

May/June 2018

Volume 10 • Number 5

# LANDSLIDE®

**ABA** A Publication of the ABA Section of Intellectual Property Law

# brave new law

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- Appellate Standing at the Federal Circuit
- Early Adjudication of Potentially Dispositive Issues at the USITC
- Economic Assessment of Duplication in PTAB Proceedings



# LANDSLIDE®

ADVANCING INTELLECTUAL PROPERTY LAW®

Volume 10 • Number 5 • May/June 2018

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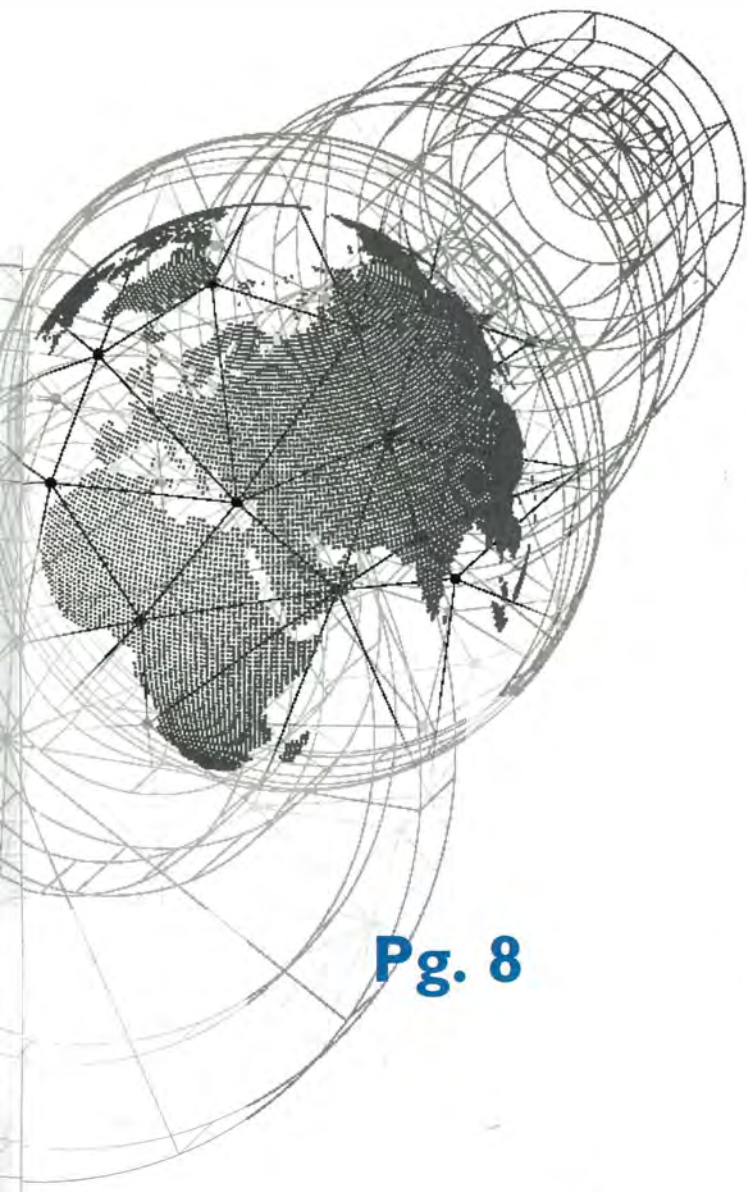
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# THE PTAB IS NOT AN ARTICLE III COURT, PART 2

## ***AQUA PRODUCTS v. MATAL* AS A CASE STUDY IN ADMINISTRATIVE LAW**

BY DAVID BOUNDY AND ANDREW B. FREISTEIN

**A***qua Products, Inc. v. Matal*<sup>1</sup> illustrates a principle raised in two recent articles in *Landslide*<sup>®2</sup>—not every patent case is a *patent law* case. Aqua’s briefs presented the case as statutory interpretation of the Patent Act. The Federal Circuit en banc ruled against Aqua’s position. However, the court threw Aqua a remarkable lifeline: despite near-complete silence in Aqua’s briefs on administrative law principles, seven judges in three opinions sua sponte decided the case on those grounds. Only because of that lifeline did the court decide in Aqua’s favor—the U.S. Patent and Trademark Office’s (USPTO’s) attempt to give rulemaking authority to the Patent Trial and Appeal Board (PTAB) and the PTAB’s attempt to make law by mechanisms outside the Administrative Procedure Act (APA) were invalid.

*Aqua Products* concerned the authority of the PTAB, in deciding a motion to amend claims during an inter partes review (IPR), to place on the patent owner the initial burden to explain patentability of proposed amended claims over prior art. This rule had not been promulgated through notice and comment, as required by the APA. Instead, the PTAB acted by nonprecedential decision, in *Idle Free Systems, Inc. v. Bergstrom, Inc.*<sup>3</sup> At the Federal Circuit, one majority found that the *Idle Free* burden-allocation rule was not foreclosed by the patent law, and thus satisfied “step one” of the *Chevron* test for judicial deference. However, a different majority, in three opinions, found that the PTAB did not comply with its *procedural obligations for rulemaking*, and thus the *Idle Free* rule was invalid.

