

1993

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Recommended Citation

Karl P. Kilb, *Arbitration of Patent Disputes: An Important Option in the Age of Information Technology*, 4 Fordham Intell. Prop. Media & Ent. L.J. 599 (1993).

Available at: <https://ir.lawnet.fordham.edu/iplj/vol4/iss2/4>

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Arbitration of Patent Disputes: An Important Option in the Age of Information Technology

INTRODUCTION

The term "information technology" is becoming more and more prevalent,¹ as the interaction of the computer, telephone, cable and television industries creates new opportunities to share information and programming.² Billions of dollars are already involved in the transfer of information and entertainment.³ The so-called "information superhighway" will be made possible in the near future by a number of technological advances, including the ability to translate all audio and video communications into digital information and the use of fiber-optic wiring to provide a vast transmission pipeline.⁴

Companies want to protect what they have worked to develop, but they may also have a need to share the rights to certain technology in order to remain competitive. The "information superhighway" is likely to result in the merger of television, telecommunications, computers, consumer electronics, publishing, and infor-

1. For example, *Time* recently used the term on its cover in reference to a story on new technology linking sources of information and programming to telephones and computers. *TIME*, Apr. 12, 1993 (cover).

2. Bell Atlantic Corp. and Tele-Communications Inc. have recently agreed to a \$33 billion merger. Their combined resources will be used in an effort to build the "information superhighway" of the future. John Markoff, *A Phone-Cable Vehicle for the Data Superhighway*, *N.Y. TIMES*, Oct. 14, 1993, at A1.

3. According to Wilkofsky Gruen Associates, a market research firm specializing in the communications industry, the electronic delivery of business information will generate \$12.8 billion in 1993, three times the level of less than a decade ago. Stephen Kindel, *The Phantom Tollbooth*, *FIN. WORLD*, Oct. 12, 1993, at 57. Then Apple Computer Chairman John Sculley estimated that revenue generated by the "information superhighway" will reach \$3.5 trillion worldwide by the year 2001. Philip Elmer-DeWitt, *Take A Trip into the Future on the Electronic Superhighway*, *TIME*, Apr. 12, 1993, at 50, 54. Sculley left Apple Computer and joined Spectrum Information Technologies as Chief Executive Officer on October 19, 1993.

4. Elmer-DeWitt, *supra* note 3, at 51.

mation services into a single, interactive industry.⁵ Telephone companies⁶ and power companies⁷ are expected to dramatically increase their involvement in the transfer of information, through the addition of greater information-carrying capabilities to their existing lines.

Each road in the information superhighway is likely to involve intellectual property and, in particular, a patented invention.⁸ As the superhighway is built, patent disputes will arise. For example, Spectrum Information Technologies recently obtained a patent on its "direct connect" method of connecting portable computers with cellular telephones using a simple wire connection.⁹ There are conflicting opinions on the need to license this patent, creating potential disputes.¹⁰ The prevalence of such newly-developed, highly-technical inventions will increase the likelihood of patent disputes, and the value of resolution through arbitration.

This Note will explore ways in which arbitration—the voluntary submission of a dispute to a disinterested person or persons for final and binding determination¹¹—can be highly effective in re-

5. *Id.* at 52.

6. Rich Brown, *Cable Sees Positives In Telco Entry Ruling*, BROADCASTING & CABLE, Aug. 30, 1993, at 11. See also *Chesapeake & Potomac Tel. Co. v. United States*, No. CIV.92-1751-A, 1993 WL 321669 (E.D. Va. Aug. 24, 1993). In *Chesapeake & Potomac Telephone Co. v. United States*, plaintiffs, two wholly-owned subsidiaries of Bell Atlantic Corp., successfully challenged the constitutionality under the First Amendment of section 522(b) of the Cable Communications Policy Act of 1984, 47 U.S.C. § 533(b) (1988). No. CIV.92-1751-A, 1993 WL 321669 (E.D. Va. Aug. 24, 1993). The court found that the statutory ban against common ownership of telephone and cable systems in the same market violated the First Amendment. *Id.*

7. Steven R. Rivkin, *While The Cable and Phone Companies Fight . . . Look Who's Wiring the Home Now*, N.Y. TIMES, Sept. 26, 1993, (Magazine), at 46.

8. See *infra* notes 12-15 and accompanying text.

9. See David Evans, *Spectrum Information Gets Patent On 'Direct Connect' For Cellular*, BLOOMBERG BUSINESS NEWS, Sept. 28, 1993; *infra* notes 67-71.

10. *Id.*

11. Agreements to arbitrate are valid and fully enforceable by statute:

A written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of such contract.

solving patent-related disputes. Part I will review the legislative acts that have made arbitration an option in the resolution of patent disputes and explain how parties can develop arbitration agreements. Part II will examine the benefits of the arbitration process, which allow experts in a high-technology area, such as computer equipment and programming, to make quick, well-informed decisions after relatively inexpensive hearings. In addition, Part II will explore the use of arbitration in international patent disputes. Part III will address the concerns expressed about arbitration of patent disputes with regard to bias and secrecy.

This Note will conclude that companies concerned about protection of their patents should consider the efficiency, affordability, flexibility and privacy found in the arbitration process. Although companies must keep in mind that the reasons behind arbitration decisions are never disclosed, thereby leaving future parties with similar disputes without the guidance provided by court opinions, the nature of patent disputes makes the privacy found in arbitration an important option.

I. PATENT LAW AND THE ROLE OF PATENT ARBITRATION

A. *An Overview of Patent Law*

The United States Constitution provides Congress with the power to promote the progress of technology by securing for inventors the exclusive rights to their discoveries for limited periods of time.¹² Pursuant to this authority, Congress has established the Patent and Trademark Office ("PTO"),¹³ to, inter alia, issue patents.¹⁴

9 U.S.C. § 2 (1988).

12. See U.S. CONST. art. I, § 8, cl. 8. "The Congress shall have the Power . . . To promote the Progress of Science and useful Arts, by securing for limited Times to Authors and Inventors the exclusive Right to their respective Writings and Discoveries." *Id.*

13. The PTO is the federal agency in the Department of Commerce headed by the Commissioner of Patents and Trademarks. The PTO is responsible for the examination of patent and trademark applications, issuance of patents, and registration of trademarks. 35 U.S.C. § 153 (1988).

14. A "patent" is a grant from the Patent and Trademark Office giving the holder

The basic requirements for patentability are utility, novelty and non-obviousness.¹⁵ Three types of patents are granted by the PTO: utility, plant and design. Utility patents are awarded for a period of seventeen years for "any new and useful process, machine, manufacture, or composition of matter, or any new and useful improvement thereof."¹⁶ Plant patents also have a term of seventeen years, and are awarded for "any distinct and new variety of plant."¹⁷ Design patents are awarded for a period of fourteen years for "any new, original and ornamental design for an article of manufacture."¹⁸

In the 1960s, Congress recognized the unique problems often presented by patent issues and the length of time necessary to resolve patent cases through litigation.¹⁹ For example, in 1968, 1969 and 1970, more than 90 percent of all civil litigation was concluded within three full trial days.²⁰ In comparison, less than half of the patent cases were concluded in such a period of time.²¹ In 1969 and 1970, patent disputes accounted for more than twenty percent of the civil cases requiring 20 or more days to resolve.²²

New discoveries produce new controversies on what is patentable. In the 1980s, the scope of patentable subject matter became broader with two United States Supreme Court decisions. In one case, the Court found that microorganisms created by humans are

a right to exclude others from making, using or selling one's invention, as well as the exclusive right to license others to make, use or sell the invention for seventeen years. 35 U.S.C. § 154 (1988).

