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Winter December 7, 2012

The U.S. Patent Office's Proposed Fees Under the America Invents Act—Part I: The Scope of the Office's Fee-Setting Authority

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The U.S. Patent Office's proposed fees under the America Invents Act – Part I: the scope of the Office's fee-setting authority†

By Ron D. Katznelson

This two-part article discusses the Patent and Trademark Office's recent proposed rulemaking setting new patent user fees. In Part I the author argues that the PTO can raise fees in accordance with its aggregate costs but lacks authority to set national patent policies, or to skew certain fees to discourage or encourage a particular service. The author also asserts that the America Invents Act does not vest with the PTO discretion to set the level of its operating reserve – a determination reserved solely for congressional appropriations. In an upcoming Part II, the author will discuss the deference accorded the PTO to set specific fees and their public policy implications, will critique the PTO costing methodology used to set fees, and will propose a simple legally compliant approach for setting fees by increasing fees to match the aggregate costs while maintaining their relative magnitudes so as to preserve the salient congressional patent policy goals.

On September 6, 2012, the United States Patent and Trademark Office (the "PTO" or the "Office") published a Notice of Proposed Rulemaking entitled *Setting and Adjusting Patent Fees*, *77 Fed. Reg.* 55,028 (Sept. 6, 2012). The NPRM proposes to set fees under the fee-setting authority in the Leahy-Smith America Invents Act of 2011.[1] There is a need to adequately fund the operation of the PTO, after years of being under-resourced. The Office has made substantial progress in reducing its backlog in the last few years. However, the Office must exercise care in its stewardship of the fee-setting process and not exceed its authority under the law. The following sections examine the legal scope of the Office's fee-setting authority.

1 Recovery of aggregate costs is the *only* purpose of the PTO's fee setting authority.

The operative text of the AIA is § 10(a) (uncodified):

> (a) FEE SETTING.—
>
> (1) IN GENERAL.—The Director may set or adjust by rule any fee established, authorized, or charged under title 35, United States Code, or the Trademark Act of 1946 (15 U.S.C. 1051 et seq.), for any services performed by or materials furnished by, the Office, subject to paragraph (2).
>
> (2) FEES TO RECOVER COSTS.—Fees may be set or adjusted under paragraph (1) only to recover the aggregate estimated costs to the Office for processing, activities, services, and materials relating to patents (in the case of patent fees) and trademarks (in the case of trademark fees), including administrative costs of the Office with respect to such patent or trademark fees (as the case may be).

Section 10 of the AIA grants the PTO authority to adjust fees *only* to recover aggregate costs. Further, the Office must comply with other relevant law. For example, the Office must also consider the Independent Offices Appropriations Act

† Reproduced with permission from BNA's *Patent, Trademark & Copyright Journal*, 85 PTCJ 206, (Dec. 7, 2012). This is a corrected version of the article, correcting Tables 1 and 2.

[1] P.L. 112–29, 125 Stat. 284 (Sept. 16, 2011). See Sections 10, 11 and 22.

of 1952, 31 U.S.C. § 9701, the Antideficiency Act of 1982, 31 U.S.C. § 1512, the Chief Financial Officers Act of 1990, 31 U.S.C. § 902, the Administrative Procedure Act, 5 U.S.C. § 551 *et seq*., the Regulatory Flexibility Act of 1980, 5 U.S.C. § 601 *et seq*., the Paperwork Reduction Act of 1980, 44 U.S.C. § 3501 *et seq*., the limits on PTO authority set forth in 35 U.S.C. § 2, and the United States Constitution's delegation of taxing authority exclusively to Congress. Without express congressional delegated authority or waiver, the Office's fee-setting authority must be exercised within *all* current law, not just the AIA.[2]

1.1 Constitutional limits.

Congress may delegate fee-setting authority to agencies, but that authority is limited by the Constitution's delegation of taxing authority to Congress. As discussed in section 2.2 below, using fees to "encourage or discourage a particular activity" is a "tax" that requires an explicit delegation from Congress, a delegation that the PTO does not have.

1.2 The Independent Offices Appropriations Act (IOAA).

Since 1952, agencies with fee-setting authority have been governed by the IOAA. If the PTO considered the IOAA in its rule making deliberations, there is no record of it. The opinion of PTO's general counsel in support of the fee-setting rule and the rationales stated in the NPRM do not reflect PTO's awareness of the statute or its associated case law.[3]

The IOAA (31 U.S.C. § 9701) provides as follows, in relevant part:

> (b) The head of each agency (except a mixed-ownership Government corporation) may prescribe regulations establishing the charge for a service or thing of value provided by the agency. Regulations prescribed by the heads of executive agencies are subject to policies prescribed by the President and shall be as uniform as practicable. Each charge shall be—
> (1) fair; and
> (2) based on—
> (A) the costs to the Government;
> (B) the value of the service or thing to the recipient;
> (C) public policy or interest served; and
> (D) other relevant facts.
> (c) This section does not affect a law of the United States—
> (1) prohibiting the determination and collection of charges and the disposition of those charges; and
> (2) prescribing bases for determining charges, but a charge may be redetermined under this section consistent with the prescribed bases.

[2] *Federal Communications Commission v. Nextwave Personal Communications*, 537 U.S. 293, 305 (2003) ("when two statutes are capable of co-existence, it is the duty of the courts, absent a clearly expressed congressional intention to the contrary, to regard each as effective." Internal quotation and citations omitted).

[3] *See* General Counsel Bernard J. Knight, Jr., Memorandum, *USPTO Patent Fee Setting*, http://www.uspto.gov/about/offices/ogc/Fee_Setting_Opinion.pdf, (Feb. 10, 2012) (silent on IOAA); NPRM (silent on IOAA).

Subsections (b)(2)(A-D) are written in the conjunctive and have been so construed by the courts. Following the Supreme Court's 1974 landmark decision in *Nat'l Cable Television Ass'n, Inc. v. U.S.* ("*NCTA"*)[4] interpreting the IOAA, the U.S. Court of Appeals for the District of Columbia Circuit further interpreted the IOAA in several key opinions. As to the "cost to the Government" and the "value of the service or thing to the recipient," the D.C. Circuit explained "that the proper standard is not value *derived* by the recipient but rather value *conferred* on the recipient. In our view, this standard requires the fee assessed to bear a reasonable relationship to the *cost of the services rendered to identifiable recipients*"[5] (emphasis added.)

As to the IOAA's "public interest served" consideration, the D.C. Circuit explained that "[i]n *NCTA*, the [Supreme] Court invalidated the cable television annual fee because it charged cable operators a fee based in part upon 'public policy or interest served'".[6] Although some language of the IOAA "appears to allow a fee [based on agency perception of 'public policy'], charging in part for an independent public interest served (rather than solely for value conferred upon the recipient) makes the assessment a tax rather than a fee."[7] The D.C. Circuit observed that the Supreme Court "concluded that the IOAA must be narrowly read to prohibit this since there was no indication in the statute of an intent on the part of Congress to delegate the power to tax to the [agency]."[8] Rather, the IOAA's Subsections (b)(2)(C-D) identify considerations that require specific and express statutory authorizing language for agencies to encode policy through fees. Such language does not exist in the AIA.