*Aqua Products* is an example of a case that is really tough on patent law grounds but a clear winner on administrative law grounds. This article looks at issues presented in *Aqua Products* and explains various administrative law principles pertinent to PTAB proceedings, along with opportunities for parties to present the law to the PTAB and to courts to guide better decision-making. The article also suggests several reforms that might be adopted by the PTAB to promote procedural regularity.

### **The IPR/PGR Regulations, *Idle Free*, *MasterImage*, and Allocation of Burden**

A century of ex parte patent prosecution establishes that the act of “amending claims” and “establishing patentability” are distinct steps, with different burdens. An applicant may amend claims relatively freely (limited by “final rejection” practice under 37 C.F.R. § 1.116). Applicants have the burden of explaining 35 U.S.C. § 112(a) support for claim amendments; many voluntarily provide explanations with their amendments. However, the patent examiner has the initial burden of production (for both evidence and explanation) to address patentability over the art, and the ultimate burden of persuasion. This allocation makes intuitive sense—allocating the procedural initial burden to the party who must make the affirmative substantive showing avoids requiring a party to prove a negative. An amendment that is “entered” only puts claims in play—the claims do not issue without the examiner’s approval.

Conduct of IPRs is governed by 35 U.S.C. § 316. Subsection (e) provides that “the petitioner shall have the burden of proving a proposition of unpatentability by a preponderance of the evidence.” Subsection (d) provides a right for the patent owner to file a motion to amend claims, with several enumerated conditions analogous to those of applicants in *ex parte* prosecution, but does not demand any specific supporting showings and is silent on burden of proof for the conditions. Subsection (a) (9) delegates broad rulemaking authority to the USPTO: “The Director shall prescribe regulations . . . setting forth standards and procedures for allowing the patent owner to move to amend the patent . . .” Overall, § 316 tracks the *ex parte* allocation of burdens for amendments—not locking down all possible ambiguity, but enough that any other reading comes as a surprise.

When the USPTO promulgated its IPR and PGR (post-grant review) implementing regulations in August 2012, the regulations tracked traditional *ex parte* prosecution principles. Entry of an “amended claim” and “determination of patentability” are distinct legal concepts.<sup>4</sup> The IPR regulations set three elements for a motion to amend:

1. The amendment must “respond to a ground of unpatentability involved in the trial” (37 C.F.R. § 42.121(a)(2)(i))—the regulation does not require that the “response” be explained.
2. The amendment may not “seek to enlarge the scope of the claims . . . or introduce new subject matter” (37 C.F.R. § 42.121(a)(2)(ii)). Likewise, the regulation only specifies content of claims, without calling for an explanation.
3. The amended claims must have § 112(a) support (37 C.F.R. § 42.121(b))—this is the only element for which the regulation calls for compliance by the amended claims *and* for the patent owner to explain.<sup>5</sup>

For any motion, 37 C.F.R. § 42.20 provides that “the moving party has the burden of proof” but does not specify *what elements* have to be proved. Nothing in the notice of proposed rulemaking (NPRM) (or final rule notice, for that matter) suggests that § 42.20, as applied to motions to amend, somehow adds another element or explanation not explicitly set forth in § 42.121 in order for the amendment to be entered. The NPRM itself does not mention “patentably distinct features”—the public had no notice that the issue was even in play, let alone an opportunity to comment on it.

Among the materials the USPTO published with the NPRM, the closest antecedent to the *Idle Free* rule is in the “Practice Guide for Proposed Trial Rules,” that the patent owner “should clearly state the patentably distinct features for proposed substitute claims.”<sup>6</sup> At rule proposal, the USPTO never suggested a patentability showing over the art was required; rather, the proposed Trial Practice Guide only

recommends this statement as a means to comply with elements that are expressly stated in the proposed regulation, to “aid the Board in determining whether the amendment narrows the claims and if the amendment is responsive to the grounds of unpatentability involved in the trial.”

In the final rule notice, in August 2012, the preamble discussion of § 42.121 reiterated that the above list—three elements, one explanation—is exhaustive,<sup>7</sup> and contrasted these elements for amendment against the burden of proof on final patentability.<sup>8</sup> The final rule notice further stated that “[t]he motion [to amend claims] will be entered so long as it complies with the timing and procedural requirements.”<sup>9</sup> In the final Trial Practice Guide, the USPTO proposed an example motion to amend—the example tracks the “three elements, one explanation,” with no mention of patentability over the art.<sup>10</sup> The “clearly state patentably distinct features” statement is carried over from the proposed Trial Practice Guide into the final Guide as a “should” recommendation, not a “must.”