15. Patent Act, 35 U.S.C. §§ 101-03 (1988). For a discussion of the requirements for patentability, see generally HERBERT F. SCHWARTZ, *PATENT LAW AND PRACTICE* 43-56 (1988).

16. 35 U.S.C. § 101 (1988).

17. 35 U.S.C. § 161 (1988).

18. 35 U.S.C. § 171 (1988).

19. ANALYSIS OF PATENT LITIGATION STATISTICS, STAFF REPORT OF THE SUBCOMM. ON PATENTS, TRADEMARKS, AND COPYRIGHTS OF THE SENATE COMM. ON THE JUDICIARY, 86TH CONG., 2D SESS. 2 (1961).

20. See *Blonder-Tongue v. University Found.*, 402 U.S. 313, 337 n.31 (1971) (citing the Annual Report of the Director of the Administrative Office of the United States Courts for the Fiscal Year Ended June 30, 1970).

21. *Id.*

22. *Id.* at 338.

patentable.²³ Another decision held that the use of a computer program in a process did not render the process unpatentable.²⁴ The broader scope of patentability and the need for uniformity in patent and other law led to the creation of the United States Court of Appeals for the Federal Circuit in 1982.²⁵ The Federal Circuit has jurisdiction over appeals from a district court's decision in a patent law action.²⁶

An examination of whether a patent has been infringed requires determining whether someone (1) without a proper license (2) makes, uses, or sells (3) the patented invention (4) within the United States or its territories (5) during the term of the patent.²⁷ Victims of infringement recover damages that are "in no event less than a reasonable royalty."²⁸ Traditional remedies for patent infringement include preliminary and permanent injunctions,²⁹ monetary damages for the loss of profits,³⁰ an increase of damages of up to three times the original at the discretion of the court,³¹ and attorney's fees.³² In recent years, some patent infringement actions have resulted in extremely large monetary awards and settlements.³³

The broadening of patentable subject matter and an increase in

23. See *Diamond v. Chakrabarty*, 447 U.S. 303, 308-09 (1980) (holding that a live, human-made microorganism is patentable subject matter, as a composition of matter that is a new substance resulting from the combination of two or more different ingredients).

24. See *Diamond v. Diehr*, 450 U.S. 175, 187 (1981) (holding that a process for curing synthetic rubber which includes the use of a mathematical formula and a programmed digital computer is patentable subject matter).

25. SCHWARTZ, *supra* note 15, at 3.

26. See *Atari, Inc. v. JS & A Group, Inc.*, 747 F.2d 1422 (Fed. Cir. 1984) (holding that the Federal Circuit has jurisdiction over JS & A Group's appeal of preliminary injunction on patent infringement claim).

27. 35 U.S.C. § 271(a) (1988).

28. 35 U.S.C. § 284 (1988).

29. 35 U.S.C. § 283 (1988).

30. 35 U.S.C. § 284 (1988).

31. *Id.*

32. 35 U.S.C. § 285 (1988).

33. See, e.g., *Polaroid Corp. v. Eastman Kodak Co.*, 16 U.S.P.Q.2d (BNA) 1481 (D. Mass. 1990), *amended on reconsideration*, 17 U.S.P.Q.2d (BNA) 1711 (D. Mass. 1991) (awarding \$873,158,971); *Minolta Settles Suit on Honeywell Patents*, N.Y. TIMES, Mar. 5, 1992, at D4 (settling for \$127,500,000).

the number of cases of infringement were followed by congressional efforts during the 1980s to promote alternative dispute resolution of patent issues.

B. The Development of Patent Arbitration

1. *Legislative Initiatives Advancing Arbitration*

Beginning in 1982, Congress enacted a series of legislative acts which provided that contracts may contain a provision requiring the use of arbitration to resolve any patent dispute.³⁴

34. President Reagan signed Public Law 97-247 on Aug. 27, 1982, specifically providing for the voluntary arbitration of patent disputes. Pub. L. No. 97-247, 96 Stat. 317 (1982) (codified as amended at 35 U.S.C. § 294 (1988)). The legislation became effective on February 27, 1983.

Section 294 provides:

(a) A contract involving a patent or any right under a patent may contain a provision requiring arbitration of any dispute relating to patent validity or infringement arising under the contract. In the absence of such a provision, the parties to an existing patent validity or infringement dispute may agree in writing to settle such dispute by arbitration. Any such provision or agreement shall be valid, irrevocable, and enforceable, except for any grounds that exist at law or in equity for revocation of a contract.

(b) Arbitration of such disputes, awards by arbitrators and confirmation of awards shall be governed by title 9, United States Code, to the extent such title is not inconsistent with this section. 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.

(c) An 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. The parties to an arbitration may agree that in the event a patent which is the subject matter of an award is subsequently determined to be invalid or unenforceable in a judgment rendered by a court of competent jurisdiction from which no appeal can or has been taken, such award may be modified by any court of competent jurisdiction upon application by any party to the arbitration. Any such modification shall govern the rights and obligations between such parties from the date of such modification.

(d) When an award is made by an arbitrator, the patentee, his assignee or licensee shall give notice thereof in writing to the Commissioner. There shall be separate notice prepared for each patent involved in such proceeding. Such notice shall set forth the names and addresses of the parties, the name of the inventor, and the name of the patent owner, shall designate the number of the patent, and shall contain a copy of the award. If an award is modified by a court, the party requesting such modification shall give notice of such modification to the Commissioner. The Commissioner shall, upon receipt of either notice, enter the same in the record of the prosecution of

In 1984, two federal laws further expanded the role of arbitration in the resolution of patent disputes. First, the Patent Law Amendments Act of 1984³⁵ replaced subsection (a) of 35 U.S.C. § 135.³⁶ Section 135(d) already provided for arbitration of patent interferences, which are disputes created by two or more applications claiming a patent on the same subject matter.³⁷ The new subsection (a) broadened what constitutes an interference by the

such patent. If the required notice is not filed with the Commissioner, any party to the proceeding may provide such notice to the Commissioner.

(e) The award shall be unenforceable until the notice required by subsection (d) is received by the Commissioner.

Id.

35. Pub. L. No. 98-622, tit. I, § 105, tit. II, § 202, 98 Stat. 3385, 3386 (1984) (codified as amended at 35 U.S.C. § 135(a) (1988)).

36. The Patent Law Amendments Act of 1984 replaced subsection (a) of 35 U.S.C. § 135 with the following:

Whenever an application is made for a patent which, in the opinion of the Commissioner, would interfere with any pending application, or with any unexpired patent, an interference shall be declared and the Commissioner 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 such 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 Commissioner 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 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) (1988).

37. Section 135(d) was also amended. It states:

Parties to a patent interference, within such time as may be specified by the Commissioner by regulation, may determine such contest or any aspect thereof by arbitration. Such arbitration shall be governed by the provisions of title 9 to the extent such title is not inconsistent with this section. The parties shall give notice of any arbitration award to the Commissioner, and such award shall, as between the parties to the arbitration, be dispositive of the issues to which it relates. The arbitration award shall be unenforceable until such notice is given. Nothing in this subsection shall preclude the Commissioner from determining patentability of the invention involved in the interference.