While Section 10 of the AIA authorizes the PTO to charge fees and generally recover aggregate costs, it makes no specific reference that sets aside the IOAA. The AIA § 10(a)(1)(2) provides:

> Fees may be set or adjusted under paragraph (1) ***only*** to recover the aggregate estimated costs to the Office for ***processing, activities, services, and materials*** relating to patents [ ] including administrative costs of the Office ***with respect to such patent*** [ ] ***fees*** ….(emphasis added).

Thus, the plain language limits fee adjustments *only* for purposes of cost recovery. Moreover, the AIA's legislative history forbids the PTO from setting fees based on "the public interest served" or any "other relevant facts" except those explicitly

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[4] *National Cable Television Association, Inc. v. United States,* 415 U.S. 336 (1974) ("*NCTA*").

[5] *Capital Cities Communications, Inc. v. Federal Communications Commission*, 554 F.2d 1135, 1138 (D.C. Cir. 1976) ("*Capital Cities"*); *Seafarers International Union v. U.S. Coast Guard*, 81 F.3d 179, 185 and n.4 (D.C. Cir. 1996) ("*Seafarers"*) ("the measure of fees is the cost to the government of providing the service, not the intrinsic value of the service to the recipient"); For a detailed discussion of the court's construction of "value to the recipient" standard see *National Association of Broadcasters v. Federal Communications Commission*, 554 F.2d 1118, 1130, n. 28 (D.C. Cir. 1976) ("*NAB"*).

[6] *NAB*, 554 F.2d, at 1128, citing *NCTA*, 415 U.S. at 341.

[7] *NAB*, 554 F.2d, at 1128.

[8] *NAB*, 554 F.2d, at 1128, citing *NCTA*, 415 U.S. at 342.

delegated by Congress: it states that the AIA allows the PTO to set or adjust fees "so long as they ***do no more*** than reasonably compensate the Office for the services performed."[9] In setting fees not in accordance with the costs but for "public interest" purposes, the PTO seeks to ***do more*** than merely recover its aggregate costs – it seeks to implement through the fee structure policies which Congress did not intend. Neither the NPRM nor the PTO general counsel's opinion address these limitations.

Because there is nothing in the AIA or its legislative history to compel a different result, the AIA must be regarded as being in *pari materia* with the IOAA—that is, statutes dealing with the same subject matter or having a common purpose—to be construed together as part of an overall statutory scheme. Where this principle applies, courts look to the body of law developed under the IOAA for guidance in construing the other statute.[10] In fact, the AIA clarifies that the PTO's authority is precisely cabined within the IOAA. To the extent that the patent statutes "prescribe bases for determining charges" as contemplated by Subsection (c)(2) of the IOAA, these bases are found explicitly in the statute – "aggregate costs" bases.

1.3 The PTO's proposed fee schedule.

The NPRM details the key proposed fee changes and costs in Tables 4-36.[11] It then provides what it calls an "overall comparison" of patenting costs, but it does so in anecdotal cases,[12] arriving at meaningless conclusions such as "initial appeals fees decrease," when what matters is end-to-end costs. The NPRM fails to account for the actual incidence rate for each fee item in patent applications and therefore fails to estimate the average fee increase for applicants. This is particularly important when one considers the radical fee increases proposed for claims, Requests for Continued Examination ("RCE") and appeals. When incident rates for all these are accounted for, a far different picture emerges.

Table 1 compares the average fees for large entities, demonstrating that the average fees for a patent application incurred before it issues or abandoned (front-end fees) would increase by 37 percent. Because a smaller share of small entity applicants tend to file RCEs or appeals (perhaps due to their limited financial resources), the average front-end fee increase they would incur under the PTO proposal is 36 percent (see Table 2.)

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[9] House Report 112–98, Part 1, (Jun. 1, 2011), p. 49.

[10] U.S. General Accounting Office, *Principles of Federal Appropriations Law,* Vol. III, Ch. 12, pp. 172–174, (3rd Ed. Sep. 2008) (describing various agency-specific user fee statutes and collecting cases where those were treated by the courts in *pari materia* with the IOAA); *See also FCC v. Nextwave,* note 2 supra.

[11] NPRM, at 55,039-57.

[12] NPRM, at 55,057-59.

Table 1. Proposed fee costs for average essential patenting activities (large entity).

Fee Item	Average incidence per unit	Present fees set by AIA		USPTO Proposed fees (NPRM)		Large-Entity cost increase over that enacted in AIA
		Large-Entity fee	Large-Entity average cost	Large-Entity fee	Large-Entity average cost	
	u	f_1	$f_1 \cdot u$	f_2	$f_2 \cdot u$	
For filing, search & examination	1	$1,250	$1,250	$1,600	$1,600	28%
For each independent claim in excess of 3	0.50 *a*	$250	$125	$420	$210	68%
For each claim in excess of 20 total claims	3.26 *a*	$60	$195	$80	$261	33%
For a Request for Continued Examination	0.55 *b*	$930	$509	$1,350 *g*	$739	45%
For an Appeal:						
Filing Notice of Appeal	0.120 *c*	$620	$74	$1,000	$120	
Filing an Appeal Brief	0.078 *c*	$620	$48			
Filing an Appeal	0.048 *d*			$2,000	$96	
Total for Appeals			$122		$216	77%
Average Front-End Application fees			**$2,202**		**$3,025**	**37%**
Issue fee	1	$1,740	$1,740	$960	$960	-45%
Maintenance Fees:						
At 3.5 years	0.99 *e*	$1,130	$1,123	$1,600	$1,590	42%
At 7.5 years	0.71 *e*	$2,850	$2,029	$3,600	$2,563	26%
At 11.5 years	0.50 *e*	$4,730	$2,365	$7,400	$3,700	56%
Average Back-End Patent fees			**$7,257**		**$8,814**	**21%**
Total Average patent fees			**$9,459**		**$11,839**	**25%**

a. FY 2010 Fee Report, Appendix 1 to USPTO FY 2012 President's Budget, p. 139 ("Fee Report"). Number of excess claims is the ratio between the total fee collection for each fee category and the fee set for that category. Incidence is the number of Large-entity excess claims normalized by the number of all Large-entity UPR applications in FY 2010.
b. Fee Report, p. 140; Number of RCE filings is the ratio between the total fee collection for each fee category and the fee set for that category. Incidence is Large-entity RCE filings normalized by the number of all Large-entity UPR applications in FY 2010.
c. Fee Report p. 141 and USPTO Response to FOIA Request No. F-12-00105. Normalized by number of Large-Entity UPR applications in FY 2010.
d. FY 2010 appeal filings at BPAI at http://www.uspto.gov/ip/boards/bpai/stats/receipts/index.jsp. Normalized by Large-Entity share of appeals (note c) and the total number of UPR applications in FY 2010.
e. USPTO Ammual Report FY 2011, p.63. FY 2010 renewal rates.
g. RCE fee is average of first ($1200) and second or subsequent ($1700) RCE fees, weighted per usage rates of 70% and 30% respectively as published at 77 FR 55043.

