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ARBITRATION: A QUICK AND EFFECTIVE MEANS FOR PATENT DISPUTE RESOLUTION

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Entering into a contract containing a carefully crafted arbitration clause provides a level of predictability with respect to the investment and liability associated with patent license and/or research agreements, thereby providing the respective companies a better estimation of the risk factors associated therewith. Specifically, when parties enter into an agreement to arbitrate they have the opportunity to obtain assurance through the careful drafting of the arbitration clause that any dispute arising out of the contract will be decided by a technologically knowledgeable neutral arbitrator in a manner that will be relatively inexpensive. Having this assurance can provide stability of the business relationship which is further strengthened by the knowledge that the proceedings will be confidential and the awards rendered will be final and non-appealable, so that the companies can quickly resume with their business transactions without concern for negative publicity or the uncertainty of appeals. Accordingly, using arbitration as a means to quickly and effectively settle patent disputes, not only can be beneficial for both parties should a dispute arise, but can also provide pre-emptive benefits that remain even if the agreement to arbitrate is never enforced.

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I. INTRODUCTION

Arbitration is a process of dispute resolution wherein parties submit their dispute to at least one impartial "judge" who will render a binding decision. This process differs from mediation or conciliation, where the impartial authority is authorized only to facilitate the discussion of the parties in dispute, but will not render any decision on the matter.[1] In arbitration, the parties agree that by submitting themselves to arbitration, the decision rendered by the arbitrator will be binding and is "non-appealable" absent any defense of invalidity of the arbitration clause.[2] Although this sounds like a dangerous approach for patent disputes, which often last for several years from Markman hearings[3] through appeals, there are many positive aspects to this type of agreement that may prove worthwhile for both parties.

Voluntary arbitration as a remedy for patent infringement is authorized by 35 U.S.C. § 294.[4] Specifically, section 294 authorizes either submission to arbitration by execution of a contract, comprising an "arbitration clause" whereby parties preemptively attest their intent to arbitrate, or by a written agreement to arbitrate, which may be executed independently of the contract either before or after the dispute arises.[5] Section 294

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[1] *See* AMERICAN ARBITRATION ASSOCIATION, http://www.adr.org/sp.asp?id=28749 (last visited Feb. 26, 2011).

[2] While 9 U.S.C. § 16 provides for appeal of certain aspects relating to an arbitration proceeding, an arbitration award is appealable only under certain very specific situations, such as an award "procured by fraud, corruption, or undue means," or by acts of the arbitrators constituting partiality, corruption, misconduct, or "exceed[ing] their powers." 9 U.S.C. §§ 10, 16 (2006).

[3] In *Markman v. Westview Instruments, Inc.*, the U.S. Supreme Court held that judges, not juries, would interpret the meaning of the words used in patent claims as their interpretation is a matter of law not a question of fact. 517 U.S. 370 (1996). Although juries determine questions of fact, judges determine matters of law. *See* U.S. CONST. amend VII; Chevron U.S.A. Inc. v. Natural Res. Def. Council, Inc., 467 U.S. 837 (1984). *Markman* Hearings are now held in many jurisdictions to construe patent claims prior to the start of trial.

[4] 35 U.S.C. § 294 (2006).

[5] *See id.* § 294 (a).

has also been extended to include interference claims[6] and questions of inventorship.[7]

As can be expected, it is uncommon for an agreement to arbitrate to be executed post-dispute, as it will inevitably become much more difficult for competing or disputing parties at that stage to reach a written agreement on the logistics of the arbitration. Accordingly, most arbitrations find their authority in arbitration clauses that are executed pre-dispute, which are often added to patent license agreements and research and development contracts.[8] As will be discussed below, there are many potential benefits associated with arbitration that may prove advantageous for both sides of a patent dispute. Likewise, there are concerns that both sides should take into consideration before entering into an arbitration agreement or otherwise submitting a patent dispute to arbitration. Overall, however, arbitration warrants serious consideration as an effective alternative means of patent dispute resolution when a properly drafted arbitration clause is used to preserve a party's best interests.

For example, the costs of arbitration, while not insignificant, are not nearly as high as the costs that parties may incur during years of patent litigation.[9] In addition, since the decision of the arbitrator is binding, the time for resolution of a patent dispute via

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[6] *See* 35 U.S.C. § 135(d) (2006). An interference is an *inter partes* administrative proceeding held before the Board of Patent Appeals and Interferences ("BPAI") of the United States Patent Office ("USPTO") to determine the priority of multiple patent applications. This proceeding is a by-product of the first to invent system of the United States, and provides a party who was first to invent but not first to file the opportunity to challenge another party's claim to inventorship.

[7] *See* Miner Enters., Inc. v. Adidas AG, No. 95 C 1872, 1995 WL 708570, at *3 (N.D. Ill. Nov. 30, 1995).

[8] *See* Kevin R. Casey, *The Suitability of Arbitration for Intellectual Property Disputes*, 71 PAT. TRADEMARK & COPYRIGHT J. 143 (2005).

[9] *See* AM. INTELL. PROP. L. ASS'N, 2009 REPORT OF THE ECONOMIC SURVEY 29 (2009) [hereinafter AIPLA ECONOMIC REPORT]; Richard D. Margiano,Cohen Pontani Lieberman & Pavane LLP, New York, *U.S. - Litigation: Cost and duration of patent litigation*, MANAGING INTELLECTUAL PROPERTY, (Feb. 1, 2009), *available at* http://www.managingip.com/Article/2089405/Cost-and-duration-of-patent-litigation.html; COMMERCIAL ARBITRATION RULES AND MEDIATION PROCEDURES (Am. Arbitration Ass'n amended 2010).

arbitration can be as short as a matter of months. In contrast to litigation, which can involve multiple layers of appeal, following the issuance of an award in arbitration the parties may continue with their business activities with the assurance that the dispute is finally settled and will no longer affect or impede their business plans. Moreover, since the parties to the arbitration pick the arbitrators, they have a better opportunity to ensure that the decision maker is knowledgeable in both the field of patent law and the technology at issue, avoiding some of the uncertainty associated with Markman hearings and jury decisions on validity and infringement.[10] Finally, as arbitration is private, the parties do not need to be concerned that challenges to their business practices and/or the validity of their patents will be broadcast throughout the industry, to their clients, or to their competitors.

