



September 13, 2018

The Honorable Andrei Iancu
Under Secretary of Commerce for Intellectual Property and
Director of U.S. Patent and Trademark Office
U.S. Patent and Trademark Office
600 Dulany Street
Alexandria, VA 22314
Attn: Brendan Hourigan

Via email: fee.setting@uspto.gov

Re: Comments of Internet Association in Response to the Notice of the Patent Public Advisory Committee Public Hearing on the Proposed Patent Fee Schedule

Dear Director Iancu and Members of the Advisory Committee:

Internet Association is pleased to provide the following input to the Patent Public Advisory Committee in response to the Federal Register notice of the *Patent Public Advisory Committee Public Hearing on the Proposed Patent Fee Schedule* and accompanying request for comments. 83 Fed. Reg. 37487 (August 1, 2018).

Internet Association represents the interests of America's leading Internet companies and their global community of users.¹ It is dedicated to advancing public policy solutions that strengthen and protect Internet freedom, foster innovation and economic growth, and empower users. IA's members include some of the largest patent owners in the world as well as companies with few (or no) patents. While our members' patent holdings vary dramatically, their views on this issue do not. All believe that, for the patent system to play its intended role in fostering innovation and economic growth, the USPTO must have a strong financial footing and patent quality must be improved significantly.

To advance these important goals, we respectfully submit that two high-level changes to the overall structure of the proposed patent fee schedule are necessary:

1. Reduce the subsidy for patent application and examination by shifting fee burdens forward and recovering a significantly lower proportion of the Office's operating budget from maintenance fees in latter half of a patent's life; and
2. Increase patent fees over time in order to fund more robust examination.

The reasons for, and anticipated benefits of, these structural changes to patent fees are discussed in more detail below.

¹ Internet Association's members include Airbnb, Amazon, Coinbase, Doordash, Dropbox, eBay, Etsy, Eventbrite, Expedia, Facebook, Google, Groupon, Handy, IAC, Intuit, Letgo, LinkedIn, Lyft, Match Group, Microsoft, Netflix, Pandora, PayPal, Pinterest, Quicken Loans, Rackspace, reddit, Salesforce.com, Snapchat, Spotify, Stripe, SurveyMonkey, Thumbtack, TransferWise, TripAdvisor, Turo, Twilio, Twitter, Uber Technologies Inc., Upwork, Vivid Seats, Yelp, Zenefits, and Zillow Group.



I. The Director has broad authority and discretion in setting fees, which should be more effectively employed to strengthen patent quality, increase efficiency, and improve the financial stability of USPTO.

Section 10 of the AIA authorizes the Director of the USPTO to set or adjust all patent fees established, authorized, or charged under Title 35 of the U.S. Code. Section 10(a)(2) limits this authority to fees necessary “to recover the aggregate estimated costs to the Office.” However, the Director has broad discretion to set individual fees that depart from actual costs so long as the total fees collected recover the aggregate of estimated costs. This flexibility enables the Director to structure fees in a manner that furthers the USPTO’s policy goals.

While IA recognizes that it is appropriate for the Director to exercise this discretion in pursuit of policy goals and, to a large extent, agrees with the Office’s stated objectives and considerations, we feel that too high a priority has been placed on subsidizing filing, search, and examination fees “to enable lower cost of entry into [the] patent system” and structuring fees such that “an applicant pays individual fees at points in time where he/she has more information to make a decision about proceeding with the patent process.”² At the same time, we feel the proposed fee structure – which maintains large subsidies for application and examination and sets overall fees at a level too low to support robust examination – reflects too low a priority placed on patent quality, efficient allocation of examination resources, and ensuring stable funding for patent operations.

To address this, IA respectfully suggests that two high-level, systemic changes should be made to the fee structure

- Shift fee burdens forward to recover a significantly higher proportion of USPTO’s operating budget from pre-issuance and initial issuance fees and reduce the subsidy for application and examination; and
- Increase overall patent fees over time in order to pay for more robust examination.

