

i.e. mainly for processes, production sequences, recipes, etc., which are not protected by patents. Appropriate securities help against this, e.g. the licensor also remains a supplier.

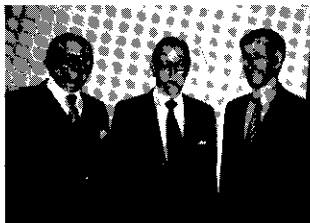
9. *The freezing of licensing fees in a blocked account* can sometimes occur in many overseas countries. But: the possibility always exists that international credit measures can lead to a thaw, so that the license fees can eventually be transferred to the licensor. Furthermore: this danger can be transformed into an advantage for the licensor. The frozen funds can be used in the licensee's country to meet his company's or even his own personal needs. The possibility also often arises for participation in an enterprise that hitherto was merely a licensee.
10. *Language difficulties* stand in the way of many a licensing project. In contrast to transactions in goods much more writing and negotiating is involved in licensing business. Many potential licensors shun the work that is arising from this. However, the multifarious written exchanges can be taken care of by an experienced correspondent in the appropriate foreign language. Drawing in an interpreter is advisable for licensing negotiations, since the use of an international auxiliary language (e.g. English or French) does not completely remove the dangers of misunderstanding or false interpretation.

#### CONCLUSION

Manufacture under license abroad usually leads to mutual success if the following three "essentials" are secured: —

1. The RIGHT licensing partner
2. The RIGHT licensing analysis
3. The RIGHT licensing agreement.

*Left to right: Peter F. Casella; U.S. Commissioner of Patents, the Honorable Robert Gottschalk; David Dougherty.*



*(On the evening of the adjournment of the Midwest Regional Meeting, David Dougherty, President of the Niagara Frontier Patent Law Association and Peter F. Cassella, his co-worker, invited several LES Members to be their guests at the meeting of the Niagara Frontier Patent Law Association. Commissioner Gottschalk was the speaker of the evening. The text of his remarks appear below:)*

An address by The Honorable Robert Gottschalk Commissioner of Patents, U.S. Department of Commerce, delivered before the Niagara Frontier Patent Law Association, Continental Inn, Tonawanda, New York, April 25, 1972.

#### THE NATION'S NEEDS AND THE SCOTT AMENDMENTS

The Constitution, you will recall, contemplated that Congress would establish a patent system to promote the progress of the useful arts.

I have long held a deep conviction that our patent system, so established, is sound in principle, morally right, and desperately important — and that we are all under a heavy obligation to make as sure as we can that the system functions effectively, as the founding fathers intended.

We had an open house at the Patent Office a few weeks ago on a Sunday afternoon. It was an all-time first. It was a great thing to see our Patent Office people — of all grade levels, and all ages, professionals and non-professionals alike — come and bring their families. One of our objectives, of course, was to help bring home to all of them the nature of our work and a sense of our mission — and some appreciation of the many contributions we have made over the long course of our history.

The thought struck me rather forcefully that afternoon that while there are today a great many Government agencies — and while we're not the biggest by a long shot — none are older than we are, and very few, in the long view, have been more important than we have.

There is no question that, from the very beginning, our patent system has been a vital factor in the growth and the progress of this country. To me it's particularly important to realize this at this time — because, as I see it, our country is facing today a challenge greater than any that has confronted it in perhaps more than a century — a challenge to our national stature, our industrial and commercial leadership, our quality of life and our social progress.

You'll recall that some-years ago the launching by the USSR of "Sputnik" had a tremendous impact on this country. It gave us a jolt. It did a lot to stimulate and reshape the thinking here about education, technology, and many aspects of our national life.

Our response was dramatic. There was a great upsurge in technological activity, and, literally, we shot for new highs. We put men on the moon. We really made history at a terrific clip.

Well, it seems to me that we are facing today something that I think of personally as Sputnik II. We've had another shock, another rude awakening. We have another challenge.

We've come to realize, as the President put it, that we're no longer "running against the clock" — today we're running against very real competition. And unless we're successful in this new contest, the very things that we have taken so often for granted, as basic and inherent in the American way of life, will be lost to us.

We've taken for granted our progress, convenience, high standards of living, and superiority across the board.

We're no longer justified in making those assumptions. We're no longer wise, if we pursue our activities on the basis that we're way out front — when

the facts indicate that we are not. We've got to recognize the reality of the challenge and its seriousness — and react properly to it.