Table 2. Proposed fee costs for average essential patenting activities (small and micro entities)

Fee Item	Average incidence per unit	Present fees set by AIA		USPTO Proposed fees (NPRM)			Small-Entity cost increase over that enacted in AIA	Micro-Entity cost increment over Small Entity cost enacted in AIA
		Small Entity fee	Small Entity average cost	Small Entity fee	Small Entity average cost	Micro Entity average cost		
	u	f_1	$f_1 \cdot u$	f_2	$f_2 \cdot u$	$0.5 f_2 \cdot u$		
For filing, search & examination	1	$625	$625	$800	$800	$400	28%	-36%
For each independent claim in excess of 3	0.54 *a*	$125	$68	$210	$114	$57	68%	-16%
For each claim in excess of 20 total claims	4.35 *a*	$30	$131	$40	$174	$87	33%	-33%
For a Request for Continued Examination	0.30 *b*	$465	$139	$675 *g*	$202	$101	45%	-27%
For an Appeal:								
Filing Notice of Appeal	0.072 *c*	$310	$22	$500	$36	$18		
Filing an Appeal Brief	0.047 *c*	$310	$15					
Filing an Appeal	0.029 *d*			$1,000	$29	$15		
Total for Appeals			$37	$1,500	$65	$33	77%	-11.7%
Average Front-End Application fees			**$1,000**		**$1,356**	**$678**	**36%**	**-32%**
Issue fee	1	$870	$870	$480	$480	$240	-45%	-72%
Maintenance Fees:								
At 3.5 years	0.99 *e*	$565	$562	$800	$795	$398	42%	-29%
At 7.5 years	0.71 *e*	$1,425	$1,015	$1,800	$1,282	$641	26%	-37%
At 11.5 years	0.50 *e*	$2,365	$1,183	$3,700	$1,850	$925	56%	-22%
Average Back-End Patent fees			**$3,629**		**$4,407**	**$2,203**	**21%**	**-39%**
Total Average patent fees			**$4,629**		**$5,763**	**$2,881**	**25%**	**-38%**

a. FY 2010 Fee Report, Appendix 1 to USPTO FY 2012 President's Budget, p. 139 ("Fee Report"). Number of excess claims is the ratio between the total fee collection for each fee category and the fee set for that category. Incidence is the number of small-entity excess claims normalized by the number of all small-entity UPR applications in FY 2010.
b. Fee Report, p. 139. Number of RCE filings is the ratio between the total fee collection for each fee category and the fee set for that category. Incidence is small-entity RCE filings normalized by the number of all small-entity UPR applications in FY 2010.
c. Fee Report, p. 141 and USPTO Response to FOIA Request No. F-12-00105. Normalized by number of Small-Entity UPR applications in FY 2010.
d. FY 2010 appeal filings at BPAI at http://www.uspto.gov/ip/boards/bpai/stats/receipts/index.jsp. Normalized by Small-Entity share of appeals (note c) and the total number of UPR applications in FY 2010.
e. USPTO Ammual Report FY 2011, p.63. FY 2010 renewal rates.
g. RCE fee is average of first ($600) and second or subsequent ($850) RCE fees, weighted per usage rates of 70% and 30% respectively as published at 77 FR 55043.

The strongest indication that the PTO is deviating materially from Congress' fee policies is the fact that it proposes percentage increases for the front-end fees that are nearly ***double*** that of the increases in back-end fees, which are dominated by the maintenance fees.

While the analysis in Table 1 and Table 2 does not include elasticity effects on filing and incident rates due to higher fees, it is indicative of the relative focus of the Office on increasing disproportionately fees that can suppress applicant filings for its own administrative convenience, rather than this Nation's interests in securing inventors' rights. So much for the Office's purported policy goal of "fostering innovation." The deference that the Office is entitled to and the significance of this point and the public policies associated with the front to back-end fee ratios will be discussed in Part II of this article.

2 The PTO has neither power nor expertise to set policy for the Nation's patent system.

In an ambitious attempt to grab power reserved for Congress, the PTO asserts that the AIA "[s]ection 10 authority includes *flexibility* to set individual fees in a way that furthers *key policy considerations*, while taking into account the cost of the respective services"[13] (emphasis added). Neither the AIA nor any other law contains a basis for this assertion. Yet, the NPRM further explains that in setting its proposed fee structure the PTO "considers three key *policy factors*: (1) Fostering innovation; (2) facilitating effective administration of the patent system; and (3) offering patent prosecution options to applicants."[14] While these goals are laudable in the abstract, there is no law that empowers the PTO to set fees based on its own "policy factors." This proposed rule and its "policy" rationale are *ultra vires*. Rather, as shown below, Congress retained for itself the power to regulate and balance these policy factors.

Section 2(b)(2) of Title 35 empowers the PTO to "establish regulations, not inconsistent with law," for several enumerated purposes, *none of which include the broad policy factors* which the PTO claims to rely on in setting fees. While the Patent Act authorizes the PTO to promulgate rules governing "the conduct of proceedings in the Office" (35 U.S.C. §2(b)(2)(A)), it does not empower the Office to regulate the "administration of the *patent system*." There are no policy "gaps" in the statute for the agency to fill. When Congress delegates authority to the PTO to consider public interests such as "the effect of any such regulation on the economy, the integrity of the *patent system,* the efficient administration of the Office, and the ability of the Office to timely complete proceedings," it does so narrowly and *explicitly* in *selected* statutes *specific* to certain proceedings (*see* AIA § 6, 35 U.S.C. §§ 316(b), 326(b) governing *inter partes* and post grant reviews). No such delegation exists in Section 10 or elsewhere in the AIA.

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13 NPRM, at 55,028, emphasis added.

