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BILATERAL WTO-PLUS FREE TRADE AGREEMENTS IN THE  
MIDDLE EAST: A CASE STUDY OF OFTA  
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Mohamed R. Hassanien\*

**Introduction**

Free trade agreements (FTAs) are no longer about trade; these agreements cover foreign investment, labor protection, procurement of services, government contracts, environmental regulation, international dispute resolutions, and a host of other issues.<sup>1</sup> In terms of intellectual property rights,<sup>2</sup> FTAs have been the most active forums for protecting such rights.<sup>3</sup> Moreover, international protection of intellectual property (IP) is becoming the most dynamic area of international law these days.<sup>4</sup> In the post-TRIPS (Agreement on Trade Related Aspects of Intellectual Property Rights) era, a multilateral

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<sup>1</sup> Sydney M. Cone, III, *The Promotion of Free-Trade Areas Viewed in Terms of Most-Favored-Nation Treatment and Imperial Preference*, 26 MICH. J. INT'L L. 563, 565 (2005); see, e.g., U.S.-Oman Free Trade Agreement, U.S.-Oman, Jan. 19, 2006 [hereinafter OFTA], available at [http://www.ustr.gov/Trade\\_Agreements/Bilateral/Oman\\_FTA/Final\\_Text/Section\\_Index.html](http://www.ustr.gov/Trade_Agreements/Bilateral/Oman_FTA/Final_Text/Section_Index.html). The U.S.-Oman Free Trade Agreement includes chapters entitled Investment, Government Procurement, Financial Services, Labor, Environment, Intellectual Property Rights, Dispute Settlement, and others.

<sup>2</sup> Intellectual property, for the purposes of this article, includes all forms of intellectual property, such as patents, copyright, trademarks, and trade secrets, unless otherwise indicated.

<sup>3</sup> Cortney M. Arnold, *Protecting Intellectual Property in the Developing World: Next Stop—Thailand*, 2006 DUKE L. & TECH. REV. 0010 at ¶ 1, 11.

<sup>4</sup> JOHN BARTON ET AL., INT'L CTR. FOR TRADE & SUSTAINABLE DEV., BRIEF NO. 1, VIEWS ON THE FUTURE OF THE INTELLECTUAL PROPERTY SYSTEM 1 (2007).

front is not the only avenue to protect IP. Bilateral and regional fronts remain more prevalent; these fronts build on and strengthen the minimum standards established by TRIPS.<sup>5</sup> After the signing of TRIPS, bilateralism dominates the international regulation of IP.<sup>6</sup>

In the Middle East, OFTA is the last FTA to be signed between the United States and an Arab country.<sup>7</sup> OFTA is the U.S.-Oman Free Trade Agreement.<sup>8</sup> The U.S.—a conceptual economy—“has been persistent in promoting the adoption and enforcement of intellectual property regimes throughout the Middle East.”<sup>9</sup> Currently, the U.S. has shifted the new frontier of international IP protection from the multilateral sphere to the bilateral one.<sup>10</sup> On the other side of the table, the prospect of privileged access to the American market convinces Oman, as a developing country, to adhere to TRIPS and agreements with the U.S. Oman is the third Middle East Free Trade Initiative (MEFTA) partner in 2006.<sup>11</sup> Oman has repeatedly hosted U.S. military facilities, and has been its partner in national security; Oman has been especially active in supporting U.S. efforts to close funding for terrorists.<sup>12</sup> OFTA mirrors the previous FTA between the

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<sup>5</sup> Daniel Gervais, *Intellectual Property, Trade & Development: The State of Play*, 74 *FORDHAM L. REV.* 505, 535 (2005) (arguing that two diverging directions may be taken in the post-TRIPS era; the TRIPS-related development within the WTO, which wants to be more responsive to the perceived needs of developing countries, and, on the other hand, the bilateral and regional trade agreements that mirror the maximalist approach).

<sup>6</sup> Ruth L. Okediji, *Back to Bilateralism? Pendulum Swings in International Intellectual Property Protection*, 1 *U. OTTAWA L. & TECH. J.* 125, 141 (2003-2004).

<sup>7</sup> Press Release, Office of the U.S. Trade Representative, United States and Oman Sign Free Trade Agreement (Jan. 19, 2006), available at [http://www.ustr.gov/assets/Document\\_Library/Press\\_Releases/2006/January/asset\\_upload\\_file25\\_8774.pdf](http://www.ustr.gov/assets/Document_Library/Press_Releases/2006/January/asset_upload_file25_8774.pdf).

<sup>8</sup> OFTA, *supra* note 1.

<sup>9</sup> John Carroll, *Intellectual Property Rights in the Middle East: A Cultural Perspective*, 11 *FORDHAM INTELL. PROP. MEDIA & ENT. L.J.* 555, 566 (2000).

<sup>10</sup> See OFFICE OF THE U.S. TRADE REPRESENTATIVE, 2004 SPECIAL 301 REPORT: EXECUTIVE SUMMARY (2004), available at [http://www.ustr.gov/assets/Document\\_Library/Reports\\_Publications/2004/2004\\_Special\\_301/asset\\_upload\\_file963\\_5996.pdf](http://www.ustr.gov/assets/Document_Library/Reports_Publications/2004/2004_Special_301/asset_upload_file963_5996.pdf) (indicating that the foreign policy of the U.S. is committed to strengthening IP by negotiating FTAs with other countries).

<sup>11</sup> Robert Z. Lawrence, *Recent U.S. Free Trade Initiatives in the Middle East: Opportunities but no Guarantees* 2, 4 (John F. Kennedy Sch. of Gov't Faculty Research Working Paper Series, Working Paper No. RWP06-050), available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=939656](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=939656).

<sup>12</sup> *Id.* at 12-13.

U.S. and Morocco which, in turn, is the model for other FTAs in the Middle East.<sup>13</sup>

IP laws are private laws;<sup>14</sup> however, there is an increasing importance of public international law in this area. Consider the Berne Convention, which is a private international agreement that entitles private parties with rights in literary and artistic works.<sup>15</sup> TRIPS, by contrast, is a public international law instrument which governs disputes between public entities and nation states, and has procedures to adjudicate such disputes and to sanction states for violating its rules.<sup>16</sup> Bilateral free trade agreements are not that different from TRIPS. Although Chapter 15 (IP chapter in OFTA) gives investors certain rights, the obligations laid down are for governments to implement.<sup>17</sup> In most of the current literature, the private aspect of IP is discussed; far less attention is given to the public law aspects of international IP law, which is the focus of this article.

In this article, Part I depicts the protection of IP in Islamic law. This Part will provide the context that will be helpful in analyzing how an international agreement like a free trade agreement affects the IP domestic laws and regulations in the region, and will follow with a profile of Oman. Part II illustrates the importance of international protection of IP rights and of free trade agreements in U.S. trade policy, and their role in effecting this protection overseas through exporting U.S. norms to other countries. Part II also discusses the three phases of U.S. policy in protecting IP rights. Part III provides a brief background to OFTA, including the political and economic concerns in both the U.S. and Oman. Part IV analyzes the interaction between international law and domestic law through analyzing the IP chapter in OFTA and how it affects the IP laws and regulations in Oman, and highlights the judicial and legislative challenges in adapting to the law; this Part focuses on the specific OFTA provisions related to IP and offers recommendations on how Oman can fully benefit from its commitment to OFTA, which can then be extrapolated to other developing countries in similar circumstances.

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<sup>13</sup> OFTA, *supra* note 1.

<sup>14</sup> Peter Yu, *World Trade, Intellectual Property and the Global Elites: An Introduction*, 10 *CARDOZO J. INT'L & COMP. L.* 1, 1 (2002).

<sup>15</sup> See World Intellectual Property Organization, Berne Convention for the Protection of Literary and Artistic Works, May 4, 1896, *available at* [http://www.wipo.int/treaties/en/ip/berne/trtdocs\\_wo001.html](http://www.wipo.int/treaties/en/ip/berne/trtdocs_wo001.html).

<sup>16</sup> Agreement on Trade-Related Aspects of Intellectual Property Rights, Apr. 15, 1994, 1869 U.N.T.S. 299, *available at* [http://www.wto.org/english/tratop\\_e/trips\\_e/t\\_agm0\\_e.htm](http://www.wto.org/english/tratop_e/trips_e/t_agm0_e.htm).

<sup>17</sup> OFTA, *supra* note 1.

## **PART I**

This Part proceeds in two sections. The first section analyzes the protection of IP in Islam, and the second gives a profile of Oman—the last Arab country to sign a free trade agreement with the U.S.—and its relationship with the U.S.

### **IP Protection in Islamic Law and the Culture of the Middle East**

The protection of poetry was the Arabs' introduction into the realm of IP; poetry played an essential role in the cultural life of ancient Arabs.<sup>18</sup> Fine poetry was highly regarded by Arabs in Jahilya (an Arabic term used to describe the pre-Islam period).<sup>19</sup> It is considered to be the major artistic expression of the Jahilya era.<sup>20</sup> Arabs recognized copyright from the very early days, while trademark and patent evolved in later stages.<sup>21</sup> Desert living required mutual reliance for the sake of survival, and poetry was easily adaptable to transient lifestyles and has been used for millennia to express shared ancient ideals. Although this article is devoted to analyzing the role of free trade agreements in strengthening IP protection in the Middle East, turning a blind eye to the relevant historical, moral, conceptual, and legal background of Islam with respect to the protection of IP will create a distorted view of the topic. This would isolate the free trade agreement from the whole framework provided by Islamic law.

IP is part of property; there is no absolute ownership in Islam, as property belongs to God and goes down to the people through inheritance in Islam.<sup>22</sup> However, ownership is sacred and absolute in scope, and any trespass would be a sin against the Sharia.<sup>23</sup> This is the main overarching principle in Islam which protects private ownership. Therefore, an understanding of the enforcement and the recognition of IP rights in the Middle East is incomplete without an understanding of the cultural and religious forces that are deeply rooted in the history of

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<sup>18</sup> Amir H. Khoury, *Ancient and Islamic Sources of Intellectual Property Protection in the Middle East: A Focus on Trademarks*, 43 IDEA 151, 153 (2003).

<sup>19</sup> *Id.*

<sup>20</sup> *Id.*

<sup>21</sup> See Amir Khoury, *The Development of Modern Trademark Legislation and Protection in Arab Countries in the Middle East*, 16 TRANSNAT'L LAW. 249 (2003).

<sup>22</sup> Heba Raslan, *Sharia and the Protection of Intellectual Property—The Example of Egypt*, 47 IDEA 497, 515-18 (2007).

<sup>23</sup> *Id.* at 515-16.

the Middle East.<sup>24</sup> Islam is not only an integral part of the Middle Eastern heritage; it is more than a faith, as it defines the law of many countries in the Middle East.<sup>25</sup>

Sharia—the most influential law in the region—was developed and assembled during the first three centuries after Prophet Mohamed’s death, and consists of the holy Quran, the pronouncements and deeds of Mohamed and his companions (Hadith), and Ijma—the agreement of Muslims on a certain issue—and Ijtihad, which is the use of mentality to explore new rules not expressly mentioned in either the Quran or the Hadith.<sup>26</sup>

Sharia—a religiously-based law—has tremendous force, both legally and economically, throughout the Middle East. Islamic law offers guidance on spiritual duties, personal status, and inheritance, and provides general principles in other areas, like contract law.<sup>27</sup> IP is an area that Islamic law has not taken a stance on from the beginning; however, it is important to depict the academic debate about whether IP is protected under the main principles in Islamic law.<sup>28</sup> There are two contemporary schools in Sharia regarding the protection of IP.<sup>29</sup> The first is against the protection of IP rights, arguing that the concept of ownership in Sharia is confined to tangible objects only; intangible objects were not subject to any protection under the Quran, the Sunnah, or the juristic views of the earlier Muslim jurists.<sup>30</sup> The second school, which represents the majority of Muslim scholars, contends that there is nothing in Sharia that enjoins or contravenes protection and enforcement of IP rights, and that Muslims should abide by their contracts and the laws applied in their countries.<sup>31</sup>

In the Middle East—an area where cultural issues inform policy—IP protection goes largely unenforced due to combined social and political factors.<sup>32</sup> Yet, the legal regimes remain ineffective in many instances, or have enforcement problems.<sup>33</sup> In general, many Middle Eastern countries have stringent IP laws and regulations; for example, Egyptian laws and regulations are in accordance with international standards, and some governments have created IP

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<sup>24</sup> Khoury, *supra* note 18, at 158.

<sup>25</sup> Carroll, *supra* note 9, at 583.

<sup>26</sup> Raslan, *supra* note 22, at 505-09.

<sup>27</sup> Steven Jamar, *The Protection of Intellectual Property Under Islamic Law*, 21 CAP. U. L. REV. 1079, 1080-1083 (1992).

<sup>28</sup> *See id.*

<sup>29</sup> Raslan, *supra* note 22, at 501.

<sup>30</sup> *Id.* at 501-02.

<sup>31</sup> *Id.* at 502.

<sup>32</sup> Carroll, *supra* note 9, at 560-61.

<sup>33</sup> *See id.* at 560.

enforcement divisions.<sup>34</sup> Lebanon has enacted a comprehensive IP regime, while Oman and Bahrain have copyright issues.<sup>35</sup> “Middle Easterners retain a strong sense that their culture is separate and distinct from that of the West. Middle Eastern culture is derived from particular perceptions of history and religion.”<sup>36</sup> This region has noticed two equally important events; the first is the coming of Islam, and the second is the intrusion of the West.<sup>37</sup>

IP protection in the Arab world has long been considered one of the weaknesses in the region’s economic development framework.<sup>38</sup> Despite desires to meet the social and economic demands of the region’s growing population, the lack of sufficient IP protection—whether in terms of adequate legislation or enforcement of existing legislation—holds back development in that region.<sup>39</sup> However, the last decade has witnessed significant changes in Arab countries’ IP regimes, and some of the most important changes in the region’s history are on the immediate horizon. Arab countries resisted establishing minimum standards of IP protection because they felt this would benefit only the developed countries, while the rest of the world paid more for technology and advancement. This is the perspective of developing countries.<sup>40</sup> Recent IP laws and regulations and poor enforcement are major problems in the Arab world; there are not many legislative or judicial decisions with respect to enforcement of IP laws and regulations in this region. Minimum international standards in copyrights, patents, trademarks, designs, and geographical indications have been introduced by TRIPS to Arab countries who signed this agreement.<sup>41</sup> However, it is questionable that the legal environment in the Middle East can sustain more enhanced IP standards, like those enshrined in the bilateral free trade agreements.

Infringements of IP rights in the Middle East include every aspect of those rights, and are not limited to copyright violations only, which are more prevalent in countries like Egypt, Iran, and Israel. Trademarks are also violated in the United Arab Emirates (UAE),

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<sup>34</sup> *Id.* at 559-60.

<sup>35</sup> *Id.* at 560.

<sup>36</sup> *Id.* at 573.

<sup>37</sup> *Id.* at 576-77.

<sup>38</sup> TALAL ABU-GHAZALEH, INTELLECTUAL PROPERTY LAWS OF THE ARAB COUNTRIES xi (Kluwer Law Int’l 2000) (1938).

<sup>39</sup> *Id.*

<sup>40</sup> *Id.* at xiii.

<sup>41</sup> *Id.* at xiv.

particularly with regard to automobile parts.<sup>42</sup> Computer software in the Middle East is rarely genuine, and most of the time illegal copies are circulated among the people in banks and firms. In Saudi Arabia and Egypt, many companies still consider it their right to buy one legal package of each software product and copy it internally, without permission of the owner of the software package.<sup>43</sup>

John Carroll highlighted two main reasons for such reluctance despite the TRIPS-compliance laws and regulations. The West is perceived by Middle Easterners as damaging the Middle East since the times of the Crusades and colonization until now. Also, the Western culture is seen as corrupt and immoral, and granting IP rights means extending this culture. Ironically, Middle Easterners decry copying as immoral and promote a fundamental respect for the works of other Middle Easterners, while at the same time indiscriminately pirating Western goods.<sup>44</sup>

These practices contradict Sharia, which calls for strong punishment for transgressions against personal property.<sup>45</sup> There is neither an excuse in Sharia for denying national and foreign IP owners their rights, nor an excuse for lax enforcement of IP laws. On the contrary, the principles of Sharia enjoin any transgression against these rights and obligate Muslim governments to strongly guard and enforce them.<sup>46</sup> Hence, one can say that protection of IP is compatible with Islamic notions and concepts.

### **Profile of Oman**

#### **Relationship between Oman and United States**

Located in southwest Asia, the Sultanate of Oman displays the following characteristics: it is an Islamic, Asian, and Arabic country. Over the years, Oman's legal system has been mainly influenced by Egyptian and French law; hence, it is similar to a civil law system.<sup>47</sup> The Omani constitution has likewise acknowledged the necessity to bring its laws into accord with international recommendations.<sup>48</sup> Article 11 of the Omani constitution provides that "[t]he basis of the

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<sup>42</sup> Carroll, *supra* note 9, at 558.

<sup>43</sup> *Id.* at 558-59.

<sup>44</sup> *Id.* at 589-90.

<sup>45</sup> Raslan, *supra* note 22, at 558.

<sup>46</sup> *Id.* at 559.

<sup>47</sup> See generally GIL FEILER, MIDDLE EAST IN THE NEW MILLENNIUM: ECONOMIC DEVELOPMENT AND BUSINESS LAW (2000), for further discussion on the influence of French law on Arab countries.

<sup>48</sup> SULTANI DECREE NO. (101/96) [Constitution] art. 10 (Oman), available at [http://www.mola.gov.om/basic\\_statute.pdf](http://www.mola.gov.om/basic_statute.pdf).

national economy is justice and the principles of a free economy.”<sup>49</sup> Oman is a member country and signatory of a number of international conventions—particularly IP conventions. Oman has been a party to the Paris Convention for the Protection of Industrial Property since July 14, 1999.<sup>50</sup> Oman joined the World Trade Organization on November 9, 2000.<sup>51</sup>

The Omani economy has been radically transformed over a series of development plans, beginning with the First Five-Year Plan (1976-1980).<sup>52</sup> Sultan Qaboos—the ruler of the country—encourages market-orientated policies and private sector development as the mechanism for prosperity and growth. Since the fall of oil prices in 1998, Oman has made active plans to diversify its economy and is placing a greater emphasis on other areas of industry, such as tourism and natural gas.<sup>53</sup>

Based on a clearly-defined set of principles that encourage the building of bridges with other nations and, wherever possible, the opening up of opportunities for increased co-operation, Oman’s foreign policy is set.<sup>54</sup> The Sultanate believes strongly in maintaining contacts and dialogue with other nations and peoples in order to develop continued mutual understanding and co-operation.<sup>55</sup> It supports any genuine efforts to develop closer relations or resolve differences through dialogue and within the context of international law and legitimacy, and also believes that peace and stability can best be established through tolerance and recognition of common interests.<sup>56</sup> This is why Oman has been an active member in the

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<sup>49</sup> THE WHITE BOOK—THE BASIC LAW OF THE SULTANATE OF OMAN [Constitution] art. 11, available at [http://servat.unibe.ch/icl/mu00000\\_.html](http://servat.unibe.ch/icl/mu00000_.html).

<sup>50</sup> World Intellectual Property Organization, Contracting Parties to the Paris Convention, [http://www.wipo.int/treaties/en/ShowResults.jsp?country\\_id=135C & start\\_year=ANY&end\\_year=ANY&search\\_what=C&treaty\\_id=2](http://www.wipo.int/treaties/en/ShowResults.jsp?country_id=135C&start_year=ANY&end_year=ANY&search_what=C&treaty_id=2) (last visited Mar. 24, 2008).

<sup>51</sup> World Trade Organization, Members and Observers, [http://www.wto.org/english/thewto\\_e/whatis\\_e/tif\\_e/org6\\_e.htm](http://www.wto.org/english/thewto_e/whatis_e/tif_e/org6_e.htm) (last visited Mar. 24, 2008).

<sup>52</sup> Sultanate of Oman: Ministry of National Economy, Planning & Development, [http://www.moneoman.gov.om/dev\\_strategy1.asp](http://www.moneoman.gov.om/dev_strategy1.asp) (last visited Mar. 24, 2008).

<sup>53</sup> Ministry of Information: Sultanate of Oman, Overview: The Seventh Five Year Plan (2006-2010), <http://www.omanet.om/english/commerce/econ1.asp?cat=comm> (last visited Mar. 24, 2008).

<sup>54</sup> Ministry of Information: Sultanate of Oman, Government: Foreign Affairs, <http://www.omanet.om/english/government/foreign.asp?cat=gov> (last visited Mar. 24, 2008).

<sup>55</sup> *Id.*

<sup>56</sup> *Id.*

United Nations and international organizations such as UNESCO, the World Health Organization (WHO) and the World Trade Organization (WTO).<sup>57</sup>

Looking back at the nation's history, the Omanis were among the first people to embrace Islam voluntarily, around 630 A.D., when Prophet Mohamed sent his envoy, Amr ibn Al As, to meet the nation's joint rulers, Jaifar and 'Abd, to invite them to accept Islam.<sup>58</sup> In accepting this faith, Oman became an Ibadhi state under the rule of an elected leader, the Imam.<sup>59</sup> During the early years of the Islamic mission, Oman played a large role in the Wars of Apostasy following Mohamed's death, and was also involved in the great Islamic conquests by land and sea in Iraq, Persia, and beyond.<sup>60</sup> However, its most prominent role in this respect came via its extensive trading and seafaring activities in East Africa, especially throughout the 19th century, when it propagated Islam in many of the coastal regions of East Africa, as well as in certain areas of Central Africa; Omanis also carried the message of Islam to China and the Asian ports.<sup>61</sup> Oman defined itself clearly as a Muslim, Arab, and Asian country, which has limited resources but a wealth of hopes and potential in the Middle East.

## **PART II**

### **International Protection of Intellectual Property (IP)**

This Part will explore the link between international trade and IP; however, a brief orientation of the international law on IP is critical.

#### **International Protection of IP**

The Berne and Paris Conventions form the foundation of the multilateral IP regime; however, they lacked detailed provisions on effective enforcement of rights and a binding dispute resolution mechanism.<sup>62</sup> The inadequacy of these two conventions motivated the U.S. and the European Union (E.U.) to push for a supranational code

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<sup>57</sup> *Id.*

<sup>58</sup> Ministry of Information: Sultanate of Oman, History, <http://www.omanet.om/english/history/overview.asp> (last visited Mar. 24, 2008).

<sup>59</sup> *Id.*

<sup>60</sup> *Id.*

<sup>61</sup> *Id.*

<sup>62</sup> Olivier Vrins & Marius Schneider, ENFORCEMENT OF INTELLECTUAL PROPERTY RIGHTS THROUGH BORDER MEASURES 38 (2006).

(the TRIPS Agreement).<sup>63</sup> This dates back to the beginning of the Uruguay Round of the GATT negotiations in the 1980s.<sup>64</sup> Earlier in the history of IP, international treaty regimes governed IP for many years under the auspices of the World Intellectual Property Organization (WIPO), a U.N. organization founded in 1970 to promote new treaties and cooperation, and to centralize the administration of resulting international conventions.<sup>65</sup> WIPO's primary goals are promoting the protection of IP across the globe through cooperation among nations and in collaboration with other international organizations, and ensuring cooperation in administrative matters among IP unions.<sup>66</sup> As a specialized arm of the United Nations, WIPO is empowered to promote creative intellectual activity and to facilitate the transfer of IP-related technology to developing countries.<sup>67</sup> WIPO's mission is to accelerate developing nations' economic, social, and cultural development, within the boundaries inherent to the U.N. and its organs.<sup>68</sup> However, out of dissatisfaction with the progress of WIPO in protecting IP, the U.S. rallied the developed countries in shifting the forum from WIPO to GATT, thus linking IP to trade.<sup>69</sup> Accordingly, TRIPS was designed so that IP protection is now related to trade concessions.

During the negotiation of TRIPS, both developing and developed countries had very divergent views on the level of protection that should be granted to IP. Developed countries argued that the exploitation of IP protection is the engine of economic growth and technical competence for developing countries.<sup>70</sup> Developing countries, on the other hand, perceived a sophisticated IP regime as disproportionately benefiting foreign investors while administrative

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<sup>63</sup> See Peter K. Yu, *Currents and Crosscurrents in the International Intellectual Property Regime*, 38 LOY. L.A. L. REV. 323, 354-64 (2004).

<sup>64</sup> *Id.*

<sup>65</sup> Frank Garcia, *Protection of Intellectual Property Rights in the North American Free Trade Agreement: A Successful Case of Regional Trade Regulation*, 8 AM. U. J. INT'L L. & POL'Y 817, 821 (1993).

<sup>66</sup> Laurinda L. Hicks & James R. Holbein, *Convergence of National Intellectual Property Norms in International Trading Agreements*, 12 AM. U. J. INT'L L. & POL'Y 769, 782 (1997).

<sup>67</sup> *Id.*

<sup>68</sup> *Id.*

<sup>69</sup> See Yu, *supra* note 63, at 354-64.

<sup>70</sup> George Y. Gonzalez, *An Analysis of the Legal Implications of the Intellectual Property Provisions of the North American Free Trade Agreement*, 34 HARV. INT'L L.J. 305, 310 (1993).

costs consumed strained domestic resources.<sup>71</sup> The economic and social costs of TRIPS have been high in the developing countries, even though the prevailing view was that establishing IP rights would encourage technology transfers and make developing countries more attractive to foreign investment, which would lead to economic growth and development.<sup>72</sup> Therefore, any future multilateral agreements on increased protection of IP are highly unlikely.

Accordingly, due to little hope in having progress in IP protection multilaterally, regional and bilateral free trade agreements turned out to be an attractive option to developed countries, which were clearly looking for more protection. Hence, current international IP systems mirror the international trading system; both of them have two tracks, the multilateral track and the regional/bilateral track.<sup>73</sup>

Peter Yu has mentioned that the international IP regime is subject to currents of multilateralism which push for uniformity and the crosscurrents of resistance which call for national autonomy and international diversity. In fact, the regime is not fully harmonized; he highlighted five factors disharmonizing the international regime of IP.<sup>74</sup>

Nonetheless, there is no single source of international standards for IP, as these standards are derived from a multitude of international sources, including multilateral and bilateral treaties, regional harmonization derivatives, and key decisions from recognized courts like the European Court of Justice.<sup>75</sup>

Professor Helfer described the complexity of international IP regimes when he explained that what began as a regime with a single intergovernmental organization [WIPO] then became a bimodal regime with two predominant organizations [WTO and WIPO], and has now morphed into a multi-model or conglomerate regime populated by numerous intergovernmental bodies and networks of regional and bilateral agreements.<sup>76</sup> The international IP regime is a complex one, representing an amalgam of national laws, multilateral

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<sup>71</sup> *Id.*

<sup>72</sup> *Id.* at 311; see also A. Samuel Oddi, *International Patent System and Third World Development: Reality or Myth?*, 1987 DUKE L.J. 831 (discussing seven costs borne by the state that institutes an IP protection system).

<sup>73</sup> See Larry Crump, *Global Trade Policy Development in a Two-Track System*, 9 J. INT'L ECON. L. 487, 487-90 (2006).

<sup>74</sup> See Peter K. Yu, *Five Disharmonizing Trends in the International Intellectual Property Regime* (Mich. State Univ. Legal Studies Research Paper No. 03-28), available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=923177](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=923177).

<sup>75</sup> GRAEME B. DINWOODIE ET AL., *INTERNATIONAL INTELLECTUAL PROPERTY LAW AND POLICY* 41, 51-52 (2001).

<sup>76</sup> Laurence Helfer, *Regime Shifting: The TRIPS Agreement and New Dynamics of International Intellectual Property Lawmaking*, 29 YALE J. INT'L L. 1, 82 (2004).

conventions, bilateral and regional agreements, and supranational codes.<sup>77</sup>

### Free Trade and Intellectual Property in U.S. Trade Policy

Various economic and political interests associated with free trade and with the growth of commercial enterprise have affected the regulation of IP rights between countries.<sup>78</sup> IP has become a major component of international trade in the U.S.; the American information-based economy, in the increasingly globalized world, has become vulnerable to piracy, expropriation, and otherwise inadequate protection of its IP in foreign countries—particularly third-world countries.<sup>79</sup> Simultaneously, new technological developments have burst upon the international marketplace. These developments, like the production and advancement of products such as computers, semiconductors, and software, as well as biotechnology goods and pharmaceuticals, usually fall under the legal protection of IP rights.<sup>80</sup> Consequently, adequate protection of IP rights has become an increasingly important issue in the world of trade. The multinational corporations in the U.S. are concerned about, and affected by, the inadequate protection of IP rights and the non-enforcement of these rights, which imposes a significant burden on worldwide trade.<sup>81</sup>

In response, the U.S.—the lead exporter of technology and copyright protection—developed a strategy to expand the scope of IP protection. This strategy revolved around three overlapping concepts: (1) the creation of an effective dispute settlement mechanism for substantive IP rights; (2) the expansion of the definition of investment to include IP rights; and (3) the non-violation complaint alleging nullification or impairment of benefits. This strategy was successfully implemented in NAFTA<sup>82</sup> and in the WTO and bilateral and

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<sup>77</sup> Yu, *supra* note 63, at 443.

<sup>78</sup> Okediji, *supra* note 6, at 133.

<sup>79</sup> Marshall A. Leaffer, *Protecting United States Intellectual Property Abroad: Toward a New Multilateralism*, 76 IOWA L. REV. 273, 274 (1991).

<sup>80</sup> Anwar Imam, Note, *Reconciling the FTAA and TRIPS; Can a Free Trade Area of the Americas be a Fair Trade Area of the Americas? Implications of a Hemispheric Intellectual Property Agenda*, 1 LOY. U. CHI. INT'L L. REV. 217, 219 (2003).

<sup>81</sup> *Id.* at 222.

<sup>82</sup> Ralph Fischer, *The Expansion of Intellectual Property Rights by International Agreement: A Case Study Comparing Chile and Australia's Bilateral FTA Negotiations With the U.S.*, 28 LOY. L.A. INT'L & COMP. L. REV. 129, 132 (2006).

multilateral agreements.<sup>83</sup> Tackling all these agreements goes beyond the scope of this article, hence I will limit my research to bilateral free trade agreements.

Recognizing the importance of IP and innovation for the future growth and enhanced productivity of the U.S. economy, the Office of Intellectual Property and Innovation for the United States Trade Representative (USTR) utilizes a wide variety of bilateral and multilateral trade tools for the promotion of strong IP laws and effective enforcement throughout the world.<sup>84</sup> Some of these tools include:

- Bilateral engagement with U.S. trading partners;
- The annual “Special 301” review (Special 301), and reviews of compliance with the intellectual property requirements of U.S. trade preference programs;
- Negotiation of intellectual property chapters of bilateral and regional trade agreements; and
- Multilateral engagement through the World Trade Organization (WTO).<sup>85</sup>

The USTR also provides leadership for trade policies among all the interagency initiatives in order to help enforcement of IP rights.<sup>86</sup> In addition to focusing on IP, the USTR’s Office of Intellectual Property and Innovation creates and implements trade policy for many U.S. innovations, including those in the pharmaceutical and medical technology industries.<sup>87</sup>

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<sup>83</sup> *Id.*

<sup>84</sup> Office of the United States Trade Representative, Focus on Intellectual Property and Innovation, [http://www.ustr.gov/Trade\\_Sectors/Intellectual\\_Property/Section\\_Index.html](http://www.ustr.gov/Trade_Sectors/Intellectual_Property/Section_Index.html) (last visited Mar. 21, 2008).

<sup>85</sup> *Id.*

<sup>86</sup> *Id.*

<sup>87</sup> *Id.*

Phases of Protection of IP in U.S. Trade Policy

**First Track/Unilateral Remedies**

Looking back at history, the industries in the U.S. have requested the government to “withhold economic aid from developing countries that refused to provide strong levels of protection for foreign investors.”<sup>88</sup> This practice later became Special 301, which is a set of provisions under the Trade Act of 1974, requiring the USTR to identify countries that deny adequate and effective IP rights protection or deny fair and equitable market access to U.S. companies that rely on IP protection.<sup>89</sup> Foreign countries are either placed onto a priority foreign countries list (“watch list”), or the Section 306 monitoring list, according to how deficient existing IP protection is.<sup>90</sup>

Priority foreign countries are those that have the most egregious acts being performed against the U.S. and its products.<sup>91</sup> The USTR has the authority to initiate investigations into a country’s activities if it fails within thirty days to enforce agreements or to make efforts to stop the illegal activities that occur.<sup>92</sup> Priority watch list countries lack adequate IP protection or market access, so there will be ongoing negotiations about IP rights problems while a country is on this list.<sup>93</sup> The U.S. expects watch list countries to pass legislation or to develop remedies that conform to an agreement or to U.S. standards.<sup>94</sup>

The U.S. has unilaterally taken it upon itself to monitor the trade and business practices of other countries in order to discern instances in which unfair trade practices warrant U.S. warnings or threats of retaliation to the offending countries if such countries do not agree to rectify their offensive behavior.<sup>95</sup> Unilateral measures adopted by the U.S. have been subject to criticism worldwide. Special

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<sup>88</sup> Okediji, *supra* note 6, at 139.

<sup>89</sup> Arnold, *supra* note 3, ¶ 6.

<sup>90</sup> *Id.*

<sup>91</sup> Alisa Wrase, *U.S. Bilateral Agreements and the Protection of Intellectual Property Rights in Foreign Countries: Effective for U.S. Intellectual Property Interests or a Way Out of Addressing the Issue?*, 19 DICK. J. INT’L L. 245, 252 (2000).

<sup>92</sup> *Id.* at 252-53.

<sup>93</sup> *Id.* at 253.

<sup>94</sup> *Id.*

<sup>95</sup> DINWOODIE ET AL., *supra* note 75, at 782.

301 not only violates the multilateralism system through introducing unilateral measures, but it also contradicts the principle of non-discrimination and brings an element of discretion to trade relations that creates potential for abuse by the developed countries.<sup>96</sup>

### Second Track/Multilateralism

The U.S. has been an ardent supporter of the multilateral trading system during the Uruguay Round, as one of the major issues that triggered a controversy was whether the covered agreements would include IP rights.<sup>97</sup> Developing countries strongly opposed the idea, but the U.S. and several Western countries called for integrating IP into the GATT system.<sup>98</sup> The U.S. was looking for adequate worldwide protection of American IP, given the fact that the U.S. was not satisfied with the enforcement provisions in the Berne and Paris agreements.<sup>99</sup>

Yet, until the Uruguay Round, international protection standards were decided under the auspices of WIPO and its predecessor non-trade-related organizations. By contrast, TRIPS was negotiated wholly under the auspices of GATT—a trade organization.<sup>100</sup> The main achievement—as highlighted by the Reagan administration at this time—was to subject IP standards to an effective dispute settlement mechanism.<sup>101</sup> Its provisions were the result of bargain-linkage diplomacy, whereby IP protection was expressly linked to trade concessions in non-IP-related areas, such as agriculture and textiles.<sup>102</sup> GATT, unlike WIPO, is a multilateral trade negotiation forum, which offers opportunities for creative bargaining. Moreover, since the beginning of the Uruguay Round, efforts on both regional and international levels to create a harmonized international IP system have intensified. The topic of the debate has expanded from the need to combat global piracy to the role of IP protection in such diverse areas as sustainable development, treatment of medical pandemics, protection of biota, and the stewardship of the cultural heritage of indigenous peoples. There is no question that important multiregional treaties, such as the TRIPS Agreement and the Paris and

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<sup>96</sup> *Id.* at 783.

<sup>97</sup> Helfer, *supra* note 76, at 20-21.

<sup>98</sup> *Id.*

<sup>99</sup> *Id.*

<sup>100</sup> *Id.*

<sup>101</sup> *Id.*

<sup>102</sup> Gerald J. Mossinghoff, *National Obligations Under Intellectual Property Treaties: The Beginning of a True International Regime*, 9 FED. CIR. B.J. 591, 599 (1999-2000).

Berne Conventions, establish international minimum substantive standards of protection for traditional forms of IP.<sup>103</sup>

IP becomes more important as developed countries progress in their economic growth and industrial development.<sup>104</sup> Indeed, the industrialized states have increased their IP protection in parallel with increases in their technological and cultural development.<sup>105</sup> However, the U.S. was slow to recognize IP rights for foreign creators, doing so only when its own IP industries were highly developed, and it, in effect, built its cultural industries partly by permitting piracy of the works of foreign writers. The U.S. became a signatory to the Berne Convention for the Protection of Literary and Artistic Works only in 1989, and the U.S. was also slow to recognize foreign activities in patent law, in an effort to encourage importation of new techniques into the country.<sup>106</sup>

### Third Track/Bilateralism

Since the U.S. succeeded in shifting the forum from WIPO to WTO in relation to the protection of IP, bilateral and regional agreements have been pursued by the U.S. to effectuate the benefits of forum-shifting and to overcome limitations imposed by TRIPS.<sup>107</sup> The

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<sup>103</sup> Doris Estelle Long, Book Note, 96 AM. J. INT'L L. 755, 756 (2002) (reviewing G. GREGORY LETTERMAN, *BASICS OF INTERNATIONAL INTELLECTUAL PROPERTY LAW* (2001)).

<sup>104</sup> Anna Kingsbury, *Intellectual Property Provisions in Bilateral and Regional Free Trade Agreements: What Should New Zealand Expect from a New Zealand/United States Free Trade Agreement?*, 10 N.Z. BUS. L.Q. 222.

<sup>105</sup> *Id.*

<sup>106</sup> *Id.*

<sup>107</sup> "New bilateralism is clearly a tool to effectuate the benefits of forum shifting . . . and to sustain the expansion of intellectual property rights at the expense of the public interest both in developed and developing countries." Okediji, *supra* note 6, at 141.

Forum shifting is the practice of utilizing different institutional fora to accomplish desired goals. For example, the shift from WIPO to the WTO was classic forum shifting by the United States, which at the time was frustrated with WIPO's institutional weaknesses. Similarly, the shift from the WTO to bilateral and multilateral arrangements is another example of forum shifting to accomplish specific goals with respect to intellectual property.

*Id.* at 141, n.95.

U.S. has consistently raised IP protection standards abroad through the use of unilateral, bilateral, and multilateral action. For several reasons, including the breakdown of negotiations in Cancun and the unlikely success of any multilateral agreement seeking more protection of IP rights, the U.S. has become increasingly involved in FTA negotiations. FTAs are one of the tools used by the U.S. to globalize the norms of IP at a remarkable rate.<sup>108</sup> In order to lower the transaction costs of bilateralism, the U.S. developed a model or prototype of the kind of bilateral treaties it wishes to have with other countries. The minimum standards of TRIPS have been exceeded by IP chapters in FTAs.