I think this must be of great interest and concern to all of us here — and this certainly includes my colleagues from the Department of Commerce — not just from the standpoint of patents, but the broader aspects of trade generally.

What we've got to realize is this: that it's only as we compete effectively internationally, that we can regain the economic advantages we have enjoyed in the past. And that it's from those economic advantages that we have been able to derive the pleasures and comforts, and the social progress, which have come to be so important in our way of thinking about life in this country.

In all of this, the patent system must play a vital role. The patent system must be effective in helping to meet this new challenge.

It was very heartening to me to find in the President's Message to the Congress of March 16th on Science and Technology, that he had this to say, about improving the climate for innovation:

"There are many ways in which the Federal Government influences the level and quality of private research and development. Its direct supportive efforts are important, but other policies — such as tax, patent, procurement, regulation, and antitrust policies — also can have a significant effect on the climate for innovation.

We know, for instance, that a strong and reliable patent system is important to technological progress and industrial strength. The process of applying technology to achieve our national goals calls for a tremendous investment of money, energy, and talent by our private enterprise system. If we expect industry to support this investment, we must make the most effective possible use of the incentives which are provided by our patent system."

Now as I'm sure you are all aware, the Administration is determined to do everything possible to support the role of technology and the patent system in meeting this challenge. Secretary of Commerce Petersen has so committed himself on, to the best of my knowledge, every occasion when he has spoken about this situation publicly, since he became Secretary, and also on several occasions before he did.

He has stressed the importance of technology. He has stressed the importance of patents and patent policy.

It's in that context that we are doing our job in the Patent Office today. It's with a sense of purpose and mission which has always been present, but which has never been more important, more keenly felt, than it is at this time.

I've had a long time interest in what might be called the commercial aspects of patent activity — licensing, for example. To me one of the great things about the patent system is that it draws on every talent that each of us has. It affords each of us an opportunity to be effective — doing what we like best, and what we can do best.

The dissemination of new technical information

by means of patents is a basic necessity, if progress of the useful arts is to continue. But the actual application, on a commercial and industrial scale, of what does result from the innovative act — from the process of invention — depends upon far more than technology alone. All of the skills of business and management are called into play.

Even so, in the majority of situations, none of this would mean a thing if it were not for the fact that our patent systems, as we have known it, provides the incentive to which the President referred — the incentive to invest in the very risky, and very costly, development work that is necessary to translate the crude form of a new invention into something which is commercially salable, commercially usable.

It's only as that process occurs successfully — it's only as new processes are adopted, and new products enter the market place — that the progress of the useful arts really materializes.

This is why we have chosen the type of patent system we have. The inventor would be rewarded by a bonus or a prize — but these alone would provide no such incentive for the commercialization of new ideas. They would not provide the kinds of incentive and support that our patent system provides.

So it seems to me that it's very important to have the engineer and the scientist at one end of the spectrum, the businessman at the other end of it, and the patent system available and functioning effectively to bridge the gap between them.

The new term, of course, is "technology transfer" — and this is what it's all about. What that really means to me, and I think to most people nowadays, is that what exists in the pure technological state is translated into terms of practical commercial reality.

It's only as the entire process is complete and effective in all its phases — innovation, transfer and application — that we can achieve the national goals to which the President is referring.

Now against that background, let me suggest this. As I've often said — and you would agree, I am sure — I regard a sound patent system as dependent upon a sound Patent Office. But a sound Patent Office alone is not enough. Other elements are involved. The courts are involved, the bar is involved, the public is involved, other government agencies are involved, and the Congress is involved.

Unless each of the actors in this total drama understands what the play is about — unless we're guided by the same script, toward the same objectives — we may not achieve the results toward which the founding fathers pointed with that Constitutional provision. We've got to be sure that we don't work at cross purposes, and cancel out each other's efforts.

We've got to stop, I think, some of the circular conversation which has been so costly in terms of time and effort — and perhaps even more costly in terms of diverting our attention from the real objectives and needs of the system.

There's a great deal that can be said about what ought to be done, I think, in each of these areas.

I'd like, however, to direct my remarks at this time to the area of patent licensing.

The success of the entire patent system, of course, is predicated on the assumption that patents are worth having. Often, patents are worth having only if they may be licensed or assigned.

Freedom and certainty for a patent owner to license, or otherwise transfer, his patent rights are vitally important to the proper functioning of the patent system. The greater this freedom and certainty, the greater the incentives to invent and invest in the commercialization of new inventions, and to license others to use the new technology.