35 U.S.C. § 135(d) (1988) (as amended by the Patent Law Amendments Act of 1984, Pub. L. No. 98-622, §§ 105, 202, 98 Stat. 3385, 3386 (1984)).

PTO, thus encouraging the use of arbitration in resolution of these matters.³⁸ The second act, the Semiconductor Chip Protection Act of 1984,³⁹ sanctions litigation of disputes over royalties payable for innocent infringement of chip-product rights unless they are resolved by voluntary negotiation, binding arbitration, or mediation.⁴⁰

2. Arbitration and Mediation Clauses and the Role of the American Arbitration Association

The federal initiatives on patent arbitration prompted the American Arbitration Association ("AAA")⁴¹ to revise its rules to include guidelines for voluntary arbitration of patent disputes.⁴² The AAA rules dictate that such arbitration shall be private and the result of

38. See 35 U.S.C. § 135(a).

39. Pub. L. No. 98-620, tit. III, § 302, 98 Stat. 3347-55 (1984) (codified as amended at 17 U.S.C. §§ 901-914 (1988 & Supp. IV 1992)).

40. 17 U.S.C. § 907 (1988) states in pertinent part:

Limitation on Exclusive Rights: Innocent Infringement

(a) Notwithstanding any other provision of this chapter [17 U.S.C. §§ 901-914], an innocent purchaser of an infringing semiconductor chip product . . .

(2) shall be liable only for a reasonable royalty on each unit of the infringing semiconductor chip product that the innocent purchaser imports or distributes after having notice of protection with respect to the mask work embodied in the semiconductor chip product.

(b) The amount of the royalty referred to in subsection (a)(2) shall be determined by the court in a civil action for infringement unless the parties resolve the issue by voluntary negotiation, mediation, or binding arbitration.

17 U.S.C. § 907(a)(2), (b) (1988).

41. Founded in 1926, the American Arbitration Association defines itself as a public-service, not-for-profit organization offering a broad range of dispute resolution services. These services, which include arbitration, mediation, factfinding and election administration, are available through AAA headquarters in New York City and through offices located in major cities throughout the United States. Hearings may be held at locations convenient for the parties and are not limited to cities with AAA offices. See AMERICAN ARBITRATION ASSOCIATION, *COMMERCIAL DISPUTE RESOLUTION: A GUIDE TO AAA RESOURCES* (1993).

42. Parties to a contract may voluntarily agree to arbitrate their patent disputes, both pending and future, under the AAA's Patent Arbitration Rules. AMERICAN ARBITRATION ASSOCIATION, *PATENT ARBITRATION RULES, REVISED RULES AND FEES FOR CASES FILED ON OR AFTER MAY 1, 1992* 4 (1992).

the award shall be final and binding.⁴³ Awards are enforceable when notice of an award is filed with the Commissioner of Patents and Trademarks.⁴⁴ In patent arbitration, the parties may agree that the award will be modified or disregarded if the patent that is the subject of the arbitration is subsequently determined to be invalid or unenforceable.⁴⁵

Under 35 U.S.C. § 294(c), an arbitration award may not serve as a legal precedent because the resolution of the dispute is binding only on the parties to the arbitration.⁴⁶ Thus, the doctrine of collateral estoppel would not apply to an arbitration award. On the other hand, collateral estoppel is an available defense in a patent infringement action.⁴⁷

Arbitration may be the result of a pre-dispute contract or a post-dispute agreement to arbitrate.⁴⁸ Parties who voluntarily agree to arbitrate their disputes are bound by their arbitration clause.⁴⁹ The following is a standard arbitration clause involving future disputes:

43. *Id.*

44. Patent Arbitration Rule 45 states:

The AAA shall, upon the written request of a party, furnish to the party, at its expense, certified copies of any papers in the AAA's possession that may be required in judicial proceedings relating to the arbitration or as required for filing with the Commissioner of Patents and Trademarks.

Id. at 19.

45. *Cf. Ballard Medical Prods. v. Wright*, 823 F.2d 527, 531-32 (Fed. Cir. 1987) (arbitration boards have power to enforce arbitration contracts involving existing patents but do not have power to rule on validity of patents).

46. 35 U.S.C. § 294(c) provides that: "An 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) (1988).

47. *See Blonder-Tongue v. University Found.*, 402 U.S. 313, 330-31 (1971) (a patentee whose patent is held invalid in his suit against one alleged infringer may be precluded, under the doctrine of collateral estoppel, from asserting the validity of the patent in a suit against a different alleged infringer).

48. AMERICAN ARBITRATION ASSOCIATION, *supra* note 42, at 5.

49. For a discussion of the parties which are bound by an arbitration clause, see American Arbitration Association, *Governmental Bodies as Parties to Arbitration Agreements*, in LAWYERS' ARBITRATION LETTER, Vol. 5, No. 1 (1981) and American Arbitration Association, *Effect of Arbitration Agreements on Assignees, Guarantors and Other Non-Parties*, in LAWYERS' ARBITRATION LETTER, Vol. 1, No. 17 (1977).

Any controversy or claim arising out of or relating to this contract, or the breach thereof, shall be settled by arbitration in accordance with the Patent Arbitration Rules of the American Arbitration Association, and judgment upon the award rendered by the arbitrator(s) may be entered in any court having jurisdiction thereof.⁵⁰

Although the AAA has suggested this format, parties are free to create their own.

Mediation is a private, informal dispute resolution process in which a neutral third person helps disputing parties to reach an agreement. It can also be used by parties to resolve an existing dispute by entering into the following submission:

The parties hereby submit the following dispute to mediation under the Commercial Mediation Rules of the American Arbitration Association. (The clause may also provide for the qualifications of the mediator(s), method of payment, locale of meetings, and any other item of concern to the parties.)⁵¹

However, the mediator, unlike the arbitrator, has no power to impose a binding decision upon the parties.⁵²

Parties to an agreement to arbitrate or mediate may stipulate that a particular jurisdiction's law be applied on the substantive issues of the dispute, but the terms of such an agreement may be preempted. If an issue arises as to the existence of an agreement to arbitrate in a contract between merchants, the provisions of the Uniform Commercial Code may govern.⁵³ Antitrust issues⁵⁴ are

50. AMERICAN ARBITRATION ASSOCIATION, *supra* note 42, at 5.

51. *Id.* at 7.

