Government Increases Patent Fees & Gives a Dangerous Break to "Micro Entities"

by Curt Harrington

The current Government is raising patent fees under the guise of creating a "new" "micro-entity" status that may be effectively available to only a few inventors and only at a potentially dangerous cost to both patent practitioners and patent integrity.

As if it were not bad enough that capital gains for patents sold have been increased and mutilates the gain computation such that a multi-step tax computation (based upon the taxpayers income) is necessary to determine the tax, the Patent & Trademark Office has recently adopted a price increase along with introduction of a Micro Entity as a third fee status category with restrictions that require reference to U.S. tax code definitions, and U.S. median income.

Traditionally, the Patent & Trademark Office fees for patent matters depended upon two categories, Large Entity and Small Entity. The small entity designation was for employers having 500 or less employees, individual persons, and nonprofits. All others paid the large entity fees. As an illustrative example, I will use maintenance fees. (Remember than nearly all fees for filing, processing, and more, will occupy the "large", "small" and Micro Entity status; but I have chosen maintenance fees for simplicity only. The fees to maintain a patent at 3 years, 7 years and 11 years are, for the time period up to and including March 18, 2013:

Up To & Including 3/18/2013

Ent	3Yr	7Yr	11Yr
Lg.	$1150	$2900	$4810
Sm	$ 575	$1450	$2405

On and after March 19, 2013, a new Micro Entity classification was created as a third option to enable even lower fees for those who qualify. The fee structure for maintenance fees after March 19, 2013 are:

Including & After 3/19/2013

Ent	3Yr	7Yr	11Yr
Lg.	$1600	$3600	$7400
Sm	$ 800	$1800	$3700
Micro	$ 400	$ 900	$1850

Setting the Micro Entity aside, it can be seen that the large entity maintenance fees over the life of a patent increased by $3740. Similarly Small Entity maintenance fees increased by $1870.

A casual observer might naively look at the chart and believe that the Micro Entity status actually enabled a *decrease* in fees relative to the "small Entity category, and feel all warm and generous over the supposed helping hand given to small inventors. Just looking at the Micro category for 3/19/2013 & later and comparing it to the general Small Entity category for 3/18/2013 gives the appearance of a decrease of $175(3Yr), $550 (7Yr), & $555(11Yr.). For Micro Entity inventors, the cost of maintaining a utility patent over its life would seem to have decreased by $175 + $550 + $555 = $1280. However there are SEVERE &

CONFUSING RESTRICTIONS on the ability to claim the Micro Entity status.

The Micro Entity status is governed by title 37 Code of Federal Regulations (CFR) § 1.29. Without simply reproducing the section, the following is a list of requirements necessary for inventors to take advantage of the Micro Entity status:

(1) The applicant-inventor otherwise qualifies as a small entity under § 1.27.

Comment: Therefore it must first be established that an inventor or inventive entity must otherwise qualify for small entity status.

(2) Neither the applicant nor the inventor nor a joint inventor has been named as the inventor or a joint inventor on more than four previously filed (U.S. type) patent applications.

Comment: The problem with this requirement is that a loss of personal Micro Entity status controls all of the fees charged in future. Put another way if an inventor filed a first, second, third, and fourth application, had those patent issue and have the latter fourth application pay its 11.0 year maintenance fee before any other patent were filed, he or she would have taken full advantage of the Micro Entity status for four full applications. In addition, overseas inventors are treated the same as U.S. citizen inventors, and a foreign inventor may have dozens of patents filed in his or her home country.

Contrast this with the knowledge that a first filing may linger for 2 years before Examination. If an inventor files a fifth application at the time when one or two of the cases are still pending and while one or two of the cases have not yet been maintained, the filing of a fifth case will increase the fee status on all actions on the first four cases from that point on. This is not even to mention the loss of Micro Entity status of having added a single co-inventor who has had more than four previous patents.

The language of this provision is curiously mixed where it states that an applicant might have been a prior inventor. It is easily seen that a person might be an assignee of a patent where such assignee person may not have been an inventor of that patent. But a company assignee would seem nonsensical in terms of also being an inventor, since companies can't invent.

(3) Neither the applicant nor the inventor nor a joint inventor, in the calendar year preceding the calendar year in which the applicable fee is being paid, had a gross income, as defined in section 61(a) of the Internal Revenue Code of 1986 (26 U.S.C. 61(a)), exceeding three times the median household income for that preceding calendar year, as most recently reported by the Bureau of the Census.

(4) Neither the applicant nor the inventor nor a joint inventor has assigned, granted, or conveyed, nor is under an obligation by contract or law to assign, grant, or convey, a license or other ownership interest in the application concerned to an entity that, in the calendar year preceding the calendar year in which the applicable fee is being paid, had a gross income, as defined in section 61(a) of the Internal Revenue Code of 1986, exceeding three times the median

household income for that preceding calendar year, as most recently reported by the Bureau of the Census.

Comment: These provisions of elements (3) & (4) above have two problems. First, the median income figure for the prior calendar year is typically not known until March of each year. The PTO has vowed to have forms which will recite this number, but even as of March 1, 2013 this form is not available and the U.S. Median Income is not known. (Median income is an income which is midway in an ordering of all incomes within an area). Even where this number is "selected" for you by the Patent & Trademark Office, there may be scores of inventors and applicants who may argue this number, particularly if they live in a high median income state, for example (and will be vociferously argued if they are "caught" wrongfully claiming Micro Entity status.
Currently, this figure may be about $50,000 meaning that the threshold for claiming Micro Entity may lie somewhere within $5000 of about $150,000. No one knows as of this date what this number will be for calendar year 2012. This $150,000 figure will be used in illustrations following.