14 NPRM, at 55,033. See the PTO's accompanying discussion on these three "policy factors."

When Congress delegates authority to the PTO to act pursuant to public interests such as "fostering innovation," it does so *explicitly*, for example by providing for:

- 50 percent discount on small-entity fees (Act of 1982 § 1, 35 U.S.C. §§ 2(b)(2)(E) and 41(h)(1));
- 75 percent discount on micro-entity fees (AIA § 10(g), adding 35 U.S.C. § 123);
- Authority to refine the definition of "micro-entity" (AIA § 10(g), 35 U.S.C. 123(e));
- Facilitate and expedite the processing of patent applications filed electronically (35 U.S.C. § 2(b)(2)(C));
- A 75 percent discount on filing fee for electronic filing of applications ((AIA § 11, 35 U.S.C. § 41(h)(3));
- Subsidy of application processing costs by authorizing post-grant charges for maintenance fees on issued patents (Act of 1982 § 3(b), AIA § 11, 35 U.S.C. §41(b); maintenance fees set to recover 50 percent of patent processing costs.[15]);
- Authority to expedite and examine out of turn patent applications that are important to the national economy or national competitiveness (AIA § 25 adding 35 U.S.C. § 2(b)(2)(G)); and
- Dissemination of patent publications to public libraries at low fees (Act of 1982 § 3(d), AIA § 11, 35 U.S.C. §41(d)(2)(B)).

When Congress delegates authority to the PTO to act pursuant to public interests such as increasing flexibility and "offering patent prosecution options to applicants," it does so *explicitly*, for example by statutes providing for:

- Authority to prioritize and examine out of turn patent applications upon payment of an additional fee (AIA § 10(h));
- Automatic extension of time (upon payment of a fee) for applicant's reply to an action on an application (Act of 1982 § 5, AIA § 11, 35 U.S.C. § 41(a)(8));
- Authority to refund fees on abandoned applications (AIA § 11, 35 U.S.C. §41(d)(1)(D));
- Supplemental examination of issued patents (AIA § 12, adding 35 U.S.C. § 257);
- Awarding a filing date even to applications submitted with missing parts (Act of 1982 § 5, amending 35 U.S.C. § 111)
- Deeming any paper to be considered filed in the PTO when it is deposited in the U.S. Postal Service (Act of 1982 § 12, amending 35 U.S.C. § 21)
- Ability to correct inventorship in an application with no prejudice (Act of 1982 § 6(b), amending 35 U.S.C. § 256)
- Revival of unintentionally abandoned applications (Act of 1982 § 3(a), 35 U.S.C. § 41(a)(7))

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[15] P.L. 96-517, 94 Stat 3015 (Dec. 12, 1980); *See* House Report 96-1307(I), 8-9 (1980) (patent applicants should bear the Office's patent costs through the payment of fees split in equal amounts between application "processing" fees and post-grant "maintenance" fees). Prior to its taking effect, the 1980 law was amended by P.L. 97-247 on Aug. 27, 1982 ("Act of 1982"). To effect full user funding of PTO, the latter doubled both the patent processing and the maintenance fees from the levels authorized by P.L. 96-517, maintaining their relative proportions wherein each was intended to produce 50% of the Office's patent fee revenue. The increased new fees went into effect on October 1, 1982.

Note that many of the public policy driven provisions listed above were enacted alongside significant fee legislation in the Act of 1982 and the AIA, indicating Congress' awareness of the inexorable connection between patent fees and the very public policy goals which the PTO claims to be within its regulatory dominion. Note also that when Congress does delegate to the PTO limited fee-based policy power, it does so under close supervision.[16]

Congress has not intended the PTO to consider factors other than its aggregate costs of enumerated items. The PTO's seemingly constructive policy goals do not save its proposed fee schedule rule from being "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law."[17] By making up its own policy goals not found in statute, the PTO's proposed fee structure is *ultra vires* and a prima facie arbitrary and capricious rule per se: "*Normally*, an agency rule would be arbitrary and capricious if the agency has *relied on factors which Congress has not intended it to consider*."[18]

2.1 The PTO may not set fees to "encourage or discourage any particular service."

Throughout the NPRM, the PTO notes that it proposes to set fees for purposes that include "facilitating the effective administration of the patent system" – a euphemism for fees set to affect applicants' behavior. Indeed, the NPRM explains that it would "help the Office to effectively administer the patent system by encouraging applicants to engage in certain activities."[19] For example, fees for independent claims in excess of 3 are increased by 68 percent – not based on cost to the PTO – but "to facilitate the prompt conclusion of prosecution of an application."[20] Despite proposing one of the steepest fee increases, the Office provides no cost data related to claim fees in its costing methodology document[21] and admits that for claim fees, "the PTO does not typically maintain historical cost information separate from that included in the average overall cost of activities during patent prosecution."[22] Indeed, the NPRM admits that these are "fees that will not be set using cost data."[23]

Noting that 30 percent of RCEs are *second and subsequent* RCEs, the NPRM proposes to increase fees for such applications by 83 percent and posits without any

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[16] *See* AIA § 10(g) codifying § 123(e), requiring the PTO to inform the Congressional judiciary committees at least 3 months before any PTO redefinition of "micro-entity" takes effect.

[17] 5 U.S.C. § 706(2)(A).

[18] *Motor Vehicle Manufacturers Association v. State Farm Mutual Automobile Insurance Co.*, 463 U.S. 29, 43 (1983) ("*State Farm*") (emphasis added.)

[19] NPRM, at 55,054.

[20] NPRM, at 55,030.

[21] PTO, *USPTO Section 10 Fee Setting – Activity-Based Information and Costing Methodology*, (Sept. 6, 2012) at www.uspto.gov/aia_implementation/aia_section_10_cost_supplement.pdf .

[22] NPRM, at 55,054.

[23] NPRM, at 55,040-41.

factual support that "[t]hose applications that cannot be completed with the first RCE do not facilitate an effective administration of the patent system with the prompt conclusion of patent prosecution."[24] It therefore concludes that "[s]etting the second and subsequent RCE fees higher than the fee for the first RCE helps to recover costs for activities that strain the patent system"[25] – clearly indicating that the higher fee is set to discourage this particular service on no basis other than a *non sequitur* assertion that a second RCE prolongs prosecution of an application.

As to these PTO policy goals, the PTO general counsel's opinion states: "[w]hile Section 41 authorizes setting fees to recover costs of individual services, Section 10 authorizes setting fees for a broad range of services to recover *aggregate* costs"[26] (emphasis in original). The opinion then leaps to an incredible inference: "Section 10 thus permits any individual patent fee to be set or adjusted so as *to encourage or discourage any particular service*, so long as the aggregate revenues for all patent fees match the total costs of the Patent operation"[27] (emphasis added.) This conclusion undergirds the NPRM's fee structure under the Office's *ultra vires* efforts to promulgate patent policy rules that are "not in accordance with law" and therefore unlikely to withstand judicial review.

2.2 The IOAA forbids agencies from exercising undelegated "policy" authority to deviate from cost-recovery or "value to the recipient."