There is one mislaid sentence in the final rule notice. In a comment on “policy” in the “umbrella rule” notice, tens of pages away from the discussion of either the IPR or PGR specific “motion to amend” rules, the sentence reads:

In the event that a patent owner files a motion to amend the claims, the patent owner must include a statement of the precise relief requested and a full statement of the reasons for the relief requested, including a detailed explanation of the significance of the amended claims (*e.g.*, a statement that clearly points out the patentably distinct features for the proposed new or amended claims).<sup>11</sup>

Note that this sentence—which is only in the comments, not the regulations—does not require a *showing*, only an identification of a “feature.” The regulation does not expressly or even implicitly support any burden on the patent owner.

The PTAB’s first decision on a motion to amend came nine months into the IPR regime. *Idle Free*<sup>12</sup> explains that § 42.121(a)(2)(i) and (ii) requires that substitute claims “respond to a ground of unpatentability involved in the trial” and not “seek to enlarge the scope of the claims.” *Idle Free* then notes that § 42.121(b) requires showing § 112(a) support for the amendment. Each of these requirements properly flows from the “three elements, one explanation” regulatory text itself.

Then, the PTAB announced a new element imposed on the patent owner:

For each proposed substitute claim, *we expect* a patent owner: (1) in all circumstances, to make a showing of patentable distinction over the prior art; (2) in certain circumstances, to make a showing of patentable distinction over all other proposed

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substitute claims for the same challenged claim; and (3) in certain circumstances, to make a showing of patentable distinction over a substitute claim for another challenged claim. . . . For a patent owner's motion to amend, 37 C.F.R. § 42.20(c) places the burden on the patent owner to show a patentable distinction of each proposed substitute claim over the prior art.<sup>13</sup>

*Idle Free* fails to explain several important factors:

- § 42.121, the most relevant regulation;
- The renunciation of the USPTO's earlier assurances that a "motion [to amend claims] will be entered so long as it complies with the timing and procedural requirements";
- The source of authority for the PTAB to add a new element above those stated in § 42.121, other than "we expect";
- The balancing of "competing interests" and "conflicting policies" that went into the statute or IPR/PGR regulations; and
- Any limiting principle—*Idle Free* demands a patent

## IDLE FREE IS AN "INFORMATIVE" OPINION AND SHOULD NOT BE CITED AS PRECEDENT.

owner show patentability "over the prior art," apparently including prior art not involved in the trial.

Also absent from *Idle Free* are other procedural concomitants of agency rulemaking—notice in the *Federal Register*; analyses required by the Regulatory Flexibility Act, Paperwork Reduction Act (PRA), or Executive Order 12,866<sup>14</sup>; etc.

Some months after its initial issue, *Idle Free* was reissued as an "informative" opinion. The PTAB's "Standard Operating Procedure 2"<sup>15</sup> requires that "informative" opinions not be cited as precedent.

In June 2015, the Federal Circuit in *Microsoft Corp. v. Proxyconn, Inc.*<sup>16</sup> approved the *Idle Free* rule as a valid exercise under the patent law. (The *Proxyconn* briefs did not argue administrative law challenges to *Idle Free*, and *Proxyconn* did not decide them.)

The PTAB extended *Idle Free* in July 2015 in *MasterImage 3D, Inc. v. RealD Inc.*<sup>17</sup> *MasterImage* requires the patent

owner to "set forth a *prima facie* case of patentability."<sup>18</sup>

- The term "*prima facie* case of patentability" over the prior art (requiring the patent owner to prove a negative) is apparently novel to patent law.
- *MasterImage* cites no authority for its allocation of a burden of proof on an element not mentioned in the regulation.
- *MasterImage* does not explain any exception to the petitioner's burden to prove any "proposition of unpatentability," § 316(e).

*MasterImage* was originally issued as a "routine" opinion and redesignated "precedential" about a year later.

In 2015 and 2016, the USPTO amended the regulations for IPRs, PGRs, and CBMs.<sup>19</sup> With respect to motions to amend, the only change to the regulation was to increase the page limits.<sup>20</sup> The amendments offer no textual support for the *Idle Free* rule.

### Aqua Products—The PTAB's and Federal Circuit's Decisions

In an IPR, patent owner Aqua Products moved to substitute claims. The PTAB denied the motion, even after expressly finding that Aqua had complied with the elements of § 42.121. "[W]e [the PTAB] are not persuaded that Patent Owner has demonstrated the patentability of the proposed substitute claims over" the prior art, citing *Idle Free* as its only authority for denial.<sup>21</sup> Aqua's proposed amended claims were not substantively considered.