The converse, however, is equally true: the impairment or loss of effective licensing substantially negates the incentives, and the effectiveness, of the patent system. And in view of the challenge we are facing today to our technological leadership, I feel this is a matter of grave national concern, which commands our urgent attention.

Just two weeks ago, for example the Secretary of Commerce discussed the continued deterioration in our trade position, in testimony before the House Subcommittee on Science, Research and Development. Our overall balance of trade, he said, showed a deficit in 1971 for the first time since 1893. Among the factors contributing to this deficit, Secretary Peterson pointed out that our performance in the generation of new technology has been lagging relative to other countries.

Clearly, we now need to use, with maximum efficiency, every means at our disposal for stimulating the development and commercialization of new technology.

Unfortunately, for some time now the right of patent owners to utilize their patent rights and inventions has been under attack. In recent years, many questions have been raised as to the freedom of patentees to license or otherwise transfer their patent rights.

This has come about through so-called "case-by-case development" of the law. It has been intensified by many speeches and writings highly critical of existing and traditional practices. And the Congress has provided no guidance.\*

The result has been that a great uncertainty now exists concerning patent licensing.

The hearings before the Senate Subcommittee on Patents, in May of last year, brought this out most clearly.

One witness said:

"At present, there is great confusion and uncertainty as to the legality of certain patent licensing practices under the Anti-trust laws, as presently construed."

Another stated:

"The resultant problem is that there is a tremendous turmoil and uncertainty in this country as to what are the values of patent rights and what you can do with regard to licensing your patent on a reasonable basis."

Many others testified to the same effect. Several gave striking examples from their own experiences as to how this uncertainty has discouraged development and commercialization of patented inventions.

It was to arrest the further development of the trend in judicial decisions toward restriction of the

patentee's rights — and to restore a sense of stability and confidence with respect to the licensable nature of patent rights — that the Scott Amendments were introduced.

You will, of course, recall that when these Amendments were introduced by the senior Senator from Pennsylvania, he noted that various patent law associations had approved them in principle.

The Department of Commerce also believed, and continues to believe, that there is an increasingly urgent need for *statutory* clarification and stabilization of national law and policy with respect to the licensing of patents.

We recommended to the Senate Subcommittee, in May 1971, statutory provisions along the same lines as the Scott Amendments. Developments during the year since then have confirmed and strengthened the views we then expressed.

What happened, of course, is well known to most of you. The Amendments were vigorously opposed by the Department of Justice and others holding similar views.

Last October, the Senate Subcommittee reported out the McClellan bill, S. 643, without any patent-antitrust amendments. Since that time, there has been continuing discussion of the Amendments, and the possibility that they might receive further consideration in the Congress.

I certainly hope they will — for the Scott Amendments would provide the greater certainty and stability with respect to patent licensing which are so sorely needed today.

They would provide these by clarifying and stabilizing prevailing case law. In brief, they would codify the legitimacy of a number of commonly-used license provisions, and codify the "rule of reason" of the 1926 *General Electric* case, which is already the prevailing test for judging the legality of licensing arrangements.

The Amendments would make no significant changes in prevailing patent law.

The opponents of the Amendments have insisted that they would effect major changes in existing law. In my opinion, these charges are entirely unfounded.

I believe the fundamental reason for opposition to the Scott Amendments is that the critics want the law to be developed by the courts on a case-by-case basis; and many times, in repetitive rhetoric, they have strongly urged that point of view.

I submit that this is wrong. The public interest would be far better served by — and it urgently requires — clarification of the patent-antitrust relationship through legislation.

Let's consider a few examples of what's been happening under the case-by-case approach.

Defendants in patent litigation continue to raise the "exorbitant royalty" defense that was recognized in the *American Photocopy* case\*\* in 1966 — although it certainly is not prevailing law, and has been expressly rejected in subsequent cases. Even the Government raised the exorbitant royalty defense in the recent *Carter Wallace* litigation in the Court of Claims.

Nevertheless, in opposing the Scott Amendments, the Department of Justice testified, at the Senate

hearings, that legislation on this subject was unnecessary, because the defense had been adopted by the Courts in only a single case.

In the absence of legislation, this issue may continue to be litigated, and some other court may well decide to condemn "exorbitant royalties." That such developments are not unlikely, and by no means impossible, is abundantly clear from what happened in the wake of *Lear*.