Under the IOAA, the PTO has no authority to adjust fees "to encourage or discourage a particular activity."[28] This is because fee charges set to achieve public interest *policy* goals are *taxes.* While "taxes that seek to influence conduct are nothing new,"[29] the power to levy such taxes is reserved for Congress. The Supreme Court explained this in *NCTA* by noting that "[t]he lawmaker may, in the light of the 'public policy or interest served,' make the [tax] heavy if the lawmaker wants to discourage the activity; or it may make the levy light if a bounty is to be bestowed. … Such assessments are in the nature of 'taxes' which under our constitutional regime are traditionally levied by Congress."[30] The PTO's proposed fee structure would therefore infringe "on Congress' exclusive power to levy taxes."[31] Rather,

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[24] NPRM, at 55,043.

[25] NPRM, at 55,043.

[26] PTO General Counsel's Opinion, p. 3.

[27] *USPTO Patent Fee Setting Opinion*, Memorandum of Bernard J. Knight, Jr., General Counsel (Feb. 10, 2012), p. 4 at http://www.uspto.gov/aia_implementation/fee_setting_opinion.pdf .

[28] *Seafarers,* 81 F.3d at 183 ("Such policy decisions, whereby an agency could, for example, adjust assessments to ***encourage or discourage a particular activity***, would, according to the [Supreme] Court, 'carr[y] an agency far from its customary orbit' and infringe on Congress's exclusive power to levy taxes." Citing *NCTA*, 415 U.S. at 341) (emphasis added.)

[29] *National Federation of Independent Business v. Sebelius*, 567 U. S. __, 132 S.Ct. 2566, 2596 (2012).

[30] *NCTA*, 415 U.S. at 341.

[31] *Seafarers,* 81 F.3d at 183.

specific and express statutory authorizing language is required for agencies to encode public policy through fees.[32]

2.3 The AIA does not waive Constitutional or IOAA limits.

The AIA provides no such express authority and in any event the statute and legislative history forbids the PTO from doing so: the statute permits the Office to set fees "***only*** to recover the aggregate estimated costs to the Office"[33] and its accompanying House Report states that the AIA allows the PTO to set or adjust fees "so long as they ***do no more*** than reasonably compensate the PTO for the services performed."[34] In setting fees not "*only* to recover the aggregate estimated costs" but for purposes of discouraging certain filing activities, the PTO seeks to *do more* than merely recover its aggregate costs – it seeks to implement through the fee structure policies to suppress applicants' filings which Congress did not intend.

Had Congress wanted the PTO to set fees higher for applications that "do not facilitate an effective administration of the patent system" it would have done so. Rather, Congress has historically resisted dozens of legislative attempts for patent fee-setting schemes based on such arbitrary unsupportable judgments. While space does not permit listing these attempts exhaustively here, a few examples spanning nearly two centuries include: recent times, when Congress refused to adopt PTO's proposed progressive fee increases in 2002;[35] more than half a century ago when the PTO proposed an excess claim fee for each claim above a total of 5 "to screen" a "deluge" of applications;[36] and as early as 1830, when Congress rejected an increase in patent fees to discourage filing of "meritless applications."[37]

The PTO has no authority to throttle its workload by suppressing incoming filing rates through disproportionate fee increases. Congress has specifically instructed the PTO how to deal with the workload of *all* application types and services to avoid the "strain" on its resources: in § 10(a)(1)(2) of the AIA the Office is directed to set

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[32] *NAB*, 554 F.2d, at 1128, citing *NCTA*, 415 U.S. at 342.

[33] AIA § 10(a)(1)(2). It does ***not*** say "to recover *only the aggregate estimated costs* to the Office."

[34] House Report 112–98, Part 1, (Jun. 1, 2011), p. 49.

[35] PTO, *21st Century Strategic Plan*, fee proposal to Congress (Jun. 2002), FAQ at http://web.archive.org/web/20021005230103/http://www.uspto.gov/web/offices/com/strat2001/faq.htm#q53 ("fees for excess claims will be based on a highly progressive system aimed at *strictly limiting* applications containing very high numbers of claims. In order to prevent "end-runs" of the claims fees, high fees are also being imposed on *excess continuations* and on the submission of patentably indistinct claims." Emphasis added.) These proposed fees are compared to a subsequently-revised schedule at http://www.uspto.gov/web/offices/com/strat21/feeproposalcomparison.htm.

[36] Rejected a provision in HR 4983 proposing a $5 excess claim fee for each claim above a total of 5: *To Increase Certain Patent And Trademark Fees*, House of Representatives, Subcommittee No. 3 of the Committee on the Judiciary, 84th Cong., 1st Sess., statement of Robert C. Watson, Commissioner of Patents, p. 24 (Jun. 3, 1955) ("A substantial fee is necessary to make certain that the Patent Office is not *deluged with applications which disclose and claim devices of little value*." Emphasis added.)

[37] *See* 6 *Gale & Seaton's Register of Debates in Congress* 377 (21st Cong., 1st Sess.1830).

fees for major items in a manner that *recovers* its "aggregate estimated costs;" and § 41(d)(2) provides that the PTO "*shall* establish fees for all other processing, services, or materials relating to patents… to *recover* the estimated average cost to the Office of such processing, services, or materials…" When the PTO complies with these statutory directives for cost recovery and acquires the commensurate resources, there is no such thing as "activities that strain the patent system." In taking on a policy role not expressly specified in the statute, the PTO exceeds its authority under the AIA. The PTO does not possess plenary fee-setting authority simply because Congress has endowed it with *some* authority to set fees.[38]

2.4 The PTO has neither mandate nor agency expertise to determine the economically efficient levels for patent fees.

One cannot presume the PTO to be a neutral disinterested policy-balancer that can set fees at economically efficient levels, because it has often demonstrated having a prima facie conflict with its direct administrative stake in the outcome. More importantly, as an agency with the sole task and mandate to determine *patentability* of applications it receives, the agency lacks the necessary information and expertise to determine *any* matters bearing on *infringement* of patents and the necessary measures applicants use for appropriating returns from inventions in ways that *secure investments* that "foster innovation". These include the scope, the number of claims, and the number of applications or RCEs *necessary* to obtain claims that *adequately* protect inventions in the market place. The PTO lacks the information and expertise to determine what aspects of patent applications "do not facilitate an effective administration of the patent system." It lacks the institutional visibility into the invention development and financing process and thus lacks information and expertise required to balance the public interests that it purports to consider – "fostering innovation" and "facilitating effective administration of the patent system."

A result of this lack of expertise and the Office's disconnect from invention appropriation and patent valuation practices is its facially flawed analysis for the purported economic gain associated with its fee increase proposal. In its Regulatory Impact Analysis,[39] the PTO projects a resultant reduction of patent pendency that it believes will contribute an incremental net monetized benefit to patent stakeholders and society of nearly $7 billion for the period FY 2013 – FY 2017.[40] The PTO explains that "[r]educing pendency increases the private value of a patent because the more quickly a patent is granted, the more quickly the holder can commercialize

[38] *Railway Labor Executives' Association v. National Mediation Board.*, 29 F.3d 655, 670 (D.C.Cir.1994) (*en banc*) (An agency does not "possess[ ] plenary authority to act within a given area simply because Congress has endowed it with some authority to act in that area.")