There are, however, some negative aspects to arbitration. For example, since discovery is limited by the discretion of the arbitrator, parties on either side may have difficulty making their case, as they may not have access to the huge sum of documents normally acquired during pre-trial procedures in litigation.[11] In addition, although section 294 states that the award granted "shall be final and binding between the parties to the arbitration,"[12] the courts have not yet determined whether any finding of invalidity of the patent shall be binding on the patent holder for future disputes or will hold any weight in future court or in United States Patent and Trademark Office ("USPTO") proceedings.[13]

This paper explores the general principals of patent arbitration under U.S. law and weighs the benefits of using arbitration as a means of resolving patent disputes against the potential disadvantages that may be associated therewith but have yet to be decided by the courts. Specifically, Part II of this paper addresses the establishment of the Federal Arbitration Act and the general

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[10] Donna Gitter, *Should the United States Designate Specialist Patent Trial Judges? An Empirical Analysis of H.R. 628 in Light of the English Experience and the Work of Professor Moore*, 10 COLUM. SCI. & TECH. L. REV. 169 (2009).

[11] *See* COMMERCIAL ARBITRATION RULES AND MEDIATION PROCEDURES, *supra* note 9, § R-30.

[12] 35 U.S.C. § 294(c) (2006).

[13] *See also* Federal Arbitration Act, 9 U.S.C. §§ 1–14 (2006).

principles of arbitration. Part III addresses the specific application of arbitration to patent disputes. In Part IV, the authors discuss the pros and cons associated with arbitration of patent disputes, as compared to litigation, and Part V presents a framework for establishing agreements to arbitrate patent disputes.

II. ARBITRATION IN THE UNITED STATES

The Federal Arbitration Act ("FAA")[14] was enacted to codify a "national policy favoring arbitration and [to place] arbitration agreements on equal footing with . . . contracts."[15] The FAA ensures that agreements to arbitrate are "valid, irrevocable, and enforceable," provided their subject involves "commerce."[16] An agreement to arbitrate under the FAA must be present, either as part of a written commercial contract or as a written agreement separate from the contract itself, stating that the parties will submit to arbitration for an existing controversy.[17] This "right" to contractually agree to arbitrate disputes extends to matters of both state and federal jurisdiction.[18]

A. *Determining the Validity of an Agreement to Arbitrate*

As is standard with arbitration agreements, any such clause or agreement is valid, irrevocable, and enforceable absent any ground that exists at law or in equity for revocation of a contract.[19] "Challenges to the validity of [an] arbitration agreement upon such grounds as exist at law or in equity for the revocation of a contract" can be divided into two types."[20] The first type challenges the validity of the arbitration clause itself.[21] The second type "challenges the validity of the contract as a whole."[22]

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[14] *Id.*

[15] Buckeye Check Cashing, Inc. v. Cardegna, 546 U.S. 440, 443 (2006).

[16] 9 U.S.C. § 2 (2006).

[17] *Id.*

[18] Southland Corp. v. Keating, 465 U.S. 1, 15–16 (1984).

[19] 9 U.S.C. §§ 1–14.

[20] *Buckeye Check Cashing*, 546 U.S. at 444.

[21] *Id.* (citing *Southland*, 465 U.S. at 4–5) (challenging the agreement to arbitrate as void under California law insofar as it purported to cover claims brought under the state Franchise Investment Law).

[22] *Id.*

Challenges to the validity of the contract as a whole may involve a challenge to the entire agreement; for example, a claim of fraud in the inducement, or a challenge to the illegality of a single provision that would thus render the entire contract invalid.[23]

B. *Severability of Arbitration Agreements*

As a matter of substantive federal law, an arbitration agreement is severable from the remainder of the contract.[24] In other words, the validity of the arbitration clause is to be determined independently of the validity of the contract with each type of challenge being decided separately.[25] This principal is internationally recognized as the "doctrine of separability."[26] If the challenge is to the validity of the arbitration agreement itself, for example a question pertaining to the formation of the agreement to arbitrate, the federal courts may adjudicate it.[27] However, the statutory language of the FAA does not permit federal courts to consider challenges to the validity of the contract as a whole, including, for example, fraud in the inducement.[28] The issue of a contract's validity is to be considered by the arbitrator in the first instance.[29] Accordingly, the FAA provides that if any issue that is subject to an arbitration clause is brought in a proceeding before any court of the United States, the court shall, upon application by one of the parties, stay the trial of the action until the arbitration has been conducted in accordance with the terms of the agreement.[30]

C. *Competence-competence?*

There is a principal applied in International Commercial Arbitration recognized as "competence-competence," which stands

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[23] *Id.* at 445.

[24] Prima Paint Corp. v. Flood & Conklin Mfg. Co., 388 U.S. 395, 404 (1967).

[25] 9 U.S.C. § 4 (2006); *Prima Paint*, 388 U.S. at 403–04.

[26] PHILIPE FOUCHARD ET AL., FOUCHARD, GAILLARD, GOLDMAN ON INT'L COMMERCIAL ARBITRATION 198 (Emmanuel Gaillard & John Savage eds., 1999).