Before the Federal Circuit, Aqua argued only issues arising under the Patent Act: that the plain language of § 316(e) keeps the burden to prove unpatentability on the IPR petitioner, and the PTAB should be required to assess patentability of the amended claims on the entire record, including all arguments. The Federal Circuit panel rejected each of these arguments, based on its *Proxycorr* precedent.<sup>22</sup>

On rehearing en banc, the Federal Circuit issued five separate opinions, none commanding a majority<sup>23</sup>: a lead plurality opinion by Judge O'Malley (five judges), a concurrence by Judge Moore (for three of the O'Malley five), a concurrence in part by Judge Reyna (for two judges, joined in part by the Taranto four), and dissents by Judges Taranto (for four, joined in part by the Reyna two) and Hughes (additional views of two of the Taranto four). Some issues were unanimous:

- The PTAB, in final written decisions, must put the burden of proof on the petitioner to show *unpatentability*.
- The court unanimously rejected the USPTO's view that the statute unambiguously puts the burden of proof onto the patent owner to prove patentability in a motion to amend.

On *Chevron* step one, by a 6–5 vote the court ruled *against* patent owner Aqua on the patent law issues raised in the briefs. Six judges (opinions by Reyna, Taranto, and Hughes) interpreted § 316 as either ambiguous or delegating sufficient authority for the USPTO to promulgate the *Idle Free* rule. Only five judges (opinions by O'Malley and Moore) agreed with Aqua's patent law arguments that § 316 unambiguously placed the burden of proof onto the petitioner.

For *Chevron* step two, four of the opinions went on to answer *administrative law* questions (the USPTO's briefs had presented its half of the case on these issues, but Aqua's

briefs barely mentioned administrative law). The court asked itself, even if the Patent Act grants the USPTO *authority* to place the burden of proof on the patent owner to show patentability, did the PTAB properly *exercise* that authority within the administrative law? The opinions by O'Malley, Moore, and Reyna, for a total of seven judges, conclude that the USPTO had failed to observe requirements for rulemaking. The Reyna opinion, for the swing votes, criticizes the *Idle Free* rule for failing to comply with the APA: "The Patent Office cannot effect an end-run around [the APA] by conducting rulemaking through adjudication . . ." <sup>24</sup>

Though there is no majority reasoning, a majority of seven judges reached a common judgment that the PTAB failed to comply with administrative law requirements, and thus the *Idle Free* rule is no longer binding on the public. Judge Taranto's "dissent" expresses no disagreement with this viewpoint, but rather declined to address issues that Aqua had not briefed. Only the Hughes opinion (representing just two of 11 judges) concludes that the USPTO properly observed administrative law requirements.

### Administrative Law Simplifies Aqua Products

Some agency interpretations qualify for *Chevron* or *Auer* deference.<sup>25</sup> Supreme Court precedent sets out a two-step analysis for analyzing an agency's interpretation of ambiguity. Under step one, a court asks whether a statute or regulation is ambiguous. Under step two, a court evaluates whether an agency's interpretation of that ambiguity is "reasonable." If so, that interpretation is binding on the public, on courts, and on the agency itself, as if it had been promulgated as a regulation in the *Code of Federal Regulations*. "*Chevron* deference" applies to an agency's interpretation of an ambiguous statute, or a regulation that fills a gap in a statute (if the agency has a delegation of rulemaking authority). "*Auer* deference" applies to an agency's interpretations of ambiguities in its own regulations.<sup>26</sup> Under modern Supreme Court law, neither *Chevron* nor *Auer* delegate additional rulemaking authority to agencies—both require that the agency first act within rulemaking authority, using whatever procedure is otherwise required, and then, *only for validly promulgated rules*, courts defer at a level above the ordinary default.<sup>27</sup> Both *Chevron* and *Auer* are limited and have many preconditions for that deference—the well-known "two steps" are only the beginning of the analysis. Many of these preconditions would have been easy-winner arguments had they been raised in patent owner Aqua's brief.

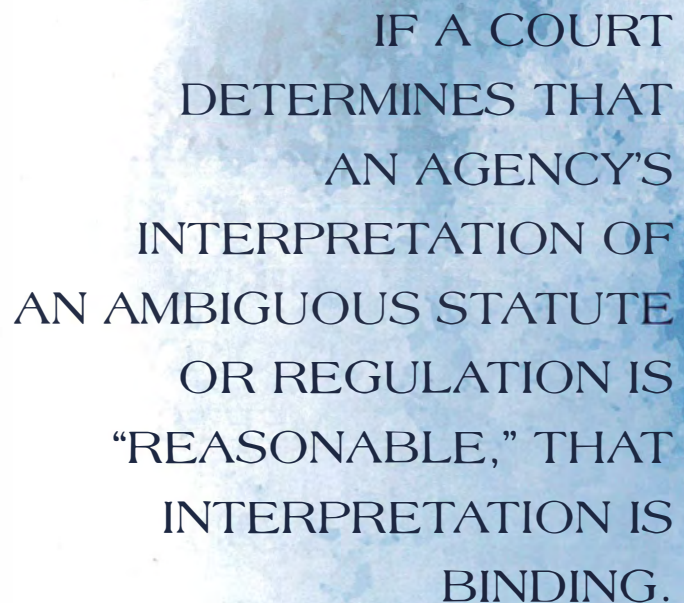
### *Chevron/Auer Interpretations Originate with the Director, Not the PTAB*