[39] PTO, *Regulatory Impact Analysis - Setting and Adjusting Patent Fees in accordance with Section 10 of the Leahy-Smith America Invents Act*, Notice of Proposed Rulemaking, Appendix A, (Sept. 6, 2012) ("RIA"). www.uspto.gov/aia_implementation/aia_section_10_ria_doc-omb_9-6-12.pdf.

[40] NPRM at 55,029; RIA at Appendix A, Tables A-1 and A-2.

the innovation."[41] Applying a discount rate to a purported earlier acquisition of the lump sum patent value, the Office then calculated the increase in patent value from the reduction in pendency under its proposed alternative relative to a set baseline. However, this analysis is predicated on counterfactual assumptions on the invention commercialization process and that the patent value is acquired and accrues to patentees *only after* patent grant.

If this analysis were credible, the PTO would have had very little trouble long ago in persuading Congress that a $7 billion return to the economy is worth much more than any other possible return on Government investment of $1 billion that Congress diverted from the Office. While there are substantial benefits for reduced pendency, the market reality is that the major portion of patent value is normally accrued shortly after the *application filing date* – not the patent issue date. Patent value is recognized in legal risk evaluation and company valuation computations long before allowance. For example, dramatic pre-money valuation changes specifically attributable to patent rights held by venture-backed startups occur mostly after the patent application filing dates and well before the grant dates.[42] Similar empirical evidence in specific industries for this major pre-grant value accrual is found in the biotechnology industry,[43] the software industry, [44] and the semiconductor industry.[45] Moreover, the PTO entirely ignored the value of applicants' provisional rights "to obtain a reasonable royalty from any person who, during the period beginning on the date of *publication of the application*" infringes a claim in the published patent application[46] – well before the patent issues, and ignored patent term adjustment that often creates value that *exceeds* any loss due to delayed issue.

By ignoring "an important aspect of the problem" – the major value of pending patent applications – the PTO calculates that pendency reduction by 6 months would result in an increase of private patent value of $1,700 to $2,600.[47] If only the lower range for this incremental value is conservatively assumed, one necessarily obtains an incremental private patent value of more than $7,000 for a pendency reduction of two years.

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[41] NPRM at 55,032.

[42] C. Häussler, D. Harhoff, and E. Müller, *To Be Financed or Not… - The Role of Patents for Venture Capital-Financing*, (2012). ZEW - Centre for European Economic Research Discussion Paper No. 09-003. Available at http://dx.doi.org/10.2139/ssrn.1393725.

[43] J.A. Baum, B.S. Silverman, "Picking Winners or Building Them? Alliance, Intellectual, and Human Capital as Selection Criteria in Venture Financing and Performance of Biotechnology Start-Ups," 19 *Journal of Business Venturing*, 411-436 (2004).

[44] Iain M. Cockburn and Megan J. Macgarvie, "Patents, Thickets and the Financing of Early-Stage Firms: Evidence from the Software Industry," 18 *Journal of Economics & Management Strategy*, No. 3, 729–773 (Fall 2009).

[45] D.H. Hsu and R.H. Ziedonis, "Resources as Dual Sources of Advantage: Implications for Valuing Entrepreneurial-Firm Patents," *Management Department Working Paper* (Aug. 2012), at http://www-management.wharton.upenn.edu/hsu/inc/doc/papers/david-hsu-signaling.pdf

[46] *See* 35 U.S.C. § 154(d).

[47] RIA at 184.

If the PTO's estimate of incremental private patent value were reasonably within the correct range, the majority of applicants would find the Prioritized Examination track a bargain they could not refuse—for only $4800 applicants get the two year acceleration that the PTO values at upwards of $7000. Yet, in FY 2012 only about 5,000 requests were made for Prioritized Examination of applications (*less than 1 percent* of those filed in the year).[48] If only 1% of *actual* applicants regard a two year reduction in pendency worth $4,800, then an estimate that the *average* applicant values it at over $7000 is incredible fiction, or in dignified legal jargon, "arbitrary and capricious." This is because the agency "entirely failed to consider an important aspect of the problem [and] offered an explanation for its decision that runs counter to the evidence before the agency"[49] in its own statistical records.

3 The AIA vests no discretion with the PTO to set fees based on its desired "operating reserve" level.

The NPRM states that the PTO proposes to set its fees higher based, among other factors, on "*building* a three-month patent operating reserve by FY 2017 to support a sustainable funding model."[50] It states the "additional revenue from the proposed fee schedule will also recover the aggregate cost of *building* a three-month patent operating reserve by FY 2017,"[51] and that in order to achieve this estimated target, "small and micro entities would pay some higher fees than under some of the other alternatives considered."[52]

The PTO hastens to "assure" the public that under the discretion it purports to possess, it would be "reducing patent fees once the operating reserve reaches an optimal level"[53] – clearly admitting that these charges are to be borne only by an arbitrary subset of applicants only to *build* assets that bear no "reasonable relationship to the cost of the services rendered to identifiable recipients." The AIA and the IOAA accord the PTO no discretion to set fees based on its desired level of an "operating reserve" because contrary to the PTO 'creative accounting' assertion, "building" the unobligated "reserve" is *not* a "cost."

3.1 Unobligated cash for PTO "operating reserve" is not a "cost" cognizable under the AIA or the IOAA.

AIA § 10(a)(1)(2) enumerates the only cost elements that the PTO may use for "the aggregate estimated costs to the Office." These are: "processing, activities, services, and materials relating to patents" – none of which are "costs" for building a reserve;

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[48] PTO, Prioritized Examination Statistics, http://www.uspto.gov/patents/init_events/Track_One.jsp.

[49] *State Farm,* 463 U.S. at 43.

[50] NPRM at 55,030.

[51] NPRM at 55,028.

[52] NPRM at 55,073.

[53] PTO, FY 2013 President's Budget, p. 9 (Feb. 13, 2012) ("FY13 Budget").

and "administrative costs of the Office with respect to such patent [ ] fees" – none of which are "costs" for building a reserve.[54]

The PTO explains that its proposed fees are based on known costs plus "an operating reserve for long-term financial stability to pay *for unknown costs* or offset revenue loss due to the fluctuation *in demand for service*."[55] This logic is perverse because when "demand for services" declines – a condition which reduces the work the Office must perform – the aggregate costs cannot increase. The AIA specifically excludes "recovery" of costs that will never occur. Furthermore, "unknown costs" are by definition non-estimable and are therefore not cognizable as part of the "aggregate *estimated* costs to the Office" under the AIA. Finally, the IOAA "requires the fee assessed to bear a reasonable relationship to the cost of the services rendered *to identifiable recipients*"[56] – neither the particular services nor the recipients are identifiable here under unobligated reserve funds because the PTO admits that the "costs" are "unknown."