The reasons for, and anticipated benefits of, such changes are discussed in more detail below.

II. USPTO should reduce the subsidy for patent application and examination by shifting fee burdens forward to recover a significantly higher proportion of USPTO’s operating budget earlier in a patent’s lifetime.

USPTO’s current fee structure creates a substantial subsidy for application and examination, which is maintained by the new fee proposal under consideration. While IA recognizes that subsidizing entry into the patent system and allowing applicants to delay costs until they have more complete information are legitimate policy goals, we believe the subsidies provided by the proposed fee schedule are excessive and fail to appropriately balance countervailing interests in patent quality, efficient use of resources, and the financial stability of the Office.

As the Office’s presentation demonstrates, a relatively small proportion of total fees are generated through “front end” application, search, examination, and issuance fees. For example, “[f]or a large entity utility filing with one RCE and lifetime maintenance, front end fees will continue to be about 18% of the total fees paid.”³ Moreover, these fees represent less than half of the costs of prosecuting an

² USPTO Patent Fee Proposal: Executive Summary, at 13.

³ USPTO Patent Fee Proposal: Detailed Appendix, at 55.



application and, similarly, less than half of USPTO's estimated operating costs (as represented by the total patent fees collected).⁴

These statistics suggest three observations: First, front end fees are relatively trivial compared to the total expected costs of obtaining a patent and maintaining it through its full term. Second, the examination of unsuccessful applications or patents that are abandoned after the first stage is heavily subsidized by the owners of granted patents that maintain the patent through its 20 year term. And, third, there is a substantial time lag between when USPTO incurs pre-allowance costs and when those costs are recovered. As discussed below, each of these has significant negative implications for the patent system.

a. Impact on applicant incentives and behavior.

The relatively trivial amount of front end fees, combined with the fact that front end costs of unsuccessful applications are subsidized through maintenance fees paid by patent owners, leads to two interrelated problems. First, low front end fees create insufficient incentives to be selective and judicious in applying for patents. Applicants have little incentive to expend resources producing a high-quality application, conducting a meaningful pre-application assessment of the potential value of the purported invention, or ensuring they are seeking appropriately scoped claims. The result is poorer-quality applications that are more likely to claim marginal inventions. Second, low front end fees allow speculative filings for the purpose of obtaining patents that have a fair chance of later being found invalid if challenged, but nevertheless are the subject of costly enforcement activities. Also, if applicants' speculation doesn't pan out, they are able to abandon the application or even an issued patent with little cost to themselves, leaving the majority of the costs incurred by USPTO to be paid by others through maintenance fees.

Both of these result in significant USPTO resources being expended for the processing and examination of applications that will ultimately be abandoned. These implicit subsidies for marginal patents predictably lower the average quality of issued patents, while reducing efficiency and increasing overall costs of examination. Moreover, because of the heavy subsidization, the backloaded fee structure effectively penalizes more judicious and responsible applicants, who pay a disproportionate amount of the overall patent operations costs (because they forego speculative filings in favor of fewer, higher quality applications that are more likely to result in valuable issued patents).

Accordingly, IA strongly believes that recovering a significantly higher proportion of USPTO's operating budget through pre-issuance and issuance fees would better align applicant incentives with the objectives of the patent system as a whole, while contributing to more efficient use of examination resources, reduced costs of patenting, and improved patent quality.

b. Impact on USPTO.

As discussed immediately above, subsidizing application, search, and examination costs through maintenance fees is likely to result in the suboptimal allocation of finite examination resources, thus decreasing efficiency and increasing the costs of patenting. In addition, the substantial time lag between when USPTO incurs costs and when those costs are recovered presents further challenges for patent quality and risk to reliable patent operations. Such a fee structure "adds additional complexities

⁴ *Id.* at 5, 35, and 36.



when analyzing, forecasting, and monitoring patent fee collections in relation to patent costs,”⁵ reducing the ability to ensure that aggregate fees will actually cover operating costs.