[27] *Prima Paint*, 388 U.S. at 403–04.

[28] *Buckeye Check Cashing*, 546 U.S. at 446.

[29] *Id.*

[30] 9 U.S.C. § 3.

for the notion that the arbitrators themselves are granted authority by the parties to determine the validity of the arbitration agreement.[31] However, this international principal has not been generally recognized by the United States federal and state courts in its strict sense.[32] Instead, the United States Supreme Court has relied on section 4 of the FAA for jurisdiction to review the validity of arbitration agreements.[33] Specifically, section 4 states:

> A party aggrieved by the alleged failure, neglect, or refusal of another to arbitrate under a written agreement for arbitration may petition any United States district court [with jurisdiction] . . . for an order directing that such arbitration proceed in a manner provided for in such agreement . . . *upon being satisfied that the making of the agreement for arbitration* or the failure to comply therewith *is not in issue,* the court shall make an order directing the parties to proceed the arbitration in accordance with the terms of the agreement. . . .[34]

In turn, the Supreme Court has held that if the challenge is to the "making" of the arbitration agreement itself, for example, inducement of the arbitration clause, then the federal court of proper jurisdiction may adjudicate the issue.[35] However, as noted above, the federal court may only consider issues relating to the making and performance of the agreement to arbitrate, not to the

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[31] UNCITRAL Model law, Art. 23; *see* FOUCHARD ET AL., *supra* note 26, at 399–400; Klaus Peter Berger, *Germany Adopts the UNCITRAL Model Law*, 1 INT'L ARB. L. REV. 121, 122 (1998). Although this notion is often expressed with the phrase *"Kompetenz-Kompetenz,"* the traditional meaning of *"Kompetenz-Kompetenz"* in German implies that the arbitrators are empowered to make a final ruling as to their jurisdiction, with no subsequent review of the decision by any court. FOUCHARD ET AL., *supra* note 26, at 399–400. This runs contrary to the intended meaning of the phrase in the international sphere, and has thus been rejected in Germany. *Id.* Accordingly, *"Kompetenz-Kompetenz"* is slowly being phased out internationally and replaced with "competence-competence," a term adopted by the French Courts as early as 1949. *Id.*

[32] William W. Park, *The Arbitrability Dicta in First Options v. Kaplan: What Sort of Kompetenz-Kompetenz Has Crossed the Atlantic?*, 12 ARB. INT'L 137 (1996); Tom Carbonneau, *A Comment Upon Professor Park's Analysis Of The Dicta In First Options v. Kaplan*, 11 INT'L ARB. REP. 18 (Nov. 1996); Lawrence W. Newman and Charles M. Davidson, *Arbitrability of Timeliness Defenses—Who Decides?*, 14 J. INT'L ARB. 137 (June 1997).

[33] *Prima Paint*, 388 U.S. at 404; *Buckeye Check Cashing*, 546 U.S. at 445.

[34] 9 U.S.C. § 4 (emphasis added).

[35] *Prima Paint*, 388 U.S. at 404; *Buckeye Check Cashing*, 546 U.S. at 445.

validity of the contract as a whole.[36] The Supreme Court has further recognized the international doctrine of separability by holding that whether the challenge is brought in federal or state court, a challenge to the validity of the contract as a whole, not to the arbitration clause itself, must be decided in the first instance by the arbitrator.[37] This holding applies even if the state law under which the challenge is made prohibits enforcement of an arbitration clause contained in a contract that is unenforceable under state law.[38]

D. *Judicial Enforcement*

Once the arbitrator renders a decision, the FAA further provides that courts "must" confirm the arbitration award unless it is vacated, modified, or corrected as described in sections 10 and 11.[39] These statutory grounds are exclusive and cannot be modified by contract.[40] These provisions substantiate "a national policy favoring arbitration with just the limited review needed to maintain arbitration's essential virtue of resolving disputes

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[36] *Prima Paint,* 388 U.S. at 404; *Buckeye Check Cashing,* 546 U.S. at 445.

[37] *Prima Paint,* 388 U.S. at 404; *Buckeye Check Cashing,* 546 U.S. at 445.

[38] Southland Corp. v. Keating, 465 U.S. 1, 10–14 (1984).

[39] *See id.*; 9 U.S.C. §§ 10–11. Specifically, § 10 provides the following grounds for vacating an award:

> (1) where the award was procured by corruption, fraud, or undue means; (2) where there was evident partiality or corruption in the arbitrators, . . . (3) where the arbitrators were guilty of misconduct in refusing to postpone the hearing, upon sufficient cause shown, or in refusing to hear evidence pertinent and material to the controversy; or of any other misbehavior by which the rights of any party have been prejudiced; or (4) where the arbitrators exceeded their powers, or so imperfectly executed them that a mutual, final, and definite award upon the subject matter submitted was not made." 9 U.S.C. § 10. Under § 11, the grounds for modifying or correcting an award include "(a) . . . evident material miscalculation of figures or an event material mistake in the description of any person, thing, or property referred to in the award, (b) . . . arbitrators have awarded upon a matter not submitted to them. . . , [or] (c) where the award is imperfect in matter of form not affecting the merits of the controversy.