The Patent Public Advisory Committee ("PPAC"), with whom the PTO must consult prior to setting fees under the AIA,[57] recognized in its memorandum soliciting comment from the public that the "cost of building a patent operating reserve" is not cognizable under the AIA:

> **a**. Should the USPTO maintain an operating reserve?
> **b**. If "yes," do you believe it is reasonable for applicants to pay fees *above and beyond the fees needed to cover aggregate costs* to fund the operating reserve?[58] (emphasis added).

Whether reasonable or not, the AIA does not delegate to the PTO the statutory authority to charge "fees *above and beyond the fees needed to cover aggregate costs*" to the Office.

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[54] FY13 Budget, at 8 (PTO admits that building a reserve is not an "administrative cost," by stating that the Office has worked to "identify options for setting patent fees to only recover the aggregate estimated cost of the patent operations, including *administrative costs* to the USPTO ***and*** a reasonable *operating reserve*" (emphasis added).)

[55] PTO, *Executive Summary: Patent Fee Proposal*, Submitted to the Patent Public Advisory Committee, p. 20, (Feb. 7, 2012) at www.uspto.gov/aia_implementation/fee_setting_-_ppac_hearing_executive_summary_7feb12.pdf#page=20

[56] *Capital Cities* 554 F.2d at 1138 (emphasis added.); *Seafarers*, 81 F.3d at 183 ("fees cannot be charged based on a perceived furthering of public policy goals if those fees are unrelated *to a specific service provided by the agency to an identifiable recipient*" (emphasis added)); Executive Office of the President, Office of Management and Budget, Circular A-25, User Charges, § 6, (revised 1993), www.whitehouse.gov/omb/circulars_a025 ("A user charge, as described below, will be assessed against each *identifiable recipient* for special benefits derived from Federal activities beyond those received by the general public.")

[57] AIA § 10(d).

[58] Patent Public Advisory Committee, Memorandum - PPAC Questions for Fee Setting Hearings, p. 1, (Feb. 7, 2012) at www.uspto.gov/about/advisory/ppac/ppac_questions_for_fee_setting_hearing.pdf

Table 3. PTO's financial projections based on its proposed fees.

Item (Dollars in millions) (a)	FY 2011	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016	FY 2017
Planned "Operating Requirements"			$2,549	$2,702	$2,809	$2,846	$2,945
Less Other Income			-18	-18	-18	-18	-18
Net "Operating Requirements"			2,531	2,684	2,791	2,828	2,927
Planned Deposit in Operating Reserve			73	200	143	125	95
Total Aggregate "Cost Estimate"			2,604	2,884	2,934	2,953	3,022
Aggregate Revenue Estimate			2,604	2,884	2,934	2,953	3,022
Target Operating Reserve			637	676	702	712	736
Operating Reserve Ending Balance		121	194	394	537	662	757
Utility, plant, and reissue (UPR)	(c)		(b)				
Applications filed	506,924	533,308	565,300	599,200	632,200	666,900	700,300
Production Units (PU)	508,549	548,051	620,600	671,900	694,200	645,200	656,200
End of Year Backlog	690,967	633,812	529,100	421,600	329,500	328,400	358,000
Examination Capacity (Year-end)	6,690	7,831	8,700	8,600	8,300	8,300	8,200
Ratios:	(c)						
Average Examination capacity in FY	6,409	7,261	8,266	8,650	8,450	8,300	8,250
PU per Examiner	79.3	75.5	75.1	77.7	82.2	77.7	79.5
"Operating requirement" per PU	$3,594	$3,617	$4,078	$3,995	$4,020	$4,383	$4,461
Aggregate "cost estimate" per PU			$4,196	$4,292	$4,226	$4,577	$4,605
"Operating requirement" per examiner			$306,213	$310,289	$330,296	$340,723	$354,788
Aggregate "cost estimate" per examiner			$315,044	$333,410	$347,219	$355,783	$366,303

(a) - Table 3, NPRM at 55035; (b) - Table 2, NPRM at 55034; (c) USPTO Annual Report FY 2012, "Op. Req."/PU from p. 19.

As seen in Table 3, it appears that the PTO uses the term "operating requirements" to describe its estimated operating costs and the term "Aggregate Cost Estimates" to include its "Planned Deposit in Operating Reserve." That the Office plans to charge for providing patent services more than its aggregate costs per application is evident in Table 3 from the fact that the Office is projected to dispose of more applications (production units) than it receives (working on more units and reducing the backlog from 634,000 to 358,000) while still having over $750 million left over in FY 2017 – a reserve increase of $636 million. Another troubling aspect of PTO cost accounting for purposes of setting fees is evident in Table 3 – it results in significantly higher cost ("operating requirements" per PU) than that under the PTO's actual cost performance in FY 2011 and FY 2012. The NPRM does not disclose the cost components that went into the projected "operating requirements" or how the cost estimates it gave for individual services aggregate to those levels.

In any event, the PTO is not precluded from establishing an operating reserve from fees it collects (and receives through congressional appropriations) that are based solely on aggregate costs cognizable under the law. However, it must establish such reserve in accordance with law, as explained below.

3.2 The Antideficiency Act and the IOAA restrict the PTO's authority to accumulate an "operating reserve" as contingent outlays for meeting its liabilities; accordingly a reserve can only be funded and appropriated from the Office's unearned revenue accounts.

As the *Budgetary Reserve* section of the U.S. Government Accountability Office's publication on standard terms, definitions, and classifications states, "[e]xcept as specifically provided by law, no reserves shall be established other than as authorized under the Antideficiency Act (31 U.S.C. § 1512)."[59] The Antideficiency Act arises out of tussles between Congress and the President over the power of the purse. The Act, § 1512, § 1517(a), requires executive branch agencies to either spend monies appropriated for the year appropriated, or else to give Congress a specific explanation and accounting for held-over funds. If an agency wants to build a reserve, the reserve must be *apportioned* (that is, held in a specific account under specific procedures) *out only of funds appropriated* by Congress. This Act provides in pertinent part in 31 U.S.C. § 1512(c)as follows:

> (1) In apportioning or reapportioning an appropriation, a reserve may be established only—
> (A) to provide for contingencies;
> (B) to achieve savings made possible by or through changes in requirements or greater efficiency of operations; or
> (C) as specifically provided by law.
> (2) A reserve established under this subsection may be changed as necessary to carry out the scope and objectives of the appropriation concerned. When an official designated in section 1513 of this title to make apportionments decides that an amount reserved will not be required to carry out the objectives and scope of the appropriation concerned, the official shall recommend the rescission of the amount in the way provided in chapter 11 of this title for appropriation requests. Reserves established under this section shall be reported to Congress as provided in the Impoundment Control Act of 1974 (2 U.S.C. 681 et seq.).