Stable funding is critical to the efficient operation of the Office and to the reliable provision of services. As noted in USPTO’s discussions of the need for an operating reserve, stable, however, “[f]ee-funded operations [like the USPTO’s] are typically at high risk for cash flow stress.”⁶ And because front end fees account for less than half of the costs associated with application, search, and examination, full cost recovery does not occur until late in the patent cycle. The substantial time lag between when costs are incurred and when revenues to recover those costs are generated creates a risk to maintaining stable finances and the revenues necessary to fund unexpected increases in workload (*e.g.*, due to increased application rates) or shortfalls in revenue (due to lower than expected renewal rates). Due to this lag, if workload increases, the contemporaneous increase in revenues is only a portion of the anticipated cost of performing the additional work, hampering the Office’s ability to respond in the short term. And, also due to the time lag, future renewal rates and associated revenues are difficult to predict accurately, greatly complicating the Office’s ability to ensure fees that are set *ex ante* will result in full cost recovery.

While – if optimally funded – the USPTO’s operating reserve would ameliorate the potential risk of a financial shock to patent operations, the reserve is not funded at the minimum acceptable level, and – at least at present – does not provide a complete solution.⁷ In IA’s view, a viable option for augmenting the financial security provided by the reserve fund is to reduce the backloading of fees to bring the time of cost recovery closer to the time that USPTO incurs the costs. As the Office recognizes in its stated reasons for restructuring maintenance and issuance fees, “[a]s technology lifecycles grow shorter, it is important that USPTO not rely too heavily on fees paid late in the life of a patent,” and the proposed restructuring will “allow the Office to recover initial search and examination costs earlier in the patent lifecycle.” In effect, this represents and implicit acknowledgment of the risk to financial stability and how decreasing the time lag reduces that risk.

Beyond ameliorating the risk to revenues associated with shorter product cycles, recovering costs earlier in the patent lifecycle makes USPTO operations less vulnerable in general to unexpected shifts in application or renewal rates. Absent other considerations, the best way to minimize this funding risk would be to decrease or eliminate the cost recovery time lag entirely, ensuring that full cost recovery occurs contemporaneously with the activities generating such cost at each stage of process. However, this conflicts with countervailing considerations and policy goals such as facilitating entry into the patent system and allowing applicants to delay decisions until more information regarding the patentability and value of the claimed invention is available.

c. Suggested Change: Increase front end fees to further decrease backloading of fee structure.

As discussed above, the proposed fee schedule at least implicitly acknowledges the benefit of reducing the backloading of fees and shifts some of the fee burden forward in time through disproportionate increases to the issuance and first maintenance fees. However, this relatively minor shift does not go nearly far enough. An increase in pre-grant and additional increases in the issuance and first

⁵ *Id.* at 6.

⁶ *USPTO Fee Proposal: Executive Summary* at 10.

⁷ As USPTO itself notes in its Executive Summary: “USPTO ended FY 2017 below the minimum level for the patent operating reserve. In the FY 2019 President’s Budget, it was projected that the patent operating reserve would not exceed the minimum level until FY 2021.” *Id.* at 11.



maintenance fees would bring revenues even closer in time to cost drivers, providing commensurately higher benefits.

IA recognizes that some level of subsidy for pre-issuance costs may be beneficial in encouraging entry into the patent system and allowing applicants to control costs and does not propose or support the complete elimination subsidies (or the associated reduction or elimination of maintenance fees). At the same time, given the relative inelasticity of demand for patent services, IA believes that even a significant increase in pre-issuance fees is unlikely to substantially undermine these policy goals.⁸ Accordingly, USPTO should remove disincentives to patent quality and improve the Office's financial stability by shifting a higher proportion of the overall fee burden forward in the patent lifecycle by imposing moderate increases in "front end" fees.

III. USPTO should study the need to increase patent fees over time to pay for more robust examination.

Improving patent quality remains one of IA's highest priorities with respect to intellectual property reforms. It is important to recognize reducing (or even eliminating) the subsidy for application and examination as discussed above is only one step toward significantly improving patent quality. It is also critical that the USPTO devote more resources to examination.

a. Indications of need for increased examination resources and improved quality.