Some agencies have a unitary structure with rulemaking and adjudicatory authority consolidated in an agency head, usually a multimember board or commission. Other agencies have split rulemaking and adjudicatory functions. In these split-authority agencies, rulemaking is usually delegated to the agency head and adjudicatory functions are delegated to an intra-agency tribunal that is independent of the agency head. If various components of the split-authority agency disagree on interpretation, the agency component with rulemaking authority on the specific issue wins, and only that component is eligible for *Chevron* deference.<sup>28</sup>

The USPTO is a split-authority agency: § 316(a) delegates rulemaking authority to the Director, not the PTAB. The Director interpreted the IPR statutes to require only the "three elements, one explanation" set forth in § 42.121. Even if *Idle Free* could be characterized as "interpretation," the PTAB is not the rulemaking component of the USPTO, and its decisions are ineligible for *Chevron* deference.

### *The Controlling "Interpretation" of the Statute Is the One in the Regulations*

The entire case should have been governed by a single "interpretation" of § 316—the interpretation set forth in the USPTO's regulations. The relevant regulation, § 42.121, integrates and interprets the relevant statutes. It allocates the burden of proof on "three elements, one explanation" of a motion to amend to the patent owner. The final rule notice makes clear that this list is exhaustive: "The motion will be entered so long as it complies with the timing and procedural requirements."<sup>29</sup> The Trial Practice Guide gives an



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example of an adequate motion to amend—three elements, one explanation. The regulations and the USPTO's interpretive materials anchor all questions of statutory interpretation and *Chevron* deference.

The regulations were validly promulgated and meet all the other *Chevron* preconditions. Most importantly, they are *regulations* promulgated with statutory procedure, by the statutorily designated part of the agency. Under *Chevron*, § 42.121 is the interpretation of statute that binds parties before the PTAB, a *Chevron* analysis, and, most importantly for this case, *the PTAB and Solicitor*.

Rule 42.121 should have controlled all proceedings at the PTAB and Federal Circuit. The *Idle Free* and *MasterImage* PTAB panels had no authority to expand the required showings, especially not with a wave of the "we expect" hand. All *Chevron* issues in *Aqua Products* are resolvable for the simplest of reasons—§ 42.121 (including its silences) says so.



### ***“Reasonableness” of an Interpretation Requires Ex Ante Explanation, Not Ex Post Rationalization***

Under *Chevron* step two, the “reasonableness” of an interpretation is not evaluated ex post by a “reasonable” explanation in an agency’s litigation brief. *Chevron* itself notes the importance of an agency’s explanation, considering “competing interests” and “conflicting policies.” In the last three years, the Supreme Court has clarified that the “reasonableness” inquiry, just like any other review of any other agency action, rests on the ex ante explanation the agency gave when it adopted the interpretation.<sup>30</sup>

Judges O’Malley, Moore, and Reyna note the absence of explanation in the *Idle Free* decision and hold that that silence is “unreasonable.” This divests *Idle Free* of any deference. Judge Taranto notes the statute does “not negate” the PTAB’s *Idle Free* rule.<sup>31</sup> While “not negate” was used as a test for *Chevron* “reasonableness” in older statutory cases and is still current in *Auer* regulatory cases, “not negate” has not been a valid test for a *Chevron*-eligible interpretation for some years.<sup>32</sup> Failure to explain and failure to ground an

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interpretation in the statute itself are both failures of agency “reasonableness,” divesting the PTAB of deference.

### ***Rulemaking by Adjudication May Only Interpret—NLRB v. Bell Aerospace***

The PTAB is not an Article III court. Judges Reyna and Hughes allude to a sentence from the Supreme Court’s *NLRB v. Bell Aerospace Co.*: “the [NLRB] is not precluded from announcing new principles in an adjudicative proceeding and . . . the choice between rulemaking and adjudication lies in the first instance within the [PTAB’s] discretion.”<sup>33</sup> This single sentence, out of context, omits several important qualifications on agency rulemaking by adjudication.

Agencies have discretion to choose between rulemaking through rulemaking procedure or by adjudication *only if* the rule meets all statutory requirements:

- The agency component that adjudicates acts within its

rulemaking authority. The PTAB has no rulemaking authority.

- No statute requires otherwise—that is, only for rules that fit the “interpretative,” “statement of policy,” or “procedural” exemptions of § 553(b)(A) and (d). The *Idle Free* rule is ineligible for any § 553 exemption.<sup>34</sup>
- If an agency relies on the “interpretative” exemption to § 553 notice and comment, the agency may create a rule by adjudication only as an interpretation of an ambiguity. Gap-filling in a *regulation* is ineligible for *Auer* deference, as discussed below.
- The rule does not implicate the PRA. The *Idle Free* rule is a “rule of general applicability” calling for information to be filed with the agency, and thus comes within the coverage of the PRA.<sup>35</sup> Without full PRA procedures, the *Idle Free* rule is unenforceable, as discussed below.
- The agency accepts the risk of losing *Chevron* or *Auer* deference, and is willing to stand on *Skidmore* deference for a nonlegislative rule.