9 U.S.C. § 11.

[40] Hall St. Assocs., L.L.C. v. Mattel, Inc., 552 U.S. 576, 582 (2008).

straightaway."[41] In addition, should one of the parties refuse to submit to the arbitration, any United States district court that would have jurisdiction over the matter, absent the agreement, may order the arbitration to proceed in the manner provided for in the agreement.[42]

III. ARBITRATION OF PATENT DISPUTES

The Patent Act was amended in 1982 to recognize voluntary arbitration as a course of remedy for patent disputes relating to validity or infringement.[43] Specifically, section 294 now authorizes either submission to arbitration by execution of a contract comprising an "arbitration clause," whereby parties preemptively attest their intent to arbitrate, or by a written agreement to arbitrate, which may be executed independent of the contract either before or after the dispute arises.[44] This provision has also been extended by the courts to include interference claims[45] and questions of inventorship.[46]

The Patent Act specifies that "[a]rbitration of [patent] disputes, awards by arbitrators[,] and confirmation of awards shall be governed by title 9" of the FAA, discussed above, to the extent that it is not inconsistent with section 294 of the Patent Act.[47] Furthermore, section 294 provides that the arbitrator in a patent dispute must consider the patent defenses provided in section 282 "if raised by any party to the proceeding."[48] These enumerated defenses "involving the validity or infringement of a patent" include but are not limited to: non-infringement, absence of

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[41] *Id.* at 588.

[42] 9 U.S.C. § 4.

[43] *See* 35 U.S.C. § 294 (2006); Act of Aug. 27, 1982, Pub. L. No. 97-247, 96 Stat. 317, 322.

[44] *See* 35 U.S.C. § 294(a).

[45] 35 U.S.C. § 135(d).

[46] *See* Miner Enters., Inc. v. Adidas AG, No. 95 C 1872, 1995 WL 708570, at *3 (N.D. Ill. Nov. 30, 1995).

[47] 35 U.S.C. § 294(b).

[48] 35 U.S.C. § 282.

liability for infringement, unenforceability, invalidity of the patent or any claim in suit.[49]

A. *Reporting Requirement*

Any decision rendered by the arbitrator, referred to as an "award," must be reported to the Director of the USPTO.[50] There must be separate notice given for each patent involved in the proceeding, and each notice must "set forth the names and addresses of the parties" as well as the name of the inventor and the patent owner, must "designate the number of the patent, and [must] contain a copy of the award."[51] The award "shall be unenforceable until" the Director receives notice thereof.[52] Upon receipt of the notice, the Director is required to enter the notice in the patent's prosecution record.[53] Although there is no database of such notices maintained by the USPTO, the statute dictates that the "Director shall, upon receipt of either notice, enter the same in the *record of the prosecution of such patent*."[54] Accordingly, it would follow that any patent about which such a notice was issued would have a copy thereof listed in the Patent Application Information Retrieval database ("PAIR").[55] Although it is not clear if the notice

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[49] *Id.* The enumerated defenses specifically include:

> (1) non[-]infringement, absence of liability for infringement[,] or unenforceability, (2) [i]nvalidity of the patent or any claim in suit on any ground specified in part II of [] title [35 U.S.C. §§ 100 et seq.] as a condition for patentability, (3) [i]nvalidity of the patent or any claim in suit for failure to comply with any requirement[s] of [35 U.S.C. §§ 112 or 251], (4) [a]ny other fact or act made a defense by title [35 U.S.C.].

Id.

[50] *See* 35 U.S.C. § 294(d).

[51] *Id.*

[52] 37 C.F.R. § 1.335(c) (2010); filing of notice of arbitration awards.

[53] *See* 35 U.S.C. § 294(e); 37 C.F.R. § 1.335.

[54] 35 U.S.C. § 294(d) (emphasis added).

[55] Status information relating to patent applications is available through the Patent Application Information Retrieval ("PAIR") system. There is both a public and private side to PAIR. In public PAIR, information is available relating to issued patents, published patent applications, and applications to which a patented or published application claims domestic priority. In private PAIR, an applicant (or his or her registered patent attorney or registered patent agent) can securely track the progress of his or her application(s) through the

would be placed in Public PAIR or Private PAIR, which is restricted in access, we note that it is unlikely that the notice is placed in Private PAIR because it does not involve an unpublished patent application or non-patent (copyrighted) literature.[56] Accordingly, section 294(d) appears to require the Director to enter the notice of an arbitration award in the public prosecution record of the patent, which undermines the confidential nature of arbitration proceedings.[57]

B. *Effect of the Arbitration Award on Third Parties*

Although section 294 states that the award granted shall be final and binding between the parties to the arbitration, the courts have not yet determined whether any finding of invalidity of the patent shall be binding on the patent holder for future disputes or shall hold any weight in future court or in United States Patent and Trademark Office (USPTO) proceedings.[58] Accordingly, the question remains whether the arbitration procedure itself, even if confidential, will have any effect on the patent validity.

Section 294(c) of the Patent Act specifically states that awards issued by the arbitrator shall be final and binding between the parties to the arbitration but shall have "*no force or effect*" on any other person.[59] In parallel, the Patent Act's interference arbitration sub-section, section 135(d), specifically states that the award rendered "shall, *as between the parties to the arbitration*, be dispositive of the issues to which it relates."[60] However, it has

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USPTO. Private PAIR makes available information relating to unpublished patent applications, but the applicant must associate a Customer Number with the application to obtain access. *See* U.S. PAT. & TRADEMARK OFFICE, U.S. DEP'T OF COMMERCE, MANUAL OF PATENT EXAMINING PROCEDURE § 1730(1)(c) (8th ed., 8th rev. 2010) [hereinafter MPEP].

[56] *See id.* Private PAIR is used: (1) to access non-patent (copyrighted) literature, § 707.05(a), and (2) to provide information related to unpublished patent applications.

[57] 35 U.S.C. § 294(d).

[58] *Id. See also* 9 U.S.C. §§ 1–14 (2006). Matthew A. Smith, *Arbitration of Patent Infringement and Validity Issues Worldwide,* 19 HARV. J. LAW & TECH. 299, 323 (2006).