Bilateralism is the main route taken to support U.S. industry in its inexorable campaign to increase the levels of IP protection worldwide. Some scholars accuse bilateralism of operating in a context of deep asymmetry, as the U.S. chooses to negotiate with developing countries that have little bargaining power.<sup>109</sup> It is clear that FTAs are an effective tool in depriving developing countries of the flexibilities allowed by the TRIPS Agreement. Multinational corporations were behind the linkage of trade and IP, first in the domestic U.S. context and then in the WTO.<sup>110</sup> Again aiming at gaining more profits and shareholder value, these multinational corporations lobbied to pressure the USTR in bilateral agreements not to accompany TRIPS implementation with strong measures destined to optimize local research, development, and innovation in developing countries.<sup>111</sup> Rather, those companies had no choice but to pursue this course of action and to consider new export markets and lower cost production centers, while maintaining the technological superiority of the West and its economic dominance.<sup>112</sup>

The strategy to seek greater protection of IP through unilateral pressure has been supplemented by more effective approaches. "TRIPS-plus" obligations are extracted in exchange for trade concessions in the context of free trade agreements.<sup>113</sup> FTAs remain a strategic, rather than a commercial, objective for the U.S.<sup>114</sup> They are a reaction toward the growing resistance that the U.S. encounters in multilateral settings.<sup>115</sup> Unlike multilateralism, which is based on non-

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<sup>108</sup> Ewell E. Murphy, Jr., *Charting the Transnational Dimension of Law: U.S. Free Trade Agreements as Benchmarks of Globalization*, 27 HOUS. J. INT'L L. 47, 67 (2004).

<sup>109</sup> Carlos Correa, *Bilateralism in Intellectual Property: Defeating the WTO System for Access to Medicines*, 36 CASE W. RES. J. INT'L L. 79, 93 (2004).

<sup>110</sup> See generally Yu, *supra* note 74.

<sup>111</sup> *Id.*

<sup>112</sup> *Id.*

<sup>113</sup> See generally Okediji, *supra* note 6.

<sup>114</sup> *Id.*

<sup>115</sup> *Id.*

discrimination, bilateralism is based on a preferential or reciprocal basis.<sup>116</sup> The willingness of developing countries to enter into bilateral or regional trade agreements which cost more in terms of IP is simply “a reflection of an extant and established wisdom handed down by the international agenda of the post-World War II era to assimilate developing countries into the world economic order on terms predetermined by the developed countries based on their own historical experiences and priorities.”<sup>117</sup>

Two benefits appear for the U.S. due to the switch to bilateralism. “First, by effectuating forum-shifting and reducing the number of negotiating parties, the U.S. can provide side payments that it would not be able to offer in a multilateral forum, given the diversity of interests the U.S. has *vis a vis* the contracting states.”<sup>118</sup> Secondly, by switching to bilateralism, the U.S. can also prevent less developed countries from reopening the TRIPS negotiations with a better bargaining position, so bilateral FTAs are used to dismantle the coalition of the developing countries in negotiations.<sup>119</sup>

FTAs are clearly expanding IP rights worldwide through a bilateral regime. Bilateral FTAs are the new dynamic of international IP lawmaking. Simultaneously, the U.S. focused on intra-regime shifts to divide and conquer the opposing parties to stronger IP protection as WTO negotiations progressed. On the other side, the developing countries started forming a veto coalition against the ratcheting up of IP standards, and they successfully obtained the Doha Declaration in November 2001.<sup>120</sup> The U.S. responded by adopting bilateral free trade agreements which would help the U.S. in picking off the developing countries one by one and would maximize IP standards.<sup>121</sup> The key here is whether bilateral free trade agreements can be used to create new norms of IP. TRIPS has many provisions that reflect the concerns of the developing countries with respect to IP, while the provisions of FTAs reflect the disparate bargaining power between developed and developing countries; moreover, FTAs take away all the gains of the developing countries found in TRIPS.<sup>122</sup>

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<sup>116</sup> *Id.*

<sup>117</sup> *Id.*

<sup>118</sup> See Yu, *supra* note 74, at 16.

<sup>119</sup> *Id.*

<sup>120</sup> Okediji, *supra* note 6, at 144-45.

<sup>121</sup> *Id.*

<sup>122</sup> *Id.* at 144.

Bilateralism is a strategic tool for the developed countries to ameliorate the dead-weight loss which is associated with multilateralism. This simply means that some developing countries will benefit from the concessions that developed countries give even though their markets are either insignificant or not currently attractive to the developed countries in the multilateral system.<sup>123</sup>

Bilateralism is a bundle of opportunities and risks for both developing and developed countries. Developing countries have to realize that there is a certain policy which motivated the developed countries to enter into these agreements, and the more important step is to find a way to secure benefits like strengthening the friendly principles contained in TRIPS or interposing principles independently. Otherwise, FTAs will create a one-way increase in IP standards which may splinter the coalition of developing countries in negotiating IP in the WTO, and they may have a tremendous negative effect on the competition, innovation, and public welfare in access to knowledge goods given the premature economy of these developing countries.

#### IP Chapters in Bilateral Free Trade Agreements

Recently, free trade agreements (FTAs) have proven to be one of the best ways to open foreign markets to U.S. exporters.<sup>124</sup> The United States currently has FTAs with fourteen countries; in 2006, FTAs were reached with Bahrain, El Salvador, Guatemala, Honduras, Morocco, and Nicaragua.<sup>125</sup> Also during that year, trade with countries with whom the United States had FTAs was significantly greater than those nations' relative share of the global economy; although comprising 7.5% of global gross domestic product (not including the United States), those FTA countries accounted for over 42% of U.S. exports.<sup>126</sup>

FTAs and BITs are two pillars in the U.S. bilateral policy to ratchet up IP protection; however FTAs, rather than BITs, contribute more to the ratcheting process that will eventually globalize IP norms.<sup>127</sup> BITs are agreements "between two sovereign nations to establish a stable investment climate within their borders for the

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<sup>123</sup> *Id.* This is also known as "free riding" on the benefits associated with the bargain, with little immediate loss to the domestic economy, as the developing countries are not equipped to exploit technology or other knowledge goods.

<sup>124</sup> U.S. Department of Commerce, International Trade Administration, Free Trade Agreements, [http:// trade.gov/fta/index.asp](http://trade.gov/fta/index.asp).

<sup>125</sup> *Id.*

<sup>126</sup> *Id.*

<sup>127</sup> Arnold, *supra* note 3, ¶¶ 9, 11.

investors of the parties to the agreement.”<sup>128</sup> IP, as a component of investment, receives protection as a by-product. FTAs are agreements “between two or more sovereign nations to remove all substantial barriers to trade . . . between the nations.”<sup>129</sup> FTAs devote a whole chapter to IP, while BITs do not; BITs apply national treatment principles so that foreign investors enjoy the same treatment as domestic investors, while the IP chapter in an FTA completely changes the IP regimes of the parties, thus giving more protection to IP owners or foreign investors than what existed before signing the FTA.<sup>130</sup>

The U.S. has been involved in the process of exporting law or U.S. norms through FTAs to economically disadvantaged states, thereby forming extended trading blocs linked by shared legal norms.<sup>131</sup> This explains, to some extent, why there is a rise in the number of bilateral/regional trade agreements within the context of a multilateral trading system.<sup>132</sup> The focus on IP—and the drafting of a whole chapter for it in a trade agreement—serves as an example of how the U.S. is using bilateral agreements to fulfill law-exporting goals that it could not achieve in the multilateral setting. However, it remains doubtful whether FTAs contribute to the harmonization of the IP regime. To sum up, bilateralism in IP casts post-TRIPS agreements as illicit exercises of power by the U.S. to undermine policy options and sovereign discretions granted by TRIPS.<sup>133</sup> The new bilateral agreements roll back both substantive and strategic gains of TRIPS for developing countries.<sup>134</sup>

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<sup>128</sup> *Id.* ¶ 10.

<sup>129</sup> *Id.* ¶ 11.

<sup>130</sup> *Id.*

<sup>131</sup> Mark B. Baker, *No Country Left Behind: The Exporting of US Legal Norms under the Guise of Economic Integration*, 19 EMORY INT’L L. REV. 1321, 1380 (2005).

<sup>132</sup> *Id.*

<sup>133</sup> Okediji, *supra* note 6, at 129.

<sup>134</sup> *Id.*

### **PART III**

#### **Oman/US Free Trade Agreement**

The U.S. and Oman signed the US-Oman Free Trade Agreement (OFTA) on January 19, 2006.<sup>135</sup> This agreement was the second of its kind between the U.S. and a Gulf-Arab country.<sup>136</sup> Originally, Oman acted as part of the Gulf Cooperation Council, which collectively aimed to negotiate trade agreements with the major economic powers in the world, including the U.S., the European Union, and Japan; however, there was an exception with respect to the U.S., allowing individual Gulf countries to enjoy leeway in negotiating FTAs with the U.S.<sup>137</sup>

I will talk about the OFTA parties and the political and economic reasons that persuaded those parties to sign this agreement, along with an introduction to their negotiating elements.

#### **The Negotiating Parties**

Because of its overall economic power, the U.S. has been a sought-after partner for the creation of FTAs.<sup>138</sup> President Bush outlined the strategy of the U.S. toward the Middle East with a clear goal of enhancing the global competitiveness of the Middle Eastern countries. Bush proposed the establishment of a U.S.-Middle East free trade agreement area within a decade.<sup>139</sup> The Office of the United States Trade Representative (USTR) is the agency that negotiates trade agreements on behalf of the U.S.

The USTR staff is a highly committed group of professionals with decades of specialized experience in trade issues and foreign regions of the world.<sup>140</sup> One of the USTR's mandates is to negotiate

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<sup>135</sup> OFTA, *supra* note 1.

<sup>136</sup> The first FTA between the U.S. and a Gulf country was in 2004; the agreement was signed between Bahrain and the U.S. Press Release, Office of the U.S. Trade Representative, United States and Bahrain Sign Free Trade Agreement (Sept. 14, 2004), available at [http://www.ustr.gov/Document\\_Library/Press\\_Releases/2004/September/United\\_States\\_Bahrain\\_Sign\\_Free\\_Trade\\_Agreement.html](http://www.ustr.gov/Document_Library/Press_Releases/2004/September/United_States_Bahrain_Sign_Free_Trade_Agreement.html)

<sup>137</sup> Cooperation Council for the Arab States of the Gulf, Economic Cooperation, <http://gcc-sg.org/cooperation.html#coop5> (last visited Mar. 15, 2008).

<sup>138</sup> JEFFREY J. SCHOTT, INST. FOR INT'L ECON., FREE TRADE AGREEMENTS, U.S. STRATEGIES, AND PRIORITIES 12 (2004).

<sup>139</sup> Paul G. Johnson, Note, *Shoring U.S. National Security and Encouraging Economic Reform in the Middle East: Advocating Free Trade with Egypt*, 15 MINN. J. INT'L L. 457, 459 (2006).

<sup>140</sup> Office of the United States Trade Representative, Who We Are, [http://www.ustr.gov/Who\\_We\\_Are/Section\\_Index.html](http://www.ustr.gov/Who_We_Are/Section_Index.html) (last visited Mar. 15, 2008).

directly with foreign governments to create trade agreements.<sup>141</sup> Representatives also meet with governments, business groups, legislators, and public interest groups, to gather input on trade issues and to explain the President's trade policy position.<sup>142</sup> The head of the USTR is the U.S. Trade Representative, a Cabinet member who serves as the President's principal trade advisor, negotiator, and spokesperson on trade issues.<sup>143</sup> The USTR is part of the Executive Office of the President, and consults with other government agencies on trade policy matters through the Trade Policy Review Group (TPRG) and the Trade Policy Staff Committee (TPSC).<sup>144</sup> These groups, administered and chaired by the USTR and composed of nineteen federal agencies and offices, make up the sub-Cabinet level mechanism for developing and coordinating U.S. positions on international trade and trade-related investment issues.<sup>145</sup> The U.S. Congress established a private sector advisory committee system in 1974 to ensure that U.S. trade policy and trade negotiation objectives adequately reflect U.S. commercial and economic interests.<sup>146</sup> Congress expanded and enhanced the role of this system in subsequent trade acts, most recently the Trade Act of 2002.<sup>147</sup>

The USTR is encountering a spurt of negotiating activity, in parallel with the Doha Round; dozens of bilateral free trade agreement have been negotiated with many countries in different parts of the world.<sup>148</sup> The USTR uses three tests when picking an FTA partner:

1. Cooperation on foreign policy issues: Oman, after September 11, 2001, announced its commitment to support the U.S. in its war on terrorism. This is considered to be the carrot-and-stick element.<sup>149</sup> FTAs are used by the current administration to

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<sup>141</sup> *Id.*

<sup>142</sup> *Id.*

<sup>143</sup> Office of the United States Trade Representative, Who We Are, Mission of the USTR, [http://www.ustr.gov/Who\\_We\\_Are/Mission\\_of\\_the\\_USTR.html](http://www.ustr.gov/Who_We_Are/Mission_of_the_USTR.html) (last visited Mar. 15, 2008).

<sup>144</sup> *Id.*

<sup>145</sup> *Id.*

<sup>146</sup> *Id.*

<sup>147</sup> *Id.*

<sup>148</sup> SCHOTT, *supra* note 138, at 362.

<sup>149</sup> *Id.* at 370.

reward the allies of the U.S. in its war against terrorism.

2. Impact of the FTA on the economic development of the partner country, thus deepening democratic processes and rule of law: it is obvious that Oman will greatly benefit from OFTA.<sup>150</sup>
  
3. The impact and the contribution of this particular negotiation on the broader initiative of each continent: concluding the agreement with Oman is a step forward for a regional MEFTA in the future.<sup>151</sup> The President's Middle East Free Trade Agreement initiative seeks to promote free trade throughout the region and between the region and the United States. The United States recognizes the differing levels of development across the region and is taking a graduated step-by-step approach to creating a free trade area with interested countries who are willing to open their economies and liberalize their trade regimes.<sup>152</sup> In May 2003, the President announced his initiative to create a Middle East Free Trade Area by 2013. This initiative is designed to deepen U.S. trade relationships with all countries of the region, through steps tailored to individual countries' level of development. Since that announcement, the United States has concluded FTA negotiations with Morocco and Bahrain and has signed Trade and Investment Framework Agreements (TIFAs) with Saudi Arabia, the United Arab Emirates, Kuwait, Qatar, Yemen, and now with Oman.<sup>153</sup>

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<sup>150</sup> *Id.*

<sup>151</sup> *Id.*

<sup>152</sup> *Id.*

<sup>153</sup> Press Release, Office of the U.S. Trade Representative, United States to Begin Free Trade Negotiations This Week with the United Arab Emirates and Oman (Mar. 8, 2005), available at [http://www.ustr.gov/Document\\_Library/Press\\_Releases/2005/March/United\\_States\\_to\\_Begin\\_Free\\_Trade\\_Negotiations\\_This\\_Week\\_with\\_the\\_United\\_Arab\\_Emirates\\_Oman.html](http://www.ustr.gov/Document_Library/Press_Releases/2005/March/United_States_to_Begin_Free_Trade_Negotiations_This_Week_with_the_United_Arab_Emirates_Oman.html).

The other party—Oman—is a middle-income economy in the Middle East with notable oil and gas resources, a substantial trade surplus, and low inflation.<sup>154</sup> Oman became a member of the World Trade Organization in November 2000 and continues to liberalize its markets.<sup>155</sup> It ratified a free trade agreement with the United States in September 2006 and, as part of the Gulf Cooperation Council, is seeking similar agreements with the European Union, China, and Japan.<sup>156</sup> To reduce unemployment and limit dependence on foreign labor, the government is encouraging the replacement of foreign expatriate workers with local workers.<sup>157</sup> Oman is actively looking forward to having private foreign investors, especially in the industrial, information technology, tourism, and higher education fields.<sup>158</sup> Oman's industrial development plans focus primarily on the use of its gas resources, metal manufacturing, petrochemicals, and international transshipment ports.<sup>159</sup>

In Oman's case, the U.S. strategy dovetails perfectly with Oman's needs. Oman is an oil-rich nation with a fairly modest population of three million.<sup>160</sup> A relatively small country in terms of population, like the majority of the Gulf countries, Oman enjoys a good standard of living.<sup>161</sup> Oman is a Muslim country; this common faith does not mean it needs to be isolated from the rest of the world. Isolation is not a tenet of Islam—for the Quran itself, which is the constitution of all Muslims, teaches its followers to be helpful to one another according to goodness and piety, and not to embrace actions for evil or malicious intent.<sup>162</sup> The extension of economic relations with other countries—especially where it contributes to the

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<sup>154</sup> CENTRAL INTELLIGENCE AGENCY, THE WORLD FACTBOOK (2008), *available at* <https://www.cia.gov/cia/publications/factbook/geos/mu.html> (last visited Mar. 21, 2008).

<sup>155</sup> *Id.*

<sup>156</sup> *Id.*

<sup>157</sup> *Id.*

<sup>158</sup> *Id.*

<sup>159</sup> *Id.*

<sup>160</sup> *Id.*

<sup>161</sup> United States Department of State, Background Note: Oman, <http://www.state.gov/r/pa/ei/bgn/35834.htm>.

<sup>162</sup> Mosad Zineldin, Globalisation and Economic Integration Among Arab Countries, Address Before the Fourth Nordic Conference on Middle Eastern Studies: The Middle East in a Globalizing World (Aug. 13-16, 1998), *available at* <http://www.hf.uib.no/smi/pao/zineldin.html>.

improvement of the standard of living of Muslims—is definitively within such Islamic principles and notions.

Oman is a member of the Gulf Cooperation Council (GCC), one of the regional blocs which includes six rich Arab countries.<sup>163</sup> As part of the GCC, Oman is currently undergoing a drastic change in its policy since the last decade.<sup>164</sup> The leaders of this region are willing to change their traditional economic strategy and prioritize the diversification of their economies in order not to be completely dependent upon their oil revenues.<sup>165</sup> With the U.S. as a partner, Oman has a good chance to develop this diversification agenda and promote this new policy. FTAs are considered to be one of the tools for attracting the flow of investment and technology to the other partners in the agreement.<sup>166</sup> Hence the U.S.-Oman FTA would contribute effectively in pushing ahead this matter. Accordingly, Oman enthusiastically signed the FTA with the U.S. after seven months of negotiations.<sup>167</sup> It is the fourth Arab country to conclude an FTA with the U.S. after Jordan, Morocco, and Bahrain.<sup>168</sup>

By this action, both countries exhibit a desire for peace, stability, and economic opportunity in the Middle East.<sup>169</sup> Several factors played out for starting the negotiation of this agreement, namely the accession of Oman to the WTO and the U.S.-Oman bilateral trade and investment framework agreement; each paved the way for an economic dialogue, which eventually ended with the conclusion of OFTA.<sup>170</sup>

The impact of an FTA varies according to whether the party is a developed or developing country. In the case of a developing country, the benefits of the provisions which heighten the standards will not be limited to the nationals of the governments that are parties to the agreement. Thus, when the enforcement obligations become effective, it is likely that all copyright and trademark owners will be able to benefit from heightened enforcement and the need to change national legislation, because the changes that will take place in IP laws and regulations will not identify the nationals of only one country as

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<sup>163</sup> Amr Daoud Marar, *The Cooperation Council for the Arab States of the Gulf*, 10 *LAW & BUS. REV. AM.* 475, 475 (2004).

<sup>164</sup> *Id.* at 476.

<sup>165</sup> Cooperation Council for the Arab States of the Gulf, Foundations and Objectives, <http://gcc-sg.org/Foundations.html>

<sup>166</sup> See Murphy, Jr., *supra* note 108.

<sup>167</sup> Press Release, Office of the U.S. Trade Representative, United States and Oman Sign Free Trade Agreement (Jan. 19, 2006), available at [http://www.ustr.gov/assets/Document\\_Library/Press\\_Releases/2006/January/asset\\_upload\\_file25\\_8774.pdf](http://www.ustr.gov/assets/Document_Library/Press_Releases/2006/January/asset_upload_file25_8774.pdf).

<sup>168</sup> *Id.*

<sup>169</sup> *Id.*

<sup>170</sup> Press Release, Office of the U.S. Trade Representative, *supra* note 153.

being eligible for an increased level of enforcement. Instead, the changes will be a general legislative amendment addressing border measures.<sup>171</sup> For example, due to the FTA between the U.S. and Oman, the government of Oman will change the relevant codes or statutes to empower the authorities to take border enforcement actions against imports, exports, and goods in transit.<sup>172</sup> In practice, the legislative language is likely to be sufficiently general as to provide for the general authority to take the enforcement action required in compliance with the free trade agreement and to not include any reference to the nationals of the countries that can benefit from the expanded legal authority for border measures. Therefore, it is likely that a Japanese, Egyptian, German, or Chinese IP rights owner that has a registered trademark in Oman—or in any other country agreeing to increase its border enforcement in compliance with free trade agreement obligations—will be able to benefit from the heightened level of enforcement.<sup>173</sup>

If an FTA has a direct impact on the domestic laws and regulations in the developing country, this is not the same for the more advanced countries or the developed countries.<sup>174</sup> The U.S., for example, does not only export U.S. standards enshrined in U.S. statutes; these agreements also create internationally binding obligations for the U.S., which can only be found in U.S. case law, and they even obligate the U.S. to raise its own domestic standards, which would circumvent democratic governance by using backdoor negotiations to achieve what officials otherwise could not achieve in Congress.<sup>175</sup> From a domestic perspective, such expansion of domestic protection via international law is problematic since it largely excludes democratic debate in national parliaments on whether such expansion should take place.<sup>176</sup> For interested industries, FTAs are, therefore, an ideal instrument to promote IP expansion both on the international and the domestic level.<sup>177</sup> The more countries that are bound by TRIPS-plus standards of bilateral FTAs, the more likely it becomes that these often proprietary standards replace the still

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<sup>171</sup> TIMOTHY P. TRAINER, PROTECTING INTELLECTUAL PROPERTY RIGHTS ACROSS BORDERS 709-711 (2d ed. 2007).

<sup>172</sup> *Id.*

<sup>173</sup> *Id.*

<sup>174</sup> Okediji, *supra* note 6, at 146.

<sup>175</sup> Yu, *supra* note 63, at 323-74.

<sup>176</sup> *Id.* at 392-400.

<sup>177</sup> *Id.*

recognizable pro-competitive standards of the TRIPS Agreement.<sup>178</sup> Likewise, FTAs promote proprietary expansion of domestic IP standards, even in the U.S., without sufficient democratic control.<sup>179</sup> For example, the U.S. pushed Chile and Singapore to adopt the controversial provisions of the Digital Millennium Copyright Act of 1998 (DMCA) in free trade agreements.<sup>180</sup> Yu warned that this practice of having IP advanced provisions in FTAs signed by the U.S. may backfire on domestic constituencies, either through the concept of customary international law—when these provisions are consistently applied by other states—or may at least form the context which the panels, in the case of any dispute, would use to interpret any treaty to which the U.S. is a signatory.<sup>181</sup>

#### **PART IV**

##### **Oman's Relationship to Intellectual Property**

The Sultanate of Oman hosted the Arab Regional Forum on the Economic Importance of Intellectual Property from February 22-24, 1999.<sup>182</sup> Faisal Bin Ali Al-Saeed, Minister of Omani National Heritage and Culture, sponsored the forum's activities, in cooperation with the Ministry of Trade and Industry and WIPO, along with a number of other international organizations. Oman joined the WTO in 1997 under Omani Decree No. 74/96 as an instrument of accession, and became a full member as of February 1997.<sup>183</sup> Lately, Oman has enforced its IP laws through raids on audiovisual tapes stores, and will now commence enforcing the law regarding computer programs and compact discs.<sup>184</sup>

Oman has only recently adapted to a knowledge-based economy, and does not have a large number of IP owners within its borders. Thus, Oman does not appear to have an interest in increasing IP rights. However, adopting foreign standards as a part of free trade agreements is part of Oman's strategy to benefit its overall economic position and open free trade; strong domestic IP rules are essential to economic growth and development.<sup>185</sup> Although it is true that the IP provisions will protect far more foreign investors than local interests,

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<sup>178</sup> *Id.*

<sup>179</sup> *Id.*

<sup>180</sup> *Id.*

<sup>181</sup> *Id.*

<sup>182</sup> ABU-GHAZALEH, *supra* note 38, at xvii.

<sup>183</sup> *Id.*

<sup>184</sup> *Id.* at xxiv.

<sup>185</sup> Helfer, *supra* note 76, at 79.

the economic gain to the local economy from these protections will be evident through increased foreign investment.<sup>186</sup>

### **The Effect on Intellectual Property Rights of Chapter 15 of OFTA**

Through this Part, I will examine the provisions of the IP chapter in the free trade agreement between the U.S. and Oman. These provisions have influenced the domestic laws and regulations in Oman. The interaction between domestic laws and international agreements will also be explored. Although international agreements are one of the sources of international law, they need to go through the domestic legal system, as most countries maintain the dualism approach in dealing with international law issues. This Part is devoted to an objective assessment of free trade agreements and their IP chapters. Will IP chapters increase trade and foreign direct investment in developing countries, or will they simply strengthen the West's hold on the international economy as they increase Western multinationals' profits and weed out competitors from developing nations?

Under NAFTA, Mexico was obligated to make major changes to its IP laws and procedures. These changes were driven by U.S. interests in technology and its protection.<sup>187</sup> Likewise, OFTA will have a major impact on Omani IP law. Chapter 15 requires Oman and the U.S. to ratify or accede to a long list of international agreements (including TRIPS-plus agreements); in addition, all reasonable efforts must be taken to ratify the Patent Law Treaty and the Hague Agreement (concerning the international registration of industrial designs).<sup>188</sup>

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<sup>186</sup> Gonzalez, *supra* note 70, at 310.

<sup>187</sup> *Id.* at 309.

<sup>188</sup> Article 15.1 of OFTA reads as follows:

Each Party shall ratify or accede to the following agreements by the date of entry into force of this Agreement:

- (a) the *Patent Cooperation Treaty* (1970), as amended in 1979;
- (b) the *Convention Relating to the Distribution of Programme-Carrying Signals Transmitted by Satellite* (1974);
- (c) the *Protocol Relating to the Madrid Agreement Concerning the International Registration of Marks* (1989);
- (d) the *Budapest Treaty on the International Recognition of the Deposit of Microorganisms for the Purposes of Patent Procedure* (1977), as amended in 1980;

National treatment is required for all categories of IP protection, enjoyment, and benefits.<sup>189</sup> Transparency for IP laws, regulations, and procedures is another important principle, with online trademark registration and searchable databases.<sup>190</sup> There are extensive and detailed mandatory national rules for trademarks, geographical indications, domain names, copyrights (including online technology protection and rights management measures), related performers' rights, encrypted satellite signals, patents (including plant patents), and regulation of pharmaceutical and chemical products (including test data and trade secret protection).<sup>191</sup>

Furthermore, Chapter 15 broadly enumerates rules for enforcement of IP rights, including general obligations, civil and administrative penalties, temporary relief measures, border controls (especially regarding counterfeit and pirated goods), and criminal procedures and remedies.<sup>192</sup> A lengthy list of limitations on copyright liability for Internet service providers is also included.<sup>193</sup>

The IP chapter provides for strong protection of copyrights, patents, trademarks, and trade secrets, including enhanced enforcement and non-discrimination obligations for all types of IP. Through the copyright provisions, the parties will address the challenge of providing protection in the digital environment of the Internet and will provide important protection for performers and producers of phonograms. Under the FTA, the parties will provide strong protections for trademarks and will apply the principle of "first in time, first in right" to trademarks and geographic indicators applied

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- (e) the *International Convention for the Protection of New Varieties of Plants* (1991) (UPOV Convention);
  - (f) the *Trademark Law Treaty* (1994);
  - (g) the *WIPO Copyright Treaty* (1996); and
  - (h) the *WIPO Performances and Phonograms Treaty* (1996).

OFTA, *supra* note 1, art. 15.1 ¶ 2. Article 15.1 also provides that:

- Each Party shall make all reasonable efforts to ratify or accede to the following agreements:
- (a) the *Patent Law Treaty* (2000); and
  - (b) the *Hague Agreement Concerning the International Registration of Industrial Designs* (1999).

*Id.* art. 15.1 ¶ 3.

<sup>189</sup> *Id.* art. 15.1 ¶¶ 5-7.

<sup>190</sup> *Id.* art. 15.1 ¶ 11.

<sup>191</sup> *Id.* arts. 15.2-15.9.

<sup>192</sup> *Id.* art. 15.10.

<sup>193</sup> *Id.* art. 15.10 ¶ 29

to products.<sup>194</sup> The chapter streamlines trademark filing processes while providing greater protection of owners' rights.<sup>195</sup> What follows is a more detailed description of the provisions of OFTA and their impact on Omani laws and regulations.

### 1. Trademark

Pursuant to OFTA, the U.S. and Oman agreed to change Oman's definition of a trademark to match U.S. law.<sup>196</sup> The amended trademark definition went into effect, in accordance with the Agreement, on January 19, 2006.<sup>197</sup> The definition of trademark no longer contains the requirement that the trademark must be visually perceptible.<sup>198</sup> Trademark applicants may register for non-conventional marks, such as sound and scent marks.<sup>199</sup>

OFTA applies the property law principle of "first in time, first in right" to trademark and geographical indicators applied to products; the first to file for a trademark is granted the first right to use that name, phrase, or geographical place name.<sup>200</sup> Despite the wide acceptance of this principle in the Western legal system, it is still questionable if this concept may apply to non-Western legal systems; Oman's legal system is based heavily on the French legal system.<sup>201</sup> OFTA also implements various procedural changes, which may increase the efficiency of trademark and geographical indication registration.<sup>202</sup>

### 2. Copyright

Royal Decree No. 47/96, promulgating copyright law, represents the first copyright protection law in Oman.<sup>203</sup> The enforcement of copyright protection lies within the Ministry of Heritage and Culture,

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<sup>194</sup> *Id.* art. 15.2.

<sup>195</sup> *Id.*

<sup>196</sup> *Id.*

<sup>197</sup> *Id.*

<sup>198</sup> *Id.*

<sup>199</sup> *Id.* art. 15.2 ¶ 1 ("Neither Party may require, as a condition of registration, that signs be visually perceptible, nor may a Party deny registration of a trademark solely on the grounds that the sign of which it is composed is a sound or a scent.")

<sup>200</sup> *Id.* art. 15.2.

<sup>201</sup> See Raslan, *supra* note 22, at 558-59.

<sup>202</sup> OFTA, *supra* note 1, art. 15.2.

<sup>203</sup> FEILER, *supra* note 47, at 252.

the Ministry of Commerce and Industry, and the Royal Oman Police, and has been effective, as scores of pirated video and audiotapes and computer software have disappeared from local vendors' shelves.<sup>204</sup> In late 2003, sixteen companies in Oman signed the Business Software Alliance (BSA) Code of Ethics.<sup>205</sup> The Code declares that the signatories will neither commit nor tolerate the manufacture, use, or distribution of unlicensed software, and will only supply licensed software to customers.<sup>206</sup>

OFTA extends protection for copyrighted works and phonograms consistent with U.S. standards and international trends.<sup>207</sup> Uniformity is another achievement that will help foreign artists have the same duration of their copyright in Oman as in the U.S. On a different front, in 1998, the U.S. passed the Digital Millennium Copyright Act (DMCA) to resolve the issue of Internet service provider liability for transferring copyrighted material.<sup>208</sup> The U.S.-Singapore FTA was the first international agreement to implement anti-circumvention provisions similar to DMCA; these provisions form strong protection to prevent piracy and unauthorized distributions over the Internet.<sup>209</sup> OFTA has come with the same provisions; however, the challenge is how Oman will adapt its domestic laws.

Several more provisions continue to strengthen and modernize copyright protection, as OFTA ensures that only authors, composers, and other copyright owners have the right to make their works available online.<sup>210</sup> Copyright owners maintain rights to temporary copies of their works on computers, which is important to protecting music, videos, software, and text from widespread unauthorized sharing via the Internet.<sup>211</sup> OFTA also provides for some long-needed changes to prevent copyright piracy in the digital age. One change adds specific protection for satellite signals carrying encrypted programming.<sup>212</sup> This protection extends to the signals themselves, as

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<sup>204</sup> OFFICE OF THE U.S. TRADE REPRESENTATIVE, FOREIGN TRADE BARRIERS 188 (2004), available at [http://www.ustr.gov/assets/Document\\_Library/Reports\\_Publications/2004/2004\\_National\\_Trade\\_Estimate/2004\\_NTE\\_Report/asset\\_upload\\_file231\\_4191.pdf](http://www.ustr.gov/assets/Document_Library/Reports_Publications/2004/2004_National_Trade_Estimate/2004_NTE_Report/asset_upload_file231_4191.pdf).

<sup>205</sup> *Id.*

<sup>206</sup> *Id.*

<sup>207</sup> OFTA, *supra* note 1, art. 15.4 ¶ 4.

<sup>208</sup> 17 U.S.C. §§ 1201-1205 (2006).

<sup>209</sup> Kenneth Chiu, *Harmonizing Intellectual Property Law Between United States and Singapore: The United States-Singapore Free Trade Agreement's Impact on Singapore's Intellectual Property Law*, 18 *TRANSNAT'L LAW.* 489, 503 (2005).

<sup>210</sup> OFTA, *supra* note 1, arts. 15.4-15.5.

<sup>211</sup> *Id.*

<sup>212</sup> *Id.* art. 15.7.

well as to the programming.<sup>213</sup> Thus, these changes will prevent piracy of satellite television programming, which was formerly unregulated by Omani laws.

### 3. Patent

OFTA harmonized procedural matters concerning patent applications and patent duration with the U.S.<sup>214</sup> Most significant among the procedural changes, the patent term can be extended to compensate for up-front administrative or regulatory delays in granting the original patent, consistent with U.S. practice.<sup>215</sup>

In another provision, OFTA specifies protection for patents covering biotech plants and animals.<sup>216</sup> This protection restates existing patent practices and also adopts the language of the TRIPS Agreement.<sup>217</sup> Unlike the TRIPS Agreement, however, OFTA does not provide the government with the flexibility to refuse a patent based on public health and environmental concerns.<sup>218</sup> In the U.S.-Singapore FTA, the U.S. Labor Advisory Committee rejected this formation of protection, and the USTR responded by noting that the FTA did not prevent either the U.S. or Singapore from keeping products produced from a patent, such as new plant or animal forms that potentially may harm the environment, from entering the market.<sup>219</sup>

Article 31 of TRIPS provides that member countries can grant a compulsory license in limited circumstances, as an annulment of the patent right by a judicial or governmental authority, causing a temporary deprivation of a patentee's monopoly over the original subject matter; therefore, recipients of a compulsory license may make, use, and sell the otherwise patented subject matter before the expiration of the compulsory license.<sup>220</sup> The U.S. addressed this issue in two ways: first, by applying the TRIPS standard, as in the Chile FTA; and second, by limiting the use of compulsory licenses to

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<sup>213</sup> *Id.*

<sup>214</sup> *Id.* art. 15.8.

<sup>215</sup> *Id.*

<sup>216</sup> *Id.* art. 15.9.

<sup>217</sup> *Id.*

<sup>218</sup> *Id.*

<sup>219</sup> Chiu, *supra* note 209, at 505.

<sup>220</sup> Sahar Aziz, *Linking Intellectual Property Rights in Developing Countries with Research and Development, Technology Transfer, and Foreign Direct Investment*, 10 ILSA J. INT'L & COMP. L. 1, 14 (2003).

antitrust remedies, public non-commercial uses, or national emergencies.<sup>221</sup>

#### Enforcement of Intellectual Property Rights

All the previous rights mentioned have no value if there is not proper enforcement. Piracy and IP theft are major concerns in the Middle East, and are, therefore, primary focuses of OFTA. Although Oman is not known for creating IP, it has now agreed to strictly protect IP rights; but realistically, a nation with little IP development has little incentive to protect or enforce IP rights.

By agreeing to adopt these IP protections, Oman has established itself as a haven in the Middle East for all IP owners to attract future business. Oman has adopted a large amount of American IP law via OFTA. Most of this has been to satisfy U.S. concerns. Although the overall effect of OFTA is to promote trade in Oman, the majority of IP changes serve the U.S. and other foreign nations, as well. Even though the IP law changes primarily serve countries other than Oman, strong IP protection will make Oman more attractive to foreign investors and foster economic growth. Furthermore, strong IP protection will encourage the kind of domestic economic policies in the Middle East that will enable the growth of high-value, high-wage industries built on the IP assets of the region's people. Thus, Oman will attract foreign companies looking to expand, including those companies already doing business in Oman. Extending U.S. trade into the Middle East is a necessary step towards maintaining future economic growth for the U.S., and security and peace in the Middle East. However, the U.S. has to tailor IP protection to each country, rather than creating a uniform level of protection among all countries, so as not to disturb the local economies of other countries in the Middle East. Otherwise, those IP changes will stifle creativity, cause confusion, and hinder local businesses' ability to compete with foreign business.

On the other side, Oman may be signing a large array of bilateral agreements, which may create conflicting obligations. Oman, as part of the GCC, could sign a bilateral agreement with the E.U., after having already signed one with the U.S. The two economic powers of the U.S. and the E.U. have huge disagreements over many IP issues. Oman may end up with conflicting obligations and bilateral agreements which not only fail to reflect or meet its local conditions, but also force the nation to juggle two conflicting agreements.

Traditionally, IP lawmaking is a domestic affair; however, the control of national governments over the adoption and implementation

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<sup>221</sup> Arnold, *supra* note 3, ¶ 20.

of domestic IP laws is greatly reduced under an FTA. International lawmaking has begun to replace country-based assessments and domestic policymaking as the predominant mode of IP lawmaking. This may be offset by asserting the “laboratory effect” of bilateral agreements on the multilateral trading system.

### **Conclusion**

OFTA signifies that the U.S. is beginning to understand the importance of the Middle East to IP protection. In particular, the U.S.-Oman trade link will benefit the U.S. greatly. Additionally, the U.S. will strengthen its political base in the Middle East. Still, the U.S. must continue to build upon OFTA and demonstrate that the Middle East is a priority by negotiating further agreements with other partners in the region, like Saudi Arabia or Egypt. However, the U.S. must tailor IP protection to each country in the Middle East, rather than creating a uniform level of protection among all countries, so as not to disturb the local economies of those countries. Otherwise, those IP changes will stifle creativity, cause confusion, and hinder local businesses’ ability to compete with foreign businesses, as OFTA could have done if not for Oman’s ability to absorb the negative impacts of these IP changes in exchange for future economic growth. Hence, one can expect different provisions in IP chapters when the U.S. negotiates FTAs with other countries in the region, like Egypt or Saudi Arabia.

It is likely that Oman will find itself obliged to introduce a number of changes in its laws because of the IP chapter in its FTA with the U.S, meaning that its IP laws will need to be rewritten or entirely new laws will need to be passed. Oman is a small economy that is a net importer of technology; it is not in the interest of Oman to increase IP protection above TRIPS Agreement levels. The negotiators on behalf of Oman view the inclusion of stronger IP protection as a costless choice in return for tangible benefits in other trade areas, or perhaps inconsequential to their national interests, and they will obtain other trade-related concessions; this how Omanis’ interests coincided with U.S. interests in having a stronger IP protection chapter in OFTA.