*Bell Aerospace* concerned an “interpretative” rule (resolving ambiguity in the word “management”) that met all other statutory concerns. *Bell Aerospace* does *not* stand for the proposition that an agency may exempt itself from statutorily required rulemaking procedures simply by acting through common law adjudication.

Agencies may not grant themselves extra-statutory rulemaking authority.<sup>36</sup> Judge Moore expresses her skepticism of the PTAB’s Standard Operating Procedure 2 (SOP2),<sup>37</sup> while the Reyna, Taranto, and Hughes opinions seem to assume it is a valid statement of agency authority. However, SOP2 is not a statute. The USPTO’s rulemaking authority exists only as delegated by statute. The PTAB cannot grant itself rulemaking authority simply by claiming to have it, cannot create a self-waiver from statutory rulemaking procedure simply by diverting attention elsewhere, and cannot create an alternative rulemaking procedure—substituting a poll of administrative patent judges (APJs) for public notice and comment—simply by calling it “standard” procedure.

Judge Hughes’s concern for an agency’s ability to “interpret” without further full-procedure “regulation”<sup>38</sup> is readily resolved—agencies may “interpret” with minimal procedure, 5 U.S.C. § 553(b)(A), but “interpretation” requires underlying text in a statute or regulation. Adding a fourth element to a three-element regulation, *à la Idle Free*, is not “interpretation.”

### ***Agencies Do Not Have Common Law Incremental Authority***

Judge Hughes, in section II of his dissent,<sup>39</sup> observes the step-by-step progress from formally adopted regulation to *Federal Register* notice to *Idle Free* to *MasterImage*, and seems to accept that the PTAB has the power to engage in step-by-step adjudication in the manner of a common law court.

Incremental rulemaking by informal procedures is an Article III power, not an agency power. The D.C. Circuit has observed the pattern of “creeping guidance,” law being made without notice and comment or other public participation, without publication in the *Federal Register* or *Code of Federal Regulations*:

The phenomenon we see in this case is familiar. . . . The agency [promulgates] regulations containing broad language,



open-ended phrases, ambiguous standards and the like. Then as years pass, the agency issues circulars or guidance or memoranda, explaining, interpreting, defining and often expanding the commands in the regulations. One guidance document may yield another and then another and so on. Several words in a regulation may spawn hundreds of pages of text as the agency offers more and more detail regarding what its regulations demand of regulated entities. Law is made, without notice and comment, without public participation, and without publication in the Federal Register or the Code of Federal Regulations.<sup>40</sup>

The D.C. Circuit suggested (without holding) that creeping interpretation might be permissible in nonbinding advisory guidance but was impermissible if the agency gave it binding weight. The Supreme Court amplified this caution: an agency cannot, “under the guise of interpreting a regulation, . . . create *de facto* a new regulation.”<sup>41</sup>

### ***There Is No Auer Deference for Gap-Filling***

The USPTO’s brief argues in the alternative, that *Idle Free* should have received *Auer* deference as an interpretation of the regulations, and Aqua’s reply brief does not respond.

Gap-filling is one of the big differences between *Auer* and *Chevron*—under *Chevron*, an agency may have deference for *either* interpretation of an ambiguity or (where there’s delegated rulemaking authority) a gap-filling of a silence. But *Auer* is different—an agency is entitled to *Auer* deference only for an *interpretation* of an *ambiguous* rule. There is no such thing as *Auer* gap-filling:

In *Auer*, we held that an agency’s interpretation of its own regulation is entitled to deference. But *Auer* deference is warranted *only* when the language of the regulation is *ambiguous*. The regulation in this case, however, is not ambiguous—it is plainly permissive. To defer to the agency’s position would be to permit the agency, under the guise of interpreting a regulation, to create *de facto* a new regulation. Because the regulation is not ambiguous on the issue of compelled compensatory time, *Auer* deference is unwarranted.<sup>42</sup>

The difference all flows from statute—§ 553(b)(A) authorizes agencies to “interpret” regulations with few procedural safeguards but not to adopt gap-filling regulations without statutorily required procedure. That statutory principle flows into *Auer*—*Auer* is only a rule of enhanced deference to interpretations that *first* meet requirements of § 553(b)(A), not an extra-statutory grant of rulemaking authority or waiver of statutory procedural requirements. Gap-filling authority exists only when it has been delegated by statute, and no agency has blanket authority to graft new elements into its regulations or guidance whenever it would like. A silence in a regulation is just that—a silence that leaves an underlying (usually permissive) default intact—not an invitation for gap-filling.