[59] 35 U.S.C. § 294(c) (emphasis added).

[60] 35 U.S.C. § 135(d) (emphasis added).

been held that an arbitral award in the United States has the same effect as a court judgment for purposes of res judicata with respect to those issues which were covered by the award.[61] Accordingly, even though both statutes make it clear that the award will not have an effect on third parties, they do not appear to preclude the use of the award against the parties themselves in future proceedings.[62]

Specifically, if an arbitration award is issued that finds certain claims of a patent invalid, then the question of whether or not that finding of invalidity would be binding against the patent holder in later proceedings has not yet been decided. However, the language "but shall have no force or effect on any other person" might be interpreted to mean that the award shall have no force or effect on the patent owner's ability to enforce the patent in later proceedings.[63] Specifically, if the patentee is bound by an award of invalidity, then the award would technically have both force and effect on the rights of the third party to make, use, and/or sell the technology covered by that patent.[64] Thus, it could be argued that

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[61] Am. Renaissance Lines, Inc. v. Saxis S.S. Co., 502 F.2d 674, 678 (2d Cir. 1974) (citing Springs Cotton Mills v. Buster Boy Suit Co., Inc., 88 N.Y.S.2d 295 (N.Y. App. Div. 1949)). A decision by arbitrators is as binding and conclusive under the doctrine of res judicata and estoppel as the judgment of a court. *See* Schuykill Fuel Corp. v. B. & C. Nieberg Realty Corp., 165 N.E. 456 (N.Y. 1929). The test is whether the issues in this action were (a) litigated or involved in the arbitration proceeding or (b) properly could and should have been litigated there. To the extent that the facts and law which are material or incidental to the issues in this action meet this test, the plaintiff is estopped by the arbitration award. The rationale for this rule is plain. Any other result would permit a different judgment in this action, the effect of which would be to destroy or impair interests established by the first.

[62] 35 U.S.C. §§ 135(d), 294(c).

[63] 35 U.S.C. § 294 (c).

[64] *See* 35 U.S.C. § 154(a)(1) (defining the rights granted by issuance of a patent as "[e]very patent shall contain a short title of the invention and a grant to the patentee, his heirs or assigns, of the right to exclude others from making, using, offering for sale, or selling the invention throughout the United States or importing the invention into the United States, and, if the invention is a process, of the right to exclude others from using, offering for sale or selling throughout the United States, or importing into the United States, products made by that process, referring to the specification for the particulars thereof"). See also 35 U.S.C. § 154(a)(1) for a description of what constitutes infringement: "[e]xcept as otherwise provided in this title, whoever without authority makes, uses, offers

holding a patentee bound in future proceedings by an arbitration award of invalidity would be contrary to the statutory language of section 294, which prohibits force or effect of the award on third parties.[65]

In contrast, we also recognize that the U.S. federal courts and the U.S. patent system have tended to encourage challenges to the validity of patents to ensure that only the owners of truly valid patents have the right to continue excluding others from practicing the patented invention.[66] In turn, the record-keeping requirement described above combined with the patent system's encouragement of patent challenges may support a holding that any arbitration award which determines whether a disputed patent is either invalid or unenforceable shall also have an effect on parties that are not a party to the arbitration. Under such a holding, an arbitration award which finds a patent invalid would effectively serve to dedicate the patent to the public, and third parties would be able to rely upon the award in future proceedings.[67]

It is also worth noting that even if the award itself is not binding on the patent holder in future disputes, the question of whether the award, if not publicly available through the PAIR system of the USPTO, would be discoverable in future disputes has not been addressed. Specifically, it is possible that even if the statute were enforced and the arbitration award was determined to

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to sell, or sells any patented invention, within the United States or imports into the United States any patented invention during the term of the patent therefore, infringes the patent." *Id.*

[65] We point specifically to the word "shall" in "[a]n award by an arbitrator *shall* be final and binding between the parties to the arbitration but *shall* have *no force or effect* on any other person." 35 U.S.C. § 294(c) (emphasis added).

[66] *See, e.g.,* Patent Reform Act of 2011, S. 23, 112th Cong. (2011) (adopting a post grant review proceeding wherein any person other than the patent owner could file a petition for review of patent validity within nine months from patent grant).

[67] In such an instance, the third party may have a strong argument for sanctions against the patentee for patent misuse for attempting to enforce a knowingly invalid claim or knowingly unenforceable patent. *See* 35 U.S.C. § 271(d)(4); Dawson Chem. Co. v. Rohm & Haas Co., 448 U.S. 176 (1980). "Sham" or bad-faith patent enforcement—i.e., without belief that the claim is meritorious—however, can give rise to liability. *See* Prof'l Real Estate Investors, Inc. v. Columbia Pictures Indus., Inc., 508 U.S. 49 (1993).

have no effect in future proceedings, a third party may still be able to access the reasons that the patent was determined invalid or unenforceable noted in the award and assert those same reasons in court.[68]

In view of the foregoing, it may be prudent to draft an arbitration clause limiting the format of the award and the issues to be decided in order to avoid any possible *res judicata* effect of validity rulings. For example, if the arbitration clause is drafted to limit the award to determination of royalty fees and/or findings of infringement only, then there will be no findings of invalidity or unenforceability on record to be relied upon in the future by third parties.[69]

C. *Stay Requirement and Administrative Proceedings*

Under the FAA, a suit or proceeding brought in any U.S. court "shall" be stayed once the court is satisfied that there is a valid arbitration agreement.[70] However, it is not clear that administrative agencies are also required to issue a stay under the same circumstances. In a 1991 Age Discrimination in Employment Act case, the Supreme Court held that agreements to arbitrate do not preclude administrative agencies from investigating and prosecuting civil statutory claims.[71] In 1991, the Court of Appeals for the Federal Circuit held that, in an International Trade Commission ("ITC") investigation, the Commission was not authorized to halt proceedings to defer to arbitration, even when there was a valid agreement to arbitrate.[72] The Court cited 19 U.S.C. § 1377 Unfair practices in Import Trade ("section 377"),

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[68] An argument could even be made that the findings in the arbitration award should have more weight in court, since the arbitrators are usually more knowledgeable in the technology involved, as well as knowledgeable in patent law.