Following the unfortunate dicta in the *Lear* case, the business community was shaken by the district court decision in *Painton*. That decision, if it stood, would have abolished protection for trade secrets, and threatened to wipe out a large part of the favorable technological balance of payment — of over a billion dollars annually — that the United States has enjoyed from licensing technology abroad.

Even the Justice Department agreed that the decision in *Painton* had gone too far.

But when *Painton* was reversed by the court of appeals, Justice took the position that this reversal itself served to demonstrate that no legislation was necessary; and that the litigating process in the courts could be relied upon to properly control and regulate the development of such legal doctrines.

Fortunately, however, the Senate Subcommittee did approve a modified version of section 301 of the McClellan bill, which if enacted, should spare future litigants the burden of having to reexamine the *Painton* case in other district courts.

The recent decision in *Troxel v. Schwinn*, in the Western District of Tennessee, involved a specifically different legal doctrine, but it pointed up the same general problem with the dramatic impact and destructive potential of an atomic bomb. In ruling that the licensor of a patent, later found to be invalid, must refund all royalties he had ever received, this decision blasts away basic concepts of contract law and equity, and threatens to vitiate the entire concept of licensing as a means of promoting the commercialization of inventions.

It appears to me that such erratic decisions as these are occurring with increasing frequency, making the need for clarifying and stabilizing legislation even more urgent. Particularly in this time of national trial and challenge — as the President has pointed out — we need the incentives of a "sound and reliable" patent system. We can therefore hardly afford the dangerous luxury of further delay.

The case-by-case approach ignores the cumulative effects of the uncertainty, expense and delays it involves. It leaves it up to the courts to set policies and directions of the law, in areas which the legislature is far better qualified to handle. And it entails obvious and serious dangers.

The greatest danger, of course, is the debilitation and destruction of confidence in the patent system to perform its Constitutional mission of promoting the progress of the useful arts. The erosion of that confidence has been under way for some time. It continues and gains new impetus with each new decision such as those I have mentioned.

The basic question, it seems to me, is whether — as a matter of national policy — we are willing to

stand by and permit that process of erosion to continue, or whether it is to be arrested, and our patent system permitted to function effectively — in accordance with present law, but freed of the spectre of continued harassment and confusion which has been draining its vitality and force.

This case-by-case approach would permit that process of erosion to continue. The enormous litigation expenses that are so imposed on patent owners are not only destructive, but discriminatory as well — for the individual inventor and the small company are in no position to engage in such litigation over protracted periods.

Resolution of patent-antitrust issues on a case-by-case basis could take years. Moreover, without some statutory guidance — such as the Scott Amendments could provide — there might never be any real stability in the law relating to patent licensing.

Some have argued that the proposed legislation would result in even more litigation than the case-by-case approach. Naturally, any legislation in such a complex area will cause some problems in interpretation with respect to particular fact situations. But, I think it most unreasonable to say, however, that trail markers in the forest will not aid the traveller.

One of the most insidious but important consequences of the case-by-case approach is this: that it leads many patent owners — fearful of ex post facto rulings of the courts — to sacrifice the full potential of their patents, as happens when they follow very conservative legal advice.

Proponents of case-by-case development — and conservative counsel, as well — are fond of quoting the famous statement by Justice Brandeis, about walking near the edge of a precipice:

"(You) may stumble on a loose stone, you may slip and go over; but anyone can tell you where you can walk perfectly safely within convenient distance of that precipice. The difficulty which men have felt generally in regard to the Sherman law has been rather that they have wanted to go the limit than that they have wanted to go safely."

But it seems to me that in the patent-antitrust area, no one can, any longer, be sure where the precipice is. Furthermore, it keeps shifting.

In this situation, a patent owner is constrained to stay very far back from the precipice, in order to have at least some feeling of safety. If he stays back too far, he will not obtain as much benefit from his patent as he otherwise would. And if he then finds patents less valuable — which would hardly be surprising — he will have less incentive to invent or to invest in the development and commercialization of new inventions.

This is certainly contrary to national interest.

Both the patent laws and the antitrust laws represent expressions by the Congress of public policy adopted in the national interest. Neither the definition of such basic national policies, nor the striking of a balance to reconcile differences or apparent conflicts between them, should now be left for determination by lawyers and the courts in adversary proceedings.

The Congress is the only proper body for dealing with such basic and complex socio-economic issues.

I believe that our national interests and needs now

urgently require an expression of national policy with respect to the patent-antitrust relationship — and that such policy should be determined and enunciated by the Congress.