In the realm of IP disputes, a senior official of WIPO divided IP disputes in two: those of a private law nature, where the dispute arises between two private enterprises; and those of a public law nature, which arise between nations. However, there is another type which is a hybrid form of the two dispute types; this is a mixed

international arbitration (state-investor dispute arbitration). While BITs have only mixed and private nature disputes, and the WTO is limited to the public aspect of disputes, FTAs establish themselves as a forum for all three kinds of IP disputes. Hence, I would argue that an FTA is the most powerful means of enforcing IP protection. In the near future, there will be a surge of IP disputes, whether under BITs or FTAs. Two accelerators of globalization are clearly represented in FTAs; technology, as it is embodied in IP chapters, and transnational investment, as described in investment chapters.

Developed countries, and particularly the U.S., have realized that FTAs are an effective tool in stripping developing countries of their capacity to develop their own IP laws and regulations on their own terms, and a solid means of forcing them to adopt certain laws and regulations in this field which are predetermined by the developed countries based on their own historical experiences and priorities. The ever-increasing level of IP standards embodied in FTAs is necessary to secure the competitive advantages of developed countries and to maintain the hold of the U.S. on IP rights.

With respect to the international regime of IP, bilateral free trade agreements are not only disharmonizing the international IP regime, but are also creating a lot of doubts about whether these bilateral agreements can develop IP legal norms through the consistent practice of the countries that sign these agreements. Finally, other countries in the Middle East should undergo an economic and social analysis of the impact of adopting a Western-style protection of their IP rights.





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IP AS VENTURE CAPITAL  
A CASE STUDY OF MICROSOFT IP VENTURES

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### *I. Executive Summary*

In the current marketplace, many companies are unknowingly managing their intellectual property in a Closed Innovation environment – producing, developing, and monetizing intellectual property (“IP”) solely within their company. However, there is a more effective method of managing IP: Open Innovation. In an Open Innovation model, companies license their IP to other companies and alternatively seek to license another companies’ IP to develop in-house products.

This distinction between Open and Closed Innovation is all the more important to software companies, who depend on the protection of their IP for their existence. Most of a software company’s assets are in the form of intangible assets, which could not sustain a long-term competitive advantage without the protections of IP regimes. However, this phenomenon is not unique to the software industry. By some estimates at least 75% of the Fortune 100’s total market capitalization is represented by intangible assets, such as patents, copyrights, and trademarks.<sup>1</sup> While much has been written regarding the importance of monetizing new innovations through patents, trademarks, and copyrights, little has been discussed about monetizing innovations which are not incorporated or maximally utilized by the company. This latter topic will be explored in detail in this article.

The following sections of this paper will examine the shortcomings of the Closed Innovation model, and specify how the Open Innovation model addresses these issues. We will also illustrate the implementation of Open Innovation by Microsoft Corporation. Microsoft, through Microsoft IP Ventures, has expanded the concepts of Open Innovation beyond licensing and cross licensing to using IP as Venture Capital. The implementation of this aggressive IP strategy allows Microsoft to capture value from its IP in a unique way.

Finally, this paper considers some improvements upon the IP as Venture Capital model as implemented by Microsoft IP Ventures.

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<sup>1</sup> Markus Reitzig, *Strategic Management of Intellectual Property*, MIT SLOAN MGMT. REVIEW, Spring 2004, at 35.

## II. *The Problem*

Software companies invest large amounts of capital into Research and Development (“R&D”) in hopes to implement innovations into existing software products, or to create new software products altogether. The problem, as illustrated by Exhibit 1, *infra*, is that often these efforts produce more technology than a company can effectively implement into its business model. Although some of this newly developed technology may not have any business value worth pursuing, profitable technologies are often not encompassed into a company’s business model for reasons unrelated to the technology’s prospects or profitability. For example, it is common for a large company to have separate processes which determine the projects a R&D team will work on, what inventions will get developed into products, and whether to patent a particular invention.<sup>2</sup> This lack of coherence between these processes can result in promising technology being undeveloped or unused.

This problem is exacerbated in a closed value chain where there is only one opportunity to implement internally developed technology. Exhibit 2, *infra*, shows a closed value chain. A company with a closed value chain keeps all of its research and innovation in-house and adheres to the philosophy that successful innovation requires complete control over its technology. Even if given the opportunity to sell the undeveloped or unused technology, this company may choose to leave the nascent technology on the shelf and protect it as a trade secret. A trade secret is a form of protection which affords the company a competitive advantage over its competitors who do not possess it.

If the innovator cannot achieve a substantial commercial gain from a new design, but its competitors could, the release of the design to the public would differentially favor the competitor and the innovator would suffer both the costs of development and whatever further costs resulted from the strengthened competition from the second firm.<sup>3</sup>

Consequently, by such logic a company may determine that the best use of a new technology is to leave it on the shelf unknown, unused, or

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<sup>2</sup> HENRY CHESBROUGH, OPEN BUSINESS MODELS: HOW TO THRIVE IN THE NEW INNOVATION LANDSCAPE 27 (2006) [hereinafter “CHESBROUGH”].

<sup>3</sup> Richard S. Gruner, *Corporate Patents: Optimizing Organizational Responses To Innovation Opportunities and Invention Discoveries*, 10 MARQ. INTELL. PROP. L. REV. 1, 51 (2006).

on reserve for later development into its own products. Exhibit 1, *infra*, represents this strategy in the concept called “Closed Innovation,” a term coined by Henry Chesbrough, a professor in the Management of Technology at UC Berkeley. Closed Innovation is a closed value chain model, as represented by the narrow end of the funnel-shape. The effect is that only selected technologies are developed into products, leaving a number of technologies at the open end of the funnel-shape undeveloped or unused.

This may strike one as a wasteful use of innovation, particularly from a shareholder perspective. Shareholders fund a company’s R&D in order “to produce valuable technologies that can contribute to the company’s success in the market.”<sup>4</sup> Further, concealing promising technology is also detrimental from the point of view of the public good. Concealment is contrary to the rationale governing the patent system, which seeks to avoid such waste by creating an incentive: the benefits of a temporary monopoly power are supposed to encourage the development of technologies and the disclosure of innovations to the public. Yet despite such disincentives, companies continue to conceal promising technology. A case in point, PARC (Palo Alto Research Center), owned by Xerox Corporation in the early 1970s, led to the discovery of a variety of important innovations that are now a critical part of the personal computer including: the graphical user interface, the bit-mapped screen, the Ethernet networking protocol, other higher-speed networking protocols, and numerous other technologies.<sup>5</sup> However, these innovations did not fit into Xerox’s copier and printer businesses, so the company did not develop these technologies nor did it try to capture its value through patents.<sup>6</sup> While the technology was eventually disseminated, its development was delayed and Xerox did not reap the benefits. There was loss both to the public in the delay of the technology being developed and a loss to Xerox, which invested in the research but was not able to harvest its value.

The opportunity cost for a company doing nothing with promising technology is high. Today many businesses are seeing their R&D expenses grow at a faster rate than their sales rate—this growth in R&D expense is unsustainable.<sup>7</sup> As development costs rise and the

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<sup>4</sup> CHESBROUGH, *supra* note 2, at 6-7.

<sup>5</sup> EVERETT M. ROGERS, *DIFFUSION OF INNOVATIONS* 143-47 (4th ed. 1995).

<sup>6</sup> *Id.*

<sup>7</sup> CHESBROUGH, *supra* note 2, at 13.

length of time products are in the market become shorter, companies are finding it harder to justify investing in R&D.<sup>8</sup> Consequently, companies are finding it difficult to operate under a closed value chain. The resulting paradox is that R&D is essential to a software company in sustaining and growing its competitive advantage, yet the same company finds it increasingly difficult to sustain its current investment in R&D.

### III. *Open Innovation*

Open innovation is the use of purposive inflows and outflows of knowledge to accelerate internal innovation, and expand the markets for external use of innovation, respectively. [This paradigm] assumes that firms can and should use external ideas as well as internal ideas, and internal and external paths to market, as they look to advance their technology.<sup>9</sup>

#### a. *Concept*

As knowledge gets widely disseminated the time to market has reduced. Ideas must be used with alacrity or they will be lost. Such factors create a new logic of innovation, in which the role of R&D extends far beyond the boundaries of the enterprise. Specifically, companies must now harness outside ideas to advance their own businesses while leveraging their internal ideas outside their current operations. That fundamental change offers novel ways to create value.<sup>10</sup>

The logic of an Open Innovation model solves several of the problems associated with the closed value chain model. The basis of Open Innovation is that the innovation process can be used to create value, not only from a company's product line and/or services, but also from outside business opportunities. Simply put, Open Innovation finds new ways to capture value from IP assets developed in heavily invested R&D labs. While the software industry is extremely competitive, it may be worth the risk of exposing a trade secret or licensing a patent to a competitor if the competitor would be willing to pay a license for the technology. Exhibit 3, *infra*, presents a pictorial

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<sup>8</sup> CHESBROUGH, *supra* note 2, at 13.

<sup>9</sup> HENRY CHESBROUGH, OPEN INNOVATION: THE NEW IMPERATIVE FOR CREATING AND PROFITING FROM TECHNOLOGY 177 (2003) [hereinafter "OPEN INNOVATION"].

<sup>10</sup> CHESBROUGH, *supra* note 2, at 6

representation of Open Innovation in which technologies may be in-sourced and/or outsourced through the company's value chain.

Open Innovation envisions a new role for a company's IP manager who is not only the protector of the company's IP, but also the strategist responsible for determining how the IP can expand the company's business opportunities. This may entail looking to using key assets, resources, or positions not only within the company, but also in other companies' businesses. It marks a shift from thinking of IP not as merely a legal device to protect intangible assets, but also as a business asset. The typical model of Open Innovation involves active creation of intellectual property along with active licensing of the property. When implementing this model, organizations can find new competitive advantages by in-sourcing or outsourcing IP.

The concept of Open Innovation is illustrated in Exhibit 4, *infra*, entitled Open Value Chain: Multiple Paths to Market. Open Innovation directly contrasts the closed value chain discussed earlier, where a company may have a valuable IP asset that never gets used because a company believes the only way to access IP is from within its own firm, and the only way to deploy IP is through its own products.

The Open Innovation model presents new challenges. First, is determining how to capture value by transferring the IP. Second is finding a suitable partner through whom a shelved technology can be utilized. Third is determining how to appropriate the ideas and technology stemming from R&D. Fourth is overcoming the transaction cost due to the lack of an efficient intermediate market to transfer the technology. Transaction costs may be a significant reason companies do not open up technologies for licensing; namely, because the costs are too high or uncertain, and the potential value is too hard to estimate. Therefore, rather than committing resources to these transactional costs, a company may choose to leave the innovation and IP to sit on the shelf unused. It is also often the case that information needed to efficiently transact with one another is unavailable, or the information is costly to obtain. Consequently, much of the exchange of technology and its associated IP occur between "a cottage industry of brokers and patent attorneys."<sup>11</sup> These challenges have been at least partially addressed by Microsoft IP Ventures' business model.

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<sup>11</sup> CHESBROUGH, *supra* note 2, at 6.

b. Common models of IP monetization

While Open Innovation is a new concept, general IP Monetization is not. It has been done before and garnered some impressive value for the companies who have employed it. However, IP monetization without using Open Innovation leaves value uncaptured for both the company and society as a whole.

i. IBM

Traditional Licensing – IBM is known for its success in licensing its IP - it brings in close to a \$1 billion annually. IBM recognized the bargaining value of a robust portfolio, as well as the leverage such a portfolio could provide, when seeking to compel licensing agreements from potential infringers. Its licensing strategy is based on “substantially increasing efforts to exploit the company's intellectual property assets, mandating a narrower focus on less theoretical and more product-oriented research, and slashing the R&D budget, while simultaneously initiating a campaign to increase the number of patents the company received.”<sup>12</sup> IBM secures many of its licenses through the threat of litigation.<sup>13</sup> Its strategy is not necessarily helping a company develop new technology; rather it is to collect royalties from a company that has already developed a feature that overlaps with one of IBM's patents.

ii. Texas Instruments

Licensing After the Fact – Texas Instruments (“TI”) was in the practice of acquiring patents to ensure that they themselves did not face infringement issues. After the creation of the Court of Appeals for the Federal Circuit, patents were easier to enforce and penalties assessed were larger. At this point, the TI management team realized that they had a large number of patents that gave them protection over some ideas other companies were utilizing. TI decided that they were entitled to some of this value and began a process to “extract fair value” from the money they spent developing or acquiring the IP by licensing it to the companies who were using it. This became quite

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<sup>12</sup> Gideon Parchomovsky & R. Polk Wagner, *Patent Portfolios*, 154 U. PA. L. REV. 1, 46-49 (2004).

<sup>13</sup> See generally Gary L. Reback, *Patently Absurd*, FORBES.COM, June 24, 2002, <http://www.forbes.com/asap/2002/0624/044.html>.

successful and TI became an example of successful monetization of IP.<sup>14</sup>

#### IV. *Microsoft Background*

Until recently, Microsoft managed its IP as a peripheral activity to its business development. The primary job in IP management was to keep the company out of legal trouble. That was prior to 2003. Microsoft's management of IP dramatically shifted in 2003 when they convinced IBM's Marshall Phelps to come out of retirement. Phelps brought to Microsoft a new type of IP management, including an aggressive patent strategy, which appropriated value from considerable R&D investments and implemented new ideas on how to innovate the value chain with respect to Microsoft's IP.

Microsoft has shifted the way it thinks about the innovations coming from its R&D lab. Not only is Microsoft more aggressive in capturing the value from its research through patents, it also has innovated the way it captures value by using patents and the underlying technology as venture capital in emerging companies. Microsoft's investment in developing its patent portfolio is a relatively recent trend. Exhibit 5, *infra*, indicates the number of patents Microsoft publishes by year, up through 2005. For the last two years in which the data was collected, 50% of all Microsoft patents were published. The dramatic rise in patents published corresponds to the year in which Microsoft hired Phelps.

In 2003, Microsoft established Microsoft IP Ventures. This new division is dedicated to managing Microsoft's R&D and finding suitable investment partners.<sup>15</sup> By leveraging its existing network, Microsoft is well equipped to find companies who could successfully commercialize its technology.<sup>16</sup> These innovations to Microsoft's organization enabled Microsoft to further capture the value of its IP. Exhibit 6, *infra*, shows the Innovation Radar as developed by Dr. Robert Wolcott, Inigo Arroniz, and Mohanbir Sawhney of Northwestern University's Kellogg School of Management. It

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<sup>14</sup> Pamela Banner Krupka, *Patents in the Financial Services Industry: What You Need to Know: Patent Licensing as a Source of Revenue*, 830 PLI/PAT 235, 240 (Oct. 2004).

<sup>15</sup> Telephone Interview with David Harnett, Senior Director of IP Ventures, Microsoft, in Redmond, WA. (Feb. 22, 2007).

<sup>16</sup> *Id.*

provides a way to visualize the different dimensions in which Microsoft has invigorated its IP management since the arrival of Phelps. Microsoft increased its value capture by morphing its patenting strategy, creating Microsoft IP Ventures, and increasing its network by tapping Microsoft's vast network. Each of these developments are discussed below.

## V. *Microsoft IP Ventures*

### a. *Origins*

Microsoft IP Ventures licenses Microsoft Research technology to entrepreneurs and start-up companies in order to foster innovation and new product development. IP Ventures also fosters the relationships of Microsoft IP licensees and corresponding product groups, marketing teams, etc. Marshall Phelps created the group. Phelps was instrumental in developing IBM's standards, telecommunications policy, industry relations, patent licensing program and intellectual property portfolio development. His success is illustrated by IBM's current IP licensing program that generates over \$1 billion in revenue annually.

David Harnett, formerly of Microsoft's Corporate Strategy Group, currently leads IP Ventures. Today, IP Ventures consists of three people with business backgrounds and three people with technical backgrounds. The IP Ventures group works closely with Microsoft research and product groups to identify technologies/inventions that can be monetized.

### b. *Microsoft Research*

*"We're focusing more on research than ever. We're building the technology that will enable computers to see, listen, speak, and learn so people can interact with them as naturally as they interact with other people."*

- Bill Gates, Microsoft chairman and chief software architect<sup>17</sup>

*"Our researchers are here to push ahead the state of the art in computer science. When we have great ideas that work, we strive to move those ideas and*

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<sup>17</sup> About Microsoft Research, Microsoft, <http://research.microsoft.com/aboutmsr/overview/default.aspx>.

*technologies into Microsoft products as rapidly as possible.”*

- Rick Rashid, Senior Vice President, Microsoft Research<sup>18</sup>

No discussion on Microsoft IP Ventures is complete without a discussion about the R&D expenditure at Microsoft and Microsoft Research. Microsoft spent \$6.8 billion on R&D in fiscal year 2004. It is roughly equal to the annual R&D budgets of Oracle, Hewlett-Packard, Dell, Apple, and Sun Microsystems combined. Only IBM, with a budget of \$5 billion, even comes close.<sup>19</sup>

In 1991, Microsoft Corporation became the first software company to create its own computer-science research organization. Microsoft Research is a unique entity among corporate research labs, balancing an open academic model with an effective process for transferring its research to product-development teams. "The reason we have Microsoft Research is so Microsoft will still be here 10 or 15 years from now," said Rick Rashid, the senior vice president who heads Microsoft Research.<sup>20</sup> Microsoft Research today has five labs worldwide – two in the US, one in Europe and two in Asia (*see*, Exhibit 7, *infra*).

While Microsoft Research's annual budget is relatively small, comprising \$250 million of the \$6.8 billion that the company spends on R&D, there are about 700 researchers working exclusively for Microsoft Research, which is two-and-a-half times the size of Xerox Corporation's famed Palo Alto Research Center. Twelve of Microsoft Research's researchers have been inducted into the National Academy of Engineering. Two have won the Draper Prize; three more have won the A.M. Turing Award for computer science.

In the five years leading up to 2004, Microsoft has acquired 2,188 patents to protect its researchers' work. Patent Ratings LLC (now a part of OceanTomo) evaluates patents on three main criteria: the number of unique technology claims, probable revenue and profits,

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<sup>18</sup> Microsoft Research Tech Transfers: Better Decisions Faster, Microsoft, Oct. 31, 2005, <http://www.microsoft.com/presspass/features/2005/oct05/10-31TechTransfer.mspx>.

<sup>19</sup> Carleen Hawn, *What Money Can't Buy*, Dec. 2004, <http://www.fastcompany.com/magazine/89/Microsoft.html> [hereinafter "Hawn"].

<sup>20</sup> Benjamin J. Romano, *Microsoft Research: 15 Years of Ideas*, THE SEATTLE TIMES, Sept. 27, 2006, available at [http://seattletimes.nwsourc.com/html/business/technology/2003277256\\_msftresearch27.html](http://seattletimes.nwsourc.com/html/business/technology/2003277256_msftresearch27.html).

and the likelihood that they can be defended. Patent Ratings gives Microsoft's average patent an "intellectual property quotient," or IPQ, of 123, well above the average rating. As software patents are harder to acquire, and consequently harder to defend, than hardware patents, it is especially impressive that Microsoft's average IPQ score is higher than those of hardware makers IBM and Hewlett-Packard – the two most prolific patent claimants in technology. Patent Ratings also estimates that of those 2,188 patents, 75% are original, as opposed to continuing patents. In the past decade, Microsoft was issued proportionally more original patents than either Intel (71%) or Apple (68%).<sup>21</sup>

The open academic model of Microsoft Research means that researchers are more or less free to pursue topics that are of interest to them rather than topics that are a great fit to Microsoft's product roadmap. This freedom allows Microsoft Research to hire and retain the best and the brightest. However, there is always pressure to make the research "relevant" by contributing to the company's product line or bottom line. This is where Microsoft IP Ventures can help. Each of the Microsoft Research labs has an identified point of contact within Microsoft IP Ventures. These contacts work closely with their contact at IP Ventures to identify the IP which can move from research labs to monetization. One significant change since Marshall Phelps started at Microsoft is the focus on patenting all the technology being generated from Microsoft Research.

c. *Open Innovation at Microsoft IP Ventures*

As illustrated in Exhibit 8, *infra*, licensing and cross-licensing provide the basis for Open Innovation. Microsoft IP Ventures attempts to monetize its IP using two different models of Open Innovation. The first model utilizes the traditional licensing and cross-licensing opportunities. The traditional method of licensing results in cash payments based on upfront sums, royalties, or continuing payments, while cross-licensing usually results in an exchange of IP between two separate firms. IBM represents the most successful implementation of traditional licensing and cross-licensing, with revenues over \$1 billion per fiscal year from licensing and cross-licensing alone.<sup>22</sup> In this model Microsoft will seek out existing technology firms using or intending to use Microsoft's IP.

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<sup>21</sup> Hawn, *supra* note 19.

<sup>22</sup> See Kevin G. Rivette & David Kline, *Discovering New Value in Intellectual Property*, HARV. BUS. REV., Jan.-Feb. 2000, at 3-4.

The second and most intriguing aspect of Microsoft IP Venture's Open Innovation model is the use of IP as venture capital. Typically, venture capital is defined as providing private start-up entities with cash in return for equity in that company.<sup>23</sup> This opportunity exists because the entrepreneur needs cash to operate his potentially high growth business,<sup>24</sup> while the cash-heavy venture capital firm wants to show its investors a high rate of return.<sup>25</sup>

However, there are other forms of capital that entrepreneurs need. Entrepreneurs need human capital,<sup>26</sup> business acumen,<sup>27</sup> and intellectual property.<sup>28</sup> Microsoft is a company rich in human capital, business acumen, and intellectual property. However, as the current stock price over the past several years suggests, Microsoft's growth prospects are not what they once were.<sup>29</sup> Exchanging intellectual capital for an equity position in a high growth potential business will increase Microsoft's growth potential while providing the entrepreneur with much needed resources.

Microsoft IP Ventures seeks to capitalize on this opportunity by licensing its IP in exchange for an equity stake in a potentially high

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<sup>23</sup> Curtis J. Milhaupt, *The Market for Innovation in the United States and Japan: Venture Capital and the Comparative Corporate Governance Debate*, 91 NW. U.L. REV. 865, 876 (1997) (citing William A. Sahlman, *Insights from the Venture Capital Model of Project Governance*, 29 BUS. ECON. 35, 35 (1994)) [hereinafter "Milhaupt"].

<sup>24</sup> *Id.* at 887 ("[t]he entrepreneur-managers receive a critically important infusion of capital.").

<sup>25</sup> *Id.* at 892-93 (citing J. William Petty et al., *Harvesting the Entrepreneurial Venture: A Time for Creating Value*, 7 J. APPLIED CORPORATE FIN. 48, 56 (1994)) ("Venture capitalists in the United States seek to invest in projects with an expected rate of return of 30% to 50% per year.").

<sup>26</sup> See Hayden R. Brainard, *Survey and Study of Technology Development and Transfer Needs in New York*, 9 ALB. L.J. SCI. AND TECH. 423, 426 (citing Stuart P. Meyer, *Exploiting Intellectual Property Assets Through Licensing: Strategic Considerations*, 468 PLI/PAT 29, 60 (1997) (outlining the disparity in resources that start-up companies, as compared with established firms, can dedicate to an intellectual property strategy)).

<sup>27</sup> See *id.*

<sup>28</sup> See *id.* (citing ALAN S. GUTTERMAN, *TECHNOLOGY-DRIVEN CORPORATE ALLIANCES: A LEGAL GUIDE FOR EXECUTIVES* 1 (1994)).

<sup>29</sup> Microsoft's stock price for the past 10 years: once a high growth company, growth has trailed off in recent years. See MSFT NASDAQ Quotes, NASDAQ, <http://quotes.nasdaq.com/quote.dll?page=charting&mode=basics&intraday=off&timeframe=10y&charttype=ohlc&splits=off&earnings=off&movingaverage=None&lowerstudy=volume&comparison=off&index=&drilldown=off&symbol=MSFT&selectd=MSFT> (last visited Mar. 6, 2007).

growth start-up company. The license will be a “field of use” exclusive license, essentially restricting Microsoft from licensing this IP to other companies within the same field or market as the licensee. Additionally, this company can leverage Microsoft’s human capital and business acumen by connecting frequently with product teams and departments within Microsoft. In fact, as part of the agreement, the start-up company will receive training, documentation, and access to researchers and developers. However, the start-up’s control of the IP has its limits. Microsoft IP Ventures often times will set goals and milestones the start-up must reach, or else the start-up risks losing the “field of use” exclusivity of the IP. In all cases, Microsoft always retains the right to use its own IP.

Microsoft IP Ventures will only seek an equity position in two instances, as tracked in the flowchart, Exhibit 9, *infra*. In the first instance, Microsoft IP Ventures will approach an existing and financed start-up company which has the expertise to build or use a particular Microsoft IP. It is important to note that Microsoft IP Ventures is not seeking companies who are competitors of Microsoft; specifically, Microsoft IP Ventures seeks companies which build or seek to build products on Microsoft’s platforms (i.e. Windows, Office, etc.). To identify these companies, Microsoft IP Ventures will do typical market research analysis, similar to what venture capitalists do to identify potential investments. Indeed, Microsoft IP Ventures will be able to utilize its network of venture capitalists and government-sponsored economic development agencies.

After the entity is identified, Microsoft IP Ventures must determine if the IP provides a basis for a new product within this company. Only then will Microsoft seek an equity stake in that company. In these cases, Microsoft does not seek a right of first refusal if there is a company buy-out offer. This is because a “right of first refusal” clause will make a purchase of the company more difficult, and thus conflict with the interests of the venture capitalists or financiers of the company.

On the other hand, if the IP simply provides an add-on or enhancement to an already existing product within the start-up entity, Microsoft will only seek licensing fees in the form of up front cash payments and royalties. In both cases, Microsoft will present a “package” deal that includes source code, training, and documentation.

If Microsoft IP Ventures is unsuccessful in discovering an already existing high growth potential start-up company, Microsoft IP Ventures may seek out an entrepreneur to start a wholly new entity. In order to find the appropriate entrepreneur to start this venture, Microsoft IP Ventures will turn to its vast network of venture capitalists. After a suitable entrepreneur is found, Microsoft IP

Ventures will present an equity arrangement similar to the equity arrangement presented above.<sup>30</sup>

However, it is important to note that this business model – exchanging IP for an equity stake in a potentially high growth start-up company – does not represent the full extent of our comparison between intellectual property and venture capital. In fact, from the limited information we were able to gather in our interviews with Microsoft IP Ventures,<sup>31</sup> we noticed some striking similarities, but also notable differences in contract formation.

As pointed out by Ronald Gilson in *Engineering a Venture Capital Market: Lessons from the American Experience*, “all contracts respond to three central problems: uncertainty, information asymmetry, and opportunism in the form of agency costs. The special character of venture capital contracting is shaped by the fact that investing in early stage, high technology companies presents these problems in an extreme form.”<sup>32</sup> To combat these problems, venture capital firms implement several interesting provisions. One is staged financing, which gives the venture capitalist the option to abandon the contractual relationship if the company is not performing up to expectations.<sup>33</sup> The second is giving the venture capitalist disproportionately more control than equity.<sup>34</sup> The third directs the compensation of the entrepreneur to be based upon “high-powered performance incentives that serve to align the incentives of the [start-up] and the venture capital fund.”<sup>35</sup> The fourth contractual provision will return control to the entrepreneur if the start-up is successful.<sup>36</sup>

Microsoft IP Ventures mirrors a venture capitalist contract by implementing a form of staged financing, setting milestones and goals for the start-up to reach. If the start-up fails to satisfactorily reach these goals or milestones, Microsoft has a right to rescind the “field of use” exclusive license. This is an important provision for both

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<sup>30</sup> Microsoft will seek an equity stake in the entity, will grant a “field of use” exclusive license to entity, right to market its partnership with Microsoft, access to source code and Microsoft researchers, developers, and other resources.

<sup>31</sup> Of course there were important contractual provisions Microsoft IP Ventures would not disclose. Nonetheless, there was enough information to form the basis of our conclusion.

<sup>32</sup> Ronald J. Gilson, *Engineering a Venture Capital Market: Lessons from the American Experience*, 55 STAN. L. REV. 1067, 1076 (2003).

<sup>33</sup> *Id.* at 1078.

<sup>34</sup> *Id.* at 1082.

<sup>35</sup> *Id.* at 1083.

<sup>36</sup> *Id.* at 1084.

traditional venture capitalists and Microsoft IP Ventures to hedge against this risky endeavor.<sup>37</sup> It is important to both Microsoft and a traditional venture capitalist to have an exit option if the start-up is not performing to expectations, thereby not tying up the cash or intellectual property in one entity.

One notable difference in the structure of the deal is in the amount of control a typical venture capitalist seeks in the start-up as opposed to the amount of control Microsoft IP Ventures seeks in the start-up. As noted above, a typical venture capitalist seeks a disproportionate amount of control-to-equity in the start-up entity.<sup>38</sup> Although Microsoft IP Ventures obtains an equity position and sits on the board of directors of the start-up, similar to a typical venture capitalist, it does not seek much control in the day-to-day business operations or overall strategy. A typical venture capitalist, on the other hand, seeks and needs this control to manage the uncertainty of the venture.<sup>39</sup> The venture capitalist is keen on knowing the exit strategy of the firm and managing it to realize returns on the investment. Microsoft IP Ventures does not treat exit strategy at the same level of importance as the venture capitalists. It takes non-voting seats on the board and leaves exit strategy decisions to management and other investors.

Of course the differences in investment mechanisms, intellectual property versus cash, drive this difference. Since Microsoft IP Ventures does not provide any cash for the start-up entity, the expectation is that the start-up will obtain its own financing or has already obtained financing through a typical venture capitalist. If Microsoft sought to obtain as much control as a typical venture capitalist in the start-up, it would be difficult for the start-up to obtain cash financing via a typical venture capitalist, as these entities require a significant amount of control. Accordingly, if a sizeable portion of control in the start-up has already been ceded to Microsoft IP Ventures, the venture capitalist may not be left with the amount of control it requires in exchange for the cash financing. This dynamic ostensibly drives Microsoft IP Venture's decision to not seek much control of the start-up entity.

Finally, the differences in the expectations of the investors help understand why this difference exists. While investors in a typical venture capital firm expect a high rate of return on their investments,<sup>40</sup>

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<sup>37</sup> *Id.* at 1079.

<sup>38</sup> *Id.* at 1082.

<sup>39</sup> *Id.*

<sup>40</sup> Milhaupt, *supra* note 23, at 892-93 (citing J. William Petty et al., *Harvesting the Entrepreneurial Venture: A Time for Creating Value*, 7 J. APPLIED CORPORATE FIN.

Microsoft's expectations for return on the intellectual property are less lofty.

The following section discusses three examples illustrating Microsoft IP Venture's business model.

## VI. *Case Studies*

### a. *Skinkers – Partnering with an Established Company*

Skinkers is a United Kingdom based company with a mission to produce market leading direct-to-desktop event notification and content delivery technology. Skinkers was founded in 2001 with the idea of delivering high value, one-to-many communications to the business desktop. The next step of their product evolution was to develop a push technology that is compatible with different platforms, such as handheld devices and cell phones. Skinkers also wanted to add internet-based real-time event notification and the ability to push large amounts of content over the web.<sup>41</sup> The Skinkers product also adds value to content delivery by decentralizing content locations. This allows other Skinkers clients to have access to a file without downloading it from the main source, reducing download time and network traffic.<sup>42</sup>

In 2006, a venture capital firm introduced Skinkers to the idea of working with Microsoft to help reach their vision. Microsoft Research labs developed a technology that would assist Skinkers in their multiplatform goal. Microsoft IP Ventures and Skinkers were able to negotiate an "equity for IP" deal that allowed Skinkers a "field of use" exclusive license for the necessary Microsoft technology in exchange for a 10% equity stake in their company.<sup>43</sup>

To those familiar with Microsoft product offerings, this deal may not make sense because Microsoft offers MS Communicator, a product with similar features to Skinkers' offerings. Upon further investigation, however, MS Communicator is based on one-to-one

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48, 56 (1994)) ("Venture capitalists in the United States seek to invest in projects with an expected rate of return of 30% to 50% per year.").

<sup>41</sup> Posting of David Rowe to Microsoft Startup Zone Blogs, <http://microsoftstartupzone.com/Blogs.aspx> (Jan. 4, 2007, 18:46 GMT).

<sup>42</sup> Dan Matthews, *Real Money: Skinkers*, REAL BUSINESS (U.K.), Aug. 30, 2007, available at <http://realbusiness.co.uk/archive/4777416/real-money-skinkers-.thtml>.

<sup>43</sup> Telephone Interview with Andy Kelly, Former Microsoft IP Ventures Executive, at Northwestern University School of Law (Jan. 29, 2007).

communication while Skinkers is interested in one-to-many communication. This difference allows the two products to act as compliments, rather than substitutes.

Beyond the superficial terms of the deal, this partnership created additional value. Skinkers is able to access Microsoft's vast business and technical resources. Microsoft placed a senior executive on Skinkers's Board of Directors, as a non-voting member, to advise the company on strategy and market direction. Microsoft also benefited because they were able to get positive press in the European Union. Since the technology was developed in the U.K. offices of Microsoft Research, the European Union was happy to know that Microsoft kept intellectual capital developed in Europe in a European company.<sup>44</sup>

*b. Wallop: Using IP to Found a New Company*

Social networking is quickly becoming a popular offering on the web. Wallop was formed to take social networking to the next generation by solving some of the problems that plague current networking sites. Their goal is to completely revamp the user experience to allow users to connect with people of their choosing, instead of the "friend of a friend" model current sites employ.<sup>45</sup>

Wallop offers three main features. First, the on-line experience is by invitation only, so the user can limit others from connecting with him or her. Second, it offers a great deal of customizability and multimedia content management without the need for any scripting or coding. Third, users can purchase or create "mods," which are Flash Player movies to add to their site to further express themselves.<sup>46</sup>

These technologies were developed in the Microsoft Research facilities and then spun off by Microsoft IP Ventures. This case is different than Skinkers' because in this case Microsoft IP Ventures decided to establish a wholly new corporation, Wallop, and join-in as a partner. Microsoft IP Ventures tapped veteran entrepreneur Karl Jacob to raise the capital and start the company. Jacob had a long history of raising venture capital and advancing businesses from start-up to profitability or acquisition.<sup>47</sup> Microsoft IP Ventures acquired an

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<sup>44</sup> European Businesses Strengthened by Microsoft Technology, June 5, 2006, <http://www.microsoft.com/presspass/press/2006/jun06/06-05EuropeBusinessTechPR.mspx>.

<sup>45</sup> Microsoft Spins out a Wallop, Apr. 25, 2006, <http://www.microsoft.com/presspass/press/2006/apr06/04-25WallopPR.mspx>.

<sup>46</sup> Wallop, Modders, <http://www.wallopcorp.com/modders.html>. (last visited Apr. 2, 2008).

<sup>47</sup> Wallop, About, <http://www.wallopcorp.com/about.html> (last visited Apr. 2, 2008).

equity stake in the company, while Wallop received the code, the patents and access to the researcher who developed the technology.<sup>48</sup>

c. *SoftEdge – Licensed Based Partnership*

Based out of Ireland, SoftEdge is a company that specializes in e-enablement and multimedia document generation. Unfortunately for SoftEdge, the field of e-enablement and multimedia document generation is a crowded market space.

In May of 2005, Microsoft IP Ventures approached Enterprise Ireland, a government office that provides funding and assistance to Irish start-up companies. Microsoft IP Ventures was seeking to license imaging technology called Interactive Image Cutout developed at Microsoft Research labs in China.<sup>49</sup> Enterprise Ireland introduced them to an existing company, SoftEdge. SoftEdge welcomed the partnership with Microsoft, as they were seeking a way to differentiate themselves from the other multimedia companies.

This case is different from both Skinkers' and Wallop's. SoftEdge was an existing company and did not need a fundamental technology to build their product around. Instead, SoftEdge only needed an add-on or enhancement to their current product offerings to make them more competitive. As a result, the structure of the deal with SoftEdge was different. Microsoft offered a "field of use" exclusive license of the Interactive Image Cutout technology in exchange for an up front payment and a royalty based on a percentage of the net sales of their product.<sup>50</sup> SoftEdge was also given the application with a fully developed API, which they could use with their product, as well as source code and training resources. SoftEdge also benefited because it was able to access early releases of Microsoft Products and was invited to become a launch partner for Vista and Office 2007. Microsoft benefited because SoftEdge provided valuable feedback and free quality assurance testing for the new version of Microsoft Word.<sup>51</sup>

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<sup>48</sup> Telephone Interview with Andy Kelly, *supra* note 43.

<sup>49</sup> Telephone Interview with Vikas Sahni, CEO Softedge Systems, in Dublin, Ireland. (Feb. 21, 2007).

<sup>50</sup> Telephone Interview with David Harnett, *supra* note 15.

<sup>51</sup> Telephone Interview with David Harnett, *supra* note 15.

### *VII. Opportunities, Challenges, and Improvements*

In contrast to the method employed by Microsoft IP Ventures to monetize its IP, is the method used by “IP investment banks.” The Microsoft IP Ventures model of IP monetization has some advantages over typical IP licensing/auctions schemes offered by IP investment banks. The biggest advantage is that Microsoft is able to monetize technologies that cannot be readily packaged and sold or licensed to another party. The licensee/partner is advantaged in IP Ventures’ model by not only getting early access to innovative technologies, but also receiving assistance from Microsoft Research teams and various groups at Microsoft to aid in getting the technology to market. Unlike the typical investment bank deals, which are typically purely transactional, IP Ventures’ partnerships are relationship oriented. Furthermore, unlike the typical investment bank, IP Ventures has more knowledge of the IP and greater interest in the success of the IP. On the other hand, some companies may view IP Ventures as a potential competitor, and as a result may be reluctant to work with it as compared to an IP investment bank.

There is very little risk incurred by Microsoft in entering these licensing or partnership deals. Microsoft has very little financial commitment to the partner or licensee, and it has a moderate amount of resource commitment. However, despite the low levels of investment from Microsoft, there is a significant amount of financial upside should the licensee or partner’s product become commercially viable. Every deal is an opportunity to commercialize Microsoft’s IP and ultimately add to an ecosystem of companies which are connected to Microsoft. This model also allows Microsoft Research researchers to continue to focus on any area of research, and then actually see it being implemented commercially.

In addition, the partners or licensees tend to use Microsoft’s platform to launch their products. Therefore, in the process of developing the product, the partners will necessarily be testing and providing feedback on core Microsoft products. For example, Skinkers was a Microsoft Vista launch partner and SoftEdge Systems was an Office 2007 launch partner.

The partners will not only have a jumpstart on their competition through the technology license, but they also have the opportunity to reference experienced Microsoft business and technical resources. In partnership deals, Microsoft IP Ventures will have at least one non-voting seat on the board of the company.