[69] *See* 9 U.S.C. § 4 (2006). We note that if the award is limited to infringement, claim construction should be excluded from the award.

[70] 9 U.S.C. § 3.

[71] Gilmer v. Interstate/Johnson Lane Corp., 500 U.S. 20, 27 (1991). "An individual ADEA claimant subject to an arbitration agreement will still be free to file a charge with the EEOC, even though the claimant is not able to institute a private judicial action."

[72] Farrel Corp. v. United States ITC, 949 F.2d 1147, 1155 (Fed. Cir. 1991).

which at the time only authorized limited and specific circumstances for termination of an ITC investigation.[73] However, to follow the national policy favoring arbitration and the FAA, in 1994 Congress amended section 377 to provide that on the basis of an agreement to arbitrate, the Commission *may* terminate the investigation, in whole or in part, without making a determination.[74] Accordingly, although the U.S. Supreme Court holding may be applied to justify the refusal to stay other administrative proceedings pending arbitration, it appears as though Congress' revision of section 377 in response to the Federal Circuit's decision in *Farrel Corp.* makes it clear that it is the intent of Congress to have both administrative agencies and courts honor parties' intent to arbitrate disputes.[75] This is further evidenced by the Patent Act's reference to the arbitrability of interferences: "Parties to a patent interference . . . may determine such contest or any aspect thereof by arbitration."[76] In turn, although the question

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[73] *Id.*

[74] 19 U.S.C. § 1337(c) (2006) ("The Commission shall determine, with respect to each investigation conducted by it under this section, whether or not there is a violation of this section, except that the Commission may, by issuing a consent order or on the basis of an agreement between the private parties to the investigation, including an agreement to present the matter for arbitration, terminate any such investigation, in whole or in part, without making such a determination."); *see also Farrel Corp.*, 949 F.2d at 1155 (holding that commission cannot halt investigation to defer to arbitration agreement).

[75] 19 U.S.C. § 1337.

[76] 35 U.S.C. § 135(d) (2006). An interference occurs:

> Whenever an application is made for a patent which, in the opinion of the Director, would interfere with any pending application, or with any unexpired patent, an interference may be declared and the Director shall give notice of such declaration to the applicants, or applicant and patentee, as the case may be. The Board of Patent Appeals and Interferences shall determine questions of priority of the inventions and may determine questions of patentability. Any final decision, if adverse to the claim of an applicant, shall constitute the final refusal by the Patent and Trademark Office of the claims involved, and the Director may issue a patent to the applicant who is adjudged the prior inventor. A final judgment adverse to a patentee from which no appeal or other review has been or can be taken or had shall constitute cancellation of the claims involved in the patent, and notice of such

of whether re-examination[77] would be stayed pending arbitration has not been addressed by the courts, it follows from the above rationale that such a stay would be granted, especially in view of the statutory right granted under section 294(a) to arbitrate "any dispute relating to patent validity."[78]

It should be noted, however, that although the administrative proceedings noted above may be stayed on the basis of an agreement to arbitrate, the respective agencies are not required to do so. Specifically, the language "may" in section 377 indicates that it is not mandatory for the Commission to honor the arbitration agreement.[79] In addition, section 135(d) of the Patent Act states that although the parties to an interference "may determine such contest or any aspect thereof by arbitration[,] . . . nothing in this subsection *shall* preclude the Director from determining patentability of the invention involved in the interference."[80] However, section 135(d) further notes that the award rendered "*shall*, as between the parties to the arbitration, be dispositive of the issues to which it relates."[81] Accordingly, it is possible that the statement in section 135(d) that the Director is not precluded from making his own determination is a reflection of the intent that the award rendered should not have an effect on any third person or

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> cancellation shall be endorsed on copies of the patent distributed after such cancellation by the Patent and Trademark Office.

35 U.S.C. § 135(a).

[77] 35 U.S.C. § 302. Reexamination has been defined as:

> Patent reexamination is a procedure by which a post grant review of an issued U.S. Patent is performed by a team of three experienced primary examiners of the United States Patent & Trademark Office's Central Reexamination Unit ("CRU"). Ex parte patent reexamination may be initiated by the patent owner, the Director of the USPTO or a member of the public ("third party requester").

Stephen G. Kunin et al., *Patent Reexamination: Frequently Asked Questions*, PATENTS POST-GRANT, http://www.patentspostgrant.com/wp-content/uploads/2009/11/Reexam-FAQ-Updated-11_30_09.pdf (last updated Nov. 30, 2009).

[78] 35 U.S.C. § 294(a).

[79] 19 USC § 1337(c).

[80] 35 U.S.C. § 135(d) (emphasis added).

[81] *Id.* (emphasis added).

entity who was not a party to the arbitration.[82] This rationale would be in agreement with section 294(c) of the Patent Act, which specifically states that awards issued by the arbitrator "shall be final and binding between the parties to the arbitration but shall have *no force or effect* on any other person."[83]

IV. PROS AND CONS OF ARBITRATING PATENT DISPUTES

There are many potential benefits associated with arbitration that may prove advantageous for both sides of a patent dispute including brevity, cost, technical knowledge of the arbitrators, and confidentiality of the proceedings.