52. AMERICAN ARBITRATION ASSOCIATION, SUPPLEMENTARY PROCEDURES FOR LARGE, COMPLEX DISPUTES, Mar. 1, 1993, at 6.

53. *See* *Lea Tai Textile Co. v. Manning Fabrics, Inc.*, 411 F. Supp. 1404 (S.D.N.Y. 1975) (applying the Uniform Commercial Code as the appropriate source of federal law, the court determined that contract for the sale of cotton cloth did not contain an enforceable agreement to arbitrate); *see, e.g.*, *Imptex Int'l Corp. v. Lorprint Inc.*, 625 F. Supp. 1572 (S.D.N.Y. 1986) (holding that a textile buyer, pursuant to industry practice, is bound by an arbitration clause for failure to object to that clause in the order confirmations or sales contracts); *Just In-Materials Designs, Ltd. v. ITAD*

generally not arbitrable.⁵⁵ Where antitrust concerns exist, a court may stay an arbitration proceeding pending resolution of the antitrust issues, provided that the antitrust issues are not viewed as "permeating the entire case."⁵⁶

II. THE BENEFITS OF ARBITRATION FOR PATENT DISPUTES IN THE AGE OF INFORMATION TECHNOLOGY

A. Arbitration As A Fast and Efficient Alternative To Lengthy Litigation of Patent Disputes

Arbitration is a quick, efficient form of patent dispute resolution before neutral arbitrators. An arbitration hearing before experts in a field allows the parties to avoid lengthy litigation that could leave a disputed patent out-dated before it reaches its potential. Throughout this century, courts have commented that the very nature of patent litigation can make the court system seem inefficient, because "patent litigation can present issues so complex that legal minds, without appropriate grounding in science and technology, may have difficulty in reaching a decision."⁵⁷

Assoc., Inc., 462 N.E.2d 1188 (N.Y. 1984) (holding that matter must be arbitrated where buyer ratified agreement which included provision for arbitration); *Marlene Indus. v. Carnac Textiles*, 380 N.E.2d 239 (N.Y. 1978) (staying an arbitration because buyer did not expressly agree to arbitration clause contained in seller's acknowledgment of an orally placed order of goods).

54. Federal and state statutes exist to protect trade and commerce from unlawful restraints, price discriminations, price fixing and monopolies. The principal federal antitrust acts are: Sherman Antitrust Act, ch. 647, §§ 1-8, 26 Stat. 209 (1890) (current version at 15 U.S.C. §§ 1-7 (1988 & Supp. IV 1992)); Clayton Act, ch. 323, § 7, 38 Stat. 730, 731-32 (1914) (current version at 15 U.S.C. § 12-27 (1988 & Supp. IV 1992)); Federal Trade Commission Act, ch. 311, §§ 1-11, 38 Stat. 717 (1914) (current version at 15 U.S.C. § 41-58 (1988 & Supp. IV 1992)); Robinson-Patman Act, 15 U.S.C. §§ 13a-13b, 21a (1988).

55. See *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 723 F.2d 155, 163 (1st Cir. 1983), *aff'd in part, rev'd in part*, 473 U.S. 614 (1985) (holding that the general rule precluding the arbitration of antitrust issues includes international agreements governing the sale and distribution of products in the United States).

56. *Cobb v. Lewis*, 488 F.2d 41, 50 (5th Cir. 1974) (holding that an arbitration clause is not valid when antitrust concerns cannot be separated from the other issues in the dispute).

57. *Blonder-Tongue v. University Found.*, 402 U.S. 313, 331 (1971); see also *Nyssonson v. Bendix Corp.*, 342 F.2d 531, 532 (1st Cir. 1965), *cert. denied*, 382 U.S.

Today, the conclusion of patent litigation can take a tremendous amount of time and an exorbitant amount of money. It took twenty-five months and millions of dollars to resolve a patent infringement lawsuit over the drug azidothymidine ("AZT").⁵⁸ AZT was developed by Burroughs Wellcome Co. of North Carolina for use in the treatment of people infected with Human Immunodeficiency Virus ("HIV").⁵⁹ The defendants, two pharmaceutical companies, Barr Laboratories of Pomona, New York, and Novapharm Ltd., of Canada, were prevented by the court from manufacturing AZT.⁶⁰

The initial complaint in this consolidated patent infringement action was filed on May 14, 1991.⁶¹ In the opinion, Judge Malcolm J. Howard of the Eastern District of North Carolina wrote:

The sixty-year-old courtroom in New Bern, North Carolina, has been converted into a contemporary "high tech" facility utilizing "real time" court reporting and six computer-integrated video display monitors. It is highly conceivable that the cost of this trial for the parties exceeds \$100,000 per day, in addition to the time and expense associated with this court and the jury.⁶²

Before the commencement of the trial on June 28, 1993, approximately 541 pleadings were filed, and dozens of hearings on motions and discovery matters were conducted by the court.⁶³ The court entered eighty-eight written orders and numerous bench rulings.⁶⁴

When the trial finally concluded, Burroughs Wellcome had

847 (1966); *Harries v. Air King Prods. Co.*, 183 F.2d 158, 164 (2d Cir. 1950); *Parke-Davis & Co. v. H.K. Mulford Co.*, 189 F. 95, 115 (S.D.N.Y. 1911), *aff'd in part, rev'd in part*, 196 F. 496 (2d Cir. 1912).

58. *Burroughs Wellcome Co. v. Barr Labs., Inc.*, No. 91-41-Civ-4-H, 1993 WL 294572 (E.D.N.C. July 22, 1993).

59. *Id.* at *1.

60. *Id.* at *7.

61. *Id.* at *1.

62. *Id.*

63. *Id.*

64. *Id.*

successfully defended the six patents it holds on AZT that expire in 2005.⁶⁵ A quicker, less expensive resolution of such issues through arbitration could have saved the parties money, allowed for a faster resumption of research, and benefitted consumers who are concerned about the development and cost of pharmaceuticals. However, the value of some patents may make companies reluctant to use arbitration, which does not have the procedural safeguards of discovery and an appeals process.

In the computer industry, weeks, months, and even years could pass before an action is resolved. This could be devastating to the parties involved. There are often issues, such as the definition of terms in an on-going contract, that must be resolved quickly in order to allow the manufacturing of a product to continue.⁶⁶ Pre-dispute arbitration agreements provide for quick resolution of these problems.

The inevitable interaction of different information technologies in creating the "information superhighway" will increase the potential for disputes involving a growing number of special inventions and designs. For example, Spectrum Information Technologies ("Spectrum") has developed and patented a method called "direct connect." This new method makes a connection between portable computers and cellular telephones without the use of a separate interface box.⁶⁷ Spectrum has been conducting "an aggressive campaign" to require manufacturers of computers and modems that send data over cellular telephones to license its "direct connect" patent.⁶⁸ A licensing agreement has been signed with American Telephone & Telegraph Corp. ("AT&T") for use of Spectrum's patents involved in the sending of data over cellular telephones.⁶⁹

65. *Id.*

66. *See, e.g.,* Management Sys. Assocs., Inc. v. McDonnell Douglas Corp., 762 F.2d 1161 (4th Cir. 1985) (dispute over the meaning of the term "software"); Renfro Hosiery Mills Co. v. National Cash Register Co., 552 F.2d 1061 (4th Cir. 1977) (dispute over the phrase "greater, increased and improved reliability"); S & H Computer Sys., Inc. v. SAS Inst., Inc., 568 F. Supp. 416 (M.D. Tenn. 1983) (dispute over the meaning of "use" in the context of a software licensing agreement).

67. The U.S. patent number on Spectrum's "direct connect" is 5,249,218.

68. Evans, *supra* note 9.

69. *Id.*

Other companies have products on the market similar to Spectrum's "direct connect," creating a potential for patent disputes with Spectrum.⁷⁰ To avoid creating roadblocks on the information superhighway, potential licensees of patented inventions as well as competitors who have potential patent infringement problems with the licensor should consider contracts with pre-dispute agreements to arbitrate.⁷¹

B. *The Affordability of Arbitration*

Arbitration is a relatively inexpensive process for resolving patent problems between parties. The cost of lengthy litigation may make some companies reluctant to go to court, or make a

70. Five companies have licensed Spectrum's four U.S. patents relating to data transmission over cellular telephones, but Motorola Inc., the largest maker of cellular data equipment, says it has no plans to license Spectrum's patents. See David Evans, *Spectrum Info Cites License Fees For \$646,374 2nd Qtr Profit*, BLOOMBERG BUSINESS NEWS, Nov. 12, 1993. Compaq Computer Corp. ("Compaq") is one of several companies that currently sells "direct connect" type products for sending data over cellular telephones. According to a brochure for Compaq's Speedpack 144, introduced in November 1992, the product requires "a simple cable interface" between a computer and a cellular telephone, eliminating the need for an interface box. In an August 1993 interview with Bloomberg Business News, Compaq's general counsel, David Cabello, said "we're not aware of any infringement [on Spectrum's patents]." Evans, *supra* note 9.