Microsoft also generates non-market value, in particular its trademark or brand value. The partnerships enable Microsoft to develop goodwill in the technology start-up community, thus

increasing the probability more start-ups will use Microsoft platforms to develop products. It also creates goodwill with regional economic development agencies. The Skinkers deal is a great example of this. The deal created a good deal of positive press at a time when Microsoft was facing a case brought by the European Union for alleged antitrust abuse.<sup>52</sup>

The key challenge for Microsoft is that its model of IP monetization is not easily scalable from transaction to transaction. Every deal is unique and requires a fair amount of due diligence and time commitment upfront.

To improve Microsoft IP Venture's current business model, we believe that Microsoft can proliferate its brand by creating a specific logo program for all products that use IP licensed from Microsoft. In an interview with Vikas Sahni, CEO of SoftEdge Systems, he indicated a program similar to "Intel Inside" would be very valuable for his product, an add-on feature to Microsoft Word. However, Microsoft IP Ventures did not feel the need for a separate logo program. David Harnett of IP Ventures felt that existing product logo certification programs were sufficient.<sup>53</sup> He felt that having a separate logo program may create confusion in the minds of end consumers as to whose product it is. Furthermore, being that Microsoft does not retain express control in the start-up, it would not be able to regulate the quality of the product being released. Despite this, we believe there is an overall positive value in a separate logo program, such as "Powered by Microsoft Research." For a company like SoftEdge Systems, this logo program will offer additional differentiation for its product helping its product in the marketplace, while Microsoft can increase customer mindshare regarding innovation and strengthen its brand.

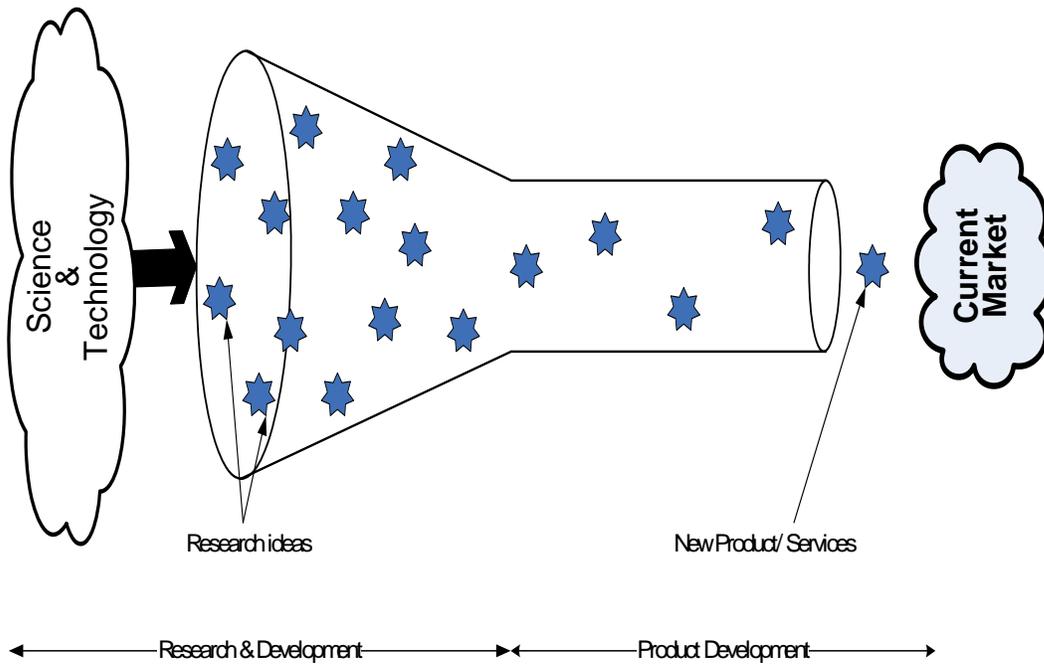
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<sup>52</sup> Telephone Interview with Andy Kelly, *supra* note 43.

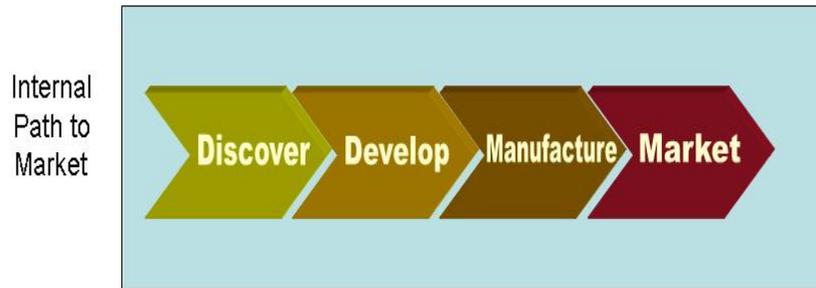
<sup>53</sup> Telephone Interview with David Harnett, *supra* note 15.

**Exhibit 1: Closed Innovation**

Closed Innovation

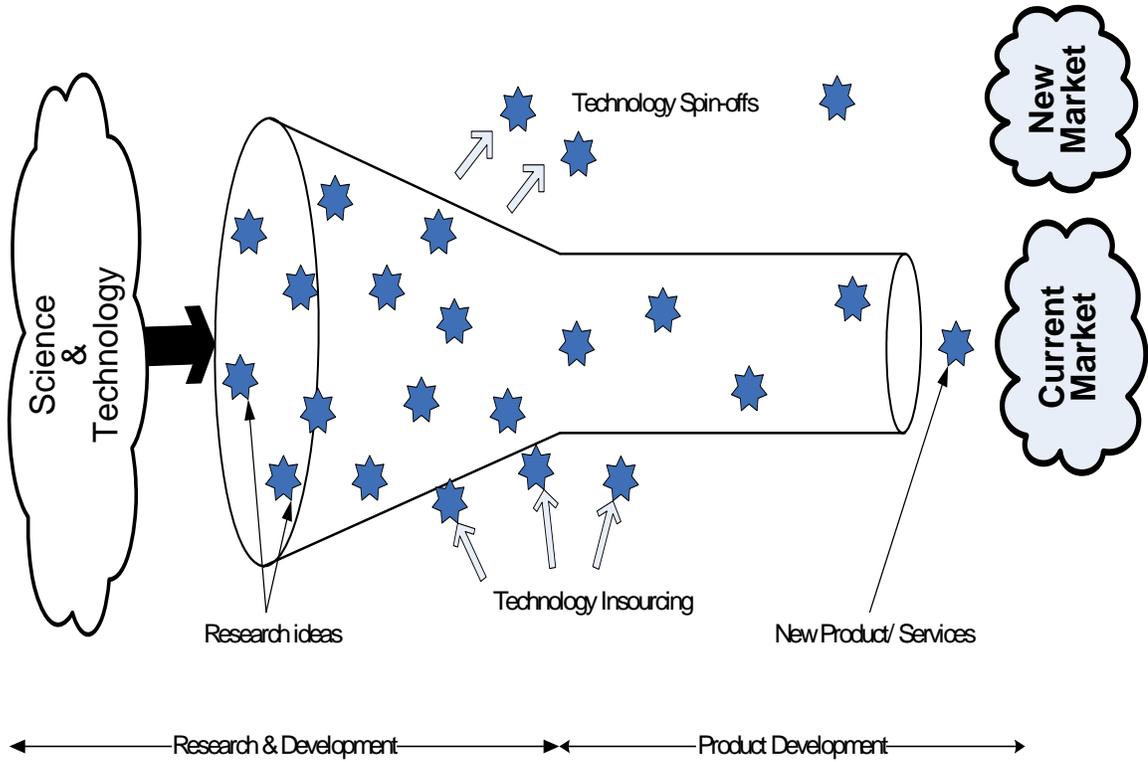


**Exhibit 2: Closed Value Chain: Internal Path to Market**

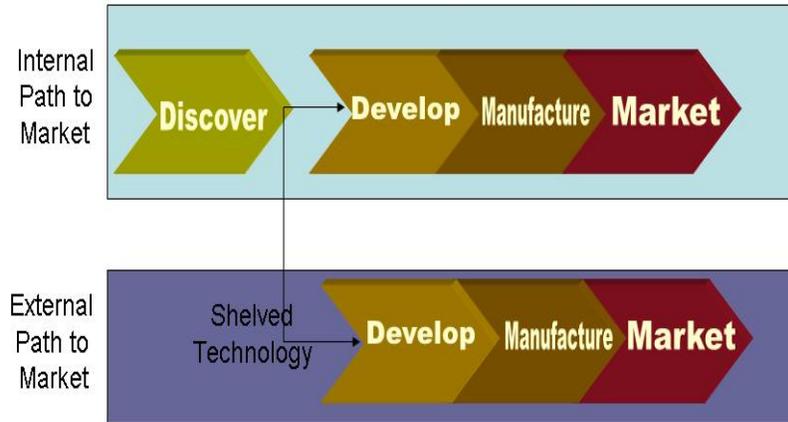


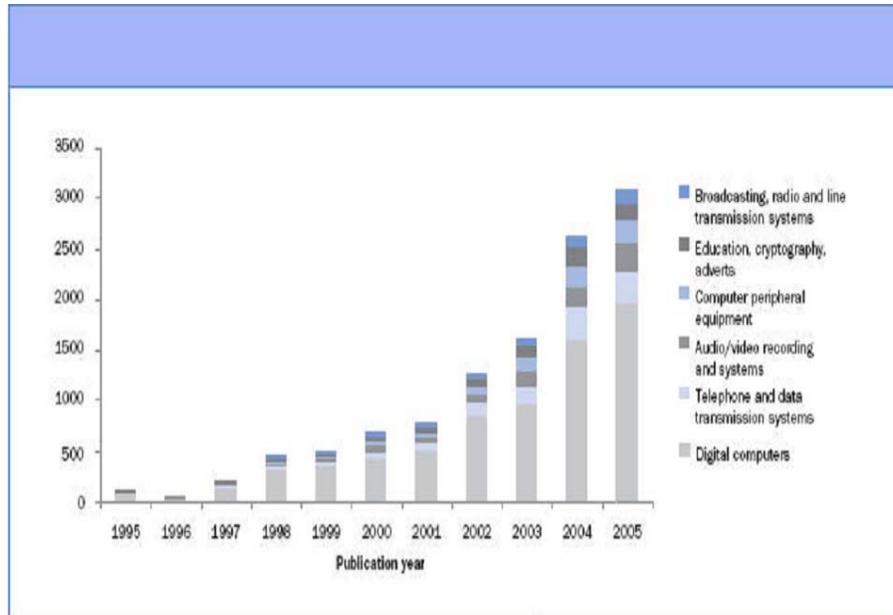
**Exhibit 3: Open Innovation**

# Open Innovation



**Exhibit 4: Open Value Chain: Multiple Paths to Market**



**Exhibit 5: Microsoft Number of Published Patents**

54

<sup>54</sup> Bob Stembridge, Back to the future: tacking patents to see where the path leads, [http://www.buildingipvalue.com/06intro/013\\_017.htm](http://www.buildingipvalue.com/06intro/013_017.htm).

**Exhibit 6: Microsoft IP Ventures on the Innovation Radar**

Innovation  
Radar

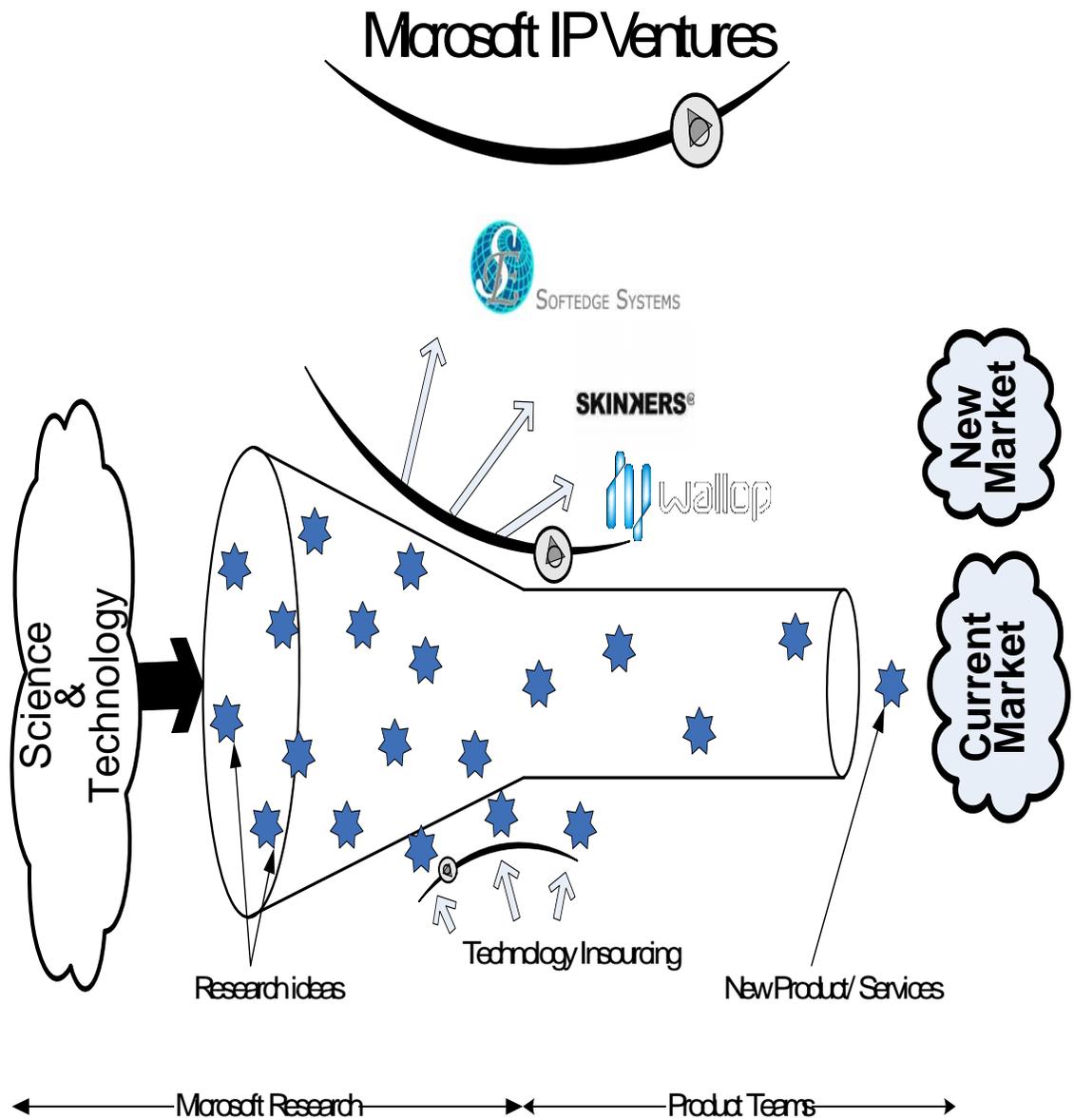


Value Capture – Appropriating research by patenting more  
Organization – IP Ventures, new division to commercialize shelved technology by transferring technology outside the company.  
Networking – Working w/ new State Agencies like Enterprise Ireland and VC's to find emerging companies to partner with  
Brand – Yellow line equals potential, through our suggestion in last section.

**Exhibit 7: Microsoft Research Labs**

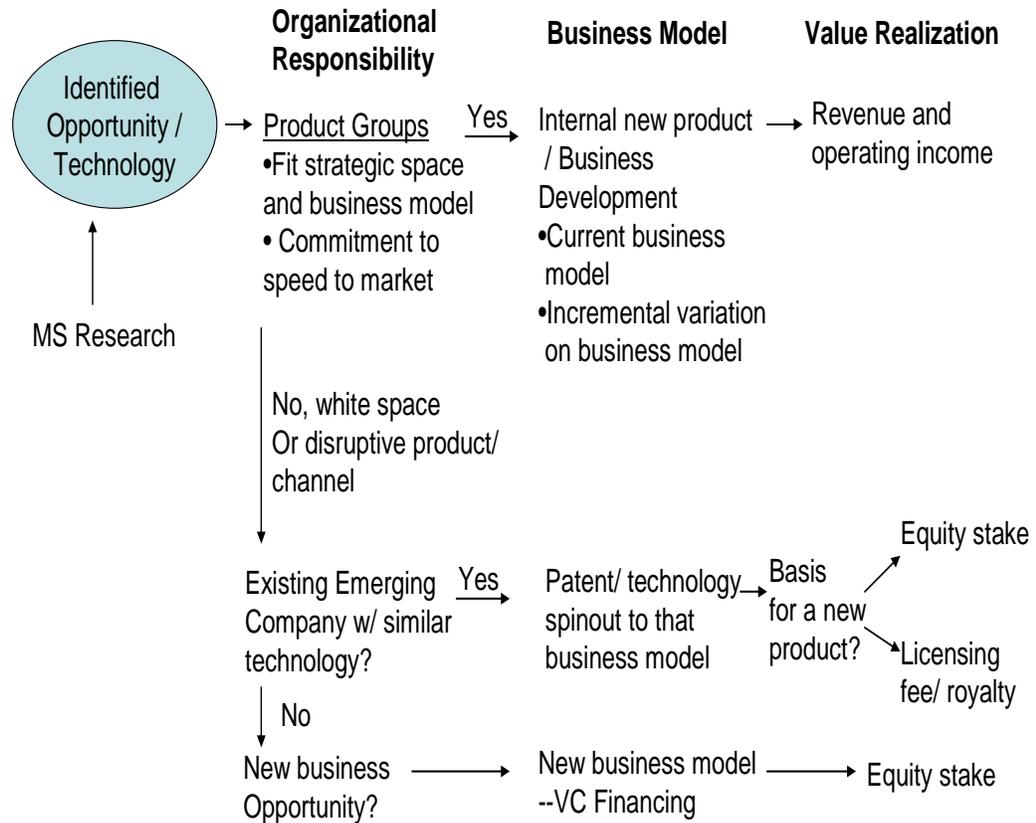


**Exhibit 8: Microsoft IP Ventures Innovation Model**



**Exhibit 9: Value Capture Structures**

**Microsoft's Innovation Model for Commercializing New Technology:  
Value Capture Structures**





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ALL'S FAIR IN LOVE AND NEWS: HOW THE CURRENT  
APPLICATION OF THE FAIR USE DOCTRINE FAVORS THE  
TRADITIONAL MEDIA OVER AMATEUR PROVIDERS OF  
NEWS CONTENT

Collette Leland\*

I. INTRODUCTION

With camera phones in an estimated 106 million purses and pockets in the United States alone,<sup>1</sup> it is no longer unusual for significant events to be documented by the man on the street who happens to be in the right place at the right time. News agencies have come to rely on their presence to provide immediate coverage of disasters, such as the 2004 tsunami in Southeast Asia<sup>2</sup> and the London subway bombings.<sup>3</sup> When cell phone footage of Michael Richards hurling racist epithets at hecklers surfaced on a celebrity news site, it was picked up by traditional news organizations and broadcast on the nightly news.<sup>4</sup> An unknown observer of Saddam Hussein's hanging surreptitiously filmed the event with his camera phone so that he could market the work to Al-Jazeera and Arabiya.<sup>5</sup> On the campus of Virginia Tech, Jamal Albarghouti ran toward the sound of gunfire,

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<sup>1</sup> *Cameraphones Pass 50% Penetration Mark in USA*, CELLULAR NEWS, Apr. 18, 2007, <http://www.cellular-news.com/story/23224.php>.

<sup>2</sup> Yuki Noguchi, *Camera Phones Lend Immediacy to Images of Disaster*, WASH. POST, July 8, 2005, at A16, available at <http://www.washingtonpost.com/wp-dyn/content/article/2005/07/07>.

<sup>3</sup> *Id.*

<sup>4</sup> Andrew Gumbel, *We're All Under the Microscope Now*, THE INDEPENDENT, Dec. 29, 2006, available at 2006 WLNR 22646885.

<sup>5</sup> Terry McCarthy, *New Saddam Hanging Video Reveals Testy Exchange*, ABC NEWS, Dec. 30, 2006, <http://www.abcnews.go.com/print?id=2761888>.

camera phone ready, recording images that were broadcast on CNN the day of the Virginia Tech massacre.<sup>6</sup> Recognizing the value of this new source of content, many news organizations actively solicit amateur photographs and footage of newsworthy events.<sup>7</sup> Reuters media group president, Chris Ahern describes Reuters's new program: "This is looking out and saying, 'What if everybody in the world were my stringers?'"<sup>8</sup>

Because it is unlikely that all uses of amateur footage will be through a licensing agreement, this trend creates a new challenge for courts, as amateurs and professionals are bound to clash with increasing frequency over what is a fair use of this growing source of news content.

Although amateur photographers and videographers are serving the purposes of copyright by creating socially beneficial expression, and often making it accessible to the world at large via the Internet, the trend among lower court opinions on the fair use of images indicates that, where news organizations engage in the unauthorized use of newsworthy amateur images, the use is likely to be considered transformative and fair based solely upon a change in context or purpose.

The Ninth Circuit's recent decision in *Perfect 10, Inc. v. Amazon.com, Inc.*<sup>9</sup> highlights the vulnerability of amateur photographers. There, the court held that Google's use of copyrighted images was transformative because it reproduced the images in a socially beneficial context—moving them from a fee-based pornography site to an Internet search engine.<sup>10</sup> In spite of the lack of any change other than size to the images themselves, the court found the use to be "significantly transformative."<sup>11</sup> In finding the use transformative, the court largely discounted the strength of Perfect

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<sup>6</sup> Ellen Gray, *Cell Phones: Turning Witnesses Into Reporters*, PHILA. DAILY NEWS, Apr. 17, 2007, available at [http://www.philly.com/dailynews/local/20070417\\_Ellen\\_Gray\\_CELL\\_PHONES\\_\\_Turning\\_witnesses\\_into\\_reporters.html](http://www.philly.com/dailynews/local/20070417_Ellen_Gray_CELL_PHONES__Turning_witnesses_into_reporters.html).

<sup>7</sup> Saul Hansell, *Have Camera Phone? Yahoo and Reuters Want You for Their News Service*, N.Y. TIMES, Dec. 4, 2006, available at <http://www.nytimes.com/2006/12/04/technology/04yahoo.html>; David Bauder, *Cell-Phone Cameras Change Face of News*, PITTSBURGH POST-GAZETTE, Jan. 9, 2007, at C4, available at 2007 WLNR 385484; see Reuters.com, You Witness News, Terms of Use, <http://www.reuters.com/youwitnessTerms>; CNN.com, iReport Terms of Use, <http://www.cnn.com/exchange/ireports/toolkit/index.html> (last visited Apr. 3, 2008).

<sup>8</sup> Hansell, *supra* note 7.

<sup>9</sup> 508 F.3d 1146 (9th Cir. 2007).

<sup>10</sup> *Id.* at 1167.

<sup>11</sup> *Id.* at 1166.

10's arguments on the remaining fair use factors, finding the use by Google to be a fair use primarily because it was a *different* use.<sup>12</sup>

*Perfect 10* is typical of the lower courts' movement away from the traditional definition of transformative use as one which furthers the purpose of copyright by adding to and changing the original work with "new expression, meaning, or message,"<sup>13</sup> to a definition based on a change in function which does not require the secondary user to transform the copyrighted expression itself. In many cases, the secondary use serves the same broad purpose as the original, but places the original work in a new context which—particularly in news reporting—the courts view as socially beneficial.<sup>14</sup> This diluted definition of transformation, together with the increasing presumption of fair use where a transformative use is found, frustrates the purpose of copyright by discouraging the creation and dissemination of new works by photographers who are not members of the traditional news media.

The fair use test prescribed by Congress and by the Supreme Court serves the purposes of copyright by recognizing that new works may build on, but not supplant, protected works.<sup>15</sup> When applying the fair use test to the copying of images, lower courts have departed from this test in two ways. First they have made finding a use transformative the "golden ring" which determines the ultimate case outcome.<sup>16</sup> Second, they have diluted the definition of transformation to the point where it requires no transformation at all.<sup>17</sup> These

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<sup>12</sup> *Id.* at 1166-68.

<sup>13</sup> *Campbell v. Acuff-Rose Music, Inc.*, 510 U.S. 569, 579 (1994).

<sup>14</sup> *See Kelly v. Arriba Soft Corp.*, 336 F.3d 811, 820 (9th Cir. 2003); *Perfect 10, Inc. v. Amazon.com, Inc.*, 487 F.3d 701, 723 (9th Cir.) (use of images in search engine is transformative because such use serves a different and socially beneficial purpose), *amended by* 508 F.3d 1146 (9th Cir. 2007); *Mathieson v. Associated Press*, No. 90 Civ. 6945 (LMM), 1992 WL 164447, at \*2-3 (S.D.N.Y. June 25, 1992).

<sup>15</sup> *Harper & Row, Publishers, Inc. v. Nation Enters.*, 471 U.S. 539, 548 (1985); *Campbell*, 510 U.S. at 575-76.

<sup>16</sup> Matthew D. Bunker, *Eroding Fair Use: The "Transformative Use Doctrine" After Campbell*, 7 COMM. L. & POL'Y 1, 15 (2002); Jeremy Kudon, *Form Over Function: Expanding the Transformative Use Test for Fair Use*, 80 B.U. L. REV. 579, 583 (2000); Jisuk Woo, *Redefining the "Transformative Use" of Copyrighted Works: Toward a Fair Use Standard in the Digital Environment*, 27 HASTINGS COMM. & ENT. L.J. 51, 70-71 (2004); Diane Leenheer Zimmerman, *The More Things Change the Less They Seem "Transformed": Some Reflections on Fair Use*, 46 J. COPYRIGHT SOC'Y U.S.A. 251, 260 (1998).

<sup>17</sup> Woo, *supra* note 16, at 65, 68; Paul Goldstein, *Copyright's Commons*, 29 COLUM. J.L. & ARTS 1, 6 (2005).

departures have disadvantaged the creators of copyrighted images to the extent that the incentive to create quality content and make it available to the public is threatened. To reverse this trend, this article advocates that lower courts return to the traditional definition of transformative use and the statutory factor-by-factor analysis. Such a move would continue to allow for uses which truly are fair and reasonable without granting an almost *per se* finding of fair use where the user has copied the original expression of a non-competitor.

## II. THE EVOLVING FAIR USE ANALYSIS

Copyright law is intended to promote the creation of original works of expression by protecting the interests of authors and artists.<sup>18</sup> By granting a limited monopoly to authors, copyright seeks not to benefit the author, but to encourage the creation of new works by providing an incentive for their creation.<sup>19</sup> This constitutional bargain results in a certain tension. Too much protection of an author's exclusive rights would squelch creativity; too little would reduce the incentive to create. Recognizing that new works necessarily build on what has gone before, the doctrine of fair use provides a safety valve, preventing authors from exercising an absolute monopoly over the use of their original expression, but requiring that unauthorized uses be reasonable so that the incentive to create is not significantly reduced.<sup>20</sup> Thus, the fair use defense provides "a necessary counterbalance to the copyright law's goal of protecting the creator's work product."<sup>21</sup>

Under common law, fair use was based on the premise that, by publishing his work, the author granted implied consent for "reasonable use."<sup>22</sup> Because of the impossibility of defining in advance a use that is fair, courts have developed a fact-intensive balancing test focusing on four factors deemed relevant to the determination of whether a secondary use serves the purposes of copyright or merely supersedes the original.<sup>23</sup> Justice Story famously stated these factors in *Folsom v. Marsh* as ". . . the nature and objects of the selections made, the quantity and value of the materials used,

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<sup>18</sup> U.S. CONST. art. I, § 8, cl. 8; *Sony Corp. of Am. v. Universal City Studios, Inc.*, 464 U.S. 417, 429 (1984); *Eldred v. Ashcroft*, 537 U.S. 186, 216 (2002).

<sup>19</sup> U.S. CONST. art. I, § 8, cl. 8; *Twentieth Century Music Corp. v. Aiken*, 422 U.S. 151, 156 (1975).

<sup>20</sup> *Sony*, 464 U.S. at 478-80 (Blackmun, J., dissenting).

<sup>21</sup> *Perfect 10, Inc. v. Amazon.com, Inc.*, 487 F.3d 701, 719 (9th Cir.) (citing *Campbell v. Acuff-Rose Music, Inc.*, 510 U.S. 569, 575 (1994)), *amended by* 508 F.3d 1146 (9th Cir. 2007).

<sup>22</sup> *Harper & Row, Publishers, Inc. v. Nation Enters.*, 471 U.S. 539, 549-50 (1985); S. REP. NO. 102-141, at 3 (1991).

<sup>23</sup> H.R. REP. NO. 94-1476 (1976), *as reprinted in* 1976 U.S.C.C.A.N. 5659.

and the degree to which the use may prejudice the sale, or diminish the profits, or supersede the objects, of the original work.”<sup>24</sup> In 1976, Congress codified the multi-factor common law test in 17 U.S.C. § 107,<sup>25</sup> stating that its intention was to adopt existing case law while allowing courts the freedom to continue to develop the doctrine of fair use on a case by case basis.<sup>26</sup>

In determining whether a use is fair, courts are to examine each factor separately and then to weigh the results in light of the purpose of copyright, namely “to promote the Progress of Science and useful Arts” by ensuring that authors have a limited monopoly on the use of their works.<sup>27</sup> Uses that are fair do not threaten to replace the original, but build upon the original or complement it.<sup>28</sup> The first factor in the four-part analysis—purpose and character of the accused use—

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<sup>24</sup> *Folsom v. Marsh*, 9 F. Cas. 342, 348 (C.C.D. Mass. 1841) (No. 4901).

<sup>25</sup> Notwithstanding the provisions of section 106 and 106A, the fair use of a copyrighted work, including such use by reproduction in copies or phonorecords or by any other means specified by that section, for purposes such as criticism, comment, news reporting, teaching (including multiple copies for classroom use), scholarship, or research, is not an infringement of copyright. In determining whether the use made of a work in any particular case is a fair use the factors to be considered shall include—

- (1) the purpose and character of the use, including whether such use is of a commercial nature or is for nonprofit educational purposes;
- (2) the nature of the copyrighted work;
- (3) the amount and substantiality of the portion used in relation to the copyrighted work as a whole; and
- (4) the effect of the use upon the potential market for or value of the copyrighted work.

The fact that a work is unpublished shall not itself bar a finding of fair use if such finding is made upon consideration of all the above factors.

17 U.S.C. § 107 (2006).

<sup>26</sup> H.R. REP. NO. 94-1476, *supra* note 23, at 66.

<sup>27</sup> U.S. CONST. art. I, § 8, cl. 8.; *Campbell v. Acuff-Rose Music, Inc.*, 510 U.S. 569, 578 (1994); Mitch Tuchman, *Judge Leval’s Transformative Standard: Can it Really Distinguish Foul from Fair?*, 51 J. COPYRIGHT SOC’Y U.S.A. 101, 105-06 (2003).

<sup>28</sup> *See Ty, Inc. v. Publ’ns Int’l, Ltd.*, 292 F.3d 512, 517 (7th Cir. 2002) (“[W]e may say that copying that is complementary to the copyrighted work (in the sense that nails are complements of hammers) is fair use, but copying that is a substitute for the copyrighted work (in the sense that nails are substitutes for pegs or screws), or for derivative works from the copyrighted work, . . . is not fair use.”) (citation omitted).

addresses the creation of new works, while the remaining factors—nature and character of the original work, amount of the original work used, and the effect of the use on the value and potential market for the original—examine the effect on the copyright owner's incentive to create.<sup>29</sup>

A. Factor One: “the purpose and character of the use, including whether such use is of a commercial nature or is for nonprofit educational purposes.”

The goal of the courts in evaluating the purpose and character of the infringing use is to determine whether “the new work merely ‘supersede[s] the objects’ of the original creation,”<sup>30</sup> or whether it promotes the goal of copyright by creating a new work that uses the original only as the raw material for a new work.<sup>31</sup> In other words, is the use justified?<sup>32</sup> Congress suggested some examples of uses that would likely weigh in favor of fair use and directed the courts to also consider whether the use was for commercial or non-profit purposes.<sup>33</sup> In evaluating this factor, courts have also considered public policy, the good faith (or lack thereof) of the user, whether the use was productive, and to what extent the use is transformative.<sup>34</sup> These sub-factors aid the courts in determining whether the use is one which promotes the goal of copyright and should, therefore, be granted the “breathing space” provided by the fair use privilege.<sup>35</sup>

Judge Pierre Leval argued in *Toward a Fair Use Standard* that courts have tended to find uses fair when they were “transformative.”<sup>36</sup> Transformative uses, he explained, were those that did more than repackage the original expression, but had instead used the original work as raw material, “transformed in the creation of new information, new aesthetics, new insights and understandings.”<sup>37</sup> Leval's transformative use concept was discussed in just three Second Circuit opinions following the publication of *Toward a Fair Use*

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<sup>29</sup> Tuchman, *supra* note 27, at 107.

<sup>30</sup> *Campbell*, 510 U.S. at 579.

<sup>31</sup> *Castle Rock Entm't, Inc. v. Carol Publ'g Group, Inc.*, 150 F.3d 132, 141 (2d Cir. 1998).

<sup>32</sup> Pierre N. Leval, *Toward a Fair Use Standard*, 103 HARV. L. REV. 1105, 1111 (1990).

<sup>33</sup> 17 U.S.C. § 107(1) (2006).

<sup>34</sup> *See, e.g., Campbell*, 510 U.S. at 579; *Fitzgerald v. CBS Broad., Inc.*, 491 F. Supp. 2d 177, 184 (D. Mass. 2007).

<sup>35</sup> *Campbell*, 510 U.S. at 579.

<sup>36</sup> Leval, *supra* note 32, at 1111.

<sup>37</sup> *Id.*

*Standard*, one by Judge Leval himself,<sup>38</sup> before it received the apparent endorsement of the Supreme Court in *Campbell v. Acuff-Rose Music*.<sup>39</sup>

A unanimous Court in *Campbell* stated that copyright favors “transformative uses,” suggesting that the more transformative the use, the less significant will be the other fair use factors.<sup>40</sup> The Court concluded that 2 Live Crew’s parody of “Oh, Pretty Woman” was transformative because it used elements of the original work for purposes of commentary and criticism.<sup>41</sup> Rather than making transformative use the sole, or even primary, focus of its analysis, however, the Court went on to examine elements which contributed to making parody a purpose that weighed in favor of fair use,<sup>42</sup> and to consider factors two through four separately, in light of that use.<sup>43</sup>

The lower courts subsequently adopted the transformative use inquiry,<sup>44</sup> reasoning that, where a use fails to transform the original in any meaningful way, it supersedes the purpose for which the original was created and does not advance the goal of copyright.<sup>45</sup> For example, in *On Davis v. The Gap*, Judge Leval, writing for the Second Circuit, held that the use of copyrighted, non-functional, designer eyeglasses in a photograph in an advertisement for items of clothing was not transformative because the glasses depicted in the advertisement were being used for their intended purpose: to be worn.<sup>46</sup> The fact that the glasses were placed in a different medium (a photograph) and used to help sell another product (clothing) did not add new meaning or expression. Likewise, in *Ringgold v. Black Entertainment Television*, the Second Circuit found that the

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<sup>38</sup> *Twin Peaks Prods., Inc. v. Publ’ns Int’l, Ltd.*, 996 F.2d 1366, 1375 (2d Cir. 1993) (Martin, J.); *Basic Books, Inc. v. Kinko’s Graphics Corp.*, 758 F. Supp. 1522, 1530 (S.D.N.Y. 1991) (Motley, J.); *Am. Geophysical Union v. Texaco Inc.*, 802 F. Supp. 1, 12-14 (S.D.N.Y. 1992) (Leval, J.), *amended and superseded by* 60 F.3d 913 (2d Cir. 1994).

<sup>39</sup> *Campbell*, 510 U.S. at 576-79 (citing Leval, *supra* note 32, at 1111, 1132-34), 585 (citing Leval, *supra* note 32, at 1126-27), 587 (citing Leval, *supra* note 32, at 1123), 591-94 (citing Leval, *supra* note 32, at 1124-25).

<sup>40</sup> *Campbell*, 510 U.S. at 579.

<sup>41</sup> *Id.* at 583.

<sup>42</sup> *Id.* at 579-86.

<sup>43</sup> *Id.* at 586-94.

<sup>44</sup> Since Justice Souter’s opinion in *Campbell*, the lower courts have applied the transformative use test in sixty-four copyright cases.

<sup>45</sup> *Am. Geophysical Union v. Texaco Inc.*, 60 F.3d 913, 923 (2d Cir. 1994).

<sup>46</sup> *On Davis v. The Gap, Inc.*, 246 F.3d 152, 174 (2d Cir. 2001) (Leval, J.).

defendant's use of a poster depicting the plaintiff's copyrighted story quilt as a set decoration for a television program was in no sense "transformative."<sup>47</sup> The defendant had used the quilt for the same purpose for which it had been designed: to be decorative.<sup>48</sup>

In other decisions, however, the lower courts have confused transformation of the work itself with transformation of the use.<sup>49</sup> As Professor Paul Goldstein has observed:

Under the putative authority of Justice Souter's opinion in *Campbell v. Acuff-Rose*, contemporary decisions have stretched the notion of transformative use to the breaking point. A substantial majority of courts have taken the view that transformative use doctrine will excuse a use even if the user has done no more than alter the context in which the copyrighted work is used—changing the frame, not the picture.<sup>50</sup>

Such was the case in *Bill Graham Archives v. Dorling Kindersley*, where, in contrast to its earlier holding in *On Davis*, the Second Circuit held that the use of reduced images of copyrighted concert posters in a biographical work on the Grateful Dead was transformative because the images were being used, not to advertise rock concerts, but to illustrate a timeline which included those same concerts.<sup>51</sup> Both uses marked the same events. Both used the works in their entirety, although Dorling Kindersley did considerably shrink them before placing them along a timeline of the Grateful Dead's career.<sup>52</sup> Yet, the Second Circuit found the secondary use different enough from the original to be transformative.<sup>53</sup>

The Ninth Circuit has gone down a similar path, holding in two separate instances that images were transformed by reduction in size and display as a result of using an Internet search engine.<sup>54</sup> Despite its

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<sup>47</sup> *Ringgold v. Black Entm't Television, Inc.*, 126 F.3d 70, 79 (2d Cir. 1997) (Newman, J.).

<sup>48</sup> *Id.*

<sup>49</sup> Woo, *supra* note 16, at 65.

<sup>50</sup> Goldstein, *supra* note 17, at 6.

<sup>51</sup> *Bill Graham Archives v. Dorling Kindersley Ltd.*, 448 F.3d 605, 612 (2d Cir. 2006).

<sup>52</sup> *Id.* at 607.

<sup>53</sup> *Id.* at 609.