While IA is mindful of the fact that perfect patent quality is unattainable (and would be vastly cost-prohibitive even if it were), we believe that the experience to date with PTAB trials strongly indicates that insufficient resources are currently devoted to prior art search and examination and that significant increases in quality are both desirable and achievable. Patent rights can only become reliable if the USPTO increases the thoroughness of examination so that patents which issue are more likely to be valid and able to withstand further scrutiny in either an AIA trial or district court litigation.

A strong indication that insufficient resources are being devoted to patent examination involves a comparison of the cost of examination and the cost of PTAB trials. In fiscal year 2016, the Patent Office estimated that the average cost to USPTO of examining a patent application was about \$4,200, and the large-entity examination fee was \$1,600.⁹ By contrast, USPTO's estimated historical costs of AIA trials during roughly the same time period ranges from around \$32,000 (for IPRs) to about \$49,000 (for PGRs, which are filed within just a year of a patent's issuance).

Both examination of an application and an AIA trial focus on a determination by USPTO regarding patentability. However, the cost of this determination in a PGR trial is more than ten times as much as the amount expended by USPTO to make the same determination during examination. Although some of the increased costs of PTAB trials can likely be attributed to additional procedural requirements, including having a panel of three judges involved instead of a single examiner, the patentability determination in a PTAB trial is much narrower in scope than the determination made during examination. This is because the PTAB review does not consider whether the entire patent satisfies all the statutory requirements of patentability, but rather is generally constrained to specific arguments

⁸ It is not IA's intent to significantly increase fees for small or independent inventors and, to the extent changes in the fee structure or increases in fees would make entry into the patent system overly burdensome for such inventors, IA believes that further discounts for these entities should be considered.

⁹ See U.S. Patent and Trademark Office, *Performance and Accountability Report* (2016).



and grounds raised by the petitioner. In addition, the petitions are often directed to only a subset of a patent's claims.

Even though this does not provide a perfect apples-to-apples comparison, IA believes this enormous disparity in resources expended on patentability determinations – particularly for a PGR, which takes place soon after a patent's initial issuance -- is difficult to rationalize. While the optimal amount of resources for USPTO to expend to ensure a fully-reasoned and reliable determination of patentability is likely somewhere between the cost of AIA trials and the estimated cost of examination, it is likely to be substantially more than \$4,200.

b. Suggested Change: USPTO should assess the benefits of an increase in total patent fees to pay for more robust examination.

While IA recognizes that it would be unreasonable to expect an immediate and significant increase in fees, we do believe that the current fee levels (and associated amount of resources devoted to examination) are insufficient. Accordingly, we respectfully suggest that USPTO should amend its proposed fee schedule to impose a moderate overall increase in aggregate patent fees sufficient to provide cost recovery for the increase in examination resources necessary to conduct a more robust examination to narrow at least some of the disparity between examination and PTAB post-issuance reviews. Going forward, we believe USPTO should also consider further increases in examination resources (in particular, increased time allocations) as part of its ongoing strategic planning and budgeting processes to bring the resources devoted to examination¹⁰ into line with the European and Japanese patent offices.

IV. Conclusion

Internet Association commends the USPTO for its ongoing efforts to strengthen the patent system, improve patent quality, and appropriately balance the interests of patent applicants, patent owners, and the public. We also appreciate and look forward to the Patent Public Advisory Committee's review of and recommendations on the USPTO's proposed exercise of its fee setting authority. We are gratefully for the strong commitment of both the USPTO and the Advisory Committee a fair and rational fee setting process and stand ready to provide any assistance or further feedback that would be helpful in finalizing and implementing an updated patent fee schedule.

¹⁰ Pierre M. Picard & Bruno van Pottelsberghe de la Potterie, *Patent Office Governance and Patent System Quality*, Discussion Paper no. DP8338. Center for Economic Policy Research (2011) (finding that the EPO and JPO expend more resources in examination than USPTO).