Rule 42.121 lists three elements, one explanation; § 42.20(c) says who must prove or explain them. No conflict, no ambiguity. Numerous statements in the USPTO’s rulemaking notices and Trial Practice Guide reinforce this

interpretation. If there is no ambiguity, the *Auer* analysis ends at step one, and *Auer* offers no protection for *Idle Free*.

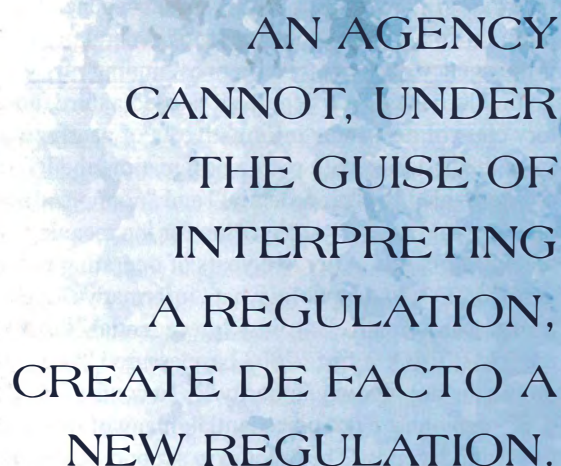
### ***Violations of the PRA***

Under the PRA, an agency may not promulgate a rule that demands paperwork from a party unless it has taken certain steps to analyze the effect of that rule and obtained clearance from the Office of Management and Budget (OMB).<sup>43</sup> In absence of that clearance, the USPTO may not impose any penalty on a party for failure to comply with an agency’s requirements.<sup>44</sup>

OMB’s website<sup>45</sup> shows that the USPTO obtained clearance for the three elements of § 42.121 in August 2012. OMB’s website shows nothing later reflecting any attempt by the USPTO to obtain clearance for the additional elements of *Idle Free*.

Without such clearance, the USPTO cannot penalize a party for failure to comply with the *Idle Free* rule.

### ***The Idle Free/MasterImage Rule Fails Requirements for Notice***



AN AGENCY  
CANNOT, UNDER  
THE GUISE OF  
INTERPRETING  
A REGULATION,  
CREATE DE FACTO A  
NEW REGULATION.

The PTAB, like any other agency, must give some level of prior notice before promulgating a rule of general applicability. An agency may not finalize a rule that is not a “logical outgrowth” of the rule as proposed without a further round of notice and comment.<sup>46</sup> Even in a final rule notice, an agency cannot use responses to comments to do anything more than interpret the actual text of regulations.<sup>47</sup> We know of no legal authority granting an agency power to do by adjudication what it cannot do by statutory rulemaking.

As noted earlier, the NPRM specifies three elements, one explanation for an amendment to claims. There is no suggestion of any burden to show a fourth, relating to substantive patentability. The final rule notice goes further, reassuring the public that the USPTO would not impose new requirements beyond § 42.121. The absence of comments establishes that the USPTO gave no notice that any possibility of such an interpretation was worth commenting on.



An agency may amend a rule, but it must use the same level of procedure that was used to promulgate the rule in the first instance.<sup>48</sup> Here, § 42.121 is a legislative rule, promulgated by notice and comment—if the PTAB wanted to add further requirements for a motion to amend, it had to go through the same procedures. Similarly, an agency is allowed to change its mind about a rule, but it must acknowledge that it is doing so and provide an explanation for its new position.<sup>49</sup> Here, the *Idle Free* opinion does not even acknowledge the absence of “patentability over the art” from § 42.121 or the several statements in the final rule notice, let alone acknowledge the change or explain reasons for a new interpretation.

### ***The PTAB’s Reliance on “Informative” Opinions Is Systemically Problematic***

There are two kinds of agency decisions recognized by the APA: “precedential” and “nonprecedential.” In particular, 5 U.S.C. § 552(a)(1)(C) and (a)(2)(A) tells us that an agency may not assert a nonprecedential decision against any party but itself, unless it has been published in the *Federal Register*, the person against whom it was asserted had “actual and timely notice,” or it has been electronically published and indexed.<sup>50</sup> Likewise, § 553(b)(A) grants agencies authority to promulgate hortatory “statements of general policy,” but only if the agency does not treat them as binding.

In 2006, the PTAB decided it needed a third, nonstatutory class of decision: “informative.” For nearly two years from the first case with such a designation, the PTAB’s SOP2 only provided for “precedential” and “nonprecedential” opinions and gave no explanation for the meaning of “informative” opinions. After two years of operating in the dark, the USPTO told the public what “informative” means, contrasting “informative” against “precedential.”<sup>51</sup> All versions of the PTAB’s SOP2 since 2008 have assured “[a]n informative opinion is not binding authority.”<sup>52</sup> To confirm that “informative” opinions are not precedential, many of them bear the following legend: “The opinion in support of the decision being entered today was *not* written for publication and is *not* binding precedent of the Board.”