<sup>54</sup> *Kelly v. Arriba Soft Corp.*, 336 F.3d 811, 819 (9th Cir. 2003) (because Arriba had "created a different use for [Kelly's reduced] images, Arriba's use is transformative"); *Perfect 10, Inc. v. Amazon.com, Inc.*, 487 F.3d 701, 721 (9th Cir.) ("a search engine puts [thumbnail] images 'in a different context' so that they are 'transformed into a new creation'"), *amended by* 508 F.3d 1146 (9th Cir. 2007).

previous holding in *Napster* that merely transferring a work to a different medium was not transformative,<sup>55</sup> in *Perfect 10* and in *Kelly*, the Ninth Circuit concluded that a change in medium *was* transformative where the new medium served a socially beneficial purpose—that of illustrating websites within a search engine.<sup>56</sup>

Since *Campbell*, the lower courts have tended to allow a finding of transformation to color their analysis of both the purpose and character of the secondary use and the remaining factors.<sup>57</sup> Melville and David Nimmer in *Nimmer on Copyright* caution that a finding of transformative use does not mean that the defendant will prevail on the other factors as well.<sup>58</sup> In practice, however, where a court finds a use transformative, it is likely to hold that other considerations weigh in favor of fair use. For example, Section 107 directs courts to consider whether the purpose and character of the use was commercial or non-profit,<sup>59</sup> but after finding a use to be transformative courts tend largely to ignore a secondary user's commercial purpose.<sup>60</sup> Further, where a court finds a transformative use, it tends to give less weight and less real analysis to factors two through four. For a creator of photographs or video, this means that, not only are courts likely to find a transfer of their work to a news context transformative, but upon finding it transformative, courts are even more likely to find the use fair as well.

#### B. Factor Two: “the nature of the copyrighted work.”

The second factor in the fair use analysis looks to where the original work lies along the spectrum of copyright protection, as well as whether the work is published or unpublished. Copyright protects “original works of authorship.”<sup>61</sup> Accordingly, the work must be both independently created, and must have “some minimal degree of creativity.”<sup>62</sup> Facts are discovered rather than created, and, therefore,

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<sup>55</sup> *A&M Records, Inc. v. Napster, Inc.*, 239 F.3d 1004, 1015 (9th Cir. 2001).

<sup>56</sup> *Kelly*, 336 F.3d at 818-20; *Perfect 10*, 487 F.3d at 721, *amended by* 508 F.3d 1146 (9th Cir. 2007).

<sup>57</sup> *Bunker*, *supra* note 16, at 2, 9; *Zimmerman*, *supra* note 16, at 260.

<sup>58</sup> 4 MELVILLE NIMMER & DAVID NIMMER, NIMMER ON COPYRIGHT § 13.05[A][1][b] (2007).

<sup>59</sup> 17 U.S.C. § 107(1) (2006).

<sup>60</sup> *E.g.*, *On Davis v. The Gap, Inc.*, 246 F.3d 152, 175 (2d Cir. 2001).

<sup>61</sup> 17 U.S.C. § 102(a) (2006).

<sup>62</sup> *Feist Publ'ns, Inc. v. Rural Tel. Serv. Co.*, 499 U.S. 340, 345 (1991).

do not fall within the constitutionally mandated monopoly granted to the writings of authors.<sup>63</sup> Because facts cannot be original expression, factual elements within a work are not protected, even though the work as a whole enjoys protection.<sup>64</sup> Where works are primarily factual, there is a greater public interest in providing broader access to those works.<sup>65</sup> Thus, the further the original work is from the creative “core of intended copyright protection,” or the more factual it is, the thinner the copyright and the more the second factor will weigh in favor of fair use.<sup>66</sup> As the fair use doctrine seeks to balance incentives to authors of creative works against the public interest in access to information,<sup>67</sup> works that are factual are more vulnerable to a fair use defense.<sup>68</sup> Judge Leval noted that it is unclear whether fictional works receive more protection in a fair use analysis primarily because they do not lend themselves to productive uses as well as do factual works, or simply because they contain less unprotected expression.<sup>69</sup> Regardless, the nature of the copyrighted work factor carries little weight in the overall fair use analysis.<sup>70</sup>

Whether a work is published or unpublished receives greater attention because of the one-time value of the author’s right of first publication and his or her interest in privacy and control.<sup>71</sup> Fair use is based in part on the assumption that an author who has placed her work in the market has impliedly consented to reasonable use.<sup>72</sup> Authors of unpublished works have not given that consent.<sup>73</sup> Additionally, where an infringer uses an unpublished work, he or she also appropriates the creator’s right of first publication, “an important marketable subsidiary right” which cannot be replaced.<sup>74</sup> Because an author should be able to choose when and where she wishes to first publish her work, the Supreme Court held that the unauthorized use of an unpublished work is rarely fair.<sup>75</sup> Recent decisions have extended this reasoning, holding that, in many cases, not only does a work’s

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<sup>63</sup> U.S. CONST., art. I, § 8, cl. 8; *Feist*, 499 U.S. at 347.

<sup>64</sup> *Harper & Row, Publishers, Inc. v. Nation Enters.*, 471 U.S. 539, 547 (1985); *Feist*, 499 U.S. at 347-48.

<sup>65</sup> *Harper & Row*, 471 U.S. at 563.

<sup>66</sup> *Id.*; *Campbell v. Acuff-Rose Music, Inc.*, 510 U.S. 569, 586 (1994).

<sup>67</sup> *Pac. & S. Co. v. Duncan*, 744 F.2d 1490, 1495 (11th Cir. 1984).

<sup>68</sup> *Harper & Row*, 471 U.S. at 563 (“The law generally recognizes a greater need to disseminate factual works than works of fiction or fantasy.”).

<sup>69</sup> *Am. Geophysical Union v. Texaco Inc.*, 802 F. Supp. 1, 17 (S.D.N.Y. 1992), *amended and superseded by* 60 F.3d 913 (2d Cir. 1994).

<sup>70</sup> WILLIAM F. PATRY, *THE FAIR USE PRIVILEGE* 505 (2d ed. 1995).

<sup>71</sup> *Harper & Row*, 471 U.S. at 562-64.

<sup>72</sup> *Id.* at 550.

<sup>73</sup> *But see id.*

<sup>74</sup> *Id.* at 549.

<sup>75</sup> *Id.* at 553-55.

unpublished nature weigh strongly against fair use, but a work's *published* nature favors fair use, counterbalancing the creative nature of the work.<sup>76</sup> Works that are unpublished are to receive greater protection, but there is no *per se* rule that copying of unpublished works is unfair.<sup>77</sup>

A photograph is considered to contain original creative expression even where its subject matter is factual.<sup>78</sup> The photographer's depiction of the original scene "is the personal reaction of an individual upon nature"<sup>79</sup> formed by a series of choices made by the photographer.<sup>80</sup> Thus, almost any photograph may be protected under copyright.<sup>81</sup> The amount of protection that each photograph receives varies with its level of originality.<sup>82</sup> Photographs receive their originality from three basic sources: rendition, timing, and

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<sup>76</sup> See *Kelly v. Arriba Soft Corp.*, 336 F.3d 811, 820 (9th Cir. 2003); *Perfect 10, Inc. v. Amazon.com, Inc.*, 487 F.3d 701, 723 (9th Cir.), *amended by* 508 F.3d 1146 (9th Cir. 2007).

<sup>77</sup> Congress clarified that the fact that a work is unpublished is not a bar to fair use in 1992, by adding a sentence of explanation following the four factors: "The fact that a work is unpublished shall not itself bar a finding of fair use if such finding is made upon consideration of all the above factors." Congress was reacting to a series of Second Circuit opinions concerning the use of unpublished writings in biographies. H.R. REP. NO. 102-836, at 8-9 (1992), *as reprinted in* 1992 U.S.C.C.A.N. 2553, 2560-61. See *Salinger v. Random House, Inc.*, 650 F. Supp. 413 (S.D.N.Y. 1986), *rev'd*, 811 F.2d 90 (2d Cir. 1987); *New Era Publ'ns Int'l, ApS v. Henry Holt & Co.*, 695 F. Supp. 1493 (S.D.N.Y. 1988), *aff'd*, 873 F.2d 576 (2d Cir. 1989); *Wright v. Warner Books, Inc.*, 748 F. Supp. 105 (S.D.N.Y. 1990), *aff'd*, 953 F.2d 731 (2d Cir. 1991).

<sup>78</sup> *Bleistein v. Donaldson Lithographing Co.*, 188 U.S. 239, 249-50 (1903).

<sup>79</sup> *Id.* at 250.

<sup>80</sup> Christine Haight Farley, *The Lingering Effects of Copyright's Response to the Invention of Photography*, 65 U. PITT. L. REV. 385, 394 (2004) ("The seeming transparency of photography works to deny that it is a complex construction. However, each photograph involves a series of choices made by its producer.").

<sup>81</sup> *Strauss v. Hearst Corp.*, No. 85 Civ. 10017, 1988 WL 18932, at \*5 (S.D.N.Y. Feb. 19, 1988) (photographs of fishing gear held to be "plainly creative expressions"); *E. Am. Trio Prods., Inc. v. Tang Elec. Corp.*, 97 F. Supp. 2d 395, 417-18 (S.D.N.Y. 2000) (photographs of common industrial items for catalog possessed sufficient originality and creativity); *SHL Imaging, Inc. v. Artisan House, Inc.*, 117 F. Supp. 2d 301, 310-11 (S.D.N.Y. 2000) (photographs of picture and mirror frames possess requisite level of originality). *Cf.* *Oriental Art Printing, Inc. v. Goldstar Printing Corp.*, 175 F. Supp. 2d 542, 546-47 (S.D.N.Y. 2001) ("rare case" in which photographs lack expressive elements necessary for copyright protection where photographs depicted common Chinese dishes on plates bearing a common pattern, and where plaintiff failed to describe how the photographs were taken).

<sup>82</sup> *Mannion v. Coors Brewing Co.*, 377 F. Supp. 2d 444, 451 (S.D.N.Y. 2005).

subject matter.<sup>83</sup> Rendition concerns the choices that the photographer made in depicting his or her subject matter.<sup>84</sup> For example, in Abraham Zapruder's famous film of President Kennedy's assassination, the district court found creativity in Zapruder's choice of camera, film, lens, and viewing point.<sup>85</sup> A photographer achieves originality in timing simply by being at the right place at the right time.<sup>86</sup> Others are free to attempt to duplicate the photograph by creating the same subject matter, but they may not copy the photograph itself.<sup>87</sup> Lastly, a photograph may possess originality in its subject matter to the extent that the photographer actually created the scene.<sup>88</sup> A famous example of originality in subject matter is the photograph of Oscar Wilde taken by Napoleon Sarony.<sup>89</sup> The Supreme Court found creativity not only in the rendition of the photograph, but in the pose and setting, as well.<sup>90</sup> The infamous posed photographs of the guards and prisoners at Abu Ghraib prison are a more recent example. Because the photographers posed their subjects, as well as made choices affecting the rendition of each photograph, their work should be accorded a greater degree of protection than the short video of Saddam Hussein's hanging, in which the scene was not created by the photographer.

As with written works, films and photographs enjoy no protection for their factual elements.<sup>91</sup> Facts and the news of the day are part of the public domain.<sup>92</sup> Hence, the newsworthy subject matter of a photograph or film is not protected.<sup>93</sup> Nevertheless, the fact that a film or photograph depicts newsworthy events does not obviate its protection under copyright law.<sup>94</sup> As explained in *Harper & Row*, if courts were to hold that copying was more likely to be fair because of strong public interest in the subject matter of a work, there would be

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<sup>83</sup> *Id.* at 451-53; *see also* *Rogers v. Koons*, 960 F.2d 301, 307 (2d Cir. 1992) ("Elements of originality in a photograph may include posing the subjects, lighting, angle, selection of film and camera, evoking the desired expression, and almost any other variant involved.") (citations omitted).

<sup>84</sup> *Mannion*, 377 F. Supp. 2d at 452.

<sup>85</sup> *Time Inc. v. Bernard Geis Assocs.*, 293 F. Supp. 130, 143 (S.D.N.Y. 1968).

<sup>86</sup> *Mannion*, 377 F. Supp. 2d at 452-53.

<sup>87</sup> *Id.* at 453; *SHL Imaging, Inc. v. Artisan House, Inc.*, 117 F. Supp. 2d 301, 311 (S.D.N.Y. 2000) (noting that copyright protection extends only to the photographer's contribution to the work).

<sup>88</sup> *Mannion*, 377 F. Supp. 2d at 453.

<sup>89</sup> *Burrow-Giles Lithographic Co. v. Sarony*, 111 U.S. 53, 55 (1884).

<sup>90</sup> *Id.* at 60.

<sup>91</sup> *Id.*; *Int'l News Serv. v. Associated Press*, 248 U.S. 215, 234 (1918).

<sup>92</sup> *Int'l News Serv.*, 248 U.S. at 234.

<sup>93</sup> *Bleistein v. Donaldson Lithographing Co.*, 188 U.S. 239, 249 (1903).

<sup>94</sup> *Harper & Row, Publishers, Inc. v. Nation Enters.*, 471 U.S. 539, 557 (1985).

reduced incentive to produce any works of value.<sup>95</sup> “It is fundamentally at odds with the scheme of copyright to accord lesser rights in those works that are of greatest importance to the public.”<sup>96</sup>

Nevertheless, even where a work is found to be creative and within the core protection of copyright, the second fair use factor may not weigh in favor of the copyright owner when the work is deemed to be transformative.<sup>97</sup> In *Campbell*, the Court reasoned that, because parodists “almost invariably copy publicly known, expressive works,” the nature of the original works is of little help “in separating the fair use sheep from the infringing goats.”<sup>98</sup> Subsequent to *Campbell*, many lower courts have discounted the expressive nature of original works whenever the secondary work is found to be transformative, regardless of whether the secondary use is one, like parody, which requires the copying of core protected expression.<sup>99</sup> For example, after finding Google’s use of reduced copies of images “significantly transformative” in *Perfect 10*, the Ninth Circuit concluded that, although Perfect 10’s images of nude models were creative, this was countered by the fact that they had been previously published,<sup>100</sup> a factor weighing in favor of fair use. In *Bill Graham Archives*, the Second Circuit recognized that the creative nature of the plaintiff’s artistic concert posters placed them within the core of copyright protection, but it nonetheless found that creativity of little relevance in light of Dorling Kindersley’s transformative use of the images in an illustrated biography.<sup>101</sup>

The fair use doctrine provides courts with room to maneuver when it appears that rigidly enforcing the monopoly of copyright

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<sup>95</sup> *Id.* at 559. *But see* Time Inc. v. Bernard Geis Assocs., 293 F. Supp. 130 (S.D.N.Y. 1968).

<sup>96</sup> *Harper & Row*, 471 U.S. at 559.

<sup>97</sup> *Campbell v. Acuff-Rose Music, Inc.*, 510 U.S. 569, 586 (1994) (nature of the work is a neutral factor where the infringing use is parody); *Bill Graham Archives v. Dorling Kindersley Ltd.*, 448 F.3d 605, 612-13 (2d Cir. 2006) (creative works’ use by infringer for historical purpose).

<sup>98</sup> *Campbell*, 510 U.S. at 586.

<sup>99</sup> *Blanch v. Koons*, 467 F.3d 244, 257 (2d Cir. 2006) (finding that creative nature of original photograph has limited weight where the secondary work is transformative).

<sup>100</sup> *Perfect 10, Inc. v. Amazon.com, Inc.*, 487 F.3d 701, 723-24 (9th Cir.), *amended by* 508 F.3d 1146 (9th Cir. 2007); *see also* *Kelly v. Arriba Soft Corp.*, 336 F.3d 811, 820 (9th Cir. 2003) (where secondary was use found to be transformative and work was previously published, creative nature of artistic photographs weighed only slightly against fair use).

<sup>101</sup> *Bill Graham Archives*, 448 F.3d at 612-13.

would stifle the very creativity it was designed to promote.<sup>102</sup> With the dissemination of creative expression as the goal, it makes sense to give greater weight in a fair use analysis to those works that are closer to this ideal. Despite this, lower courts have largely ignored the extent to which the original work adds to the collective pool of creative expression. Where lower courts find the challenged use to be transformative, the creative nature of the original work is given short shrift, even where that work is significantly more creative than the secondary work. Thus, where news organizations engage in the unauthorized use of even significantly creative works, it is unlikely that the work's creativity will prevent a finding of fair use if the secondary use is deemed transformative.<sup>103</sup>

C. Factor Three: “the amount and substantiality of the portion used in relation to the copyrighted work as a whole.”

The third factor of the fair use analysis directs the courts to weigh “the amount and substantiality of the portion used in relation to the copyrighted work as a whole.”<sup>104</sup> This is consistent with copyright's goal of encouraging the dissemination of creative expression through incentives to creators. When courts allow secondary users to take too much of the original work or copy its most valuable portions, they decrease the incentive to create, throwing the balancing act of copyright out of kilter. This third factor then looks to whether the use was reasonable in light of the quantity and quality of material taken.<sup>105</sup> The quantity and quality of the portion taken from the original indicates whether the secondary use is likely to be a superseding use.<sup>106</sup> If there is extensive copying from the original, the new work is more likely to serve the same purpose as the original, and thus to replace or to compete with the original in the market.<sup>107</sup> Where

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<sup>102</sup> *Iowa State Univ. Research Found., Inc. v. Am. Broad. Cos.*, 621 F.2d 57, 60 (2d Cir. 1980).

<sup>103</sup> *Mathieson v. Associated Press*, No. 90 Civ. 6945 (LMM), 1992 WL 164447, at \*8 (S.D.N.Y. June 25, 1992).

<sup>104</sup> 17 U.S.C. § 107(3) (2006).

<sup>105</sup> *Folsom v. Marsh*, 9 F. Cas. 342 (C.C.D. Mass. 1841) (No. 4901) (“look to...the quantity and value of the materials used”); *Campbell v. Acuff-Rose Music, Inc.*, 510 U.S. 569, 587 (1994).

<sup>106</sup> *Campbell*, 510 U.S. at 587; *Hustler Magazine, Inc. v. Moral Majority, Inc.*, 796 F.2d 1148, 1155 (9th Cir. 1986).

<sup>107</sup> NIMMER, *supra* note 58, § 13.05[D][1] (in general, complete copying is not necessary where the new work serves a different purpose from the original); *Harper & Row, Publishers, Inc. v. Nation Enters.*, 471 U.S. 539, 566-68 (1985) (actual

a secondary use incorporates substantial portions of the original, or portions that would be considered the “heart” or qualitatively most valuable portions of the original work, the use is less likely to be one that could be considered reasonable, and, consequently, less likely to weigh in favor of fair use.<sup>108</sup>

Where the “heart” of the original work is taken, the amount of use should weigh in the plaintiff’s favor, even if the amount is small.<sup>109</sup> The core or heart of a work is that portion, or portions, “most likely to be news-worthy and important in licensing serialization.”<sup>110</sup> Verbatim copying<sup>111</sup> and the manner in which the secondary work uses the excerpts from the original<sup>112</sup> indicate the value of the excerpts to both the author and the alleged infringer. For example, the Supreme Court found that the use of only three hundred words lifted from President Ford’s autobiography weighed against fair use where *The Nation* chose those portions that were the “heart of the book,” and structured its article around verbatim quotes from the book.<sup>113</sup> Similarly, in *Elvis Presley Enterprises*, the Ninth Circuit found that the amount used weighed against fair use where the defendant’s sixteen-hour documentary used short clips from Presley’s television appearances, but the excerpted portions featured copyrighted footage of Presley singing the most familiar portions of his most popular songs.<sup>114</sup>

In the case of parody, which requires extensive copying in order to succeed, the Court held that wholesale copying, or even taking the heart of the original, was a fair use,<sup>115</sup> because in order for a parody to succeed it must evoke the original.<sup>116</sup> Once the user has

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damage from *The Nation*’s use of excerpts when *Time* canceled its serialization of *A Time to Heal*).

<sup>108</sup> See *Harper & Row*, 471 U.S. at 564-66 (third factor weighed against fair use where *The Nation* used verbatim quotes representing the “heart” of the original work); *Elvis Presley Enters. v. Passport Video*, 349 F.3d 622, 630 (9th Cir. 2003) (when using the heart of a film clip, the use is more likely to require licensing).

<sup>109</sup> *Harper & Row*, 471 U.S. at 564-65.

<sup>110</sup> *Campbell*, 510 U.S. at 587, see *L.A. News Serv. v. CBS Broad., Inc.*, 305 F.3d 924, 941 (9th Cir. 2002).

<sup>111</sup> *Harper & Row*, 471 U.S. at 565; *Worldwide Church of God v. Phila. Church of God, Inc.*, 227 F.3d 1110, 1118 (9th Cir. 2000) (citing *Hustler*, 796 F.2d at 1155).

<sup>112</sup> *Harper & Row*, 471 U.S. at 566.

<sup>113</sup> *Id.* at 564-66.

<sup>114</sup> *Elvis Presley Enters. v. Passport Video*, 349 F.3d 622, 630 (9th Cir. 2003).

<sup>115</sup> *Campbell*, 510 U.S. at 588-89.

<sup>116</sup> *Id.* at 580-81, 588.

copied enough for the parody to succeed, how much more he may legitimately borrow from the original depends upon whether the parody is likely to supersede the original.<sup>117</sup> In *Campbell*, 2 Live Crew took the heart of the original song, but sufficiently added to it so that the end product was not primarily made up of verbatim copying from the original.<sup>118</sup>

There is no clear line indicating how much is too much as to the amount of the original material used.<sup>119</sup> The amount required to reduce the incentive to create necessarily depends on the nature of the secondary use.<sup>120</sup> A greater portion of the original may be used to the extent that the secondary work is non-superseding.<sup>121</sup> In *Hustler*, the Ninth Circuit observed that, where a defendant uses all or nearly all of the plaintiff's original work, the secondary work necessarily performs the same function as the original.<sup>122</sup> This is consistent with the traditional fair use analysis, in which the likelihood that the secondary work is transformative is inversely related to the amount of the original that is taken.<sup>123</sup> Despite this, where a work is found to be transformative on the basis of a different function or medium, the trend has been to find that even the use of all or nearly all of an image is justified.<sup>124</sup>

As the fair use inquiry has continued to zero in on whether the infringing use is transformative, lower courts have cited *Campbell* for the proposition that even wholesale copying does not weigh against fair use when the secondary use is transformative.<sup>125</sup> This is especially true where the original work is visual rather than written. For example, in *Bill Graham Archives*, the Second Circuit concluded that

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<sup>117</sup> *Id.* at 588.

<sup>118</sup> *Id.* at 589.

<sup>119</sup> *Maxtone-Graham v. Burtchaell*, 803 F.2d 1253, 1263 (2d Cir. 1986).

<sup>120</sup> *Campbell*, 510 U.S. at 586-87.

<sup>121</sup> *Id.* at 587-88.

<sup>122</sup> *Hustler Magazine, Inc. v. Moral Majority, Inc.*, 796 F.2d 1148, 1154 (9th Cir. 1986).

<sup>123</sup> *Campbell*, 510 U.S. at 587; *On Davis v. The Gap, Inc.*, 246 F.3d 152, 175 (2d Cir. 2001) (“[F]ragmentary copying is more likely to have a transformative purpose than wholesale copying.”).

<sup>124</sup> *Núñez v. Caribbean Int'l News Corp.*, 235 F.3d 18, 24 (1st Cir. 2000); *Kelly v. Arriba Soft Corp.*, 336 F.3d 811, 820-21 (9th Cir. 2003); *Perfect 10, Inc. v. Amazon.com, Inc.*, 487 F.3d 701, 724 (9th Cir.), *amended by* 508 F.3d 1146 (9th Cir. 2007); *Bill Graham Archives v. Dorling Kindersley Ltd.*, 448 F.3d 605, 613 (2d Cir. 2006).

<sup>125</sup> *Kelly*, 336 F.3d at 821 (finding that images of artwork used in their entirety did not weigh against fair use where the images were reduced and used in a search engine); *Núñez*, 235 F.3d at 23-24 (concluding that complete photographs used in news story did not weigh against finding of fair use where the photos served a different purpose than that originally intended).

importing entire images of creative works into a coffee table book did not weigh against a finding of fair use because the images served a different, transformative purpose in the infringing work.<sup>126</sup> The visual analogy to *Campbell*, however, is not copying an entire image into a new medium, but altering an image for purposes of parody, as was seen in *Liebovitz v. Paramount Pictures*.<sup>127</sup> In that case, the court found that copying more than was strictly necessary of Liebovitz's portrait of a pregnant Demi Moore for the purposes of parody did not weigh significantly against fair use because the use commented on the original and was unlikely to interfere with the market for the original work.<sup>128</sup>

By diluting the definition of transformative use and then reasoning that the user may copy as much as is necessary for that purpose—even the entirety of a work—the lower courts have significantly reduced the analytical role of the third factor, contrary to the objectives of the statute. In the case of news reporting, where the use of an entire image may be copied to illustrate a news story, a finding of transformative use on the first factor may lead the court to ignore the fact that wholesale copying should indicate that the use was not transformative at all.

D. Factor Four: “the effect of the use upon the potential market for or value of the copyrighted work.”

The fourth factor of the fair use analysis focuses upon the extent to which the use is likely to interfere with the author's ability to obtain a fair return on his labor.<sup>129</sup> Thus, a finding of commercial use on the first factor creates a presumption of market harm on the fourth.<sup>130</sup> Here, the courts weigh the effect of the secondary use on only the protected portions of the original work—on its original expression—but also consider the effect on currently undeveloped markets.<sup>131</sup> The potential market for a work encompasses the

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<sup>126</sup> *Bill Graham Archives*, 448 F.3d at 613.

<sup>127</sup> *Leibovitz v. Paramount Pictures Corp.*, 137 F.3d 109 (2d Cir. 1998).

<sup>128</sup> *Id.* at 116-17.

<sup>129</sup> *Harper & Row, Publishers, Inc. v. Nation Enters.*, 471 U.S. 539, 547 (1985); *Rogers v. Koons*, 960 F.2d 301, 312 (2d Cir. 1992) (“The reason for this rule relates to a central concern of copyright law that unfair copying undercuts demand for the original work and, as an inevitable consequence, chills creation of such works.”).

<sup>130</sup> *Sony Corp. of Am. v. Universal City Studios, Inc.*, 464 U.S. 417, 451 (1984).

<sup>131</sup> NIMMER, *supra* note 58, § 13.05[A][4].

exclusive rights granted by Section 106: reproduction, creation of derivative works, distribution, and public display and performance.<sup>132</sup> The scope of this potential market is not unlimited. Fair use ensures that the rights of individual authors are not so strictly enforced that licensing is required for all uses, regardless of how minimal, reasonable, or transformative.<sup>133</sup> On the other hand, were this factor interpreted as protecting only those uses that the author is currently exploiting, the exclusive right to create derivative works would be virtually eliminated.

When determining whether the secondary work has harmed the potential market for a copyrighted work, courts should define the potential market as one the copyright owner is currently likely to enter.<sup>134</sup> Other sections of the Copyright Act confirm that Congress did not intend for this market to be frozen at the time of creation.<sup>135</sup> For example, the termination provisions of Section 304 were intended to give authors of works whose value was not immediately apparent an opportunity to renegotiate contracts that no longer reflect the economic value of the work.<sup>136</sup> Similarly, in Section 201(c), Congress sought to preserve the author's ability to profit from later, unforeseen markets, where the work has been published as part of a collective work, by strengthening the author's position vis-à-vis his initial publisher.<sup>137</sup>

Any unauthorized use has some potential to harm the market for the original.<sup>138</sup> Nevertheless, it is not enough for the plaintiff to assert that an infringer interfered with a potential market if the market is one the plaintiff is unlikely to exploit.<sup>139</sup> Consequently, in order for the effect on the potential market to weigh against fair use, the secondary use must be in a market that the copyright holder is

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<sup>132</sup> 17 U.S.C. § 106 (2006).

<sup>133</sup> PATRY, *supra* note 70, at 557; *see also* Lydia Pallas Loren, *Redefining the Market Failure Approach to Fair Use in an Era of Copyright Permission Systems*, 5 J. INTEL. PROP. L. 1, 24 (1997) (“[B]ecause any work inevitably builds on previous works, some to a greater extent than others, providing too large a monopoly will actually hinder the development of new works by limiting future creators [sic] use of earlier works. Herein lies the fundamental tension in copyright law.”) (footnote omitted).

<sup>134</sup> PATRY, *supra* note 70, at 559.

<sup>135</sup> 17 U.S.C. §§ 304, 201(c) (2006).

<sup>136</sup> 17 U.S.C. § 304; *Stewart v. Abend*, 495 U.S. 207, 229 (1990).

<sup>137</sup> 17 U.S.C. § 201(c); *N.Y. Times Co. v. Tasini*, 533 U.S. 483, 495-97 (2001) (holding that freelance authors' copyrights in individual works were violated where the publisher licensed publication by an electronic database that allowed users access to the works individually).

<sup>138</sup> *Princeton Univ. Press v. Mich. Document Servs., Inc.*, 99 F.3d 1381, 1387 (6th Cir. 1996).

<sup>139</sup> NIMMER, *supra* note 58, § 13.05[A][4].

currently likely to have an interest in exploiting.<sup>140</sup> Thus, the use of “Who Are You” as the theme song for *C.S.I.: Crime Scene Investigation* is within the potential market for the work under a fair use analysis, even if Pete Townsend and Roger Daltry did not contemplate such a use when The Who released the song in 1978. Conversely, use of the song in a parody is not within the potential market because it is unlikely that Townsend and Daltry would choose to exploit the market for parodies of their own work.<sup>141</sup>

Courts must also consider whether the accused use would harm the market for the original work should the use become widespread.<sup>142</sup> Changes in technology may greatly increase the potential for harm by making exact duplicates of original works readily and cheaply available.<sup>143</sup> Copying that was once customary and largely *de minimis* may grow to reduce demand for the legal copies of original works, thus reducing the incentive to create original works.<sup>144</sup> The market often reacts by reducing transaction costs and creating licensing systems in order both to protect the rights of copyright holders and to exploit the new market for their works,<sup>145</sup> as it has recently with respect to images and footage licensed to Internet sites and news organizations.<sup>146</sup> Where authors and publishers have created a licensing market, such as for stock photographs or Internet content, the courts should find market harm when copying circumvents that market by using the work for free.<sup>147</sup> Unauthorized use decreases the value of the work itself because the copyright owner is no longer able to provide a truly exclusive license.<sup>148</sup> This is especially important when

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<sup>140</sup> *Id.*

<sup>141</sup> See *Campbell v. Acuff-Rose Music, Inc.*, 510 U.S. 569, 592 (1994).

<sup>142</sup> *Id.* at 590.

<sup>143</sup> See *Am. Geophysical Union v. Texaco Inc.*, 60 F.3d 913, 917 (2d Cir. 1994); *A&M Records, Inc. v. Napster, Inc.*, 239 F.3d 1004, 1011 (9th Cir. 2001).

<sup>144</sup> *Am. Geophysical Union*, 60 F.3d at 931; *A&M Records*, 239 F.3d at 1016.

<sup>145</sup> *Am. Geophysical Union*, 60 F.3d at 930; Wendy J. Gordon, *Excuse and Justification in the Law of Fair Use: Transaction Costs Have Always Been Only Part of the Story*, 50 J. COPYRIGHT SOC'Y U.S.A. 149, 188-90 (2003).

<sup>146</sup> Hansell, *supra* note 7 (reporting on major news organizations' efforts to solicit amateur news footage); Tom Sowa, *Selling an Image: Microstock Sites Offer More Choices to Photogs, Buyers*, SPOKESMAN-REV., Aug. 6, 2007, available at [http://www.spokesmanreview.com/tools/story\\_pf.asp?ID=203264](http://www.spokesmanreview.com/tools/story_pf.asp?ID=203264) (reporting on growth of internet market for stock photography).

<sup>147</sup> See *Am. Geophysical Union*, 60 F.3d at 931.

<sup>148</sup> Brief of the Am. Soc'y of Media Photographers, Inc. et al. as Amici Curiae Supporting Plaintiff-Appellant Leslie A. Kelly at 14, *Kelly v. Arriba Soft Corp.*, 280 F.3d 934 (9th Cir. 2000) (No. 00-55521), 2000 WL 34004384.

a work is considered newsworthy because the harm from lost licensing fees and overexposure is greatest when the work is at peak demand; it is then that unauthorized use is most likely to reduce actual sales, and the value of the work is most vulnerable.<sup>149</sup>

In practice, where a court finds that a defendant's use has been transformative, it is more likely to find little or no market harm based upon the assumption that the defendant's work necessarily occupies a different market.<sup>150</sup> For example, in *Perfect 10*, the district court found that, because Perfect 10 had licensed another party to sell reduced-size images to cell phone users, "[c]ommonsense dictate[d] that [mobile users of Google Search which included thumbnail versions of Perfect 10's images would] be less likely to purchase the downloadable P10 content."<sup>151</sup> On appeal, the Ninth Circuit disagreed, reasoning instead that, where the secondary use is transformative, there is no presumptive harm to the market, even where the secondary use is commercial.<sup>152</sup> Because Perfect 10 had failed to show actual harm by presenting evidence of Google users downloading Perfect 10's images to their cell phones, the court ruled that the fourth factor did not weigh in favor of Perfect 10.<sup>153</sup>

Similarly, the Second Circuit found no market harm in *Bill Graham Archives*, despite the fact that Bill Graham had an established market for licensing its copyrighted concert posters.<sup>154</sup> Bill Graham had an established market for licensing its images and had, in fact, been negotiating a licensing agreement with Dorling Kindersley prior to its decision to publish the images without authorization.<sup>155</sup> Despite this, the court found that Bill Graham suffered no market harm from the loss of those fees because Dorling Kindersley's use fell within a transformative market for the images, over which Bill Graham could not hold a monopoly.<sup>156</sup> In so holding, the court appeared to have narrowed the definition of potential market to exclude any use that

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<sup>149</sup> *Am. Geophysical Union v. Texaco Inc.*, 802 F. Supp. 1, 20 (S.D.N.Y. 1992), *amended and superseded by* 60 F.3d 913 (2d Cir. 1994).

<sup>150</sup> *Bill Graham Archives v. Dorling Kindersley Ltd.*, 448 F.3d 605, 614-15 (2d Cir. 2006).

<sup>151</sup> *Perfect 10 v. Google, Inc.*, 416 F. Supp. 2d 828, 851 (C.D. Cal. 2006), *aff'd in part, rev'd in part by* 487 F.3d 701 (9th Cir.), *amended by* 508 F.3d 1146 (9th Cir. 2007).

<sup>152</sup> *Perfect 10 v. Amazon.com, Inc.*, 508 F.3d 1146, 1168 ("this presumption does not arise when a work is transformative because 'market substitution is less certain...' Google's use of thumbnails for search engine purposes is highly transformative, and so market harm cannot be presumed.").

<sup>153</sup> *Perfect 10 v. Amazon.com, Inc.*, 508 F.3d at 1168.

<sup>154</sup> *Bill Graham Archives*, 448 F.3d at 614-15.

<sup>155</sup> *Id.* at 614.

<sup>156</sup> *Id.* at 615.

was not originally intended by the creator, even markets for derivative works, making it almost impossible for a copyright owner to allege market harm once the secondary use is found transformative.

The recent tendency of the courts to discount even actual economic harm once a use is declared transformative is a distortion of the Supreme Court's observation that transformative uses are unlikely to harm the market for the original work. The presumption by many lower courts—that, where the court has deemed the secondary use transformative, there is no substantive effect on the market for or value of the original work—is a powerful disincentive to the development of new markets for copyrighted works.<sup>157</sup> Where this narrow definition of potential market is combined with a broad definition of transformation, copyright holders who are initially unaware of a potential market for their works are unfairly disadvantaged. Under the Second Circuit's holding in *Bill Graham Archives*, even if the copyright owner later develops and enters a new market, he will receive no protection from the courts when a secondary user opts to avoid the now customary fee.

In *Campbell*, Justice Souter observed that there is an inverse relationship between the degree of transformation and the significance of other factors in the fair use analysis.<sup>158</sup> Having found 2 Live Crew's use transformative, the Court did not ignore the remaining factors, but noted the effect that the use of the work as a parody had on the significance of these factors in evaluating whether the parody was a superseding or fair use.<sup>159</sup> The creative nature of the original work was little help in determining whether the use was fair, because "parodies almost invariably copy publicly known, expressive works."<sup>160</sup> In evaluating the third factor, the Court noted that parody must copy enough of the original for the listener to recognize the secondary work as a parody.<sup>161</sup> Lastly, the Court found that the parody was not a superseding work likely to reduce the market for the original because copyright holders are unlikely to create derivative works criticizing the original work.<sup>162</sup>

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<sup>157</sup> Jay Dratler, Jr., *Distilling the Witches' Brew of Fair Use in Copyright Law*, 43 U. MIAMI L. REV. 233, 328 (1988).

<sup>158</sup> *Campbell v. Rose-Acuff Music, Inc.*, 510 U.S. 569, 579 (1994).

<sup>159</sup> *Id.* at 586-94.

<sup>160</sup> *Id.* at 586.

<sup>161</sup> *Id.* at 588.

<sup>162</sup> *Id.* at 591-92.

Where courts require that the secondary use truly incorporate the original only as the raw material to which the infringer has added his own expression to create “new information, new aesthetics, new insights and understandings,”<sup>163</sup> this approach to the analysis of the remaining factors is reasonable, and a recognition—rather than a predetermination—of the interrelationship between transformation and the other factors. Where, however, the courts consider uses to be transformative which merely import the original work into a new medium or market, and presume that the remaining factors necessarily weigh in favor of fair use as well, the copyright owner of the original work is placed at a distinct disadvantage. If the secondary use is one, such as news reporting, that is considered to be a favored use, any use that does not usurp the works of a competitor is almost *per se* fair. As traditional news agencies continue to rely on amateur content, increasing the likelihood of litigation, the current application of the fair use doctrine will likely become a disincentive to the creation and sharing of original works of amateur news content.

### III. HOW THE LOWER COURTS APPLY THE FAIR USE DOCTRINE TO COPYING BY NEWS ORGANIZATIONS.

When Congress codified the fair use doctrine in Section 107, it suggested uses that might weigh in favor of fair use: criticism, comment, news reporting, teaching, scholarship, and research.<sup>164</sup> These uses, however, are not *per se* fair.<sup>165</sup> In particular, the Supreme Court has clearly stated that news reporting is not a presumptively fair use.<sup>166</sup> If copying were to be considered fair whenever the social benefit from access to that particular work outweighs the harm to its creator, the incentive to create socially important works would be substantially reduced.<sup>167</sup> This, in turn, would subvert the purpose of copyright to promote “the Progress of Science and useful Arts.”<sup>168</sup> Although the first factor, purpose and character of use, may shift the analysis in favor of fair use because of the productive or socially beneficial purpose of news reporting, the courts must still evaluate the

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<sup>163</sup> Leval, *supra* note 32, at 1111.

<sup>164</sup> 17 U.S.C. § 107 (2006).

<sup>165</sup> *Harper & Row, Publishers, Inc. v. Nation Enters.*, 471 U.S. 539, 558 (1985); H.R. REP. NO. 94-1476, *supra* note 23, at 65.