A. *Cost and Time*

There is a significant difference in the costs associated with arbitration of patent disputes compared to litigation.[84] A number of factors contribute to the high cost of patent litigation. Although the pretrial procedures including discovery, expert witness testimony, and depositions often initially account for a large percentage of the costs, the costs associated with appeal can ultimately overshadow the pre-trial costs.[85] The American Intellectual Property Law Association Economic Survey of 2009 reported that the median costs for Patent Infringement Litigation, wherein the amount at issue was from $1,000,000 to $25,000,000, was $2,500,000 inclusive, with $1,500,000 being the median costs for discovery alone.[86] Depending on the voracity with which the parties litigate, the costs can be significantly higher. An appeal to the Federal Circuit can add at least another $2,000,000 to the total costs.[87]

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[82] *Id.* This would further be supported by the language "as between the parties to the arbitration. . . .".

[83] 35 U.S.C. § 294 (c) (emphasis added).

[84] *See* AIPLA ECONOMIC REPORT, *supra* note 9; Margiano, *supra* note 9; COMMERCIAL ARBITRATION RULES AND MEDIATION PROCEEDURES, *supra* note 9.

[85] Margiano, *supra* note 9.

[86] *See* AIPLA ECONOMIC REPORT, *supra* note 9.

[87] Margiano, *supra* note 9.

In contrast, the costs for arbitration are often well below $1,000,000.[88] Depending on the body selected by the parties to run the arbitration, the filing fee for a case where the amount at issue varies from $1,000,000 to $5,000,000 may be as little as $12,450.[89] Although the attorney fees will remain at their standard rates, the time required to prepare and submit a dispute to arbitration is much less than that required for litigation. Moreover, "pre-trial" procedures, which can cost on average $1,500,000 in litigation, are streamlined in arbitration; it is in the discretion of the arbitrator to allow the parties to conduct any depositions and/or other pre-trial discovery procedures.[90]

In parallel to this reduction in cost, the time required to resolve a dispute through arbitration is often much shorter than the time required to resolve the same dispute through litigation.[91] This is a result of the above-mentioned streamlined procedures, which limit not only the attorney's time and thus attorney fees, but also cap the vast expenses which are often incurred in the appellate process.[92]

B. *Selection of Arbitrators*

A primary advantage of arbitration is the ability of the parties to submit their disputes to an arbitrator who is knowledgeable in both the technical issues of the patent and the governing patent laws.[93] When drafting the arbitration clause while forming the agreement to arbitrate, the parties can preemptively reserve their right to select the arbitrator or specify their requirements for appointment.[94] Specifically, the parties may specify in the arbitration clause the number of arbitrators and the manner in which they should be selected; alternatively, they may indicate

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[88] *See* COMMERCIAL ARBITRATION RULES AND MEDIATION PROCEDURES, *supra* note 9.

[89] *Id.*

[90] 9 U.S.C. §§ 7, 10 (2006).

[91] Kevin R. Casey, *The Suitability of Arbitration for Intellectual Property Disputes*, 71 PAT. TRADEMARK & COPYRIGHT J. 143 (2005).

[92] Margiano, *supra* note 9.

[93] *Id.*

[94] For example, refer to R-11. COMMERCIAL ARBITRATION RULES AND MEDIATION PROCEDURES, *supra* note 9, § R-11.

their intent by specifying laws to govern the arbitration procedure, thereby providing a framework for appointing an arbitrator.[95] In this manner, the parties can ensure that if a dispute arises, they will be able to select an arbitrator who is familiar with the most relevant issues of the case, thereby avoiding the uncertainty associated with Markman hearings, jury trials, and appeals thereof.

C. *Confidentiality*

In general, arbitrations involve private, confidential procedures. Although the FAA does not expressly address the issue of confidentiality, a number of the rules which are commonly elected to govern arbitration proceedings provide for the formation of a confidentiality agreement at the start of the proceeding.[96] Once such an agreement is created, U.S. courts have not been hesitant to enforce them.[97] However, an important factor to note is that the arbitrator does not have the authority to enforce confidentiality clauses.[98] Accordingly, if the confidentiality agreement is breached, the parties would have to obtain a court order compelling non-disclosure.[99] However, in order to guarantee that the court will enforce the confidentiality agreement, the parties should include the confidentiality agreement in the arbitration clause itself.[100]

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[95] *Id.*

[96] *See* SUPPLEMENTARY RULES FOR THE RESOLUTION OF PATENT DISPUTES (Am. Arbitration Ass'n amended 2010), *available at* http://adr.org/sp.asp?id=27417.

[97] DiRussia v. Dean Witter Reynolds, Inc., 121 F.3d 818, 826–28 (2d Cir. 1997).

[98] Tony Dutra, *Conferences/Alternative Dispute Resolution: 'Top 10' Alternative Dispute Resolution Mistakes Detailed for IP Litigators,* 76 PAT. TRADEMARK & COPYRIGHT J. 344 (2008).

[99] 9 U.S.C. § 4 (2006). This section provides that "[a] party aggrieved by the alleged failure, neglect, or refusal of another to arbitrate under a written agreement for arbitration may petition any United States district court which, save for such agreement, would have jurisdiction under Title 28 for an order directing that such arbitration proceed in the manner provided for in such agreement." *Id.*

[100] *Id.* Including the confidentiality agreement in the arbitration clause will in turn ensure that it is included in the definition of "such agreement" of § 4.