Second and more important, rather than selecting Adjusted Gross Income (AGI), Congress has selected gross income, and gross income under IRC § 61 to boot!! IRC § 61 has traditionally been used to define broadly every dollar headed toward the taxpayer as being "income". It lies at the first step of the beginning of determining both civil and criminal tax liability.

Net Income (or Adjusted Net Income) is defined on the IRS web site as is the excess of gross income for the tax year (including gross income from any unrelated trade or business) determined with certain modifications over the total deductions (including deductions directly connected with carrying on any unrelated trade or business) that would be allowed as certain deduction modifications.

What this means is that statistically the typical person for whom the IRC § 61 income figure may be known, is an employee. Consider the case of a sole proprietor who has a single business, takes in $500,000 in gross revenue and has $450,000 of allowable expenses to combine on a schedule C tax form to trigger a taxable income of $50,000. Is the revenue considered gross income so as to cause the inventor to far exceed the $150,000 threshold?

What if the inventor has two schedule C sole proprietor businesses, and one generates $200,000 of income over expenses and the other generates a $100,000 loss. Didn't the inventor have $200,000 of income? Will the inventor be able, in good faith to net out the income and loss from two schedule C businesses?

What about community property states? If an inventor and spouse live in a community property state, and both the inventor and spouse each earn $100,000, what is the correct figure to apply to the $150,000 Micro Entity threshold? Is it the community $200,000 joint income, or the inventor's community share of $100,000?

Form 1040 has lines 7-22 dedicated

to INCOME. Even if the schedule C businesses were allowed to have their differences summed & consider their contribution to form 1040 as a single income figure, it is clear that the term IRC § 61 means at least that the entries of lines 7-22 would sum to a figure which constitutes IRC § 61 income. This is *before* any of the "Adjusted Gross Income" deductions of lines 23-35.

Adjusted gross income deductions DO NOT operate against IRC § 61 income for purposes of Micro Entity status. 37 CFR 1.29 could have used the definition of "Adjusted Gross Income" from lines 37 & 38 of Form 1040, but it did not.

Further, the claiming of Micro Entity status wrongfully (perhaps recklessly) is considered FRAUD on the patent office. Even maintaining the Micro Entity status when you have lost it inadvertently is considered a breach of the rules and fraudulent. What should a patent practitioner who wants to claim Micro Entity status for his client do? The patent practitioner should use his considerable tax skills to investigate and make certain that the client is fully qualified for the lower fee status. This should involve the following (which includes the prior inventorship and financial thresholds).

1. Ask the inventor and assignee a series of all possible questions on prior inventorship and income. Although the CFR used the term applicant, (which is a little awkward as to a company which may be on its first application, but may own 10 purchased patents) the applicant's company should be fully interrogated to discover their past involvement in all patents, namely, utility, plant, & design.

2. Prepare an affidavit for the company representative, and for all inventors regarding all past patents on which they have been named inventor in which they aver under oath, and under penalty of perjury that they qualify for the (micro entity) status.

3. Patent counsel should search the PTO on the web to determine if any inventor has been named in four previous applications.

4. Counsel should obtain the prior year's tax returns of all inventors, applicants and assignees to determine that the income listed on lines 7-21 and summed on line 22 does not exceed the $150,000 threshold limit. The corporate tax returns of any companies should be inspected to insure that gross income is below the $150,000 threshold limit as well.

5. Statements and affidavits should be executed stating that the current years income has not increased over the years for which the prior tax returns are based.

6. All statements signed should warn that if Micro Entity status is sought and attained wrongfully that the patent could suffer the ultimate fate of being held invalid.

7. If there is even a colorable, low probability chance that any inventor or applicant may not be eligible for Micro Entity status, patent practitioners and inventor-applicants should simply opt for

"small Entity status if they are entitled.

(5) What about foreign inventors? There are rules for establishing a foreign currency amounts of the threshold as an average currency exchange rate reported by the Internal Revenue Service, during the calendar year in issue to determine whether the applicant's, inventor's, joint inventor's, or entity's gross income exceeds the threshold specified in § 1.29(a)(3) or (a)(4). Following IRS tradition, especially since IRC § 61 is used as a threshold amount, determining a foreign inventor or applicant's income from their tax returns may be a challenge that most tax adept patent practitioners would likely not take. More money would be spent in investigation of foreign (and some domestic) persons than would be saved by the reduced fees.

General Conclusion

In future patent litigation, the availment of Micro Entity status may be one of the first obvious attack paths. I would expect to see discovery of both prior invention status and income for every year in which the Micro Entity status was maintained.

Is the Micro Entity category some intended trap for penurious small inventors? Or is it simply a de minimis diversion to draw attention away from a quite substantial patent fee increase?

The Micro Entity status is not only onerous, troublesome, and risky for practitioners, it represents an easy target for future infringers to attack and defeat patent holders. This form of noblesse as a "fee break" for inventors is much more likely to turn out to be a "patent breaker".

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