<sup>166</sup> *See Harper & Row*, 471 U.S. at 557-61; *see also* PATRY, *supra* note 70, at 488 (“This concept of a reasonable, good faith use seems difficult for the media to grasp, perhaps because they tend, egotistically to believe they *are* the public interest and thus that everything they do must also be in the public interest.”).

<sup>167</sup> *Harper & Row*, 471 U.S. at 559; *Pac. & S. Co. v. Duncan*, 744 F.2d 1490, 1497 (11th Cir. 1984).

<sup>168</sup> U.S. CONST., art. I, § 8, cl. 8; *Harper & Row*, 471 U.S. at 557.

secondary use on the basis of all four factors.<sup>169</sup> To do otherwise subverts the purpose of copyright by discouraging the creation of new works.

With the current tendency to label a use transformative if the original work is merely put to a different purpose, photographers who create works that are not marketed as news are more likely to find that the courts will consider even wholesale copying of their photos a fair use if the secondary user is a news organization. The transfer of images to a news context is considered by many courts to “almost inevitably add[] new meaning or message to a copyrighted work,”<sup>170</sup> despite the fact that those images, like the eyeglasses in *On Davis*, still perform essentially the same function. A comparison of how courts have analyzed the fair use defense, as applied to the unauthorized use of photographs or film clips by news organizations, illustrates the uphill battle faced by photographers who do not originally market their works as news.

A. How courts treat unauthorized use by competing news organizations.

Courts tend to apply a traditional fair use analysis in cases of copying by competing news organizations. Where the secondary use is by a competitor, the use is essentially the same as the original use, even under the narrow definition applied by the lower courts in recent decisions.<sup>171</sup> Thus, the court is unlikely to find the secondary use transformative unless the user has actually transformed the original work and not made “merely the facile use of the scissors; or extracts of the essential parts, constituting the chief value of the original work.”<sup>172</sup> Without a finding of transformative use on the first factor, courts tend to conduct a more searching analysis on the remaining three factors.<sup>173</sup> In the case of copying by a competitor, the courts’ finding of effect on

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<sup>169</sup> *Harper & Row*, 471 U.S. at 561.

<sup>170</sup> Matthew D. Bunker, *Transforming the News: Copyright and Fair Use in News-Related Contexts*, 52 J. COPYRIGHT SOC’Y U.S.A. 309, 312-13 (2004).

<sup>171</sup> Compare *L.A. News Serv. v. KCAL-TV Channel 9*, 108 F.3d 1119 (9th Cir. 1997), with *Núñez v. Caribbean Int’l News Corp.*, 235 F.3d 18 (1st Cir. 2000), and *Mathieson v. Associated Press*, No. 90 Civ. 6945 (LMM), 1992 WL 16447 (S.D.N.Y. June 25, 1992).

<sup>172</sup> *Folsom v. Marsh*, 9 F. Cas. 342, 345 (C.C.D. Mass. 1841) (No. 4901).

<sup>173</sup> Compare *KCAL-TV*, 108 F.3d 1119, with *L.A. News Serv. v. CBS Broad., Inc.*, 305 F.3d 924 (9th Cir. 2002).

the market and the value of the original work will nearly always weigh against fair use, despite the increasingly narrow view of a work's potential market.<sup>174</sup>

The three Los Angeles News Service cases, in which a business providing raw footage to television news outlets sought to protect its rights in the video of the Reginald Denny beating, demonstrate that when there is no change in the original intended purpose of the work the four-factor analysis is rigorously applied.

Los Angeles News Service (LANS) was a business operating in the Los Angeles area in which a husband and wife team, Marika and Robert Tur, created aerial news footage and licensed it to local and national news organizations.<sup>175</sup> On April 29, 1992, after learning that the intersection of Florence and Normandie Avenues would be the likely center of protest if the four police officers charged in the Rodney King beating were acquitted, the Turs and other LANS personnel flew to the intersection following the announcement of the verdict.<sup>176</sup> When the beating of Reginald Denny occurred, Marika Tur filmed the event, while Robert Tur directed the crew and narrated the footage.<sup>177</sup> The feed was broadcast live by KCOP, a local television station and licensee.<sup>178</sup> LANS granted licenses to use the footage to other local stations and to NBC.<sup>179</sup> However, the use of the footage spread beyond the actual licensees, resulting in three separate lawsuits.<sup>180</sup>

#### *Los Angeles News Service v. KCAL TV Channel 9*

KCAL is a CBS affiliate in Southern California.<sup>181</sup> After KCOP broadcast the LANS footage of the riots, KCAL requested a license to use the footage, but LANS refused.<sup>182</sup> Notwithstanding that refusal, KCAL secured a copy from another station, and broadcast

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<sup>174</sup> See *Núñez*, 235 F.3d 18. *But see CBS*, 305 F.3d 924.

<sup>175</sup> *CBS*, 305 F.3d at 929.

<sup>176</sup> Brief of Petitioner-Appellant at 10-11, *L.A. News Serv. v. KCAL-TV Channel 9*, 108 F.3d 1119 (9th Cir. 1997) (No. 95-55261), 1995 WL 17066760.

<sup>177</sup> *Id.* at 11.

<sup>178</sup> *KCAL-TV*, 108 F.3d at 1120.

<sup>179</sup> *Id.*; *L.A. News Serv. v. Reuters Television Int'l, Ltd.*, 149 F.3d 987, 990 (9th Cir. 1998).

<sup>180</sup> See, e.g., *Tur v. YouTube, Inc.*, No. CV064436 FMC AJWX, 2007 WL 1893635 (C.D. Cal. June 20, 2007) (action for copyright infringement and unfair competition arising out of YouTube's publication of the Denny footage).

<sup>181</sup> See *CBS 2-KCAL 9*, <http://cbs2.com>.

<sup>182</sup> *KCAL-TV*, 108 F.3d at 1120; Brief of Petitioner-Appellant, *supra* note 176, at 12 (according to LANS, the refusal to license the tape to KCAL was based on KCAL's failure to pay for previously licensed footage).

thirty seconds of the four-minute, forty-second tape several times on April 30, 1992.<sup>183</sup> When LANS brought suit in district court, the court granted summary judgment in favor of KCAL, finding fair use.<sup>184</sup> The court based its decision on the newsworthiness of the tape, LANS's failure to identify any economic harm, and KCAL's use of the tape for purposes of news reporting.<sup>185</sup>

The Ninth Circuit reversed.<sup>186</sup> In applying the first fair use factor, it found that the purpose of the use weighed for neither party.<sup>187</sup> Although news reporting is a productive use, the fact that KCAL competed with LANS's licensees without paying the same licensing fee outweighed any merit accorded for its favored use.<sup>188</sup> The fact that the tape itself was news might have weighed in KCAL's favor had it made the tape the story, creating what is sometimes called a "meta-use" in which the user comments on the original work itself rather than its subject matter.<sup>189</sup> Instead KCAL used the footage just as if it had paid a licensing fee, presenting the tape as its own, adding only its logo and a voice-over.<sup>190</sup> The court found that this use added nothing "new or transformative to what made the LANS work valuable—a clear, visual recording of the beating itself."<sup>191</sup> Additionally, the court noted KCAL's bad faith in using an unauthorized copy after LANS's refusal to grant a license, and in superimposing its own logo on that infringing copy.<sup>192</sup>

Continuing its factor-by-factor analysis, the court found that the nature of the work was primarily factual and informational, which weighed heavily in KCAL's favor.<sup>193</sup> The court also noted that although KCAL used only a small amount of the entire tape, it chose the most valuable part, shifting the balance away from a finding of fair use.<sup>194</sup> As to the effect on LANS's market, the court noted that,

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<sup>183</sup> *KCAL-TV*, 108 F.3d at 1120-21.

<sup>184</sup> *Id.* at 1120.

<sup>185</sup> *Id.*

<sup>186</sup> *Id.* at 1123.

<sup>187</sup> *Id.* at 1121.

<sup>188</sup> *Id.*

<sup>189</sup> *Id.* at 1121-22; Bunker, *supra* note 16, at 325 (commenting that courts seem to favor meta-uses in which the user comments on the original, rather than merely on what the original depicts).

<sup>190</sup> *KCAL-TV*, 108 F.3d at 1122.

<sup>191</sup> *Id.*

<sup>192</sup> *Id.*

<sup>193</sup> *Id.*

<sup>194</sup> *Id.*

should such use become widespread, it would reduce the incentive to create news footage.<sup>195</sup> Although KCAL's use could be viewed as in the public interest because of the significance of the content of the footage, the court noted that there was no evidence that the LANS tape was the only footage of the Denny beating.<sup>196</sup> The court also noted that even though the tape had been previously published and licensed, there was no evidence that KCAL's use did not have an impact on the market for the footage.<sup>197</sup> Accordingly, the court reversed the district court's holding that fair use was the only reasonable conclusion.<sup>198</sup>

*Los Angeles News Service v. Reuters*

LANS also licensed use of the Denny tape to NBC, which broadcast the footage on the *Today* show.<sup>199</sup> Reuters and Visnews had a news supply agreement with NBC News Overseas.<sup>200</sup> When NBC broadcast the footage it simultaneously transmitted to Visnews in New York, which made a copy and transmitted it to overseas subscribers in Europe and Africa, and to the New York office of the European Broadcasting Union.<sup>201</sup> The European Broadcasting Union made its own copy and transmitted it to Reuters's London branch.<sup>202</sup> The Ninth Circuit upheld the lower court's rejection of Reuters's and Visnews's fair use defense.<sup>203</sup> The court recognized the news reporting purpose of the secondary use, but noted that the use was "not very transformative."<sup>204</sup> Reuters added nothing to the original work, and yet profited from it "without paying the customary price."<sup>205</sup> Additionally, the court found that Reuters's use was commercial, in that it provided the footage to other media outlets for a fee, making LANS a competitor with Reuters in the licensing of its own work.<sup>206</sup> This necessarily affected LANS's ability to market and to profit from the footage.<sup>207</sup> Thus, Reuters's actions stood to have "a substantially

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<sup>195</sup> *Id.* at 1123.

<sup>196</sup> *Id.*

<sup>197</sup> *Id.*

<sup>198</sup> *Id.*

<sup>199</sup> *L.A. News Serv. v. Reuters Television Int'l, Ltd.*, 149 F.3d 987, 980 (9th Cir. 1998).

<sup>200</sup> *Id.*

<sup>201</sup> *Id.*

<sup>202</sup> *Id.*

<sup>203</sup> *Id.* at 997.

<sup>204</sup> *Id.* at 993.

<sup>205</sup> *Id.* at 994 (quoting *Harper & Row, Publishers, Inc. v. Nation Enters.*, 471 U.S. 539, 562 (1985)).

<sup>206</sup> *Reuters*, 149 F.3d at 994.

<sup>207</sup> *Id.*

adverse impact” on the market for LANS’s footage.<sup>208</sup> Finding that only the factual nature of the original work weighed in Reuters’s favor, the court ruled that the district court had correctly held that the fair use defense did not apply.<sup>209</sup>

*Los Angeles News Service v. CBS*

LANS offered to license the riot footage, totaling approximately nine minutes, to Group W Newsfeed, a video news service owned at that time by Westinghouse.<sup>210</sup> Group W declined.<sup>211</sup> LANS discovered later that Group W had distributed four of LANS’s pieces covering the riot.<sup>212</sup> One of the recipients of the unauthorized footage was Court TV.<sup>213</sup> The network used a clip from the Denny footage to promote its coverage of the trial of Denny’s assailants, and incorporated some of the footage into a montage which introduced one of its programs, “Prime Time Justice.”<sup>214</sup> The clip was two seconds long, tinted orange and gray, and appeared momentarily in the changing background of an orange clock design.<sup>215</sup> Court TV also used the same clip to promote its coverage of the Damien Williams and Henry Watson trial.<sup>216</sup>

Although the court emphasized that “mere rebroadcast” is not transformative,<sup>217</sup> the Ninth Circuit agreed that Court TV’s use was fair.<sup>218</sup> Court TV’s use of a short clip combined with updates from the trial of Denny’s attackers was not transformative because it did not change the essential purpose of the footage, that of depicting the attack.<sup>219</sup> The use of the clip in the Prime Time Justice montage, however, was found to “at least plausibly incorporate[] the element of creativity beyond mere republication, [] serv[ing] some purpose

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<sup>208</sup> *Id.*

<sup>209</sup> *Id.* at 994-95.

<sup>210</sup> *L.A. News Serv. v. CBS Broad., Inc.*, 305 F.3d 924, 929 (9th Cir. 2002).

<sup>211</sup> *Id.*

<sup>212</sup> *Id.*

<sup>213</sup> *Id.*

<sup>214</sup> *Id.*

<sup>215</sup> *Id.* at 929-30; Appellee’s Answering Brief at 5, *L.A. News Serv. v. CBS Broad., Inc.*, 305 F.3d 924 (9th Cir. 2002) (Nos. 00-56470, 00-57000), 2001 WL 34091295.

<sup>216</sup> *CBS*, 305 F.3d at 929.

<sup>217</sup> *Id.* at 938.

<sup>218</sup> *Id.* at 942.

<sup>219</sup> *Id.* at 939.

beyond newsworthiness.”<sup>220</sup> The court noted that this use was commercial because it was used to promote Court TV’s coverage, but that the impact of the commercial use was reduced by the fact that Court TV had transformed the footage for the opening montage.<sup>221</sup> The court found that the use of the footage in the teasers was closer to news reporting, and thus less commercial, but that the use was also less transformative because Court TV had done nothing to alter the footage itself.<sup>222</sup> The significance of the commercial use was further discounted when the court reasoned that, because the teasers were used to promote coverage of the Williams trial and not of the Denny beating, LANS and Court TV were not in direct competition.<sup>223</sup> The purpose and character of Court TV’s use thus weighed slightly in favor of fair use.<sup>224</sup>

The court found that the nature of the original work weighed in favor of fair use as in the prior LANS cases,<sup>225</sup> and that the amount used—two to three seconds out of nine minutes of footage—was neutral, especially in light of the length of the clips used by Reuters—forty-five seconds which LANS had also claimed to be the heart of the work.<sup>226</sup> In analyzing the fourth factor, the court found that the use of the clip in the montage was unlikely to have a negative effect on the market for the work because it was transformative.<sup>227</sup> The rebroadcast of the clip during the trial coverage was a closer call, as the three-second clip was used at a time when a market for the Denny footage had reemerged.<sup>228</sup> The court was swayed by the fact that Court TV and LANS operated in “significantly different market[s],” and that the amount of footage used was much less than the forty-five seconds that LANS had claimed in *Reuters* deserved to be considered the heart of the work.<sup>229</sup> The court reasoned that most of LANS’s licensees would use the work in news coverage, which would require far more than the two to three seconds used by Court TV, and that the market for the entire work was already saturated.<sup>230</sup> Having found that none of the four factors weighed against fair use, the court upheld the district court’s finding of fair use.<sup>231</sup>

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<sup>220</sup> *Id.*

<sup>221</sup> *Id.* at 939-40.

<sup>222</sup> *Id.* at 940.

<sup>223</sup> *Id.*

<sup>224</sup> *Id.*

<sup>225</sup> *Id.*

<sup>226</sup> *Id.* at 940-41.

<sup>227</sup> *Id.* at 941.

<sup>228</sup> *Id.* at 941-42.

<sup>229</sup> *Id.* at 942.

<sup>230</sup> *Id.*

<sup>231</sup> *Id.*

The LANS cases illustrate that the lower courts' dilution of the term "transformative use" does not disadvantage professional producers of news content. The application of the fair use doctrine to disputes between competitors continues to provide protection against unscrupulous business tactics while allowing for reasonable use of the original work. Courts tend not to apply the same analysis, however, when evaluating copying by non-competitors. There, because the work is moved from a non-news to a news context, the courts' efforts to promote uses they deem socially beneficial leads them to dilute the definition of transformation in order to find the use fair. This functional view of transformation limits the rights of non-news photographers where the newsworthiness of a work emerges after its creation and initial publication.

B. How courts treat copying of works by professionals who are not competitors.

Where a photograph or film clip was not originally intended to be news, courts tend to find the infringing work transformative based solely on the transfer of the work to a news medium or context. Combined with the gravitational pull a finding of transformative use exerts on the remaining factors, the dilution of "transformative use" makes a finding of fair use almost a foregone conclusion. This holds true even when a news agency uses an entire work without adding "new information, new aesthetics, new insights [or] understandings"<sup>232</sup> In some cases, the accused use does more than simply copy the work and the work itself is the subject of the story, much like a work of fiction may be the subject of a book review.<sup>233</sup> In others, however, the work was originally intended to illustrate its subject matter, and serves exactly the same essential purpose in its infringing use.<sup>234</sup> Despite this, courts are likely both to define the purpose of the work more narrowly and to find a change in purpose to be transformative without requiring any change to the work itself, allowing news organizations to publish entire works created by non-competitors under the cover of fair use.

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<sup>232</sup> Leval, *supra* note 32, at 1111.

<sup>233</sup> Núñez v. Caribbean Int'l News Corp., 235 F.3d 18, 22 (1st Cir. 2000).

<sup>234</sup> Mathieson v. Associated Press, No. 90 Civ. 6945 (LMM), 1992 WL 164447, at \*1-\*2 (S.D.N.Y. June 25, 1992); *see also* Four Navy SEALS v. Associated Press, 413 F. Supp. 2d 1136, 1141-42 (S.D. Cal. 2005).

*Mathieson v. Associated Press*

A pre-*Campbell* case, *Mathieson v. Associated Press*, illustrates how the functional interpretation of the first factor favored the news media even before its articulation as part of the transformative use analysis. There, the District Court for the Southern District of New York granted summary judgment to the Associated Press, holding that its use of professional photographs originally published in a corporate brochure was fair because the use illustrated a news story.<sup>235</sup> Greg Mathieson did a photo shoot for Guardian Technology International's promotion of its line of body armor.<sup>236</sup> Twenty of these photographs were included in the corporation's sales brochure, including two cover shots.<sup>237</sup> One of these photographs was of Oliver North, who had personally endorsed the line, and the other was a composite photograph showing a model wearing a bulletproof vest.<sup>238</sup> The photo had been digitally altered so that, on one half of the model's torso, the armor was exposed; while on the other half, the armor was covered by a shirt.<sup>239</sup> In April 1990, the Associated Press (AP) disseminated a story covering the body armor, focusing on the manufacturer's association with Colonel North.<sup>240</sup> AP accompanied the story with the two cover shots taken by Mathieson, on which it affixed its own copyright symbol.<sup>241</sup>

AP admitted to copying and distributing the photographs, but claimed fair use based on their use as part of a news story.<sup>242</sup> The court agreed, stating that "the characterization of defendant's use as news-related carries great weight in the analysis of fair use."<sup>243</sup> The court emphasized that AP had used the photographs to illustrate the nature of the business and North's involvement.<sup>244</sup> When Mathieson pointed out that, in addition to using the photographs in conjunction with the news story, AP had made copies available for sale to the public in its subsidiary company, World Wide Photos,<sup>245</sup> the court responded that Mathieson could not object as long as AP sold his photos as part of its news reporting activities, "an expressly

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<sup>235</sup> *Mathieson*, 1992 WL 164447, at \*9.

<sup>236</sup> *Id.* at \*1.

<sup>237</sup> *Id.*

<sup>238</sup> *Id.* at \*6.

<sup>239</sup> *Id.*

<sup>240</sup> *Id.* at \*1.

<sup>241</sup> *Id.*

<sup>242</sup> *Id.* at \*2.

<sup>243</sup> *Id.* at \*5.

<sup>244</sup> *Id.* at \*3.

<sup>245</sup> *Id.* at \*1.

permissible fair use.”<sup>246</sup> When Mathieson argued that AP’s use was commercial, the court answered that, when the use is news reporting, that fact “dispels the notion of theft or of piracy which has characterized other actions.”<sup>247</sup> Upon finding that AP’s use of the photographs in news reporting weighted the first factor heavily in its favor, the court informed Mathieson that it “must lean decidedly in the direction of finding fair use even as it looks at the other three factors,”<sup>248</sup> and then did so.

The court stated that in order for the second factor to weigh against fair use, the original work must be “creative, imaginative, and original.”<sup>249</sup> Accordingly, the court found that the creative nature of the composite photograph weighed against fair use, while the lack of creativity in the head shot of Oliver North weighed for fair use.<sup>250</sup> The court found that even if each photograph were considered to be an independent and complete work, rather than a portion of the promotional brochure, the amount and substantiality of use did not weigh against fair use because the photos had been used in conjunction with news reporting.<sup>251</sup> Additionally, the court pointed out that Mathieson had failed to allege an actual instance in which a copy had been sold through World Wide Photos,<sup>252</sup> requiring a showing of actual harm, rather than merely that harm was likely to result if such use should become widespread.<sup>253</sup> The court found that Mathieson failed to show that AP’s use had harmed the market for the two photographs—ignoring the market for stock photographs—and ruled that the fourth factor weighed in favor of fair use.<sup>254</sup>

Although the district court issued its opinion prior to the Supreme Court’s endorsement of the transformative use inquiry and its later dilution by lower courts, the court’s reasoning anticipates later opinions in which the first factor of the fair use analysis falls in favor of fair use where a work is transferred to a news medium, and in

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<sup>246</sup> *Id.* at \*3.

<sup>247</sup> *Id.* at \*5.

<sup>248</sup> *Id.* at \*6.

<sup>249</sup> *Id.* (quoting *MCA, Inc. v. Wilson*, 677 F.2d 180, 182 (2d Cir. 1981)).

<sup>250</sup> *Mathieson*, 1992 WL 164447, at \*7.

<sup>251</sup> *Id.* at \*8.

<sup>252</sup> *Id.* at \*4.

<sup>253</sup> *Harper & Row, Publishers, Inc. v. Nation Enters.*, 471 U.S. 539, 568 (1985).

<sup>254</sup> *Mathieson*, 1992 WL 164447, at \*9.

which such a finding shifts the balance of the other factors in favor of fair use, even before the court conducts its factor-by-factor analysis.<sup>255</sup>

*Psihoyos v. National Examiner*

In contrast to its holding in *Mathieson*, the same district court found a similar use was not fair when the *National Examiner*, a supermarket tabloid, used a copyrighted photograph in a feature story.<sup>256</sup> The *Examiner* ran a story entitled “CAR-RAZY: Take a Ride on the Wild Side in Kookie Vehicles.”<sup>257</sup> It prominently featured Louis Psihoyos’s copyrighted photograph of Larry Fuentes and his decorative Cadillac.<sup>258</sup> When the *Examiner* claimed that its use was transformative because the photo was used in news reporting, the court stated that “the mere fact that the photo depicts a newsworthy item does not justify copying it entirely without permission.”<sup>259</sup>

Having found that the first factor weighed against fair use, the court conducted a thorough analysis of the remaining factors. Despite the *Examiner*’s argument that the work was not creative because it did nothing more than depict Fuentes and his Cadillac, the court considered Psihoyos’s choice of background and positioning of the car, finding that the photograph was creative.<sup>260</sup> Although the *Examiner* argued that its use of nearly the entire photograph did not weigh against fair use because the amount of the photograph used was necessary for its news reporting purpose, the court rejected this reasoning.<sup>261</sup> Using the entire work might have been acceptable if the purpose of the article was to comment on Psihoyos’s photography, but because the *National Examiner* had reported on the subject of the photograph itself, the court found that the amount of the use was designed to save the *Examiner* the trouble of creating its own photo, and thus weighed against fair use.<sup>262</sup>

Turning to the fourth factor, the court noted that Psihoyos was not required to show that he had experienced actual loss due to the

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<sup>255</sup> *Id.* at \*6 (“Because defendant’s use of plaintiff’s photos clearly falls within the permissible use category of ‘news reporting,’ the Court must lean decidedly in the direction of finding fair use even as it looks at the other three factors.”).

<sup>256</sup> *Psihoyos v. National Examiner*, No. 97 Civ. 7624(JSM), 1998 WL 336655, at \*6 (S.D.N.Y. June 22, 1998).

<sup>257</sup> *Id.* at \*1.

<sup>258</sup> *Id.*

<sup>259</sup> *Id.* at \*4.

<sup>260</sup> *Id.*; see, e.g., *Mannion v. Coors Brewing Co.*, 377 F. Supp. 2d 444, 451-53 (S.D.N.Y. 2005) (finding choices in the creation of the subject of a photograph and in its rendition as elements of creative expression).

<sup>261</sup> *Psihoyos*, 1998 WL 336655, at \*4.

<sup>262</sup> *Id.*

*Examiner's* use.<sup>263</sup> Responding to the *Examiner's* contention that its use would increase demand for Psihoyos's work, the court stated that even if that were true, it did not account for the licensing fee to which Psihoyos was entitled for the *Examiner's* unauthorized use.<sup>264</sup> The court also noted that the *Examiner's* publication of the photograph as a full-page spread was a market substitute for a derivative work of the original as a poster, despite the likely difference in quality.<sup>265</sup> Finding that all four factors weighed against fair use, the court denied the *Examiner's* motion for summary judgment.<sup>266</sup>

A comparison to the same court's holding in *Mathieson*, where the Associated Press likewise did not comment on the original work, suggests that it is the identity of the defendant that primarily swayed the court's decision, and that the outcome may have been different had the *National Examiner* been a conventional newspaper rather than a tabloid. Both news organizations used entire original works without paying a customary licensing fee, and in both works the court recognized the creativity in the original photographs. However, because the *Examiner* used Psihoyos's photograph in a feature article rather than as hard news, its use was not given the same deference that the unauthorized publication of Mathieson's photograph received. This, in turn, affected the court's approach to the remaining factors, even to the extent of dispensing with the requirement of actual harm that it had insisted on in *Mathieson*. This indicates that non-traditional news outlets will have to do more than show a news purpose in order to have their use declared transformative.

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<sup>263</sup> *Id.* at \*5.

<sup>264</sup> *Id.*

<sup>265</sup> *Id.*

<sup>266</sup> *Id.* at \*6.

*Núñez v. Caribbean International News Corp.*

The First Circuit's holding in *Núñez v. Caribbean International* has been cited repeatedly in support of the fair use of images based upon a change in purpose alone.<sup>267</sup> The plaintiff, Sixto Núñez, was a professional photographer who had taken photos of Joyce Giraud for her modeling portfolio.<sup>268</sup> After Giraud won Miss Puerto Rico Universe, some of Núñez's photographs portraying Giraud in semi-nude poses were reportedly circulated by rivals in an effort to unseat her.<sup>269</sup> A local television station published the photographs and polled citizens to determine if they considered the photos pornographic.<sup>270</sup> Two stations interviewed Giraud regarding her fitness to be Miss Puerto Rico.<sup>271</sup> After obtaining copies of the photos, *El Vocero*, a local newspaper, published several articles accompanied by three of Núñez's photographs without permission.<sup>272</sup>

Based primarily on its finding that placing the modeling portraits in a news context was transformative, the First Circuit agreed with *El Vocero* that its use was a fair one.<sup>273</sup> The court conceded that, in placing photos of the semi-nude Giraud on its front page, *El Vocero* was seeking to increase its circulation.<sup>274</sup> This commercial purpose, however, was tempered by the need to inform the public about the details of the controversy surrounding Giraud by placing the articles in context.<sup>275</sup> The court distinguished the copying in *Harper & Row*, where *The Nation* used unauthorized access to President Ford's memoirs to scoop a competing news organization.<sup>276</sup> Unlike *The Nation*, *El Vocero* did not usurp Núñez's right of first publication, and Núñez did not compete in the same market with *El Vocero*.<sup>277</sup>

The court found that the first factor favored fair use because *El Vocero* had used the photographs as news, whereas Núñez had created

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<sup>267</sup> Bill Graham Archives v. Dorling Kindersley Ltd., 448 F.3d 605, 613 (2d Cir. 2006); Perfect 10, Inc. v. Amazon.com, Inc., 487 F.3d 701, 722 (9th Cir.), amended by 508 F.3d 1146 (9th Cir. 2007); Kelly v. Arriba Soft Corp., 336 F.3d 811, 819-20 (9th Cir. 2003).

<sup>268</sup> *Núñez v. Caribbean Int'l News Corp.*, 235 F.3d 18, 21 (1st Cir. 2000); Miss Puerto Rico: Joyce Giraud: Beauty Queen Fights to Keep Title, <http://www.samsloan.com/miss-pr.htm> (last visited Apr. 3, 2008).

<sup>269</sup> Miss Puerto Rico: Joyce Giraud: Beauty Queen Fights to Keep Title, <http://www.samsloan.com/miss-pr.htm> (last visited Apr. 3, 2008).

<sup>270</sup> *Núñez*, 235 F.3d at 21.

<sup>271</sup> *Id.*

<sup>272</sup> *Id.*

<sup>273</sup> *Id.* at 25.

<sup>274</sup> *Id.* at 22.

<sup>275</sup> *Id.*

<sup>276</sup> *Id.* at 22-23.

<sup>277</sup> *Id.* at 23.

the photos for use in a modeling portfolio.<sup>278</sup> The court was careful to point out that it was not the newsworthiness of the photographs that justified *El Vocero*'s unauthorized use, but the fact that the use with its accompanying commentary had not superseded Núñez's original purpose of portraying Giraud in a manner designed to promote her modeling career, but instead had given the photographs new meaning and purpose.<sup>279</sup> The court did not take into account that the photos themselves, like the eyeglasses in the Gap advertisement,<sup>280</sup> still performed the same essential function of depicting Giraud. Instead, the court held that the placement of the photographs in a news context was transformative, and that this was enough to counteract the exploitive use of the photos by *El Vocero*, so that the first factor was neutral or slightly in favor of fair use.<sup>281</sup>

The court's findings on the remaining factors were shaped by its belief that the use of the photographs was transformative. Although, as posed portraits designed for a modeling portfolio, there was creative expression in both the subject matter and the rendition of the photographs, the court found the nature of the works to be a neutral factor.<sup>282</sup> It reasoned that, because Núñez's creative expression was used to showcase Giraud's modeling abilities rather than his own ideas or emotions, the creative nature of the portraits did not weigh against fair use.<sup>283</sup> Additionally, because the court agreed with *El Vocero* that its publication of all three pictures copied in their entirety, was necessary to illustrate the news stories, it found that the amount and substantiality of use was a neutral factor as well.<sup>284</sup> The court did not address the fact that the public had already seen the pictures when they were broadcast on local television stations,<sup>285</sup> nor whether the same need to inform would justify their unauthorized publication were the photos truly scandalous, as was the case in the Vanessa Williams controversy.<sup>286</sup>

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<sup>278</sup> *Id.*

<sup>279</sup> *Id.*

<sup>280</sup> On *Davis v. The Gap, Inc.*, 246 F.3d 152, 174 (2d Cir. 2001).

<sup>281</sup> *Núñez*, 235 F.3d at 23.

<sup>282</sup> *Id.*

<sup>283</sup> *Id.*

<sup>284</sup> *Id.* at 24.

<sup>285</sup> *Id.* at 21.

<sup>286</sup> Hilary Levey, *Here She Is...And There She Goes?*, 6 CONTEXTS 70, 71 (2007).

Lastly, the court examined the effect of the use on the market.<sup>287</sup> The court recognized that it was the effect on the market for the specific works, and not on Núñez's services as a photographer, that was at issue.<sup>288</sup> Núñez had previously distributed the photographs among the modeling community in order to promote Giraud as a model and himself as a photographer.<sup>289</sup> The court reasoned that the publicity created by *El Vocero's* use would likely increase demand for the portfolio, and that, even if the use became widespread, the availability of newsprint photographs would not reduce demand for higher-quality prints.<sup>290</sup> Although the court noted that the use had interfered with the potential sale of the photographs to newspapers, it found the "market for professional photographs publishable only due to the controversy of the photograph itself" to be too speculative to weigh against fair use.<sup>291</sup> This finding was made despite the fact that Giraud was already something of a local celebrity.<sup>292</sup> Finding that the only effect on the market was to increase demand for the photographs, and discounting any right that Núñez might have to exploit the increased demand for the photographs at issue, the court ruled that the fourth factor favored fair use.<sup>293</sup> Upon finding all the factors either neutral or favoring fair use, the court ruled in favor of *El Vocero*.<sup>294</sup>

The First Circuit emphasized the functional and contextual change to Núñez's photos: "[W]hat is important here is that plaintiff's photographs were originally intended to appear in modeling portfolios, not in the newspaper; the former use, not the latter, motivated the creation of the work."<sup>295</sup> The court's decision essentially endorses the unauthorized use of newsworthy photographs as long as the photographs were not originally intended to be news, and denies the creator of those photographs the opportunity to profit from their notoriety by auctioning exclusive rights to the highest bidder.

C. Applying the same analysis to the growing number of amateur news reporters.

So far, there have been few copyright cases in which amateurs have challenged the use of their works by news agencies. With the

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<sup>287</sup> *Núñez*, 235 F.3d at 24.

<sup>288</sup> *Id.*

<sup>289</sup> *Id.* at 21.

<sup>290</sup> *Id.* at 25.

<sup>291</sup> *Id.*

<sup>292</sup> *The Joyce of Life*, OPEN YOUR EYES MAGAZINE, 2003, <http://www.oyemag.com/joyce.html>.

<sup>293</sup> *Núñez*, 235 F.3d at 25.

<sup>294</sup> *Id.*

<sup>295</sup> *Id.* at 23.

pervasive presence of camera phones, and the news media's increasing reliance upon amateur footage, conflicts over whether unauthorized use is fair are bound to emerge. If the lower courts continue to apply a diluted definition of transformative use, and to allow a finding of transformation to shape their findings on the remaining factors of the fair use analysis, amateur creators will find that their exclusive Section 106 rights in their images are not so exclusive after all. As the courts' holdings in *Perfect 10*, *Bill Graham*, *Kelly*, *Núñez*, and other cases suggest, news organizations may publish the works of amateurs with impunity by merely claiming that they have "transformed" the original work by placing it in a socially beneficial context, i.e., "the news." This has the potential to dramatically reduce the monetary incentive for amateurs to create and disseminate these works. This is best illustrated by a look at how some recent publications of amateur footage would be analyzed under the current fair use analysis.

*Four Navy SEALs v. Associated Press*

In December 2004, Seth Hettena, a reporter for the Associated Press, downloaded pictures from an Internet "smugmug" account, which had been posted there by the wife of a Navy SEAL, believing that the account could not be accessed by the general public.<sup>296</sup> The thirteen photos depicted Navy SEALs with Iraqi captives.<sup>297</sup> Hettena wrote an article on prisoner abuse by Navy SEALs, which was published by nearly every American newspaper, accompanied by some of the photos from the smugmug account.<sup>298</sup> Shortly after the publication of the photographs, four unnamed Navy SEALs and the Navy wife who had maintained the smugmug account filed a complaint against the Associated Press, claiming copyright infringement and three state law claims for violation of privacy.<sup>299</sup>

The district court failed to reach the issue of whether AP's infringement was fair because it found that the plaintiffs had failed to plead ownership of a valid copyright.<sup>300</sup> Even if the plaintiffs had met this requirement, however, it is highly likely that the court would have found the infringing use fair. The Associated Press had appropriated

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<sup>296</sup> *Four Navy SEALs v. Associated Press*, 413 F. Supp. 2d 1136, 1141 (S.D. Cal. 2005).

<sup>297</sup> *Id.*

<sup>298</sup> *Id.*

<sup>299</sup> *Id.* at 1142.

<sup>300</sup> *Id.* at 1148.

images that were meant for personal use and had turned them into news, a socially beneficial use.<sup>301</sup> According to the Ninth Circuit's reasoning in *Kelly* and *Perfect 10*, a new use which provides a social benefit—even more so than parody—is transformative because it provides a new use for the original work.<sup>302</sup> Under the reasoning of the First Circuit in *Núñez*, the shift in context, from a personal website where the photos memorialized events for friends and family to newspapers where they illustrated a story on prisoner abuse, is enough to make the secondary use by the Associated Press transformative because the creator of the photographs did not originally intend for them to appear in the press.<sup>303</sup>

After finding the use transformative, the court would interpret the remaining factors in light of this finding, weighting the total analysis in favor of fair use. Thus, in considering the nature and character of the original photographs, the court would discount the fact that many of the pictures were posed<sup>304</sup> and entitled to greater protection under copyright for their greater creative expression,<sup>305</sup> in light of its finding of transformative use and the photographs' prior publication on the Internet.<sup>306</sup> The court would likely hold that the amount and substantiality of the portion used was also a neutral factor because the use of the entirety of each photograph was reasonable and necessary for AP's news reporting purpose.<sup>307</sup> The court would also likely discount the effect on the market and on the value of the work, reasoning that because the secondary use was transformative, it necessarily is a non-superseding use, and, therefore, outside of the plaintiff's potential market.<sup>308</sup>

By contrast, under a traditional fair use analysis, while the Associated Press's use would be considered a preferred use as news reporting and commentary,<sup>309</sup> it would not be considered transformative merely because the photographs had been transferred

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<sup>301</sup> *Id.* at 1146.

<sup>302</sup> *Perfect 10, Inc. v. Amazon.com, Inc.*, 508 F.3d 1146, 1165 (9th Cir. 2007) (“Indeed, a search engine may be more transformative than a parody because a search engine provides an entirely new use of the original work, while a parody typically has the same entertainment purpose as the original work.”); *Kelly v. Arriba Soft Corp.*, 336 F.3d 811, 819 (9th Cir. 2003).

<sup>303</sup> *Núñez v. Caribbean Int'l News Corp.*, 235 F.3d 18, 23 (1st Cir. 2000).

<sup>304</sup> *Four Navy SEALS*, 413 F. Supp. 2d at 1141.

<sup>305</sup> *Mannion v. Coors Brewing Co.*, 377 F. Supp. 2d 444, 453 (S.D.N.Y. 2005).

<sup>306</sup> *Perfect 10*, 508 F.3d at 1166-67.

<sup>307</sup> *Id.* at 724; *Kelly*, 336 F.3d at 821; *Bill Graham Archives v. Dorling Kindersley Ltd.*, 448 F.3d 605, 613 (2d Cir. 2006).

<sup>308</sup> *Perfect 10*, 508 F.3d at 1167-68.

<sup>309</sup> 17 U.S.C. § 107 (2006).

into a different medium with no changes to the photos themselves.<sup>310</sup> The court would also consider Seth Hettena's bad faith in taking photographs from a website that he had reason to believe was private,<sup>311</sup> and the Associated Press's commercial use of the photographs.<sup>312</sup> The court might also view the AP's use as adding nothing that made the photographs valuable—much like KCAL's rebroadcast of the Denny video. Based upon these considerations, the court would likely find the use non-transformative and first-factor neutral.