It should be further noted that even if there is a confidentiality agreement, section 294 of the Patent Act requires that notice of each award rendered in an arbitration proceeding be submitted to the Director of the USPTO along with a copy of the award.[101] Accordingly, it is difficult in patent arbitration proceedings to retain full confidentiality. Although the USPTO does not maintain a record of said awards, having the record of any such award in the file history of a patent might be very dangerous for a patentee if the award questions the validity of the patent. Accordingly, we note again the possibility of limiting in the arbitration clause the issues to be decided in the award to, for example, exclude validity.[102]

D. *Discovery*

Under the FAA, arbitrators are authorized to issue subpoenas for witness testimony and physical evidence.[103] The fees paid to the witnesses are the same as the fees to witnesses before the U.S. courts.[104] If any person summoned by an arbitrator refuses to obey such a summons, the arbitrator may petition the United States district court for the district in which the arbitrator sits to compel the attendance of the person.[105]

Accordingly, it is within the discretion of the arbitrator to determine how much and what kind of discovery may be afforded to the parties. If the parties wish to maintain the right to pursue a specific type of discovery, they may specify this intent in the arbitration agreement, which the arbitrator must honor.[106]

V. A FRAMEWORK FOR ESTABLISHING AGREEMENTS TO ARBITRATE PATENT DISPUTES

Parties can easily establish their desire to submit a dispute to arbitration either by written agreement prior to a dispute arising or by written agreement after the dispute arises—the most common

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[101] *See supra* Part III(A).
[102] *See supra* Part III(B).
[103] 9 U.S.C. §§ 7, 10.
[104] *Id.*
[105] *Id.*
[106] 9 U.S.C. § 4.

being the former.[107] The American Arbitration Association Rules of Commercial Arbitration set forth specific language by which parties can make known their intention to submit to arbitration. The following Standard Arbitration Clause, for example, can be included in any contract between parties to address this intent:

> Any controversy or claim arising out of or relating to this contract, or the breach thereof, including any dispute relating to patent validity or infringement, shall be settled by arbitration administered by the American Arbitration Association under its Supplementary Rules for the Resolution of Patent Disputes and judgment on the award rendered by the arbitrator(s) may be entered in any court having jurisdiction thereof. (The award shall be rendered within _____months of the filing of the Demand.)[108]

This clause can be further supplemented with specific selection instructions for the number and qualification of arbitrators, confidentiality, discovery, and issues to be decided in the award, if desired.[109]

If the dispute has already arisen and the parties have not previously agreed to arbitration, the parties can memorialize their interest to submit to arbitration by signing an agreement including the following provision:

> We, the undersigned parties, hereby agree to submit to arbitration administered by the American Arbitration Association under its Supplementary Rules for the Resolution of Patent Disputes the following controversy: (cite briefly). We further agree that the above controversy be submitted to (one)(three) arbitrator(s) (and that the award shall be rendered within _____months of the Demand). We further agree that we will faithfully observe this agreement and the rules, that we will abide by and perform any award rendered by the arbitrator(s), and that a judgment of the court having jurisdiction may be entered on the award.[110]

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[107] *See supra* Part I.

[108] SUPPLEMENTARY RULES FOR THE RESOLUTION OF PATENT DISPUTES, *supra* note 96.

[109] 35 U.S.C. § 294(b) (2006) states in part: "In any such arbitration proceeding, the defenses provided for under section 282 of this title shall be considered by the arbitrator if raised by any party to the proceeding." This implies that the parties can agree beforehand which issues can or cannot be raised by the parties, such as invalidity or unenforceability.

[110] SUPPLEMENTARY RULES FOR THE RESOLUTION OF PATENT DISPUTES, *supra* note 96.

If the parties so desire, these paragraphs can be further refined to specify a different governing body and rules. However, in that event, the parties should refer specifically to the rules set forth by those governing bodies for any additional or different language that may be necessary to bring the dispute under the auspices of that particular governing body.

While it is simple to express the intent of the parties to submit to arbitration, the ultimate decision of whether to submit patent disputes to arbitration or litigation must be taken with great care and deliberation. The ultimate decision is both a business and legal decision wherein the variety of factors noted above must be weighed.

Furthermore, the arbitration clause must be very carefully drafted to ensure the best interests of the parties are maintained. For example, as explored in the sections above, if the parties desire to maintain confidentiality of the proceedings, to reserve a specific form of discovery, and/or to limit the issues to be decided in the award, such as royalty payments with no mention of validity findings in order to avoid possible estoppel effects, they may preserve their rights to do so through a carefully drafted arbitration clause.

VI. CONCLUSION

Entering into a properly crafted agreement to arbitrate provides the parties to a license agreement or other contractual business relationship the assurance that any dispute arising out of the contract will be decided by a technologically knowledgeable neutral arbitrator (or panel of arbitrators) in a manner that will be relatively inexpensive, confidential, and final. Having this assurance can provide a level of predictability with respect to the investment and liability associated with patent license agreements, thereby providing the respective companies a better estimation of the risk factors associated therewith. Moreover, entering into such an agreement with the knowledge that a dispute arising therefrom will be settled in accordance with a set of rules pre-selected by both parties serves to help ensure the stability of the business relationship. The stability is further strengthened by the

knowledge that the proceedings will be confidential and the awards rendered will be final and non-appealable so that the companies can quickly resume with their business transactions without concern for negative publicity or the uncertainty of appeals. This is particularly important in instances where the parties are already (or are expecting to become) long-term business allies because it circumvents the "take no prisoners" mentality that often permeates patent litigation and can permanently damage the business relationship. Further, this stability and the corresponding assurance that that litigation will be avoided can often prompt the parties to settle the disputes through negotiation, sometimes without even filing an arbitration demand. Accordingly, using arbitration as a means to quickly and effectively settle patent disputes can be beneficial for both parties should a dispute arise, and can also provide pre-emptive benefits which remain even if the agreement to arbitrate is never enforced.