71. Spectrum's "direct connect" patent had been an issue in a lawsuit filed in U.S. District Court in San Antonio, Texas, by Spectrum against modem manufacturer Data Race Inc. of San Antonio ("Data Race"), its former development partner. Data Race had agreed to license Spectrum's technology for sending computer data over cellular telephones, but the agreement fell apart when Data Race stated that Spectrum's demands for permission to license its technology were "too large for [Data Race] to remain competitive." Evans, *supra* note 9.

Furthermore, such litigation may produce other concerns, such as the potential disclosure of trade secrets during the discussion of patents in an open courtroom. See *infra* part III.C. In the instant case, Data Race challenged the validity of two other Spectrum patents for sending data over cellular telephones. As part of that litigation, Data Race agreed not to disclose the contents of Spectrum's 58-page patent application for its direct connect. Evans, *supra* note 9.

Spectrum and Microcom Inc., a company which specializes in the transmission of data over telephone lines and cellular telephones, announced the settlement of a patent infringement suit on November 17, 1993. The companies agreed to formally acknowledge and license each other's technologies. Liz Roman Gallese, *Microcom, Spectrum Information Settle Patent Infringement Suit*, BLOOMBERG BUSINESS NEWS, Nov. 17, 1993.

patent case impossible for a smaller business or inventor to pursue. In comparison to litigation, arbitration requires only minimal fees.

Arbitration does not include discovery, a pre-trial process which can be lengthy and expensive.⁷² The final decision of the arbitrator is rendered after hearings before a panel.⁷³ The AAA remains ready to handle a dispute in a timely fashion by maintaining a pool of candidates for patent arbitration panels.⁷⁴

As a not-for-profit organization, the AAA prescribes filing and other administrative fees to compensate for the cost of providing administrative services. Filing fees for resolution of patent disputes depend on the amount of the claim or counterclaim, ranging from \$300 on claims below \$25,000, to a maximum of \$4000 for claims in excess of \$5 million.⁷⁵ When no amount can be stated at the time of filing, the filing fee is \$1000, subject to adjustment when the claim or counterclaim is disclosed.⁷⁶

In addition to the filing fees, for each day of a hearing before a single arbitrator, the AAA requires an administrative fee of \$100 per party,⁷⁷ and if before a multiarbitrator panel, \$150 per day.⁷⁸

C. *The Flexibility of Arbitration*

Parties who agree to arbitrate their disputes are free to use and to modify any provision of the AAA's procedures.⁷⁹ Arbitration,

72. In some patent cases, however, lack of discovery can be viewed as a detriment. *See infra* part III.C.

73. Although there is no discovery process in arbitration, the parties are entitled to be heard, to present evidence and to cross-examine witnesses. Notwithstanding the failure of a party duly notified to appear, the arbitrator may hear and determine the controversy upon the evidence produced. AMERICAN ARBITRATION ASSOCIATION, *supra* note 42, at 16-17. States may adopt variations of the AAA model rules. *See, e.g.,* N.Y. CIV. PRAC. L. & R. 7506 (McKinney 1980).

74. AAA Patent Arbitration Rule 4 states: "The AAA shall establish and maintain a National Panel of Patent Arbitrators, which will include individuals having experience in patent law and/or special technical expertise, and shall appoint arbitrators as provided in these rules." AMERICAN ARBITRATION ASSOCIATION, *supra* note 42, at 8.

75. *Id.* at 21.

76. *Id.*

77. *Id.*

78. *Id.*

79. Parties can tailor their arbitration agreement to their specific needs, using the AAA's booklet, *Drafting Dispute Resolution Clauses: A Practical Guide*. The Asso-

like any contractual right, may be waived by the parties to the agreement.⁸⁰ Arbitration, mediation, and other forms of alternative dispute resolution may all be incorporated under the same agreement. Further, parties can develop arbitration agreements which stipulate their choice of law.⁸¹ Such agreements can eliminate delays that may result from a dispute over jurisdiction and choice of law.

The complex dispute, *IBM v. Fujitsu Ltd.*,⁸² illustrates the ability to use a number of methods for dispute resolution, such as arbitration, mediation, neutral expert fact-finding, and negotiations by executives and attorneys.⁸³ The focus of the dispute was IBM's claim that Fujitsu, which makes IBM compatible hardware and software, had violated IBM's software copyrights.⁸⁴ IBM and Fujitsu, the world's first and fourth largest computer companies, respectively, competed in the United States, Europe, Brazil, and the Pacific Rim; thus, the dispute had worldwide implications for the computer industry.⁸⁵

After IBM alleged in October of 1982 that Fujitsu violated its copyrights, senior officials from both companies spent eight months

ciation will also critique proposed arbitration clauses if the parties desire such assistance. *AMERICAN ARBITRATION ASSOCIATION*, *supra* note 52, at 5-6.

80. *See, e.g.*, *Miller Brewing Co. v. Fort Worth Distrib. Co.*, 781 F.2d 494, 497 (5th Cir. 1986) (holding that distributor waived right to arbitration by waiting almost eight months after bringing state court suit to announce its intention to arbitrate); *Sedco, Inc. v. Petroleos Mexicanos Mexican Nat'l Oil Co.*, 767 F.2d 1140, 1150 (5th Cir. 1985) (holding that drilling company did not waive right to arbitrate during three-year-long dispute over whether district court had jurisdiction).

81. Private agreements to arbitrate are enforced in accordance with their own terms, including choice of law. *See Volt Info. Sciences, Inc. v. Board of Trustees of Leland Stanford Jr. Univ.*, 489 U.S. 468, 478-79 (1989) (parties to an arbitration agreement can provide for the application of a certain state law).

82. *IBM v. Fujitsu Ltd.*, American Arbitration Ass'n, No. 13T-117-0636-85. AAA cases are not published, because the process is designed to be a private resolution of a dispute between the parties. The AAA does assign each case a number, and it often maintains files of articles referring to major cases, some of which are available to the public.

83. *See* Eric D. Green, *Alternative Dispute Resolution In Patent and Antitrust Cases*, in *PATENT ANTITRUST* 1989, 479, 532 (PLI Patents, Copyrights, Trademarks and Literary Property Course Handbook Series, 1989).

84. *Id.*

85. Green, *supra* note 83, at 532.

negotiating a settlement.⁸⁶ Fujitsu agreed to pay substantial sums to IBM for its previous distribution of certain computer programs, and agreed to make semi-annual payments for its future marketing of them. In turn, IBM granted a license to Fujitsu, which admitted no copyright infringement, and waived all past and future claims regarding that software.⁸⁷ This settlement was the first of many steps in a long process of resolving disputes between the two companies.