In weighing the remaining factors, the creative nature of the photographs would carry greater weight, as would the fact that the photographs had not been released to the public. Although the works themselves may not be the type of work that society has an interest in promoting, they do fall within the creative original expression protected by the Copyright Act. The nature and character of the use would thus weigh in favor of the plaintiff. Under a traditional fair use analysis, the court considers that where the defendant has used an entire work, it is likely that the secondary use will supersede the original in the market.<sup>313</sup> The amount and substantiality of use would, therefore, weigh against fair use as well. Finally, the court would consider the effect of the use on the market for and value of the original. The Supreme Court has remarked that this factor is the most significant because it directly impacts the incentive to create.<sup>314</sup> Worldwide news circulation of photographs by military personnel of themselves that engendered threats of legal action and physical harm—like parody of one's own work—is not a market that the creators of the photographs were likely to enter.<sup>315</sup> This factor would weigh in favor of fair use.

Weighed together in light of the purpose of copyright, a finding of fair use is a closer call. This factor-by-factor analysis is much less likely to disincentivize amateur photographers by making

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<sup>310</sup> *A&M Records, Inc. v. Napster, Inc.*, 239 F.3d 1004, 1015 (9th Cir. 2001); *Infinity Broad. Corp. v. Kirkwood*, 150 F.3d 104, 108 (2d Cir. 1998).

<sup>311</sup> *Harper & Row, Publishers, Inc. v. Nation Enters.*, 471 U.S. 539, 562-63 (1985).

<sup>312</sup> 17 U.S.C. § 107(1) (2006).

<sup>313</sup> *Hustler Magazine, Inc. v. Moral Majority, Inc.*, 796 F.2d 1148, 1155 (9th Cir. 1986).

<sup>314</sup> *Sony Corp. of Am. v. Universal City Studios, Inc.*, 464 U.S. 417, 450 (1984); *Harper & Row*, 471 U.S. at 566 (“This last factor is undoubtedly the single most important element of fair use.”).

<sup>315</sup> *Campbell v. Acuff-Rose Music, Inc.*, 510 U.S. 569, 591-92 (1994).

unauthorized copying by news organizations nearly *per se* fair. If the market is one which the photographer might foreseeably enter, his right to profit from the newsworthiness of his photograph is protected. Furthermore, the enforcement of these rights encourages news organizations to create licensing schemes, such as those created by Reuters and Yahoo!, rather than endorses the tempting practice of cruising the Internet for free content to save news organizations the trouble of creating their own. Such licensing schemes, in turn, will increase the incentive for amateurs to create content that is socially beneficial.

*McClatchey v. Associated Press*

Where an amateur photographer immediately markets her work as news, her rights are more likely to be protected against infringing news organizations. Valencia McClatchey witnessed the crash of Flight 93 and photographed the mushroom cloud left by its impact.<sup>316</sup> Her photograph has been included in various exhibits, and McClatchey sold copies of the photograph, donating her profits to the Todd Beamer Foundation.<sup>317</sup> One year after the crash, AP reporter Charles Sheehan decided to write an article about McClatchey and her photograph, and sent an AP photographer to her home to take photos of McClatchey holding the “End of Serenity” photograph.<sup>318</sup> McClatchey claimed that the photographer took photos of the work itself without her permission.<sup>319</sup> The article and photograph depicting only “End of Serenity” were then distributed separately to AP’s PhotoStream member news organizations.<sup>320</sup> When McClatchey filed suit, AP brought a motion for summary judgment based on its fair use defense.<sup>321</sup>

Here, however, the court found that AP’s use was more commercial than it was educational.<sup>322</sup> The original photograph had lost much of its newsworthiness in the year following September 11, 2001, because the crash of Flight 93 had already received extensive coverage.<sup>323</sup> Additionally, AP had distributed the photo apart from the

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<sup>316</sup> *McClatchey v. Associated Press*, No. 3:05-CV-145, 2007 WL 776103, at \*1 (W.D. Pa. Mar. 9, 2007).

<sup>317</sup> *Id.* at \*1; Milan Simonich, *Judge Preserves Lawsuit Over Sept. 11 Photo*, PITTSBURGH POST-GAZETTE, Apr. 3, 2007, at B1, available at <http://www.post-gazette.com/pg/07093/774585-85.stm>.

<sup>318</sup> *McClatchey*, 2007 WL 776103, at \*2.

<sup>319</sup> *Id.*; Simonich, *supra* note 317.

<sup>320</sup> *McClatchey*, 2007 WL 776103, at \*2.

<sup>321</sup> *Id.* at \*3.

<sup>322</sup> *Id.*

<sup>323</sup> *Id.*

article on McClatchey.<sup>324</sup> The court also noted that AP did not change the photograph in any way, but merely copied it and made it available to its subscribers without paying the usual licensing fees.<sup>325</sup> Although the market for the photograph was not large, the court found that AP had distributed it to McClatchey's most likely customers by making it available to approximately 2,000 PhotoStream member news organizations.<sup>326</sup> The court concluded that it could not find fair use as a matter of law.<sup>327</sup>

The court's holding appears to indicate that media savvy amateurs who post their newsworthy photos on GroundReport<sup>328</sup> or Citizen Image,<sup>329</sup> where they have an opportunity to market their photographs as news, have a greater chance of having their rights protected than do amateurs who post on MySpace or YouTube. As *Psihoyos* and *Mathieson* demonstrate, the courts do not view all news outlets equally.

### *Virginia Tech*

The coverage of the April 16, 2007, shooting at Virginia Tech relied heavily on content provided by students. Dan Abrams, general manager of MSNBC, commented: "On this story, the Internet and digital technology have been a driving force like never before."<sup>330</sup> Before CNN's reporters had arrived on the scene, graduate student Jamal Albarghouti, camera phone in hand, was running toward the sound of gunshots.<sup>331</sup> CNN aired his footage and referred to him throughout the day as "our I-reporter."<sup>332</sup> CNN, like many networks,

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<sup>324</sup> *Id.*

<sup>325</sup> *Id.*

<sup>326</sup> *Id.* at \*2-3.

<sup>327</sup> *Id.* at \*4.

<sup>328</sup> <http://www.groundreport.com> (revenue-sharing internet site which features user-submitted news and opinion articles).

<sup>329</sup> <http://www.citizenimage.com> (provides marketplace for selling pictures online).

<sup>330</sup> David Zurawik, *Eyewitness Testimonies and Footage Dominate News*, BALTIMORE SUN, Apr. 17, 2007, available at <http://www.baltimoresun.com/news/nationworld/bal-te.media17apr17,0,7252873.story?coll=bal-nationworld-headlines> (last visited Apr. 6, 2008).

<sup>331</sup> *Id.*; *On the Beat with Citizen Reporters*, THE AGE (Australia), May 24, 2007, available at <http://www.theage.com.au/articles/2007/05/23/1179601421038.html> (last visited Apr. 6, 2008); Gray, *supra* note 6.

<sup>332</sup> Gray, *supra* note 6.

solicits reports, commentary, or images.<sup>333</sup> CNN specifies that, by submitting content, authors agree to a “non-exclusive, perpetual, worldwide license” without payment.<sup>334</sup> Albarghouti, however, was reportedly paid an undisclosed sum for the footage that was viewed by more than 900,000 persons on CNN.com by 3:14 p.m. on the day of the shooting.<sup>335</sup>

In search of their own citizen reporters, other networks trolled MySpace and Facebook for content.<sup>336</sup> Postings by Virginia Tech staff and students on blogs and on social networking sites created a communal record of the event.<sup>337</sup> The students posted pictures and commentary online as part of the community grieving process.<sup>338</sup> The immediate availability of firsthand accounts and images was a source few journalists could resist.<sup>339</sup> One blogger’s entry recording his wounded girlfriend’s experience triggered a slew of postings from news organizations attempting to arrange an interview.<sup>340</sup> Not all students appreciated what they perceived as the voyeurism of the media. One student wrote: “If this is where all the news broadcasters are contacting me from, stop doing it.”<sup>341</sup>

Were a news organization to copy and to broadcast one of those students’ images of his grief-stricken or wounded friends, it appears that, under the current fair use standard, the student’s rights in his original work would be unprotected. If the image was originally posted on a social networking site, the court would likely find that the use in news reporting is transformative even though the image still performed its essential function of depicting the student.<sup>342</sup> The fact

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<sup>333</sup> CNN.com, iReport Assignment Desk, <http://www.ireport.com/community/assignment> (last visited Apr. 6, 2008).

<sup>334</sup> CNN.com, iReport Terms of Use, *supra* note 7 (“By submitting your material, for good and valuable consideration, the sufficiency and receipt of which you hereby acknowledge, you hereby grant to CNN and its affiliates a non-exclusive, perpetual, worldwide license to edit, telecast, rerun, reproduce, use, syndicate, license, print, sublicense, distribute and otherwise exhibit the materials you submit, or any portion thereof, as incorporated in any of their programming or the promotion thereof, in any manner and in any medium or forum, whether now known or hereafter devised, without payment to you or any third party.”).

<sup>335</sup> Gray, *supra* note 6.

<sup>336</sup> Zurawik, *supra* note 330.

<sup>337</sup> K.C. Jones, *Cell Phones, Blogs Enable Live Reporting of Virginia Tech Shooting*, INFORMATIONWEEK, Apr. 16, 2007, <http://www.informationweek.com/news/showArticle.jhtml?articleID=199001329>.

<sup>338</sup> *Id.*

<sup>339</sup> Daniel Terdiman, *Journalists Look to Bloggers for Virginia Tech Story*, ZDNET NEWS, Apr. 16, 2007, [http://zdnet.com/2100-9588\\_22-6176579.html](http://zdnet.com/2100-9588_22-6176579.html).

<sup>340</sup> *Id.*

<sup>341</sup> Zurawik, *supra* note 330.

<sup>342</sup> See *Bill Graham Archives v. Dorling Kindersley Ltd.*, 448 F.3d 605, 609 (2d Cir. 2006) (use transformative where concert poster was originally used for artistic

that the use was commercial would be noted, but would likely have little weight in light of the public interest in the event.<sup>343</sup> The degree of creativity invested in the work or the amount used by the news organization would likely have little or no weight once the secondary use had been found to be transformative.<sup>344</sup> The fact that the image was published on an Internet site to which others have access would also count toward fair use.<sup>345</sup> The court would also likely find that the use had little or no effect on the market because the photographer had not intended to market the image at the time it was created, but instead had created it for personal and social use.<sup>346</sup> If the student provided evidence of the market for such works, including the various solicitations for content on news organization websites and the prominent use of Albarghouti's video, the court may hold that, because the student was unable to show actual damage, the fourth factor does not weigh for the student in light of the news organization's transformative use.<sup>347</sup> Upon a finding that all four

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expression and concert promotion, and secondary use was to illustrate events within a biography); *Kelly v. Arriba Soft Corp.*, 336 F.3d 811, 818-19 (9th Cir. 2006) (artist's photographs transformed when reduced to thumbnail images and used in search engine); *Perfect 10, Inc. v. Amazon.com, Inc.*, 487 F.3d 701, 723 (9th Cir.) (photographs reduced to thumbnails found "significantly transformed" by use in search engine even where copyright owner licensed sale of thumbnail versions of its images), *amended by* 508 F.3d 1146 (9th Cir. 2007). *But see* *On Davis v. Gap, Inc.*, 246 F.3d 152, 174 (2d Cir. 2001) ("nothing transformative" in use of copyrighted eyeglasses in clothing advertisement because eyeglasses still performed essential purpose); *Ringgold v. Black Entm't Television Inc.*, 126 F.3d 70, 78-79 (2d Cir. 1997) ("[i]n no sense is defendants' use transformative" where poster depicting copyrighted quilt was displayed in background during episode of television sitcom); *A&M Records, Inc. v. Napster, Inc.*, 239 F.3d 1004, 1015 (9th Cir. 2001) (conversion of music to MP3 format for transmission over the Internet is not transformative); *Infinity Broad. Corp. v. Kirkwood*, 150 F.3d 104, 108 (2d Cir. 1998) (no transformation where radio programs are broadcast over phone lines to enable advertisers to confirm commercials are being properly aired).

<sup>343</sup> See *Núñez v. Carribbean Int'l News Corp.*, 235 F.3d 18, 22 (1st Cir. 2000).

<sup>344</sup> *Id.* at 23; see generally *Kelly*, 336 F.3d at 820; *Bill Graham Archives*, 448 F.3d at 612 ("second factor may be of limited usefulness where the creative work of art is being used for a transformative purpose.").

<sup>345</sup> See *Perfect 10*, 508 F.3d at 1166-67 (creative nature of photographs weighed only slightly against fair use because works were previously published); *Kelly*, 336 F.3d at 820.

<sup>346</sup> See generally *Núñez*, 235 F.3d at 24-25; *Mathieson v. Associated Press*, No. 90 Civ. 6945, 1992 WL 164447, at \*8 (S.D.N.Y. June 25, 1992).

<sup>347</sup> See *Perfect 10*, 508 F.3d at 1168; see also *Bill Graham Archives*, 448 F.3d at 614.

factors were either neutral or weighed in favor of fair use, the court would then declare the use fair.

Such a verdict is consistent with recent lower court rulings on the use of images and on copying by news organizations, but it would have a chilling effect on the dissemination of amateur news content. When creators of images, who up until now have been happy to share their creations for free, realize that news organizations can copy and profit from their works with impunity, they are likely to become much more cautious about what they will release to the public at large. This will reduce the quality of content available on sites other than the traditional media sites. The rule of the commons, whereby a common free resource is squandered because no one is held accountable, will reduce the quality of Internet content. Some will be allowed to exploit the labors and creativity of others without paying the customary fee, and eventually those creators will get wise.

#### IV. CONCLUSION

Amateur photographers and “citizen reporters” are more likely to be disadvantaged by the current diluted transformative use standard where they have posted photographs or film clips on Internet sites that are not deemed to be traditional news outlets. As licensing fees become standard, the more savvy creators of amateur footage will become increasingly leery of making their work publicly available on non-news websites where they cannot rely on the courts to protect their rights.<sup>348</sup> As more and more creators of content find their work on the evening news without their authorization, the quality of the content on these sites will decline. Thus, the courts’ current approach, which turns a blind eye to misappropriation by news agencies if the work was taken from a non-competing source, is likely to impede, rather than promote, “the Progress of Science and the useful Arts.”<sup>349</sup>

Although some scholars argue that copyright protection has become too strong,<sup>350</sup> and that the emphasis on transformative use in

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<sup>348</sup> Recognizing the value of amateur footage of real life crime, one New Yorker produced DVDs titled “Criminals Gone Wild,” which he sells for \$26.98 each. Alison Gendar & Corky Siemasko, *N.Y. Man Films “Criminals Gone Wild,”* N.Y. DAILY NEWS, Dec. 11, 2007, available at [http://www.nydailynews.com/news/ny\\_crime/2007/12/11/2007-12-11\\_ny\\_man\\_films\\_criminals\\_gone\\_wild.html](http://www.nydailynews.com/news/ny_crime/2007/12/11/2007-12-11_ny_man_films_criminals_gone_wild.html). “The minute you come out with crime footage everybody wants to buy it.” *Id.*

<sup>349</sup> U.S. CONST. art. I, § 8, cl. 8.

<sup>350</sup> Siva Vaidhyanathan, *The Googlization of Everything and the Future of Copyright*, 40 U.C. DAVIS L. REV. 1207, 1210 (2007) (“Copyright in recent years has certainly become too strong for its own good. It protects more content and outlaws more acts than ever before. It stifles creativity and hampers discovery of and sharing of culture and knowledge.”).

the fair use analysis unfairly favors copyright owners, this is not true when the secondary use is one, such as news reporting, that courts deem to be socially beneficial. In such cases, feeling that a finding of transformative use is a prerequisite for a fair use, the courts apply a diluted definition of “transformative” which includes uses that merely place the original work in a different context or apply it to a different purpose. This results in nearly every secondary use of a work that was not originally used in news reporting being found transformative, even where the news organization has added no new expression to the existing work. Further, because a finding of transformation shifts the analysis of the remaining three factors in favor of fair use, the non-news creator of works that are appropriated by news agencies finds himself with copyright protection that is quite weak. Faced with this reality, the amateur creator must choose to either immediately license his work to a traditional news agency or to keep his photograph or footage away from the prying eyes of the media.

The combination of the diluted definition of transformative use, combined with the greater weight toward fair use given to each factor upon a finding of transformative use, thus places creators of newsworthy photography and film at a marked disadvantage. Because many courts agree that news reporting “almost inevitably adds new meaning or message to copyrighted work,”<sup>351</sup> it is currently highly unlikely that the concerned citizen who films a teacher subduing a student or a foiled kidnapping attempt will be able to defend his or her copyright against appropriation by news organizations. If a secondary user need only show that it is using the original work in a different manner that is more socially beneficial than the original purpose, the secondary user has a greater incentive to borrow rather than to create, and the creator of the original work has a decreased incentive both to create and to share. In order to promote the creation of works of amateur news photography and footage, the lower courts must apply the traditional definition of transformative use and the statutory factor-by-factor analysis—just as they do to copying by competing news organizations. Such a move will ensure that fair uses truly are fair.

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<sup>351</sup> Bunker, *supra* note 16, at 312.





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A VIEW OF THE FUTURE IN SEMICONDUCTOR PROCESS:  
PATENT PROSECUTION IN CLASS 438 UNDER THE UNITED  
STATES PATENT AND TRADEMARK OFFICE'S FINAL  
CLAIMS AND CONTINUATIONS RULES

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I. Introduction

The U.S. patent system was created by Congress on April 10, 1790 pursuant to the authority granted by Article I of the U.S. Constitution.<sup>2</sup> The first patent, issued July 31, 1790 and examined by Thomas Jefferson, was signed by George Washington.<sup>3</sup> While the process of prosecuting or seeking a patent grant is far more complex today than in 1790, it is still a negotiation with people. A patent practitioner, attorney or agent, is a client's guide through the treacherous jungle of rules and regulations promulgated by the U.S. Patent and Trademark Office (PTO).

Patent prosecution, despite its often rigidly regulated contours, is a process run by people and operates according to negotiation models rooted in the fundamentals of human nature and interaction. While seeking a patent, a practitioner must negotiate with the patent examiner, a scientifically trained non-lawyer who on average has less experience with patents and the patent system than the practitioner.<sup>4</sup>

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<sup>2</sup> U.S. Const. art. I, § 8, cl. 8; U.S. PATENT & TRADEMARK OFFICE, PRESS RELEASE #02-26, THE U.S. PATENT SYSTEM CELEBRATES 212 YEARS (April 9, 2002), available at <http://www.uspto.gov/web/offices/com/speeches/02-26.htm>.

<sup>3</sup> PRESS RELEASE #02-26, *supra* note 2; U.S. Patent No. 1 (issued July 31, 1790), available at <http://www.ptodirect.com/patent/?X000001>.

<sup>4</sup> Data from the 2007 report by the Government Accountability Office indicates that 52% of examiners have five or fewer years of experience; American Intellectual Property Law Association survey statistics indicate that of the almost 17,000

On November 1, 2007, the PTO was to implement rule changes that would end aspects of patent practice that have existed for over a century.<sup>5</sup> In the new human dynamic created by the new rules, what are the most effective actions practitioners can take with the average examiner during patent prosecution to help the application progress, specifically in class 438, semiconductor process?

Practitioners agree that the new rules carry a heavy price tag for many inventors and particularly companies with large patent portfolios.<sup>6</sup> There are numerous significant and substantive changes to the current patent system. The two changes considered in this paper that affect practically every currently pending patent application are: 1) only one Request for Continued Examination may be filed per patent family as of right,<sup>7</sup> and 2) only two continuation applications may be filed per patent family as of right.<sup>8</sup> Because the rule changes

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members of the society, 27% have six or fewer years of experience. U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-07-1102, U.S. PATENT & TRADEMARK OFFICE, HIRING EFFORTS ARE NOT SUFFICIENT TO REDUCE THE PATENT APPLICATION BACKLOG 27 tbl.4 (2007), available at <http://www.gao.gov/new.items/d071102.pdf>; LAW PRACTICE MGMT. COMM., AM. INTELLECTUAL PROP. LAW ASS'N, REPORT OF THE ECONOMIC SURVEY 6 (2007).

<sup>5</sup> Changes To Practice for Continued Examination Filings, Patent Applications Containing Patentably Indistinct Claims, and Examination of Claims in Patent Applications, 72 Fed. Reg. 46,716 (Aug. 21, 2007) (to be codified at 37 C.F.R. pt. 1); Brief for Am. Intellectual Prop. Law Ass'n as Amicus Curiae Supporting the "GSK" Plaintiffs' Motion for a Temporary Restraining Order and Preliminary Injunction 1, *Tafas v. Dudas*, 511 F. Supp. 2d 652 (E.D. Va. 2007) (No. 07-1008), available at <http://www.aipla.org/Template.cfm?Section=20079&Template=/ContentManagement/ContentDisplay.cfm&ContentID=16245>.

<sup>6</sup> IBM, for example, estimated costs for performing evaluation for compliance with the new rules for its 25,000 pending patent applications to be in excess of 10 million dollars. Brief for Am. Intellectual Prop. Law Ass'n as Amicus Curiae, *supra* note 5, at 16-19.

<sup>7</sup> See Changes to Practice for Continued Examination Filings, *supra* note 5 at 46,716. A Request for Continued Examination is permitted under 37 C.F.R. § 1.114 and allows an applicant to request continuing examination of an application subject to a final rejection. See Request for Continued Examination, 37 C.F.R. § 1.114 (2007). A patent family as defined by the PTO as "the initial application and its continuation or continuation-in-part applications." Changes to Practice for Continued Examination Filings, *supra* note 5, at 46,716.

<sup>8</sup> Generally, prior to the rule changes, a continuation application was an application filed after the initial application that claims subject matter disclosed but not claimed in the initial application; a continuation-in-part application was an application filed after the initial application that adds and claims subject matter not disclosed in the initial application. See 35 U.S.C.A. § 120 n.14 (West 2007); Application Number, Filing Date, and Completion of Application, 37 C.F.R. § 1.53(b); Claiming Benefit of Earlier Filing Date and Cross-references to Other Applications, 37 C.F.R. § 1.78(a); U.S. PATENT & TRADEMARK OFFICE, MANUAL OF PATENT EXAMINING PROCEDURE §§ 201.07-.08 (8th ed., rev. 6, Sept. 2007) [hereinafter MANUAL]. Under the new rules, continuation and continuation-in-part applications may be filed

will be retroactive upon all applications that had not received a first action on the merits by the implementation date, and upon any subsequently filed applications, tens of thousands of currently pending applications are potentially subject to these new restrictions.<sup>9</sup> These two rule changes alone dramatically alter policies companies have relied on for decades when planning their patent strategies.

Faced with just over two months and a week to assess all pending applications, and amend or abandon ones subject to the rules, Glaxo-SmithKline (GSK) and others responded by filing suit against the director of the PTO, Jon Dudas, seeking to enjoin the PTO from implementing the rules on November 1, 2007.<sup>10</sup> On October 31, after two hours of oral argument by the PTO, attorneys for GSK, and amici, Judge James Cacheris of the Eastern District of Virginia issued a preliminary injunction forbidding the PTO to implement its new rules, pending a trial on the merits.<sup>11</sup> While still waiting for the outcome of the trial and for the actual scope of the changes to be known, a practitioner can best help clients to manage the potential impacts of the rules now by 1) appreciating what motivates the average examiner, and 2) studying what prosecution tools are being used and are working in class 438 based on data from the process. Armed with this information, a practitioner can prepare successful strategies for dealing with the average examiner and help maximize the odds that patent rights can be obtained for each application. While class 438 is a limited area of technology considered by the Office, the data is concerned with prosecution behavior generally and the principles

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claiming priority to the initial application, but only continuation applications may be filed claiming priority to any divisional applications. This provision ensures that, eventually, every patent family will “die out” after all the disclosed subject matter in an initial application has been claimed. *See* Changes to Practice for Continued Examination Filings, *supra* note 5, at 46,716.

<sup>9</sup> Changes to Practice for Continued Examination Filings, *supra* note 5, at 46,716. First actions on the merits (FAOM) include allowances, *Ex parte Quayle* actions, and rejections. *See* MANUAL, *supra* note 8, §§ 201.07-.08.

<sup>10</sup> *Tafas v. Dudas*, 511 F. Supp. 2d 652 (E.D. Va. 2007).

<sup>11</sup> *Id.* at 671. Judge Cacheris found that a preliminary injunction should issue because GSK was successful in showing likelihood of success on the merits because some of the rules appear to be beyond the PTO’s authority to implement, *id.* at 668, irreparable harm if the injunction were not granted because the patent rights lost at the date of implementation of rules later proved to be invalid could not be recovered, *id.* at 669, the balance of hardships tipped in GSK’s favor because if the potentially invalid rules were implemented, GSK would immediately experience loss of investment and have to deal with the uncertainty created, *id.* at 670, the PTO would merely be required to continue with the status quo if an injunction issued, and the public has a strong interest in not implementing rules that may later be proven to be invalid, *id.*

uncovered by examination of this data are likely applicable to most other art groups and technologies.

To begin understanding examiners and the data, an overall view of the prosecution process is helpful. For this paper, class 438 was selected as a representative area of technology within the Office.<sup>12</sup> A class is a particular subdivision of the technology classification system used by the PTO to organize the examination and searching process.<sup>13</sup> After an application is filed and followed by an initial examination process, it is classified using the PTO's numerical system based on the nature of the technology disclosed. That classification is used to route the application to a specific art unit. Examiners work within an art unit, and focus their work on a particular part of the world of technology, generally a subclass or group of subclasses of a class. Any of the over eight-hundred subclasses in class 438 could be an examiner's primary responsibility.<sup>14</sup>

## II. Examiner Motivations

Understanding the average examiner begins with appreciating his or her job requirements. Because successful negotiations occur when interests, not positions, are brought into alignment,<sup>15</sup> understanding an examiner's interests permits a practitioner to read between the lines of a rejection and realize why what is happening is happening. Appreciating the examiner's interests allows a practitioner to "expand the pie"<sup>16</sup> and avoid ruling out options that are probably still available.

During the prosecution process, the average examiner faces significant challenges from inside and outside the PTO. A constant and massive flow of new applications pours in daily from inventors all over the world.<sup>17</sup> The examiner community, over 5400 strong<sup>18</sup> and

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<sup>12</sup> Class 438 was selected because of the author's prior professional experience with the technology as an engineer at Intel Corporation and his desire to better understand how to prosecute patents in this field.

<sup>13</sup> See OFFICE OF PATENT CLASSIFICATION, OVERVIEW OF THE U.S. PATENT CLASSIFICATION SYSTEM (USPC) 1 (Dec. 2007), available at <http://www.uspto.gov/web/offices/opc/documents/overview.pdf>.

<sup>14</sup> See OFFICE OF PATENT CLASSIFICATION, CLASS 438 SEMICONDUCTOR DEVICE MANUFACTURING: PROCESS (2008), available at <http://www.uspto.gov/web/patents/classification/uspc438/sched438.htm>.

<sup>15</sup> ROGER FISHER ET AL., GETTING TO YES: NEGOTIATING AGREEMENT WITHOUT GIVING IN 40-50 (2d ed. 1991).

<sup>16</sup> See RAU ET AL., PROCESSES OF DISPUTE RESOLUTION: THE ROLE OF LAWYERS 87 (4th ed. 2006).

<sup>17</sup> The PTO reported that over 467,000 patent applications were filed in 2007 at the time of the annual report in November. U.S. PATENT & TRADEMARK OFFICE, PERFORMANCE & ACCOUNTABILITY REPORT: FISCAL YEAR 2007, at 109 tbl.1 (2007),

members of their own union,<sup>19</sup> are in constant collision with management.<sup>20</sup> Management grades the average examiner's performance by metrics that are almost exclusively focused on output, not quality, and are not linked to overall organizational goals dealing with fundamental issues that face the Office like application pendency.<sup>21</sup> These organizational barriers and disconnects reward the examiner who chooses hitting deadlines over doing quality work.<sup>22</sup>

### a. Examiner Performance Metrics

#### i. The "Count"

The average examiner's life has been committed by management to production, and his or her output is scrutinized by a variety of metrics. Understanding the principal metric by which an examiner's performance is measured, the "count," explains many of the bizarre and common events observed by practitioners in patent prosecution such as first Office actions based on art that is not related at all to the invention. An examiner receives a "count" for every first

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available at <http://www.uspto.gov/web/offices/com/annual/2007/2007annualreport.pdf>.

<sup>18</sup>*Id.* at 13.

<sup>19</sup> Patent examiners are members of the independent Patent Office Professional Association (POPA), established in 1964 to represent the interests of the examiners before PTO management. See <http://www.popa.org/html/about.htm> for more information.

<sup>20</sup> For a picture of the over two decade long struggle over a collective bargaining agreement between POPA and PTO management, see U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-05-720, INTELLECTUAL PROPERTY, USPTO HAS MADE PROGRESS IN HIRING EXAMINERS, BUT CHALLENGES TO RETENTION REMAIN 26 (2005), available at <http://www.gao.gov/new.items/d05720.pdf>.

<sup>21</sup> See OFFICE OF INSPECTOR GEN., U.S. DEP'T OF COMMERCE, U.S. PATENT & TRADEMARK OFFICE, FINAL INSPECTION REPORT NO. IPE-15722, at ii fig.1 (2004), available at <http://www.oig.doc.gov/oig/reports/2004/USPTO-IPE-15722-09-04.pdf>.

<sup>22</sup> The PTO's system for monitoring patent "quality" involves 1) examining a sample of rejections written by examiners to see if the rejections are actually valid, and 2) examining a sample of issued patents to see if they should have actually issued. Wendy Garber, Group Dir. of Tech. Ctr. 2100, U.S. Patent & Trademark Office, Presentation at the Meeting of the Intellectual Property Section of the Arizona State Bar (Nov. 27, 2007). As those familiar with modern statistical process control principles will note, however, the PTO's system is essentially a final inspection based quality control process that examines final output instead of monitoring in-line process parameters that actually control that output. The net result of such a quality initiative is that management sees employees as the source of defectives and only persons who can stop defectives and prescribe performance management, rather than process change, as the remedy. Such quality systems allow management to abdicate their primary responsibility to drive quality improvement by instituting process changes.

Office action on the merits issued, and a second “disposal count” when he or she issues a notice of allowance or a practitioner abandons an application.<sup>23</sup> The combination of the two counts for a given application constitutes a balanced production unit.<sup>24</sup> Management sets goals regarding the number of counts the individual examiner must generate based on the examiner’s grade level and the technology area in which they operate.<sup>25</sup> The goals are based on the number of hours in which an examiner is supposed to be able to process a given application.<sup>26</sup> These hour targets have not been adjusted since 1976 and management and the examiner community differ widely as to whether the targets are realistic or not.<sup>27</sup> Producing counts is a key indicator used in examiner performance management, and an examiner’s count total is tracked biweekly. The importance placed on generating counts is indicated in this statement by a patent examiner:

[T]here is a large stack of Office actions that are waiting to be reviewed, having been prepared no doubt after long hours spent at the Office over the weekend by examiners who've got to get their production numbers up before the quarter ends. We've actually got until about noon today to turn in actions and have them counted toward our third quarter production numbers. It's important to have your numbers in good standing at the end of each quarter, because that is when your production numbers are evaluated.

You didn't get any counts on some given bi-week? No problem. You can make it up. Just be sure that by the end of the quarter you've made at least 95%

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<sup>23</sup> See OFFICE OF INSPECTOR GEN., *supra* note 21, at 8 fig.8.

<sup>24</sup> Wendy Garber, *supra* note 22.

<sup>25</sup> U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-07-1102, U.S. PATENT & TRADEMARK OFFICE, HIRING EFFORTS ARE NOT SUFFICIENT TO REDUCE THE PATENT APPLICATION BACKLOG 7 (2007), *available at* <http://www.gao.gov/new.items/d071102.pdf>.

<sup>26</sup> *Id.*

<sup>27</sup> *Id.* at 15-16. When asked whether, in her experience, the hours targets were appropriate, Director Garber responded that they were “about right.” Director Garber was a patent examiner and supervisory patent examiner for a number of years in the digital camera technology area prior to joining PTO management. When asked questions about other subjects relating to patent examiner overtime and reasons for attrition, Director Garber’s responses aligned very closely with other publicly stated positions of PTO management. For example, Director Garber said a major reason for examiner attrition in the office is that the job is not a “good fit” for those leaving, the sentiment expressed in the 2007 GAO report. *Id.* at 15; *see* Wendy Garber, *supra* note 22.

of your production goal, or you will receive a warning, either oral or written, which is the first step in laying the groundwork for dismissal of an examiner.<sup>28</sup>

What happens when an examiner needs to get counts at the end of a quarter? An examiner cannot just allow an application, since PTO management is not encouraging examiners to allow more applications. In fact, one of the PTO's key indicators of which they are very proud is their year-over-year decreasing allowance rate.<sup>29</sup> By the end of the quarter, the examiner already knows how many disposal counts he or she has received from abandonments.<sup>30</sup> What remains? Applications waiting for a first action on the merits. If a quick, though not very thorough, search can be coupled with some overtime hours over the weekend drafting a rejection, the needed count can emerge. Is the quality of this action critical? No, because the first action is always non-final and the examiner can now wait until the practitioner responds to do anything else.<sup>31</sup> If the rejection is really off-base, the practitioner will catch it and respond accordingly. No harm, no foul.

*ii. The "Workflow Point"*

The second key metric used to measure examiner performance has to do with the timeliness of their work. A "workflow point" is issued to each examiner every two weeks, and an elaborate system exists within the PTO for providing bonus points for work completed within recommended timeframes and point penalties for failure to meet required turnarounds.<sup>32</sup> The workflow points system explains the practitioner's receipt of Office actions that are word-for-word copies of previous rejections,<sup>33</sup> final rejections after an examiner seems willing to allow, and the frantic calls from examiners asking for

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<sup>28</sup> Housecleaning, [http://www.feedshow.com/show\\_items-feed=6e9bf2696caa2c2658eedac6a94ecea4?](http://www.feedshow.com/show_items-feed=6e9bf2696caa2c2658eedac6a94ecea4?) (June 27, 2005, 20:55).

<sup>29</sup> U.S. PATENT & TRADEMARK OFFICE, PRESS RELEASE #06-73, FISCAL YEAR 2006: A RECORD-BREAKING YEAR FOR THE USPTO (Dec. 22, 2006), available at <http://www.uspto.gov/web/offices/com/speeches/06-73.htm>.

<sup>30</sup> For an application to become abandoned, an examiner must wait the statutory period of six months from the last Office action. See 35 U.S.C. § 133 (2007).

<sup>31</sup> 35 U.S.C. § 132.

<sup>32</sup> See *OCIO Revises Position Descriptions to Seek "Younger Blood,"* POPA NEWS (Patent Office Prof'l Ass'n, Arlington, Va.), Sept. 2006, at 1, 4, available at [http://www.popa.org/pdf/newsletters/2006\\_09.pdf](http://www.popa.org/pdf/newsletters/2006_09.pdf).

<sup>33</sup> Ironically, while practitioners are required to be "responsive" in responding to a rejection and the examiner can take appropriate action, practitioners have no recourse to non-responsive rejections issued by examiners. See Reply by Applicant or Patent Owner to a Non-final Office Action, 37 C.F.R. § 1.111 (2007); MANUAL, *supra* note 8, §§ 714.02-.03.

a quick decision on a pending Office action, particularly at the end of a quarter.

To manage work in the Office, an examiner uses various dockets, each helping to govern his or her workflow point exposure.<sup>34</sup> Not surprisingly, because performance to schedule is measured by workflow points, and the docket system is the way an examiner prevents unfortunate point penalties from occurring, the choice of which application is worked on at a given moment depends upon what docket it is on right now.<sup>35</sup> Unlike practitioners, patent examiners cannot pay extension of time fees but must personally pay for each deadline they miss.

An examiner has five dockets: the regular new, regular amended, special new, special amended, and rejected.<sup>36</sup> Applications on the regular new docket are those just docketed to an examiner including continuation-in-part applications and those awaiting their first action.<sup>37</sup> Applications on the regular amended docket are cases where a response from an attorney or agent has been received.<sup>38</sup> The special new docket includes applications that have been made special or are continuations or divisional applications.<sup>39</sup> The special amended docket includes those applications that are from the special new docket that have responses from an attorney awaiting consideration, are amendments after a final rejection,<sup>40</sup> or are decisions by the Board of Patent Appeals and Interferences (the “Board”).<sup>41</sup> The rejected docket includes all applications for which the examiner has issued a rejection and which are awaiting a response from an attorney or agent. Given all the dockets to juggle, how does an examiner determine what item

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<sup>34</sup> The information for this and the succeeding paragraph are from an anonymous primary patent examiner. Information on the actual work life of a patent examiner is not well documented, but this examiner’s blog postings are extremely helpful and correlate with examiner behavior observed while collecting the data for this paper. Examiner’s Dockets, [http://www.feedshow.com/show\\_items-feed=6e9bfn2696caa2c2658eedac6a94ecea4?](http://www.feedshow.com/show_items-feed=6e9bfn2696caa2c2658eedac6a94ecea4?) (June 5, 2006, 19:34).

<sup>35</sup> *Id.*

<sup>36</sup> *Id.*

<sup>37</sup> *Id.*

<sup>38</sup> *Id.*

<sup>39</sup> *Id.*

<sup>40</sup> An amendment after final rejection is an amendment to the application written by a practitioner containing amendments to the claims and/or arguments along with a statement that the amendments either were not considered necessary at the time of the previous amendments or put the claims in better condition for appeal. *See* Amendments and Affidavits or Other Evidence After Final Action and Prior to Appeal, 37 C.F.R. § 1.116 (2007).

<sup>41</sup> The Board of Patent Appeals and Interferences is composed of administrative patent judges that hear all patent appeal decisions. *See* <http://www.uspto.gov/web/offices/dcom/bpai/index.html>.

from each of these dockets to work on? The answer is workflow points. Table 1 shows the point value of two of the bonuses and deductions that examiners can receive by managing or mismanaging applications on their regular amended or special amended dockets.

Type of Response	Processing Time Requirement	Recommended Processing Time	Workflow Point Penalty	Workflow Point Bonus
Non-Final Rejections	2 months	1 month	-1	+0.2
Amendments After Final	Within 10 calendar days of receipt	Processed within 10 calendar days, mailed within 30 calendar days.	-2	+0.5

**Table 1**<sup>42</sup>

By inspection, items on the special amended docket, like amendments after final rejection, are top priority because if the required window for reply is missed (10 days for an amendment after final) a hefty penalty is imposed (-2 points, or a month of workflow points). However, if the examiner manages to make the deadline, the potential bonus (+0.5 point) is the largest available. Because the potential for earning bonus points is only about 20-25% of most of the penalties, an examiner is required to do five times as much work by a bonus deadline to cancel the effect of most single penalties.

