system provided in the bill when such deviations are made in furtherance of the agency's mission and the public interest. Therefore, in appropriate cases when the public interest so indicates, the agency can permit the contractor to acquire more or fewer rights in inventions than it would normally receive. The bill's deviation provision provides agencies with the flexibility to take proper actions in unusual contracting situations. For example, although most inventions resulting from

federal funding are not commercially valuable, in appropriate instances, an agency could include in a contract a recoupment provision that would obligate the contractor to pay back all or part of the government's funding if the invention is successful. 3/ The intent in providing this deviation authority is to encourage the agencies to inform contractors at the outset of the contracting process that forthcoming invention rights will not be allocated in conformance with the provisions of the bill.

Most importantly, the bill adequately addresses the Department's traditional concern that contractors not receive exclusive rights in inventions before the government has had an opportunity to evaluate the invention and its potential market impact. It provides the government with the opportunity, upon disclosure of the invention and before the final vesting of any exclusive rights in the contractor, to determine whether the contractor's receipt of such rights is consistent with the public's interest in the invention. This innovative "second look" provision has not been present in previous legislative proposals providing contractors with exclusive invention rights; however, the opportunity to make such a determination after the contours of the invention have been revealed to the government should be an essential feature of any government

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3/ In addition, the implementing regulations issued under the bill could provide guidelines to be used by the agencies when making their recoupment decisions.

patent policy legislation. If, at the time of disclosure, the agency concludes that the contractor's acquisition of exclusive rights would be contrary to the agency's mission, would be detrimental to the national security, or would result in substantial competitive harm, it is essential that the government be able to prevent or otherwise limit the contractor's receipt of those rights.

To comprehend the potential impact on the federal contracting process of the government's right to conduct inquiries into identified inventions, it is important to view this right in the context of the bill's deviation provision. Because the deviation authority would exist under the bill at the contracting stage, it is anticipated that agencies will intervene at the postdisclosure stage to prevent or limit the vesting of exclusive rights only when required by the occurrence of events that were not foreseeable at the time of contracting. Thus, the scope of the government's inquiry at the time of an invention's disclosure should be quite limited. The agency's review should focus on those unforeseen circumstances of which it has become aware since the time of contracting that now require it to deny the contractor's exclusive rights request in any designated field of use. For this reason, the possibility of such an inquiry should not

significantly affect the incentives of sophisticated contractors that are considering participation in a funded project. In addition, the limited scope of the government's right will also assure that undue administrative burdens are not imposed on the contracting agencies.

The bill also addresses the Department's traditional concern that contractors should be prevented from attaining anticompetitive market power through their receipt of property rights resulting from public funding. The bill provides that the contractor's receipt of an exclusive license shall be deemed an acquisition of assets of another corporation. As such, the acquisition is subject to antitrust-type scrutiny. Under the bill, government may terminate, or prevent the initial acquisition of, a contractor's exclusive rights if, under the relevant antitrust laws, the contractor's receipt of those rights has tended, or would tend, to lessen competition substantially or to create a monopoly.

It must be stressed that the bill does not prohibit contractors from receiving exclusive rights in inventions resulting from federal funding that would be adequately commercialized even in the absence of such rights. As a result, some supracompetitive profits may be available to contractors which, in hindsight, were not necessary to call forth the required commercialization investment. However, the

Administration's proposal is premised on the view that such a result is acceptable as a trade-off for assuring the maximum commercialization rate of funded inventions and the efficient administration of the government's research and development programs. Moreover, as described above, the bill's antitrust provisions will enable the government to prevent a grant of exclusive rights from producing significant anticompetitive effects.

The preceeding discussion has focused principally on the provisions in the Administration's bill that involve large, for-profit businesses. The provisions covering small businesses and nonprofit organizations differ somewhat. As I noted earlier, such contractors will receive title in the inventions they make pursuant to federally sponsored or supported research activities. In addition, although these contractors are subject to the bill's "march-in" provisions, they are not subject to the government's "second look" authority.

Small businesses and nonprofit organizations are treated differently in the Administration's bill in recognition of their special place and function in our society. The flexible operations of small businesses and nonprofit organizations already provide those entities with strong incentives to promote an invention's commercialization to the widest possible

extent. We expect that the government's efforts both to license inventions made by government employees and to license contractor inventions in those fields of use not selected by larger contractors will be replicated by small businesses and nonprofit organizations with respect to the inventions in which they receive title under the Administration's bill.

In addition, small businesses and nonprofit institutions typically would have insufficient market power for their acquisitions to raise serious antitrust questions. This minimizes the need for "second look" scrutiny at the time of disclosure of the invention. However, if a small business or nonprofit organization's acquisition of title actually produces competitive harm, the "march-in" provisions in the Administration's bill would subject the contractor's acquisition of title to antitrust scrutiny at that time.

The Administration's bill also specifies the manner in which rights will be allocated in inventions made by government employees. This question is resolved by codifying the basic policy concepts of Executive Order 10096, 4/ which then will be

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4/ 15 Fed. Reg. 389 (1950), as amended by Executive Order 10930, 26 Fed. Reg. 2583 (1961).