In June of 1985, the companies used two neutral experts to reach a two-fold agreement.⁸⁸ The first part involved Fujitsu paying a fee for a license to use certain IBM programs. The second part of the agreement established a "Security Facility Regime," under which each company can examine, under elaborate safeguards, certain parts of the other company's software.⁸⁹ In return for what is determined to be adequate compensation, the examining party could use the obtained information in developing its own software, and be assured of immunity from claims of copyright violations. This arrangement was monitored by an independent expert.⁹⁰

The resolution of this major software dispute also incorporated an element of alternative dispute resolution known as "preventative law."⁹¹ One of the neutral experts, Stanford Law School Professor Robert Mnookin,⁹² described preventative law as follows:

[Preventative Law] provides a unique advantage as a means of settling complicated issues in evolving technological and legal fields. In the past, IBM could never know exactly how Fujitsu was using IBM programming material. In order to determine if some violation of its rights may have occurred, IBM had to wait until after the public release of

86. *Id.* at 533-34.

87. *Id.* at 534.

88. *Id.*

89. *Id.*

90. *Id.*

91. *Id.*

92. The other expert was retired railroad executive and computer expert John Jones. *Id.*

a Fujitsu program and then conduct an elaborate technical examination of the program. Then, if it chose to pursue a claim, it was extremely expensive and time-consuming. Meanwhile, of course, the Fujitsu program at issue was already in the marketplace. Even the threat that IBM might at some future point pursue a claim would create a potential problem for both Fujitsu and for the Fujitsu customers using a new Fujitsu program. [This preventative law] exposes and resolves disagreements before public release of the software.⁹³

As a result of the independent analysis in a secured facility, IBM was assured that Fujitsu would use only the material that is approved following the process. Fujitsu could go ahead with production, knowing that IBM would not make a claim with respect to the use of that material at some date in the future. The customers of each company could buy products, knowing that they would not be involved in a patent or a copyright infringement and that the software they were using would not be withdrawn.

D. Arbitration of International Patent Disputes

The AAA has a specific rule for handling disputes involving parties from different nations.⁹⁴ The rule provides for a neutral arbitrator and a neutral location for a hearing.⁹⁵ Companies that are based in different countries may consider pre-dispute and post-dispute arbitration agreements as an option to litigation.⁹⁶ These

93. *Id.*

94. Rule 15 of the AAA Patent Arbitration Rules provides guidelines for international arbitration. AMERICAN ARBITRATION ASSOCIATION, *supra* note 42, at 12.

95. *Id.* Rule 15 states:

Where the parties are nationals or residents of different countries, any neutral arbitrator shall, upon the request of either party, be appointed from among the nationals of a country other than that of any of the parties. The request must be made prior to the time set for the appointment of the arbitrator as agreed by the parties or set by these rules.

Id.

96. See discussion *infra* part III.C. *IBM v. Fujitsu* is an example of how arbitration can bridge continents. "[T]his case of global implications, involving hundreds of millions of dollars, high emotions and cultural differences, was susceptible of [alternative dispute resolution]." Green, *supra* note 83, at 535.

agreements are especially important because, in contracts involving an agreement to arbitrate, companies from different nations may also include provisions for the protection of trade secrets.⁹⁷

The ability of parties drafting an arbitration agreement to make decisions on the choice of law and the location of a hearing can simplify the resolution of an international dispute. A pre-dispute agreement on choice of law would mean that the parties to the agreement would know what rules to follow, and any resulting dispute over the interpretation of those rules could be resolved by a neutral arbitrator.

There may also be a certain reluctance to litigate a patent dispute in a foreign forum, if a party perceives itself as an outsider at a disadvantage in unfamiliar territory. For example, an observer of a series of patent disputes involving Honeywell and Minolta⁹⁸ notes that the parties provided indications of a certain level of distrust regarding court proceedings in a foreign country.⁹⁹ An arbitration agreement calling for the use of a neutral arbitrator and a neutral location for dispute resolution could eliminate such concerns.

III. ADDRESSING CONCERNS ABOUT PATENT ARBITRATION

A. *Avoidance of Bias In Arbitration*

Critics of arbitration argue that the privacy of the process, and the fact that arbitrators need not disclose a rationale for an award,

97. Trade secret protection is generally not available outside of the United States and the European Economic Community. If a country does have a trade secret law, it is most likely that trade secrets are protected by criminal laws rather than civil laws. Trade secret protection is also generally imposed by contract. See PETER B. MAGGS, ET AL., *COMPUTER LAW* 338 (1991).

98. *Honeywell, Inc. v. Minolta Camera Co.*, No. CIV.A.87-4847, 1991 WL 50063 (D.N.J. Apr. 5, 1991) (patent dispute over an automatic focus system for use in photographic cameras).

99. Interview with Ken Herman, Partner with Fish & Neave, on WBBR Radio in New York, N.Y. (July 27, 1993). While Mr. Herman stated that he generally favors the resolution of patent disputes in court, citing the precedential value of decisions and "the safeguards of litigation, including discovery and the appeals process," he noted that parties may prefer the privacy of arbitration, as well as the ability to choose a neutral arbitrator and a neutral location. *Id.*

can lead to bias. Arbitrators, however, have a duty to disclose any appearance of bias.¹⁰⁰ The AAA goes to great lengths to avoid any bias or appearance of bias by maintaining strict rules on disclosure.¹⁰¹ Arbitrators may be called to serve on a panel by the parties themselves, by appointment under the rules of an agency administering the arbitration, or by the court.¹⁰² The stakes in disputes such as the one between IBM and Fujitsu increase the desire for fair, impartial decisions.¹⁰³

In *Commonwealth Coatings Corp. v. Continental Casualty Co.*, the United States Supreme Court addressed the prevention of the appearance of bias in arbitration.¹⁰⁴ The Court held that where one of three arbitrators has had a "close business connection" with one of the parties, the failure to disclose this relationship is sufficient

100. See *Commonwealth Coatings Corp. v. Continental Casualty Co.*, 393 U.S. 145 (1968).

101. According to Canon II of the AAA's *Code of Ethics for Arbitrators in Commercial Disputes*:

A. Persons who are requested to serve as arbitrators should, before accepting, disclose:

(1) Any direct or indirect financial or personal interest in the outcome of the arbitration;

(2) Any existing or past financial, business, professional, family or social relationships which are likely to affect impartiality or which might reasonably create an appearance of partiality or bias. Persons requested to serve as arbitrators should disclose any such relationships which they personally have with any party or its lawyer, or with any individual whom they have been told will be a witness. They should also disclose any such relationships involving members of their families or their current employers, partners or business associates.

SPECIAL COMMITTEE OF THE AMERICAN ARBITRATION ASSOCIATION AND SPECIAL COMMITTEE OF THE AMERICAN BAR ASSOCIATION, *CODE OF ETHICS FOR ARBITRATORS IN COMMERCIAL DISPUTES* 7 (1977).

102. For example, according to the New York Civil Practice Law and Rules, section 7504: "If the arbitration agreement does not provide for a method of appointment of an arbitrator, or if the agreed method fails or for any reason is not followed, or if an arbitrator fails to act and his successor has not been appointed, the court, on application of a party, shall appoint an arbitrator." N.Y. CIV. PRAC. L. & R. 7504 (McKinney 1980).

