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## THE INVENTION TAX: PTO AND THE DIVERSION OF PATENT FEES

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Should the federal government tax innovation? Although the pro-technology rhetoric of most politicians would imply that such an idea would never fly, such a tax does exist in the form of fees that have been paid by inventors to the U.S. Patent and Trademark Office (PTO) and then diverted to other programs. This “invention tax” could amount to several hundred million dollars this year, for a total of some \$1 billion since 1992. Moreover, if a proposal by the PTO is enacted, total fees paid by patent and trademark applicants could rise even higher. Before this is allowed to happen, policy-makers should ensure that all user fees are used to process patents and trademarks rather than siphoned off for other purposes.

This tax is being challenged on a number of fronts. On November 14, 2002, the U.S. Court of Federal Claims heard arguments in a class-action suit claiming that the diversion of PTO funds is unconstitutional. While the suit is considered a long shot, the Bush Administration is also reviewing the practice as part of its review of PTO's FY 2004 budget request, and Office of Management and Budget (OMB) Director Mitchell Daniels is expected to make a decision on the matter by early December. Congress must act then on the Administration's proposal. While the funds at issue may seem small—amounting to less than the rounding error for the total federal budget—this tax represents a significant cost to many inventors. The decision made on this issue will also have symbolic

import as a measure of policymakers' commitment to removing barriers to innovation and technology.

**A Questionable Transfer of Funds.** The Patent and Trademark Office, one of the U.S. government's oldest agencies, celebrated its 200th anniversary last month. The agency's job, protecting innovation by issuing hundreds of thousands of patents and trademarks annually, has grown increasingly critical—and difficult—as technological advances have expanded the role of intellectual property in the economy. Unlike most other federal agencies, the PTO receives no money from general taxation, being funded entirely through fees paid by patent and trademark applicants. These fees can be substantial. Over the lifetime of a typical patent, they total about \$8,000. Although fees paid by small entities and individuals are lower, they are still significant, averaging approximately \$4,000.

For each of the past 12 years, PTO fees have outstripped the agency's spending, with the surplus going to the U.S. Treasury for other programs. Ini-

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tially, the transferred amounts were relatively small; in FY 1992, for example, \$8 million was diverted. However, the annual diversions have steadily increased; in recent years, diversions frequently totaled more than \$100 million. For FY 2003, the Bush Administration proposed a total diversion of \$162 million—approximately 10 percent of the \$1.5 billion that the PTO is projected to collect in fees. The Senate Appropriations Committee proposed an even larger diversion of \$341 million, while the House will not act on the matter until it reconvenes next year.

Overall, it is possible that by 2003, more than \$1 billion in revenue will have been diverted to other programs since 1992. In other words, \$1 billion in fees paid by America's inventors will have been sluiced off to pay for other federal activities, ranging from farm subsidies to military bands.

**A Clogged Approval Process.** Adding insult to inventors' injuries, the PTO's approval process is bogging down. The number of new patent applications received each year is skyrocketing and has increased by nearly 70 percent since 1996. Unable to keep pace with this demand, the agency now has a backlog of approximately 420,000 patent applications, and inventors are waiting ever longer to have their patents approved. Before 1995, it took about 18 months to get a patent; it now takes over two years. Without reform, the delay will soon top three years. Similar problems plague the trademark process.

The PTO and most applicants agree that the process is simply too slow for today's fast-moving technology landscape. This summer, under PTO Director James Rogan, the agency released a "21st Century Strategic Plan" that contains a comprehensive set of reforms, including expanded electronic processing of applications to reduce paperwork, outsourcing functions to the private sector, and working more closely with non-U.S. patent offices.

**A Proposal to Increase Fees.** While ambitious, the reforms proposed in the agency's strategic plan are largely sensible. However, the PTO also proposed a significant increase in total fees, arguing that greater resources are needed to handle its workload. According to this plan, total fees would rise by about 20 percent, with costs for patents rising by about a third.

It is not clear that higher fees are necessary. Although any agency's claim that it needs more money should be met with healthy skepticism, additional resources may be necessary to ease the patent and trademark bottleneck. However, it clearly does *not* make sense for the PTO to increase user fees while funds are being diverted to the general treasury. Applicants should not be asked to pay more unless and until all the payments received are applied to the job at hand: processing and granting patent and trademark applications.

**Conclusion.** The class-action suit argued at the Court of Federal Claims earlier this month (*Figueroa v. United States*) challenges the diversion of PTO fees on constitutional grounds, maintaining that the Constitution gives the federal government the power only to promote intellectual property, not to tax it. It is unlikely, though, that the courts will limit the government's taxing power in this way. That means the issue will have to be settled through the political process.

The first step of that process lies with the Bush Administration, as OMB Director Daniels and his staff craft the President's FY 2004 budget request. Their decision on this issue presents an opportunity for the Bush Administration to show its commitment to remove government barriers to innovation and technological progress. The question is, will it seize that opportunity?

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