

United States Patent & Trademark Office
International Protection Study
Public Hearing 2
University of Southern California, Gould School of Law
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Outline of Testimony – Christopher J. Palermo

1. Thank you for the opportunity to participate today. As brief personal background, I am an attorney with 22 years' experience in the patent field, principally representing Silicon Valley applicants with software, networking and computer technologies. About half my practice involves startups and other small-medium enterprises (SMEs). I direct and manage foreign filings for these SMEs principally in Europe, Canada, Japan, Australia, South Korea and China.
2. Most of the startups with which I work do not express significant interest in foreign patent filings. But some do, and for them, the cost of the process is material, and daunting. Because of the cost, most of them defer filing as long as possible—they use the entire Paris Convention priority year to defer these costs. They also view PCT solely as a fee deferral system, mainly because the International Search Reports prepared for their technologies do not result in useful information, and because examining standards for IT-related subject matter differ greatly around the world, making centralized amendments is not particularly useful.
3. These SMEs also tend to see foreign patents as a low priority benefit in the early stages of the business. Priorities are finalizing product design, marketing and sales to result in “winning” in the marketplace, and obtaining a US patent position if appropriate. Venture capitalists and other early-stage investors in IT businesses tend to view patent exclusivity as a secondary factor because the real problem is competing in the market against established behemoths on the merits of product features and functions. Patents become more important in years 3 and later when the future of the business is more apparent, second-tier investors have entered or a revenue stream exists.
4. The merits of government grant or loan programs need to be viewed in the context of all sources of the high cost of foreign patent filings, which include at least:
 - a. Official fees. The overall official fees for filing are higher in most foreign jurisdictions than in the US, and there are no small entity discounts. Excess claims fees are particularly high in the EPO.
 - b. Official annuities or taxes. Pre-grant annuities or taxes can be considerable, and can represent a serious unanticipated cost over time when the examining backlog of the patent office is long. As an example, for SMEs considering filing in the European Patent Office, the prospect of paying a tax of \$500 to \$1,000 per year for eight to ten years can be a serious deterrent to filing. Stated another way, time is an indirect cost to SMEs of the foreign patent process.

- c. Translation costs in non-English speaking countries. SMEs typically cannot negotiate for discounts, which are almost always based on volume.
 - d. US outside counsel, if they are used. Some attorneys provide SME discounts to soften the blow of foreign filing, recognizing that their main value-add is in counseling and management, rather than the mechanics of filing. But other firms see foreign filing as a profit center, and price it accordingly.
 - e. Foreign outside counsel, if they are used. SME discounts are rare overseas, if available at all. Fixed costs and hourly rates for attorneys in, say, London or Tokyo are perceived to be significantly higher than those of their US counterparts. Foreign firms do not have the kind of SME-serving culture that exists in, say, the California bar.
5. Procurement costs also need to be seen as only a portion of total overseas patent costs. Spending tens of thousands of dollars obtaining a foreign patent may be useless if the SME is not in the position to commit hundreds of thousands, or millions, to overseas enforcement mechanisms.
 6. It is possible for SMEs to “over-patent” or file too many foreign cases. The discipline imposed by a limited budget, or from the oversight of venture capitalists or other investors, tends to help SMEs focus on filings that have good business benefits.
 7. The inability of an SME to obtain a foreign patent at reasonable cost is not the only foreign patent issue that SMEs face. For example, some SMEs may have an equally compelling interest in opposing or invalidating the foreign patents of others, to obtain greater freedom of action. Government is not well positioned to determine whether society is better served by providing funds to an SME to obtain a foreign patent versus providing funds to an SME to remove the foreign patent of another.
 8. A government loan or grant, funded from taxpayer dollars or a portion of existing USPTO user fees, for the purpose of foreign patent procurement by SMEs, does not represent good policy. (a) It would represent, to at least some extent, a redistribution of US income into the social welfare programs of foreign countries with only speculative benefit to SMEs due to the subjective nature of obtaining patents. The EPO is the number two patent filing jurisdiction in the world (ignoring the effect of utility model filings in China), but the overall value offered by the EPO is often perceived to be lower than the US and it would be hard to justify moving US taxpayer funds to such an office, even given the benefit of more SME patents. For example, by Silicon Valley or US government standards, productivity in the EPO is probably lower, hours worked are fewer, and national pension and benefit schemes are more generous. A policy that indirectly moves US taxpayer dollars into European pension schemes will be hard to justify. (b) Further, a material percentage of SMEs either fail or have limited-vision management: C-level executives who are incapable of growing the company or pursuing products with a limited or immature market. It may be difficult for government to determine which SMEs merit a loan or grant. (c) Finally, it seems fair to place at least some of the burden of financing SME patents on the large entities that dominate the system and, because of their ability to pay high official fees, file large numbers of cases, and wait out the resulting backlog periods involved in foreign patenting, must be seen to contribute to the

costs faced by SMEs in the system. For all these reasons, I disfavor a government loan or grant program.

9. Alternative approaches include:

- a. First, government could establish a new research and development tax credit that provides a dollar-for-dollar credit against either investors' capital gains taxes or SME corporate income taxes for every dollar spend on foreign patent activities. "Activities" should include invalidation and opposition, not just procurement.
- b. Second, the USPTO could establish a new line item fee surcharge, such as \$5 applied to every new large entity application filing and/or \$1 for each filing of a follow-on paper, and then grant or loan the collected fees to SMEs for any foreign patent activities. This eliminates US taxpayer funds from the equation and places the burden of funding SME foreign patents on large entities who dominate patent filing overseas. It also increases transparency and awareness.
- c. The USPTO should seek to use existing funds to communicate with key overseas patent offices (EPO, JPO, SIPO, KIPO) directed to achieving a discount scheme for official fees charged to SMEs that is similar to the US small entity system. The national benefits of fostering SME growth will have to be "sold" – a difficult task in a global economy in which overseas patent offices may be skeptical about any change that results in reductions of official fee income. However, it is certainly a fair question to ask, why does the US stand alone in having a small entity fee discount?
- d. Similar outreach could be directed to overseas providers of legal services, translations, and annuity payments. One can envision a sort of "pledge" that these providers could sign and a corresponding "badge" for their websites indicating endorsement of a reduced-cost approach for SMEs.