103. For a discussion of the stakes involved in the arbitration case *IBM v. Fujitsu*, see *supra* part II.C.

104. 393 U.S. 145 (1968).

grounds to vacate the award.¹⁰⁵ The Court found a close business connection to include a "sporadic" relationship where "the patronage was repeated and significant," even though there had been no business dealings between the arbitrator and the party for "about a year."¹⁰⁶

However, in a concurring opinion,¹⁰⁷ Supreme Court Justice Byron White, after analyzing the provisions of the AAA's Code of Ethics for Arbitrators in Commercial Disputes, concluded that arbitrators "should err on the side of disclosure," but an arbitrator "cannot be expected to provide the parties with his complete and unexpurgated business biography," nor is an arbitrator called upon to disclose interests or relationships which are merely "trivial."¹⁰⁸ Justice White also recognized that some remote connections that do not put impartiality into question may inevitably be present.¹⁰⁹ As an additional safeguard against wrong-doing on the part of arbitrators, at least one lower court has held that arbitrators cannot discuss fee demands during the proceedings.¹¹⁰

B. *Vacating An Improper Arbitration Award*

Although arbitration decisions generally stand, courts have the authority to overturn arbitration decisions when a court finds evidence of fraud, corruption, or partiality.¹¹¹ Courts may also over-

105. *Id.*

106. *Id.* at 146.

107. *Id.* at 150 (White, J., concurring, joined by Marshall, J.).

108. *Id.* at 151-52.

109. "[A]rbitrators are not automatically disqualified by a business relationship with the parties before them if both parties are informed of the relationship in advance, or if they are unaware of the facts but the relationship is trivial. I see no reason automatically to disqualify the best informed and most capable potential arbitrators." *Id.* at 150.

110. *See* *Double-M Constr. Corp. v. Central Sch. Dist. No. 1, Town of Highlands*, 391 N.Y.S.2d 10 (N.Y. App. Div. 1977), *modified*, 402 N.Y.S.2d 442 (N.Y. App. Div. 1978).

111. 9 U.S.C. § 10 provides:

(a) In any of the following cases the United States court in and for the district wherein the award was made may make an order vacating the award upon the application of any party to the arbitration—

(1) Where the award was procured by corruption, fraud, or undue means.

turn decisions when arbitrators exceed their authority¹¹² or when there are antitrust concerns.¹¹³ Further, courts can vacate an arbitration award upon finding "a manifest disregard of the law."¹¹⁴ Judicial inquiry under the "manifest disregard" standard is extremely limited,¹¹⁵ requiring "something beyond and different from mere

(2) Where there was evident partiality or corruption in the arbitrators, or either of them.

(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 if any other misbehavior by which the rights of any party have been prejudiced.

(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.

(5) Where an award is vacated and the time within which the agreement required the award to be made has not expired the court may, in its discretion, direct a rehearing by the arbitrators.

(b) The United States district court for the district wherein an award was made that was issued pursuant to section 580 of title 5 may make an order vacating the award upon the application of a person, other than a party to the arbitration, who is adversely affected or aggrieved by the award, if the use of arbitration or the award is clearly inconsistent with the factors set forth in section 572 of title 5.

9 U.S.C. § 10 (Supp. IV 1992).

112. *See Barbier v. Shearson Lehman Hutton Inc.*, 948 F.2d 117, 122 (2d Cir. 1991) (arbitrators exceeded their authority in awarding punitive damages because parties chose New York law, which prohibits arbitrators from awarding punitive damages).

113. *See Cobb v. Lewis*, 488 F.2d 41, 47-50 (5th Cir. 1974) (plaintiffs' antitrust claims not subject to arbitration).

114. *Sperry Int'l Trade, Inc. v. Government of Israel*, 689 F.2d 301, 304-05 (2d Cir. 1982); *see, e.g., Fahnestock & Co. v. Waltman*, 935 F.2d 512, 515 (2d Cir. 1991) (holding that arbitrator did not manifestly disregard law in awarding compensatory damages for defamation, but punitive damages were properly vacated under New York law precluding arbitrators from awarding them); *Carte Blanche (Sing.) Pte. Ltd. v. Carte Blanche Int'l, Ltd.*, 888 F.2d 260, 265 (2d Cir. 1989)), *cert. denied*, 112 S. Ct. 1241 (1992) (holding no manifest disregard of the law where arbitrators permitted party to make consequential damages claim and terms of reference placed no limitation on such damages); *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Bobker*, 808 F.2d 930, 933-34 (2d Cir. 1986) (holding no manifest disregard of the law where arbitrators did not strictly enforce provisions in federal securities rules).

115. *Local 1199, Drug, Hosp. and Health Care Employees Union v. Brooks Drug Co.*, 956 F.2d 22, 25 (2d Cir. 1992) ("[T]he court is forbidden to substitute its own interpretation even if convinced that the arbitrator's interpretation was not only wrong,

error in the law [M]anifest disregard will be found where an arbitrator understood and correctly stated the law but proceeded to ignore it."¹¹⁶ As a last resort, a court may also refuse to enforce an arbitration award on grounds that such enforcement "would violate 'some explicit public policy' that is 'well defined and dominant, and is to be ascertained by reference to the laws and legal precedents and not from general considerations of supposed public interests.'"¹¹⁷

A recent copyright case illustrates the factors involved in an attempt to vacate an arbitration award for a manifest disregard of the law. In *SCS Business & Technical Institute v. Interactive Learning Systems Inc.*, the United States District Court for the Southern District of New York vacated an arbitrator's award for \$190,000 for copyright damages for the alleged infringement of unregistered software and remanded the case back to the arbitrator.¹¹⁸ SCS Business & Technical Institute ("SCS") had entered into an agreement with Interactive Learning Systems ("Interactive") in which Interactive granted SCS an exclusive license to use its teaching system software for five years.¹¹⁹ After becoming dissatisfied with the system, SCS exercised an option in the contract to terminate the agreement, but copied some of Interactive's software and failed to return 29,168 diskettes.¹²⁰

In accordance with their January 1989 contract, the parties entered into arbitration.¹²¹ Interactive was awarded damages for the

but plainly wrong." (quotation omitted)); *Chicago Typographical Union No. 16 v. Chicago Sun-Times, Inc.*, 935 F.2d 1501, 1505 (7th Cir. 1991) (the role of the court in setting aside an arbitrator's action is "severely limited—but not negligible").

116. *Fahnestock*, 935 F.2d at 516 (quoting *Siegel v. Titan Indus. Corp.*, 779 F.2d 891, 892-93 (2d Cir. 1985)).

117. *United Paperworkers Int'l Union v. Misco, Inc.*, 484 U.S. 29, 43 (1987) (quoting *Muschany v. United States*, 324 U.S. 49, 66 (1945)).

118. No. 92 Civ. 0724, 1992 WL 196737 (S.D.N.Y. Aug. 3, 1992). For discussion of *SCS*, see *Arbitrator's Award Vacated*, *COMPUTER LAW STRATEGIST* (Leader Publications, New York, N.Y.), Nov. 1992, at 5.

119. *SCS*, 1992 WL 196737, at *1.

