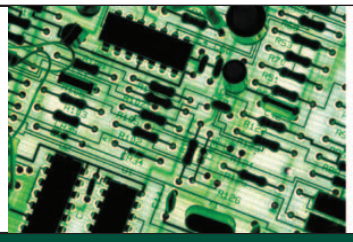
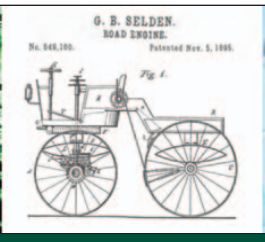
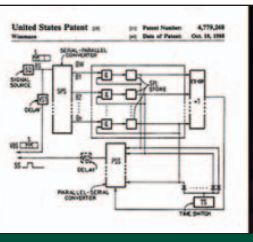
FEDERAL TRADE COMMISSION

To Promote Innovation:
The Proper Balance of Competition and Patent Law and Policy

A Report by the Federal Trade Commission
October 2003

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Acknowledgments:

The Commission wishes to note the expertise and time contributed by Hearings participants. For all of their contributions, the Commission conveys its thanks.

The Commission thanks the Antitrust Division of the Department of Justice and the Patent and Trademark Office for participating in many of the panels at, and for recommending many of the participants in, the Hearings.

The Commission thanks the Competition Policy Center and the Berkeley Center for Law and Technology at the University of California at Berkeley for providing facilities to allow some of the Hearings to be held on the West Coast.

Cover:

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Patents: Front Cover
Patent No. 549,160 - Selden Road Engine
Patent No. 4,779, 268 - Frame Decoding for Digital Signal Transmission

Patents: Back Cover
Patent No. 4,302,281 - Method for Producing Pulp
Patent No. 4,805,654 - Sun Shield for Automobiles

TO PROMOTE INNOVATION: THE PROPER BALANCE OF COMPETITION AND PATENT LAW AND POLICY

EXECUTIVE SUMMARY

Innovation benefits consumers through the development of new and improved goods, services, and processes. An economy's capacity for invention and innovation helps drive its economic growth and the degree to which standards of living increase.[1] Technological breakthroughs such as automobiles, airplanes, the personal computer, the Internet, television, telephones, and modern pharmaceuticals illustrate the power of innovation to increase prosperity and improve the quality of our lives.

Competition and patents stand out among the federal policies that influence innovation. Both competition and patent policy can foster innovation, but each requires a proper balance with the other to do so. Errors or systematic biases in how one policy's rules are interpreted and applied can harm the other policy's effectiveness. This report by the Federal Trade Commission (FTC) discusses and makes recommendations for the patent system to maintain a proper balance with competition law and policy.[2] A second joint report, by the FTC and the Antitrust Division of the Department of Justice (DOJ) (forthcoming), will discuss and make recommendations for antitrust to maintain a proper balance with the patent system.

Competition and Patent Law and Policy Promote Innovation and Benefit the Public.

Competition through free enterprise and open markets is the organizing principle for most of the U.S. economy. Competition among firms generally works best to achieve optimum prices, quantity, and quality of goods and services for consumers. Antitrust law, codified in the Sherman Act, the FTC Act, and other statutes, seeks "to maximize consumer welfare by encouraging firms to behave competitively."[3]

Competition can stimulate innovation. Competition among firms can spur the invention of new or better products or more efficient processes. Firms may race to be the first to market an innovative technology. Companies may invent lower-cost manufacturing processes, thereby increasing their profits and enhancing their ability to compete. Competition can prompt firms to identify consumers' unmet needs and develop new products or services to

[1] Federal Reserve Board Vice Chairman Roger W. Ferguson, Jr., Patent Policy in a Broader Context, Remarks at 2003 Financial Markets Conference of the Federal Reserve Bank of Atlanta (April 5, 2003), *at* http://www.federalreserve.gov/boarddocs/speeches/2003/20030407/default.htm.

[2] The Federal Trade Commission issues reports pursuant to Section 6(f) of the Federal Trade Commission Act, 15 U.S.C. § 46(f).

[3] I PHILLIP E. AREEDA & HERBERT HOVENKAMP, ANTITRUST LAW : AN ANALYSIS OF ANTITRUST PRINCIPLES AND THEIR APPLICATION ¶100a at 4 (2000).

satisfy them.

Patent policy also can stimulate innovation. The U.S. Constitution authorizes Congress "[t]o promote the Progress of Science and useful Arts, by securing for limited Times to . . . Inventors the exclusive Right to their respective . . . Discoveries."[4] To obtain a patent, an invention (that is, a product, process, machine, or composition of matter) must be novel, nonobvious, and useful. Moreover, a patentee must clearly disclose the invention. A patent confers a right to exclude others from making, using, or selling in the United States the invention claimed by the patent for twenty years from the date of filing the patent application.

This property right can enable firms to increase their expected profits from investments in research and development, thus fostering innovation that would not occur but for the prospect of a patent. Because the patent system requires public disclosure, it can promote a dissemination of scientific and technical information that would not occur but for the prospect of a patent.

Like competition policy, patent policy serves to benefit the public. "The basic quid pro quo contemplated by the Constitution and the Congress for granting a patent monopoly is the benefit derived by the public from an invention with substantial utility."[5] The public disclosure of scientific and technical information is part of the consideration that the inventor gives the public.[6]

Competition and Patents Must Work Together in the Proper Balance.

Competition and patents are not inherently in conflict. Patent and antitrust law "are actually complementary, as both are aimed at encouraging innovation, industry, and competition."[7] Patent law plays an important role in the property rights regime essential to a well-functioning competitive economy. For example, firms may compete to obtain the property rights that patents convey. Patents do not necessarily confer monopoly power on their holders,[8] and most business conduct with respect to patents does not unreasonably restrain or serve to monopolize markets. Even when a patent does confer monopoly power, that alone does not create an antitrust violation. Antitrust law recognizes that a patent's creation of monopoly power can be

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[4] U.S. CONST. art. I, § 8. Other sections of this constitutional provision authorize copyright law.

[5] *Brenner v. Manson,* 383 U.S. 519, 534-35 (1966). The consideration an inventor gives in return for a patent "is the benefit which he confers upon the public by placing in their hands a means through the use of which their wants may be supplied." 1 WILLIAM ROBINSON, THE LAW OF PATENTS FOR USEFUL INVENTIONS § 22 at 305 (1890), *cited in* ROBERT P. MERGES & JOHN F. DUFFY, PATENT LAW AND POLICY: CASES AND MATERIALS 361 (3d ed. 2002).

[6] *See* James E. Rogan, *Prepared Remarks of James E. Rogan, Under Secretary of Commerce for Intellectual Property and Director of the United States Patent and Trademark Office* (2/6/02) 2, *at* http://www.ftc.gov/opp/intellect/rogan.htm.

[7] *Atari Games Corp. v. Nintendo of Am.,* 897 F.2d 1572, 1576 (Fed. Cir.1990).

[8] ROBERT L. HARMON, PATENTS AND THE FEDERAL CIRCUIT § 1.4(b) at 21 (5th ed. 2001) ("Patent rights are not legal monopolies in the antitrust sense of the word. Not every patent is a monopoly, and not every patent confers market power.").

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