The effect of this strongly skewed bonus and penalty system resulting in a focusing of the average examiner's attention on the cases they are currently examining now and an operational priority by docket in this order: Special Amended, Regular Amended, Special New, and lastly, Regular New.<sup>43</sup> Once an examiner has begun examining enough applications, he or she can spend most of the time dealing with those already started without having to begin the process with any others, provided he or she can keep a minimum number of first action counts coming. As one examiner put it, "[p]rimary examiners will often have such a large number of applications on their

<sup>42</sup> Table adapted from table in Appendix 5, "Workflow Management Criteria," OFFICE OF INSPECTOR GEN., *supra* note 21, at 35 (note the 1987 revision date on these requirements).

<sup>43</sup> Applications in the Rejected docket require no further action unless statutory periods for response are not met, at which point the application is officially abandoned.

Rejected and Amended dockets that between allowances and [Requests for Continued Examination], they can maintain their production goals without picking up a new application for months at a time.”<sup>44</sup>

Like counts, workflow bonus points have no relation to the content of an application and cannot be used as a measure of the quality of the work product generated by an examiner.<sup>45</sup> The most insidious effect of this rewards/penalty system is a systemic bias against examination of applications on the Regular New docket. Picking up a new application will generally be the last thing an examiner will get to because of all the deadlines associated with his or her other dockets—new applications become what gets done after all the fires have been put out.

The foregoing applies principally to those examiners with more experience, who have been working long enough to build up their Amended dockets. New examiners begin by examining cases on the Regular New docket.<sup>46</sup> The PTO’s hiring of over one thousand examiners in 2006 and over one thousand in 2007 is intended to create a drop in the pendency of applications, as hundreds of new examiners take up the backlogged cases on the senior examiners’ Regular New dockets.<sup>47</sup> However, as the 2007 GAO Report observed, unless the PTO begins to reform the goals associated with counts, application pendency will only continue to rise.<sup>48</sup> What is truly remarkable in view of the PTO’s own systems is that the Office recently proclaimed that during 2004 to 2007 the agency has been successful in managing application pendency—a statement made next to a graph showing average application pendency rising by five months over those four years, continuing a trend of year-over-year increases.<sup>49</sup> In 2007, the

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<sup>44</sup> Examiner’s Dockets, *supra* note 34.

<sup>45</sup> Merely completing a particular task within a specified period of time does not mean that what was produced was work of quality. However, if the only quality measure of importance in an organization is the amount of output, then timeliness and volume become what everything else are subordinated to.

<sup>46</sup> Examiner’s Dockets, *supra* note 34.

<sup>47</sup> The PTO reported hiring 1,200 examiners in 2006 with 1,200 more planned in 2007. U.S. PATENT & TRADEMARK OFFICE, PERFORMANCE & ACCOUNTABILITY REPORT: FISCAL YEAR 2006, at 4 (2006), *available at* <http://www.uspto.gov/web/offices/com/annual/2006/2006annualreport.pdf>.

<sup>48</sup> See GAO-07-1102, *supra* note 4, at 23. The GAO recommendation represents a beginning point, but oversimplifies the solution because merely changing the counts goals without changing the workflow points system will not remove a key source of systemic bias against examination of new applications.

<sup>49</sup> See PERFORMANCE & ACCOUNTABILITY REPORT: FISCAL YEAR 2007, *supra* note 17, at 16.

average application was taking over two years to receive its first Office action.<sup>50</sup>

iii. *The “Examining Hour”*

The third and perhaps most personal metric used by PTO management to scrutinize examiner performance is the “examining hour.”<sup>51</sup> This measure exists as an attempt by management to simulate the real world by requiring that the examiners record the time they take to perform specific tasks; however, the system deviates significantly from reality in several key respects. Unlike a practitioner’s billing system, an examiner begins to receive examining hours as soon as he or she starts work—an examiner is always “on the clock” unless he or she participates in one of a list of enumerated tasks that are considered “non-examining time.”<sup>52</sup> What is most revealing about the examining hours system is the activities that are considered “non-examining time,” namely, supervising the work of junior examiners, examiner-initiated interviews with a practitioner, attending training classes, attending meetings, and, until very recently, conducting practitioner-initiated telephone interviews.<sup>53</sup>

It is not encouraging that the list of tasks that count as non-examining hours includes tasks that 1) are required to improve the average examiner’s abilities, 2) enable communication within the Office and the functioning of the examining corps, and 3) facilitate disposal of applications. Because of this, the outlook for examiner self development, the PTO’s internal communication, and application pendency is bleak. Examiners can find themselves in the position of having to work more than forty hours per week to compensate for the tasks they cannot record as examining hours but must participate in to do their jobs. Because these tasks are non-examining time, examiners cannot claim them as overtime.

Understandably, the average examiner regards the current system as unjust.<sup>54</sup> A classic vitriolic union/management dynamic has

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<sup>50</sup> *Id.* at 16. The adage, “justice delayed is justice denied,” comes to mind, particularly when the plight of the independent inventor is considered. Independent inventors are entrepreneurs who often are seeking funding with which to start a new business based on the technology disclosed in their application. Those with issued patents in hand are far more likely to get funding than those who can only say they hope their idea is patentable.

<sup>51</sup> See OFFICE OF INSPECTOR GEN., *supra* note 21, at 8.

<sup>52</sup> Wendy Garber, *supra* note 22.

<sup>53</sup> *Id.*; Extra Time for Interviews, [http://www.feedshow.com/show\\_items-feed=6e9bf2696caa2c2658eedac6a94ecea4?page=2](http://www.feedshow.com/show_items-feed=6e9bf2696caa2c2658eedac6a94ecea4?page=2) (June 23, 2006, 02:08).

<sup>54</sup> Understandably, the first year associate practitioner with a 2000 hour billing requirement feels little sympathy for the average examiner. Twenty-five percent of

been playing out for years in the PTO over this very subject.<sup>55</sup> A statement in the most recent GAO report, while not necessarily making the connection that examiner overtime is linked not just to count goals but also to examining hours and workflow points, beautifully summarizes PTO management's attitude: "[a]s with many professionals who occasionally remain at work longer to make up for time during the day spent chatting or because they were less productive than intended, examiners may stay at the office (or remote location) longer than their scheduled tour of duty to work."<sup>56</sup>

These three metrics (counts, workflow points, and examining hours) are what management expects an examiner to produce. Unfortunately, these metrics enable those who do nothing more than push paper to safely draw a paycheck and simultaneously serve to drive anyone who is willing to go above and beyond out of the Office. Indeed, in light of the counts production goals alone (not revised since 1976), 59% of patent examiners stated the unpaid overtime they had to work to meet their goals is a primary reason they would leave the PTO.<sup>57</sup> Indeed, since nearly one out of every two examiners hired since 2002 has done so, the Office has little data to support a contrary argument.<sup>58</sup> These three metrics alone provide an explanation of why the work product leaving the office and application pendency is so poor. None of them has the ability to measure or incentivize quality work.<sup>59</sup> It is the author's opinion that nothing will change what happens at the PTO with a given case until a cultural change occurs, driven by an examiner rewards system aligned with objectives determined by and measured using a statistical quality control process. Such processes are well known and implemented in the private sector; the PTO faces the decision whether to embrace such a change and focus on the customer or continue to fail in its progress.

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practitioners with less than five years experience in firms billed 2000 hours or greater in 2006. See REPORT OF THE ECONOMIC SURVEY, *supra* note 4, at 6.

<sup>55</sup> See *Raw Goal Plan is a Raw Deal*, POPA NEWS (Patent Office Prof'l Ass'n, Arlington, VA), Nov. 2006, at 1, available at [http://www.popa.org/pdf/newsletters/2006\\_11.pdf](http://www.popa.org/pdf/newsletters/2006_11.pdf).

<sup>56</sup> See GAO-07-1102, *supra* note 4, at 18.

<sup>57</sup> *Id.* at 19.

<sup>58</sup> *Id.* at Highlights.

<sup>59</sup> For example, if an examiner is in danger of losing workflow points by failing to respond in time, he or she can easily send out a copy of the last Office action adding the words "the applicant's arguments have been fully considered but are unpersuasive." This regularly encountered statement in Office actions gives the practitioner (the customer) zero insight as to what the examiner considers the real issue blocking allowance of an application.

### **b. The New Rules and the Examiner Performance Metrics**

The new rules changes do not affect any of the three examiner metrics directly.<sup>60</sup> Accordingly, while the options available to practitioners have dramatically changed, it will be business as usual at the PTO as far as performance management is concerned. This disconnect has tremendous potential to hinder the Office's work because, as is discussed in detail in the following sections, practitioners will no longer have as many options available to allow them to give examiners what they want so practitioners can get what they need. Since the average examiner with which a practitioner works has little organizational incentive to do a good job with a specific application right now, under the new rules, practitioners face the quandary of trying to make the examiner happy while not sacrificing a client's legal rights in their invention.

Appreciating this dilemma can promote two responses from the practitioner: 1) patent prosecution is an ultimately futile attempt to extract something of value from a fatally flawed and hopeless system, or 2) while results cannot be guaranteed and are becoming increasingly proscribed, a wide variety of options are available that, if used proactively, can maximize what the client will receive from the average examiner. Preferring to see the glass half full, the options available and their effectiveness are illustrated in view of data obtained from class 438.

### **III. The Data from Class 438: The Impact of the New Rules on the Status Quo**

#### **a. Negotiating Leverage and the Final Rejection**

During patent prosecution, an examiner cannot issue a final rejection of an initial application during the first action on the merits.<sup>61</sup> Accordingly, a practitioner does not "run out of time" with an application, and the examiner does not have to decide on what grounds an application is not allowable, until he or she is drafting the final rejection. In class 438, only 44.2% of all applications received a final

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<sup>60</sup> The PTO's response to Comment 280 affirms that the rule changes made no alterations to production goals. *See Changes To Practice for Continued Examination Filings, supra* note 5, at 46,818.

<sup>61</sup> *See* Final Rejection or Action, 37 C.F.R. § 1.113 (2007). However, in RCE and continuation cases, the rule allows an Examiner to issue a final rejection on the first action if no amendments to the claims are made. *See* MANUAL, *supra* note 8, § 706.07(b).

rejection at any stage during prosecution.<sup>62</sup> The rest proceeded to allowance or were abandoned prior to a final rejection being issued. A somewhat sobering statistic for the practitioner is that while only 25.5% of issued patents in class 438 received a final rejection, 64.2% of abandoned or still pending applications did. While receiving a final rejection in class 438 may be a confirmation that there are significant problems with the patentability of the invention, because other potential causes for receiving a final rejection exist other than the merits of the application (an examiner in trouble with workflow points, for example), any final rejection must always be taken with a grain of salt.

The great positive about any final rejection for the practitioner is that the examiner has handed him or her great negotiating leverage. Shell defines leverage as “your power not just to reach agreement, but to obtain an agreement *on your own terms*.”<sup>63</sup> Shell further defines three types of leverage: 1) positive, “leverage based on the relative abilities of each party to supply things the other wants...” 2) negative, “leverage based on the parties’ relative ability to take away things each currently has...” and 3) normative, “leverage based on application of the consistency principle . . . .”<sup>64</sup>

At first blush, however, final rejection appears to have little of what could be considered leverage. Prosecution on the merits of the case is officially closed;<sup>65</sup> the options are proscribed and the client may be getting hot and bothered. However, in many respects, there is much more that is good about a final rejection than is bad. A practitioner’s leverage begins with a final rejection because the examiner has now stated his or her position on the patentability of the invention. The examiner is finally finished with the back and forth process of non-final rejection and response. He or she, like the practitioner, is ready to get down to business after months or years of discussion.

The practitioner also gains leverage because the data indicates that examiners are more than willing to change their minds. With 25.5% of issued patents in class 438 coming from applications that were finally rejected at least once, a practitioner should see a final

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<sup>62</sup> All percentages in this paper were personally calculated using JMP 6.0 and Excel using a copy of the data set in Appendix A.

<sup>63</sup> G. RICHARD SHELL, *BARGAINING FOR ADVANTAGE: NEGOTIATING STRATEGIES FOR REASONABLE PEOPLE 90* (Penguin Books 2000) (1999).

<sup>64</sup> *Id.* at 102. With respect to normative leverage, Shell states “Normative leverage is the skillful use of standards, norms, and coherent positioning to gain advantage or protect a position. You maximize your normative leverage when the standards, norms, and themes you assert are ones *the other party views as legitimate and relevant to the resolution of your differences*.” *Id.* at 43.

<sup>65</sup> See 37 C.F.R. § 1.113(a) (2007).

rejection as an opportunity.<sup>66</sup> The greatest change for the practitioner facing a final rejection from the PTO's new rules is that far fewer options are available than before.

*i. Quick Leverage: The Amendment After Final Rejection*

The first option at a practitioner's disposal is to file an amendment after final rejection, amending the claims in view of the examiner's rejections and/or including arguments that the claims are now presented in better form for appeal or that the amendments made were not previously included because it was felt they were not needed.<sup>67</sup> Amendments after final were filed 73.8% of the time for issued patents and 48.5% of the time in abandoned or still pending cases. These amendments were entered 56.3% of the time for issued patents and 14.6% of the time for abandoned or pending cases, with an overall entry rate of 30%.<sup>68</sup> For issued patents, 41.6% of finally rejected applications were allowed when an amendment after final was filed. This statistic is not insignificant; entry of amendments after final was largely responsible for issuing over 12% of the patents in class 438. With a 30% entry rate overall, the success of the amendments cannot be explained as the result of the brilliance of the practitioner's arguments or the weakness of the examiner's rejections, but rather because the practitioner has played his or her leverage card.

When an amendment after final is filed by a practitioner, the workflow pressure on the examiner rapidly increases. Amendments after final go on the Special Amended docket, and Office workflow guidelines require they be responded to within 10 days after receipt by the examiner. As shown in Table 1, if the examiner responds within this timeframe, he or she can receive +0.5 workflow bonus points,

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<sup>66</sup> However, a practitioner, attorney or agent, is bound by the ethical canons and disciplinary rules contained in Canons and Disciplinary Rules, 37 C.F.R. §§ 10.20-.112. While a practitioner is to represent a client zealously, he or she is not allowed to knowingly make false statements of fact, which may be likely if the practitioner is merely keeping an obviously unpatentable case alive. *See Representing a Client Zealously*, 37 C.F.R. § 10.85.

<sup>67</sup> *See Amendments and Affidavits or Other Evidence After Final Action and Prior to Appeal*, 37 C.F.R. § 1.116.

<sup>68</sup> Entry of the amendment in this paper means the examiner has agreed with the practitioner's arguments, entered the proposed claim amendments, *and* reopened prosecution on the merits. Officially, entry of the amendment only means that the claim amendments have been entered, *see* 37 C.F.R. § 1.116(b)(3); the examiner may still refuse to reopen prosecution as to the merits. In these cases, however, the amendment after final has not been directly effective at getting to allowance by reopening prosecution, which is why these cases were not considered "entered."

with a penalty of -2 points for failure. In comparison with the paltry +0.2 workflow point bonus that can be received for responding within one month for an item on the Regular Amended docket, examiners must eye that +0.5 bonus with anticipation. In addition, by amending the claims and/or presenting arguments similar to what the examiner would face on appeal, the practitioner has placed a disposal count on the examiner's desk right in front of him or her. All the examiner must do to receive that count is allow the application.<sup>69</sup> Refusing to enter the amendment means the examiner will have to wait another six months to receive the count if the application is abandoned, or deal with an appeal. After having to drop what he or she was working on to read the amendment, the thought must cross the examiner's mind: "I could really use this count, I need the bonus points and this practitioner has given me some of what I was asking for in the last rejection. Why not split the difference and allow this one?"<sup>70</sup>

Amendments after final generate positive and normative leverage for practitioners. First, by filing such an amendment, the practitioner has handed the examiner the opportunity to get a count and a substantial workflow point bonus immediately. Secondly, the practitioner has used the principle of reciprocity to help generate normative leverage. Shell states that the power of reciprocity, or *quid pro quo*, is a well documented norm that establishes trust in negotiations. Reciprocity is effective in generating results both short and long term.<sup>71</sup> Because the practitioner has the opportunity by making the amendment (however material the change may actually be) to acknowledge the validity of the examiner's view of the application, the average examiner now feels the pressure to respond in kind. The opportunity for the count and the workflow point bonus serves to sweeten the deal (and expand the pie). The leverage available from use of amendments after final explains why practitioners succeed in reopening prosecution with amendments after final more than 50% of the time for issued patents and 30% overall. Use of amendments after final is a classic example of how, while the prosecution system is not a conventional negotiation model, careful use of the system's machinery can create conventional negotiated outcomes.

The rate of success with amendments after final, in reopening prosecution that has been formally "closed," indicates that, within the bounds of reason and a practitioner's ethical responsibilities,

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<sup>69</sup> An allowance, abandonment, request for continued examination (RCE), and the Examiner's Answer all are considered disposal counts. See MANUAL, *supra* note 8, § 1705(III).

<sup>70</sup> The human tendency under pressure during negotiation is to "split the difference" because it is inherently fair.

<sup>71</sup> G. RICHARD SHELL, *supra* note 63, at 59.

amendments after final should probably be filed as a matter of course. If the PTO's new rules are implemented, amendments after final will become absolutely critical, because, for at least a majority of applications, they are the only option that does not immediately involve a sacrifice of the client's future patent rights.<sup>72</sup>

*ii. Second Choice: The Request for Continued Examination*

If the amendment after final is not entered, the second option for practitioners is to file a Request for Continued Examination ("RCE"). The advantages of an RCE to the practitioner are that he or she can start completely over with the claims and redraft them in view of all the prior art cited by the examiner. At times, a practitioner is dealing with poorly drafted claims or claims that are overbroad because no search of the prior art was made before the application was filed. Having a chance to start over may be the key to getting a particular application allowed.<sup>73</sup> For the examiner, RCEs are great since processing an RCE request means that he or she will receive an instant disposal count followed by the opportunity to get two more counts from the same application while being able to reuse previous search results and arguments.<sup>74</sup> More counts for much less work is a definite win.

While the filing of RCEs with the Office creates great internal headaches and is disfavored by management who are seeking to reduce the amount of application "rework,"<sup>75</sup> from the perspective of

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<sup>72</sup> Pursuing the appeals process means that after an additional time frame (sometimes years), the patent may still be ultimately rejected. The Board has recently been increasingly affirming examiners (this is probably the result of the implementation of the pre-appeal brief conference process discussed later rather than greater accuracy by examiners overall). See PERFORMANCE & ACCOUNTABILITY REPORT: FISCAL YEAR 2007, *supra* note 17, at 16-17.

<sup>73</sup> However, the RCE process has been criticized as being abused by practitioners who use it as a way to "wear down" an examiner; that this practice exists is indicated by two cases in the data set that had three and four RCEs, respectively, filed during prosecution and are still pending. See U.S. Patent Application 20030003730 (filed Aug. 28, 2002); U.S. Patent Application 20040161947 (filed Feb. 9, 2004).

<sup>74</sup> See Partnership Agreement Between the United States Patent and Trademark Office and the Patent Office Professionals Association 2 (May 29, 2000), available at <http://www.popa.org/pdf/agreements/rce.pdf>, for the agreement that solidified the RCE counts policy and secured this benefit for the examiners.

<sup>75</sup> RCEs are included in the "rework" statistic the PTO uses to determine the number of applications already related to or being reprocessed that are being worked on by examiners. Joseph Rolla, Deputy Commissioner for Patent Examination Policy, U.S. Patent & Trademark Office, Presentation to the Boston Patent Law Association

the average examiner, that a high rate of rework in the Office exacerbates the backlog of applications is of no consequence. The average examiner is accountable only for generating counts, recording examining hours, and avoiding workflow point losses. As long as there is plenty of work, the average examiner has no issues being “successful.” Ultimately, both practitioners and examiners have no disincentive to use the RCE process and often do so because it represents one of the very few win-win outcomes available in today’s patent prosecution system.

Unfortunately, under the PTO’s new rules, RCE practice is severely restricted, as a practitioner can only file an RCE *once* as a matter of right *per patent family*.<sup>76</sup> This means that a practitioner gets only one RCE to use on any one of three patent applications, one or more of which may actually be filed years following the filing of the initial application now under final rejection. Under the new rules, practitioners now face a real dilemma: if they choose to file an RCE on the initial application, claiming only a portion of the patentable subject matter disclosed in an application, they will no longer be able to use an RCE for any of the two available continuation applications that may be used to claim the rest of the subject matter disclosed. What if the subject matter not claimed in the initial application winds up in the client’s commercial product and another company begins making an identical product? Having the RCE available for use on a pending continuation application would be far more important to the client now than the one used on the parent application. This situation is like those argued by the attorneys for the American Intellectual Property Law Association (AIPLA) in their brief before Judge Cacharis, where a practitioner must choose how best to sacrifice a client’s patent rights.<sup>77</sup> In this respect, the new rules present significant malpractice implications for practitioners who may have,

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13 (January 2006), *available at* <http://www.uspto.gov/web/offices/pac/dapp/opla/presentation/bostonplaslides.ppt>.

<sup>76</sup> A practitioner is required to petition to receive a second RCE, which the PTO has indicated will be rarely granted. Changes To Practice for Continued Examination Filings, *supra* note 5, at 46, 716.

<sup>77</sup> AIPLA’s attorneys discussed the dilemma of the practitioner counseling the client about filing an “Examination Support Document” (ESD) which, among other activities creating potentially damaging statements, requires a practitioner to perform a search of the prior art and explain how the claims as filed differ from that art. An ESD would be required under the new rules if more than five independent claims or twenty-five total claims were to be examined in a given application. Since the rules applied retroactively, decisions about whether to file an ESD or to cancel the excess claims in pending applications would have to be made by the practitioner and the client. These types of ethical and practical considerations flow from many of the proposed rule changes. See Brief for Am. Intellectual Prop. Law Ass’n as Amicus Curiae, *supra* note 5, at 7-8.

according to their clients, used the one available RCE “too early” and forfeited some or all of their clients’ most valuable patent rights.<sup>78</sup>

While the foregoing are significant issues raised by the new rules, perhaps the most broadly felt impact of the new RCE rules change will be simply that practitioners can no longer generate normative leverage by using RCEs to make *quid pro quo* trades with examiners. Practically speaking, the RCE’s win-win potential has been eliminated by the new rules, and both the practitioners and examiners will suffer. Moreover, the client will wind up losing a portion of, or all of his or her patent rights, which negates the purpose of the patent prosecution negotiation.

What is the potential impact in class 438 if RCEs essentially become a rarity? RCEs were filed in 46.2% of issued patents receiving a final rejection in class 438 and filed in 38.9% of issued patents.<sup>79</sup> Overall, 13.2% of all issued patents in class 438 involved an RCE; 11.3% of those were filed after a final rejection and 1.9% of those were filed *without* a final rejection. The foregoing statistics indicate that a majority of the thirty-five patents in the sample issued involving an RCE (which represent approximately 5,400 issued patents) may *not* have been issued if the PTO’s new rules regarding RCEs were implemented.<sup>80</sup>

### *iii. Last Choice? The Appeal*

Under the new rules, if an amendment after final rejection was not successful and an RCE not advised, the third option available to the practitioner is to appeal the examiner’s decision. This choice was made in 13.8% of issued patents that had a final rejection and 16.6 % of abandoned or pending patents. When negotiating with patent examiners, practitioners quickly realize that the examiner does not and will not use a standard similar to their own when gauging the patentability of the invention. Shell offers the insight that:

In these difficult cases, you will need to resort to explicit leverage and search for an ally—a third party to

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<sup>78</sup> As the brief discusses, the practitioner has essentially lost the opportunity to procedurally inform the examiner of prior art discovered late in the examination process relevant to the patentability of the invention and may later face charges of inequitable conduct for failure to disclose. This situation requires the client and the practitioner to choose between knowingly allowing an invalid patent to issue and expressly abandoning an allowed application that has been years and thousands of dollars in the making. *See id.*

<sup>79</sup> These statistics include those cases where multiple RCE filings were required (2 or 3) to bring the application to the point of allowance.

<sup>80</sup> This statistic indicates the magnitude of patent rights eliminated by the new rules.

whom your bargaining counterpart is answerable and who is sympathetic to your norms. Once you can locate such a person, you need to arrange things so you negotiate in the third party's presence or under the third party's protection. Allies serve as audiences or witnesses to guarantee the application of standards that ought, in fairness, to apply.<sup>81</sup>

### 1. Plead Your Case: The Pre-appeal Brief Conference

The appeals process allows a practitioner to obtain just such an audience through the pre-appeal brief conference. During the summer of 2005 the PTO began a pilot program of pre-appeal brief conferences to reduce the costs of the current appeal process on practitioners, their clients, examiners, and the Board.<sup>82</sup> The pre-appeal brief conference process requires that a practitioner file simultaneously with a notice of appeal a request for a pre-appeal brief conference accompanied by not more than five pages of arguments, which will be subsequently reviewed by a panel of patent examiners (the examiner currently examining the application, his or her supervisor, and another experienced examiner) before the case proceeds to the Board.<sup>83</sup> The PTO implemented this program because according to their statistics, 60% of filed appeals were not being forwarded to the Board for consideration.<sup>84</sup> The results were remarkable: in the first several months, 43% of applications considered had prosecution reopened (the final rejection withdrawn by the examiner) and 7% proceeded directly to allowance; the remaining 43% proceeded to the Board.<sup>85</sup>

The foregoing is a testimony of the power of the practitioner obtaining an audience (the two new examiners on the panel) before

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<sup>81</sup> G. RICHARD SHELL, *BARGAINING FOR ADVANTAGE: NEGOTIATION STRATEGIES FOR REASONABLE PEOPLE* 47 (Penguin Books 1999).

<sup>82</sup> Press Release, U.S. Patent and Trademark Office, *Improved Patent Appeal Process Will Save Patent Applicants \$30 Million Annually* (July 13, 2005), <http://www.uspto.gov/web/offices/com/speeches/05-31.htm>.

<sup>83</sup> Wendy A. Choi & Joseph F. Oriti, *Pre-Appeal Brief Conference Program—A Lower Cost Option for Patent Applicants*, *INTELLECTUAL PROP. PERSPECTIVES* (Woodcock Washburn LLP, Philadelphia, P.A.) Spring 2006, at 8, *available at* <http://www.woodcock.com/publications/newsletters/Intellectual%20Property%20Perspectives%20Spring%202006%20Newsletter.pdf>.

<sup>84</sup> *Id.*

<sup>85</sup> Jane Inglese, *USPTO Releases 2005 Performance and Accountability Report*, *INTELLECTUAL PROPERTY PERSPECTIVES* (Woodcock Washburn LLP, Philadelphia, P.A.), Spring 2006, at 4, *available at* <http://www.woodcock.com/publications/newsletters/Intellectual%20Property%20Perspectives%20Spring%202006%20Newsletter.pdf>.

whom to thoroughly argue his or her case. The new examiners on the panel are experienced individuals who have no personal stake, per se, in the outcome. The normative leverage available to the practitioner through such a conference is very large because average examiners, even difficult ones, can be brought to see reason.

Notwithstanding the leverage potential, many practitioners are reluctant to appeal for several reasons: 1) the cost of pursuing an appeal with the PTO is higher than filing an RCE,<sup>86</sup> 2) an adverse decision on appeal by the Board eliminates the possibility of the patent issuing without pursuing even more expensive federal court litigation and/or appeals,<sup>87</sup> and 3) the perception that taking examiners up on appeal damages the relationship between the practitioner and the examiner. Since a practitioner's client is usually filing a number of applications in a fairly narrow range of technologies, the odds that a practitioner will have to deal with the same examiner again are high. Therefore, many practitioners reserve the appeals process only for clients willing and able to pay, as well as for particularly egregious examiner actions. Because of these considerations, many practitioners had used RCEs almost as a matter of course. Under the new rules, however, the RCE option is unavailable.

The pre-appeal brief conference is likely the best way to both preserve the practitioner/examiner relationship and maximize the odds of reopening prosecution in any particular case. This is because the panel process permits the average examiner, whose decision has been appealed, to save face if he or she agrees to change position – as he or she will 46% of the time. For instance, they may employ the general reasoning: “WE agreed to reopen prosecution. WE agreed that in view of the arguments, the case should proceed to allowance.” For most people, “we” is much easier to say than “I,” particularly when what is being said is, “I was wrong.” The PTO pre-appeal brief conference process pilot has now been extended permanently across the Office.<sup>88</sup> In view of the availability of this technique and its potential to preserve practitioner/examiner relationships, practitioners should consider using the pre-appeal brief conference as their second option under the new rules instead of an RCE if an amendment after final fails to reopen prosecution on a case facing final rejection.

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<sup>86</sup> See LAW PRACTICE MGMT. COMM., REPORT OF THE ECONOMIC SURVEY 2007, AM. INTELLECTUAL PROP. LAW ASS'N 21 (2007).

<sup>87</sup> After a decision by the Board, an applicant can sue directly in federal district court or appeal directly to the Federal Circuit of the U.S. Court of Appeals. Ultimately, appeals can be taken to the United States Supreme Court.

<sup>88</sup> John Doll, *Extension of the Pilot Pre-Appeal Brief Conference Program*, OFFICIAL GAZETTE NOTICES, (U.S. Patent and Trademark Office), Jan. 10, 2006, available at <http://www.uspto.gov/go/og/2006/week06/patexcf.htm>.

## 2. Seek Justice: Take the Examiner to the Board

However, if the pre-appeal brief conference option cannot get the average examiner to yield, after completing the steps leading up to the conference, a practitioner has already started the process of taking the case to the Board and has now gained additional insight into the examiner's position and arguments. A practitioner's determination now to prosecute a case the rest of the way through the appeals process is another opportunity to generate negotiating leverage. From the examiner's perspective, the appeals process is work, which, while providing plenty of examining time, yields only one count and lots of workflow point liability.<sup>89</sup> The low rate of filing of Notices of Appeal in Class 438 (only in 7% of the publicly available applications in Class 438) means that on the average few examiners have appeals experience. Not being lawyers, like most practitioners, many of the examiners likely find the appellate process foreign, time consuming, and aggravating. These examiners may wonder: why learn something new when you can get counts doing something else?

The foregoing considerations perhaps explain the reality that, for publicly available applications in Class 438, the examiner takes the case to the Board only 13.5% of the time a notice of appeal is filed.<sup>90</sup> The other side of the coin is, however, that in every case (5 in the data set) in which a Board decision occurred (a little more than half of the cases represented by that 13.5%), the examiner was affirmed.<sup>91</sup> The foregoing indicates, however, that at least 86% of the time a practitioner files a notice of appeal, prosecution will be reopened or allowance will occur. This conclusion is borne out by the observation that nine of the issued patents in the data set were issued after a notice of appeal was filed (a number representing over 1400 issued patents over the time frame considered by this paper).

Even if the pre-appeal brief conference fails to yield results, it appears that practitioners still have, by pursuing an appeal, a good alternative to abandonment of an application under final rejection. In

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<sup>89</sup> An examiner receives a disposal count when the Examiner's Answer is filed. *See* MANUAL, *supra* note 8, § 1705(III).

<sup>90</sup> In only one case in the data set (20030102566) was a pre-appeal brief conference pursued; the case proceeded to allowance and was abandoned for failure to pay the issue fee. This data indicates that it is *not* because pre-appeal brief conferences are widely used in class 438 that the percentage of times an examiner takes the case to the Board is so low.

<sup>91</sup> As of this writing, four of the cases (20020149033, 20030203591, 20050274457, and 20060000799) are still waiting for a Board decision; accordingly, the conclusion cannot be drawn that in every case in class 438 the examiner will be affirmed on appeal by the Board.

the world of negotiation models, Ury, et al. have referred to opportunities like a Board decision as the “Best Alternative To a Negotiated Agreement” or BATNA.<sup>92</sup> The BATNA represents the best alternative to no deal, or in “patent-speak,” the best alternative to abandonment. Since statute permits filing a notice of appeal when any claim in an application has been twice rejected,<sup>93</sup> the appeals process can be started even before a final rejection has issued, even if the second rejection is non-final. Under the new rules, in certain circumstances practitioners may not want to wait for the examiner to get serious about an application, and may accordingly want to move rapidly into the appellate process.<sup>94</sup>

*iv. When in Doubt, File a Continuation*

If an amendment after final rejection is not entered, and for various other substantive reasons the practitioner believes it would be unwise to pursue an appeal,<sup>95</sup> the practitioner has one final option to create patent rights for the client without abandoning the priority date obtained by the filing of the initial application.<sup>96</sup> That option is to file a continuation or continuation-in-part application with new claims.<sup>97</sup> Prior to implementing new rules, the courts essentially allowed practitioners to file an unlimited number of continuation and continuation-in-part applications.<sup>98</sup> The PTO’s new rules represent a serious effort to rein in the many existing patent families that consist of numerous patents filed, as continuations and continuations-in-part, claiming priority to an application previously filed. Continuation patents are often used to rapidly issue claims that cover a competitor’s improvement on a patented technology, which does not infringe upon the existing patents. These improvements come years after the

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<sup>92</sup> ROGER FISHER ET AL., *supra* note 15, at 100, *cited by* RAU ET AL., PROCESSES OF DISPUTE RESOLUTION 89 (Thomson West 4<sup>th</sup> ed. 2006).

<sup>93</sup> *See* 35 U.S.C.A. § 134(a) (West 2007).

<sup>94</sup> For example, if there are no longer any RCEs available in a patent family and if negotiations are going nowhere with a particular continuation application, moving to the appeals process before final rejection may actually expedite prosecution.

<sup>95</sup> Some substantive reasons include rejections under 35 U.S.C. § 112, which state that the specification fails to provide supporting disclosure for the claims. Such rejections cannot be cured by amending the specification because no new matter can be added during prosecution. *See* MANUAL, *supra* note 8, §§ 2161, 2163.06. The only way to add new matter is to file a continuation-in-part application that includes the missing disclosure and claims priority to the original application.

<sup>96</sup> The priority date is the date of filing for applications filed in the U.S.; it is the date of national stage entry for international applications under 35 U.S.C. § 371.

<sup>97</sup> *See* 35 U.S.C.A. § 120 (West 2007).

<sup>98</sup> *See, e.g., In re Henriksen*, 399 F.2d 253, 254 (C.C.P.A. 1968); *In re Bogese*, 303 F.3d 1362, 1368 (Fed. Cir. 2002).

issuance of the initial patent. Some companies practice keeping an application pending in each patent family as long as possible, which allows them to “come up out of the water” and attack quickly. From the PTO’s perspective, such “submarine” behavior damages the rework metric, and every newly filed application can turn into a giant family of applications, each requiring examination.

From the foregoing, limiting the number of continuation applications to two under the new rules is understandable, but as implemented, represents an extremely restrictive approach. While other options to help ensure the client receives as much patent coverage of an invention or family of inventions as possible exists under the new rules,<sup>99</sup> the retroactive application of the rules will result in a substantial denial of patent rights to clients who use one of their continuation applications to correct problems caused by a drafter’s mistake or omission.<sup>100</sup> In these cases, the client loses an opportunity to claim some of the subject matter in the initial application that he or she had planned to claim using continuation applications.

The foregoing scenario is not uncommon: in 13.6% of the abandoned or still pending cases in the data set, a child continuation application was filed;<sup>101</sup> in 72.2% of those cases, the initial application was abandoned. The foregoing indicates that, statistically, in over 4,000 cases in class 438, a continuation application will be filed in favor of the initial application. This statistic indicates that a very significant number of clients will experience a substantial restriction in the patent rights they could obtain. Like the RCE situation previously discussed, the restriction on continuation applications dramatically reduces the system’s tolerance for mistakes and increases the potential for malpractice actions against practitioners.

#### IV. Conclusion

While the US patent prosecution process appears to be carefully defined, controlled, and heavily regulated, the foregoing data

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<sup>99</sup> If a practitioner files an initial application that contains several inventions under the new rules and receives a restriction requirement, he or she can potentially create multiple patent families since two continuations are allowed for each divisional application. Because the new rules forbid the filing of continuation-in-part applications from divisional applications, however, the patent family is guaranteed to end when no subject matter remains in either the initial or divisional applications.

<sup>100</sup> See Brief for Am. Intellectual Prop. Law Ass’n as Amicus Curiae, *supra* note 5, at 11.

<sup>101</sup> Patent Cooperation Treaty (PCT) continuation applications were not counted as child continuation applications in this data set since they are used to enter foreign prosecution only and confer no additional U.S. patent rights.

from class 438 indicates that the system is run by people. Accordingly, ordinary negotiating norms significantly explain the outcomes observed from the process. Those practitioners willing to spend the time necessary to understand the average examiner's interests and willing to be creative with the tools provided by the system will have ample opportunities to successfully use proven methods of negotiation with patent examiners. The PTO's rule changes, while presenting obvious restrictions on patent rights and restricting or eliminating some of the most helpful negotiating tools, still present opportunities for practitioners. Leverage, bargaining, and reciprocity have just as much place in the faceless patent prosecution process as they do in high-powered board room negotiations. While the natives at the PTO have their own customs, they are people too. Ultimately, the story behind every success in class 438 is the completion of a successful negotiation.

## APPENDIX A

### *Methodology and Statistical Information*

The data presented in this paper was derived from 265 patents randomly selected from 41,311 patents and 265 abandoned or pending applications randomly selected from 40,919 published applications with a primary classification in class 438 that issued or were published between January 2, 2001 and February 27, 2007. Gathering of the data was accomplished using custom software and the website [www.ptodirect.com](http://www.ptodirect.com) from the entirety of the publicly available PTO patent database. Random selection was accomplished, for example, by putting all of the patent numbers into a Microsoft® Excel® worksheet and using the RANDBETWEEN function to generate random numbers between 1 and 41,311 to determine the row numbers of the patents to be selected. The data for each individual application was extracted manually using the Public PAIR application available on the USPTO website and was conducted in two phases: for issued patents, the information was collected in April and May of 2007; for publications, the data was collected in October and November of 2007. The still pending applications selected represented those applications that were currently under a final rejection or that were in a stage of post-final rejection prosecution. A copy of the patents and publications chosen and the relevant data gathered is shown in Appendix B. Because the sample size is 265 for both patents and publications, all of the individual group statistics are reportable at a 95% confidence level with a confidence interval of +/- 6% as calculated using a random

sample size formula.<sup>102</sup> In addition, because the numbers of issued patents and publications produced during the time period considered are essentially statistically identical (41,311 vs. 40,919) the data obtained by combining the two randomly selected datasets is also reportable at the same confidence level and confidence interval. It is important to note that data gathered by studying only issued patents and patent publications does *not* represent a random sample from the *entire population* of filed patents over the time frame considered in this paper. Generation of an entirely random sample would require consideration of all non-published abandoned and pending applications as well as those publicly available. A sample from such a data set would most likely exhibit somewhat different statistical characteristics than the one presented here. However, compiling a completely randomly selected data set from the population of all filed applications classified in class 438 over this time period is unlikely unless conducted by the PTO itself, as the PTO is the only entity allowed to view the prosecution history for all applications in class 438.

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<sup>102</sup> Formula is embodied in a Javascript applet available at <http://www.surveysystem.com/sscalc.htm>. The applet receives input from the user and uses a standard statistical sampling algorithm to calculate the required sample size given the population size, the confidence level, and the desired confidence interval.

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