120. *Id.*

121. *Id.*

unreturned diskettes and for copyright infringement.¹²² SCS moved to vacate an arbitrator's award for copyright infringement on the grounds that Interactive failed to seek and obtain copyright registration, thereby precluding it from statutory damages.¹²³ Interactive countered by stating that the arbitrator's award was intended to "remedy the loss it suffered by being deprived of the ability to offer an exclusive contract to another potential customer, and that the arbitrator referred to copyright damages in the Award only by analogy."¹²⁴ The arbitrator testified before the court that, as an arbitrator, he was not required to follow the statute on damages for copyright infringement because "we're in arbitration, we don't have to apply the statute exactly. . . . [W]e are not in court."¹²⁵

In vacating the arbitrator's award, the court stated:

It is a fundamental axiom of copyright law that valid copyright registration is a condition precedent for recovery of statutory copyright damages To the extent that the Award was intended to remedy a purported violation of Interactive's copyright rights, the arbitrator's decision was contrary to well-established controlling principles of law. Moreover, SCS brought this rule of law to the attention of the arbitrator, who indicated that he understood the rule.¹²⁶

The court remanded the case to the arbitrator, for a clarification of the ruling, in an effort to "ensure that any award of damages for improper copying and interference with Interactive's exclusivity rights is not preempted by the Copyright Act."¹²⁷

122. *Id.*

123. *Id.* at *2.

124. *Id.* at *3.

125. *Id.* at *4.

126. *Id.* While the court was correct in its analysis of the manifest disregard standard, its decision to vacate the arbitration award is arguably erroneous. The arbitrator was within the bounds of the Copyright Act in awarding these damages. While copyright registration is required for an award of statutory damages and attorney's fees, the Copyright Act does not specifically require registration for the recovery of actual damages where there has been a copyright infringement. 17 U.S.C. § 412 (1988 & Supp. IV 1992). In addition, while the owner of an allegedly infringed copyright must register the copyright as a prerequisite to filing suit, registration is not required to arbitrate a matter. 17 U.S.C. § 411(a) (1988 & Supp. IV 1992).

127. *Id.* Indefinite, incomplete or ambiguous awards can be remanded to an arbi-

Similarly, in patent arbitration cases, arbitration awards may be vacated or modified when arbitrators are found to have exceeded their powers.¹²⁸ Arbitrators can rule on the terms of patent contracts but they cannot determine the validity of patents. Decisions of arbitrators that "constitute some sort of roving Patent Office"¹²⁹ can be vacated.¹³⁰

The loser of an arbitration is bound by the decision unless a court of law vacates the award.¹³¹ While courts have the authority to modify or vacate an arbitration award on the basis of manifest disregard for the law, it may be difficult for a court to reach such a conclusion because it must begin the process by noting that an arbitrator does not need to disclose the rationale for an award.¹³²

C. Arbitration, While Confidential, Lacks Procedural Safeguards

The nature of a patent dispute makes the protection of the patent holder's trade secrets¹³³ very important because a company does

trator when the court has questions about what it is being asked to enforce. *See* *Ottley v. Schwartzberg*, 819 F.2d 373, 376 (2d Cir. 1987) (holding that a remand is appropriate in limited circumstances such as when an award is incomplete or ambiguous); *New York Bus Tours, Inc. v. Kheel*, 864 F.2d 9, 13 (2d Cir. 1988) ("We should not undertake to construe the meaning of arbitration awards where they are unclear.").

128. *See* *Ballard Medical Prods. v. Wright*, 823 F.2d 527 (Fed. Cir. 1987).

129. *See id.* at 532.

130. 9 U.S.C. § 10(a) reads in pertinent part: "In any of the following cases the United States court in and for the district wherein the award was made may make an order vacating the award upon the application of any party to the arbitration . . . (a)(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(a) (Supp. IV 1992).

131. *See* 9 U.S.C. § 2 (Supp. IV 1992).

132. *See* *United Steelworkers of Am. v. Enterprise Wheel and Car Corp.*, 363 U.S. 593, 598 (1960) ("Arbitrators have no obligation to the court to give their reasons for an award."); *see also* *Sperry Int'l Trade, Inc. v. Government of Israel*, 689 F.2d 301, 306 (2d Cir. 1982) ("In keeping with the practice [of the American Arbitration] Association's Rules . . . the arbitrators gave no explanation for the Award.").

133. A "trade secret" is a secret formula or process that is not necessarily patented, but known only to certain individuals using it in compounding some article of trade having a commercial value. A "trade secret," as protected from misappropriation, may consist of any formula, pattern, device or compilation of information which is used in one's business. *See* BLACK'S LAW DICTIONARY 1494 (6th ed. 1991).

not want to reveal any more information than necessary to comply with patent disclosure laws.¹³⁴ The AAA's Code of Ethics for Arbitrators in Commercial Disputes contains a provision designed to safeguard the privacy of the process.¹³⁵ This, coupled with the lack of discovery, makes arbitration an attractive alternative to litigation with or without a protective order.

However, under certain circumstances, the procedural safeguards found in litigation may outweigh the benefits of arbitration's confidentiality. For example, the discovery process may be necessary to gather information required to prove infringement. Further, a patent holder may be reluctant to trust the protection of a valuable patent to the decision of an arbitrator who is not subject to an appeals process.¹³⁶ The parties to an arbitration proceeding may never know the reasons behind a decision, because an arbitrator need not discuss them.¹³⁷ In addition, the parties cannot look to the courts as a means of appealing an arbitrator's ruling on this basis because a court also must be guided by the principle that it cannot substitute its own interpretation of a contract for the interpretation of the arbitrator.¹³⁸

134. A patent is often described as a contract between an inventor and the government, in which the patent holder gets an exclusive right to an invention for a limited period of time, in return for disclosing the elements of the invention. See SCHWARTZ, *supra* note 15, at 60-61. An inventor must provide the PTO with a written description of the patentable subject matter, as well as the process of making and using it. 35 U.S.C. § 112 (1988).

135. AMERICAN ARBITRATION ASSOCIATION, CODE OF ETHICS FOR ARBITRATORS IN COMMERCIAL DISPUTES 11 (1977). Canon VI provides:

A. An arbitrator is in a relationship of trust to the parties and should not, at any time, use confidential information acquired during the arbitration proceeding to gain personal advantage or advantage for others, or to affect adversely the interest of another.

B. Unless otherwise agreed to by the parties, or required by applicable rules of law, an arbitrator should keep confidential all matters relating to the arbitration proceedings and decision.

Id.

136. Note, however, that an arbitrator's award may be vacated under limited circumstances. See *supra* part III.B.

137. See *supra* note 132.

138. See *Local 1199, Drug, Hosp. & Health Care Employees Union v. Brooks Drug Co.*, 956 F.2d 22, 25 (2d Cir. 1992); *Chicago Typographical Union No. 16 v.*

CONCLUSION

Patent arbitration is an efficient, affordable, flexible and private means of reaching solutions, allowing companies to protect their rights without subjecting themselves to long, expensive court battles. Small, emerging high-tech companies that do not have the resources to face expensive litigation should insist on arbitration clauses in their contracts, giving them a fast, affordable way to safeguard their interests. Companies from different nations should negotiate an arbitration agreement before a dispute arises dealing with the choice of law and the process for resolving disagreements.

Critics of arbitration argue that it lacks the procedural safeguards and the precedential value found in the court system. Supporters of arbitration also point to these factors, but for different reasons, asserting that the absence of discovery and lack of an appeals process dramatically reduce the time and cost of dispute resolution, while preserving privacy.

Companies that use methods to resolve their disputes in a timely, efficient manner are more likely to remain allies and less likely to face potentially costly litigation and disruptions in manufacturing. In a world where information is power and many inventions are in demand for only a limited period of time before becoming obsolete, the private, quick, relatively inexpensive dispute resolution offered by arbitration may be exactly what some companies need to remain competitive.

Karl P. Kilb