\*"Which rights may and which may not, as a matter of public policy, be waived by a patentee in a licensing contract has not yet been decided by the Congress." *Current State of Patent and Know-How Licensing* by J. Patrick Kittler, the Business Lawyer, Vol. 27 page 691, April 1972.

\*\**American Photocopy v. Rovico, Inc.*, 359 F 2d 745 (7th Cir. 1966). In overturning a preliminary injunction, the Court of Appeals held that excessive royalties was a triable issue.

#### EDITORIAL

*LES is proud to announce that Richard William Rahn has been awarded his Doctorate Degree by the Columbia University Graduate School of Business. To our knowledge, this is a "first" — the first degree so granted based upon a dissertation (thesis) in the licensing field — and LES is happy to have cooperated with and helped Dr. Rahn in obtaining information via interviews and questionnaires relative to the subject matter of his dissertation "Pricing Decisions in Foreign Licensing" (see Vol. 6, No. 5, pages 191 to 202 of the December 1971 issue of Les Nouvelles).*

*Congratulations, Dick, from all your friends in LES. It could not have happened to a nicer fellow and a better friend of the licensing executives. You earned it and we rejoice with you.*

*The Licensing Executives Society, United Kingdom Region, held a One-Day Conference on the 26th day of January, 1972. The theme of the Conference was "GOVERNMENT, RESEARCH AND DEVELOPMENT, AND INDUSTRY." Some of the talks presented at that Conference and at an evening meeting of LES/UK are given below:*

#### GOVERNMENT, RESEARCH & DEVELOPMENT, AND INDUSTRY

Opening Address

by

*The Right Honorable Lord Sherfield*

It gave me great pleasure when my old colleague and young friend from the Atomic Energy Authority, your Chairman, Mr. Gay, invited me to open this Conference, though I must admit that he has cast me for a rather longer role in the morning's entertainment than I had bargained for. And indeed, if he led any of you to expect a major pronouncement from me on the issues before the Conference, I fear that I may prove something of a disappointment to him — though not, I daresay, to you.

My main task is twofold. First, I wish to congratulate the UK Region of the Licensing Executives Society on their enterprise in arranging this Conference on "Government, Research and Development, and Industry", and even more on their nice sense of timing. If my memory is correct, this Conference was originally set for the spring of last year on another subject, but put off. Could it have been that Mr. Gay had the gift of second sight and was therefore able to arrange for this Conference to be held at the height of one of the hottest known controversies on the perennially smouldering subject of Government support for Research and Development? And further, that in successfully tempting a group of gifted and authoritative people to appear on his programme, he was able to include Mr. Teeling Smith on the needs of the pharmaceutical industry, in the middle of a tense takeover battle between three of the leading British pharmaceutical firms? However, I am sure that Mr. Teeling Smith will adopt what our Japanese friends call "a low posture" on this issue, as indeed, I intend to do on the other.

I hope that Mr. Gay's keen nose for a suitable date will not only secure good coverage of the proceedings, but will also draw public attention to the function of Licensing Executives and the important role which they perform in another area of contemporary interest and debate — I refer to the transfer of technology.

The term Licensing Executives does *not* convey an unambiguous concept to the uninstructed. Your functions should be better known, as should the role of your Society in providing opportunities and a forum for the interchange of ideas in a most important field.

My second main task is to welcome the delegates here today, and to assure them that as soon as I sit down a most interesting programme will commence.

I have already said that the subject of this Conference is topical, timely and very controversial, and that I intend to adopt what our American friends call "a low profile" in introducing the subject.

I shall simply try to paint in some background and to suggest some reasons why the subject has been such a difficult one, especially in the last decade.

The scientific and technological revolution of my generation has enormously increased the demand for scientific research and development in breadth and in depth, and, of course, has also greatly increased its cost. These demands have been especially strong in the defence field, but Government has been increasingly drawn out of the defence field into the civil field as well, partly because it is very hard to delimit frontiers in research and development, partly because research could no longer be adequately financed in the universities or indeed in industry without Government money, and also for other reasons.

So the machinery of Government has been continually adapted to meet these increased demands for Government finance for R and D. And if you think I may lay too much stress on machinery, I am fortified by the opinion of Sir Richard Clarke, the former Permanent Secretary of the Ministry of Technology, when he says in his admirable publication "New Trends in Government", that "in science it is very difficult to distinguish between policy and machinery of