Thus, the Antideficiency Act in § 1512(c)(1)(A) permits the PTO to build an "operating reserve" "to provide for contingencies" which the PTO contemplated, *but only from funds previously appropriated* by Congress. The PTO has no legal authority to *build* an operating reserve through self-help. If the PTO wants an operating reserve, it must ask for an appropriation, and must "apportion" it using statutory procedures.

The Office seeks an "operating reserve" sufficient to continue to provide patent services for a period of three months in the event that the revenue stream is disrupted. Because the First Office Action backlog is much longer than three months, in this event, the PTO would be spending the reserve on *older* applications for which fees have been previously collected as *unearned revenue*.[60] But the IOAA requires that fee revenue from identifiable applicants - applicants whose applications are drawn from the backlog – be used to provide services to those applicants, not from *higher* fee charges on new applications. The PTO must therefore seek congressional appropriations from the unearned revenue accounts to fund any reserve to be expended on the backlog.

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[59] GAO, *A Glossary of Terms Used in the Federal Budget Process* (5th ed.), GAO-05-734SP, p. 25, (Sept. 2005).

[60] Unearned revenue represents fees that have been received by the PTO for requested services that have not been substantially completed. This includes patent applications in the backlog for which the PTO has already collected upfront processing fees. As of FY 2012 end, the unearned patent revenue was $765 million. *See* PTO, FY 2012 Annual Report, at 99.

3.3 The PTO undermines Congress' statutory scheme for establishing a reserve.

Congress enacted a particular approach for establishing a reserve for the PTO and for examining the backlog. Two reserve mechanisms were established: the first is "Patent and Trademark Office Appropriation Account in the Treasury of the United States" created by 35 U.S.C. § 42(b). When applicants pay fees, and Congress does not appropriate those fees to the PTO's use, those fees accumulate in the § 42(b) account. However, Congress has not appropriated all of that money—roughly $1 billion is nominally held at this Treasury account, but cannot be expended by the PTO because of "fee diversion" over the last two decades. The AIA makes no change here—§ 42(b) still withholds the PTO's authority to spend the money it collects unless and until Congress appropriates it. The second reserve mechanism is provided in the AIA: § 22 added § 42(c)(2) as follows (emphasis added):

> "There is established in the Treasury a Patent and Trademark Fee Reserve Fund. If fee collections by the Patent and Trademark Office for a fiscal year exceed the amount appropriated to the Office for that fiscal year, fees collected in excess of the appropriated amount shall be deposited in the Patent and Trademark Fee Reserve Fund. *To the extent and in the amounts provided in appropriations Acts*, amounts in the Fund shall be made available until expended only for obligation and expenditure by the Office in accordance with paragraph (3)."

Here too, the AIA does not empower the PTO to increase its "operating reserve" with funds, unless those funds are first appropriated by Congress. Second, Congress envisioned accumulation of reserves solely based on increases in filings beyond projections, resulting in fee collections for additional workload. The money thus deposited in the Patent and Trademark Fee Reserve Fund is unearned revenue from which Congress can appropriate funds for any PTO "operational reserve." The level of the reserve established in § 42(c)(2) is derived from the degree of volatility in fee collection compared to projections wherein the reserve is used to average *over time* upward and downward fluctuations in fee collections to match the costs to the Office. This approach is consistent with GAO's view of the principles that the PTO should employ in establishing its operating reserve[61] and with PTO's prior years' practice by mere change of terminology. Prior to FY 2010, the PTO called "unobligated balance brought forward" what it now calls an "operating reserve." It reserved a portion of the amount Congress made available annually through appropriations as a designated unobligated balance, which could be carried over for use in future years. This is possible because the PTO is generally appropriated no-year funds – with no fiscal year limitation, wherein the pertinent appropriating statute provides that the funds "shall be made available until expended."

[61] GAO, *Patent and Trademark Office: User Fee Review*, p. 8, GAO-12-514R, (Apr. 25, 2012) ("an operating reserve is important for fee-funded programs to match fee collections to average program costs *over time* and because program costs do not necessarily decline with a drop in fee collections" (emphasis added.))

The PTO can make compelling presentations to Congress and recommend particular levels of reserves to be appropriated from unearned revenues in the § 42(b) account and the Patent and Trademark Fee Reserve Fund. However, it is clear that under the AIA, Congress *reserved for itself that decision* and the PTO has no authority to set its reserve levels. Congressional intent as to the appropriate level of PTO "operating reserves" was made quite clear during last year's appropriation process when the House Committee on Appropriations recommended PTO's reserve appropriations remain at a low percentage of its annual budget:

> *Carryover funds*.—The Committee is concerned that the PTO has established an operating reserve whereby it intends to carry over funds from one fiscal year to the next as a "cushion." For fiscal year 2012, PTO has proposed an operating reserve to help the agency maintain its pace of activities in years when fee collections diminish or fall below projections or during years of planned spending above collections. While some level of carryover may be advisable, the PTO is proposing to have an operating reserve of $342,470,000 at the end of fiscal year 2012. The Committee believes that given the backlog and pendency rates, *holding nearly 13 percent of its budget as a reserve into the next fiscal year is not a good management practice for an agency that is so far behind in whittling down its workload*." Accordingly, the PTO, in consultation with the Secretary of Commerce, is directed to propose in its fiscal year 2013 budget submission an exhibit stating specifically what the PTO intends to fund using carryover balances.[62]

It is remarkable that right after Congress expresses reservations regarding PTO's planned reserve of 1/8 of its annual budget and requests identification of specific obligations to be funded by the reserve, the PTO now plans to build a reserve that *doubles* that fraction to 1/4 of its annual budget and do so for "unknown" obligations. Nowhere in the AIA did Congress express its abandonment of these principles.

That the reserve cannot be a "cost" component in PTO's fees is also clear from the basic fact that its level is subject to congressional determination – an appropriation determination that has no effect on the "aggregated estimated costs to the Office." Consequently, the PTO's theory clearly leads to an absurd result, which it neglected to address in the NPRM: the Office would have to reduce its fees when Congress refuses to accept its proposed reserve levels.

It appears, however, that through this proposed fee rule which "camouflages" the reserve within every dollar of fee collections, the PTO is attempting to evade congressional control over budgetary reserve levels as codified in the AIA. The PTO's camouflage attempt is transparent and therefore its proposed "operating reserve" is hostage to the same fee diversion that has constrained the PTO in the past. The only legal remedy for establishing adequate reserves and avoiding the backlog that arose out of fee diversion is for Congress to restore the fees it failed to appropriate. This author has worked, and will continue to work hard to achieve this goal.

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To be continued

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[62] House Report 112–169 (Jul. 20, 2011), at 17 (emphasis added.)