Nonetheless, the PTAB regularly cites “informative” opinions as if they were precedential and binding. For example, *Idle Free* was the sole authority cited to deny Aqua’s motion to amend, one of 100 times the PTAB invoked *Idle Free* as binding authority before *MasterImage* was redesignated “precedential.”<sup>53</sup> Other “informative” opinions have been cited dozens of times, often as authority for overruling a square holding of the Federal Circuit.<sup>54</sup> The problem with the PTAB’s reliance on nonprecedential decisions has been flagged in several notice and comment letters, yet the practice continues.

The PTAB’s practice of citing “informative” decisions in anything other than an “interpretative” role, especially *as if they were* binding or precedential, is very difficult to square with the requirement of 5 U.S.C. § 552 to *not* cite nonprecedential cases against any party except the agency itself. Likewise, the PTAB’s own SOP2 says informative opinions are not precedential, and when the PTAB cites them as precedent, the violation of an agency’s own rules is essentially a per se basis to declare PTAB decisions “void” or “illegal and of no effect.”<sup>55</sup>

At the time of the *Aqua Products* final written decision, *Idle Free* was electronically published but not indexed. Thus, unless the PTAB specifically served copies on parties or could otherwise prove actual knowledge, *Idle Free* could not be cited in the way it was.<sup>56</sup> However, this theory was not raised in the *Aqua Products* briefing or addressed by the Federal Circuit.

### **Can the USPTO Repromulgate the *Idle Free* Rule through Regulation?**

On November 21, 2017, Chief APJ David Ruschke issued a memorandum, “Guidance on Motions to Amend in View of *Aqua Products*,”<sup>57</sup> announcing that the PTAB will no longer place the burden of persuasion on a patent owner with respect to the patentability of substitute claims presented in a motion to amend. The PTAB will determine whether the substitute claims are unpatentable based on the entirety of the record, including any opposition made by the petitioner. Beyond that, motion to amend practice will not change.

Further, Chief APJ Ruschke has indicated the PTAB’s willingness to consider changing the approach on motions to amend to become more of an iterative process.<sup>58</sup> He lamented that currently an IPR trial concludes with a final written decision on a motion to amend, without any opportunity for the parties to hash out an agreeable amendment; the final written decision grants or denies the motion with no guidance or suggestion from the PTAB to help put a motion in condition for grant. *Idle Free* justified this system by arguing that there are other ways to correct a patent, such as by ex parte reexamination or reissue.<sup>59</sup> The subsequent actual practice of the PTAB, enjoining parties from pursuing those alternative paths, has been one of the problematic double standards facing patent owners. Further, due to the one-year time restraints of the IPR, the PTAB was not willing to partake in ex parte examination.

New regulations to strike the proper balance between the one-year time constraints on IPRs and an all-or-nothing final written decision could benefit the patent owner, petitioner, and public. How can the USPTO issue (and follow) proper new regulations on motions to amend?

Rulemaking begins with roundtables, public requests for comment, and similar consultation with the public.<sup>60</sup> Rulemaking has to proceed under the aegis of the Director and the rulemaking apparatus in the Office of General Counsel. All claims for fairness and efficiency will have to be supported by evidence that meets the USPTO’s own Information Quality Guidelines. Procedural requirements arise under the APA, PRA, Regulatory Flexibility Act, and several executive orders.<sup>61</sup> Neglect of any requirement would expose the PTAB’s new rule to challenge. Once regulations issue, PTAB judges should be instructed that regulations bind both the agency and the public, and improvisation as exemplified in *Idle Free* and *MasterImage* is not consistent with the legal obligations of APJs.

### **Conclusion**

The USPTO should implement the OMB’s Good Guidance Bulletin<sup>62</sup> for all operations, including the PTAB. Extensive rewriting of SOP2 is required to reflect limits on the PTAB’s authority and to implement the Good Guidance Bulletin. Obsolete opinions on the PTAB’s “precedential” and



“interpretative” pages should be tagged appropriately. Opinions that have been over-designated at levels that exceed the PTAB’s “interpretative” authority or that opine on issues of substantive law beyond the authority of any component of the USPTO should be down-designated. The PTAB should honor its own rules for its own proceedings and cease citing “informative” opinions as if they were precedential. The PTAB should update its Trial Practice Guide.

For the bar, administrative law expertise is becoming increasingly important to successful representation of clients in intellectual property matters—the PTAB and Federal Circuit can only apply the law if briefs properly educate them, and attorneys who overlook administrative law issues risk losing easy cases. Expertise in administrative law and agency rulemaking can guide agency tribunals to favorable decisions and present compelling arguments to courts after unfavorable decisions. ■

## Endnotes

1. 872 F.3d 1290 (Fed. Cir. 2017).
2. David Boundy, *Administrative Law Observations on Cuozzo Speed Technologies v. Lee*, 9 LANDSLIDE, no. 3, Jan.–Feb. 2017 [hereinafter Boundy, *Observations on Cuozzo v. Lee*]; David E. Boundy, *The PTAB Is Not an Article III Court: A Primer on Federal Agency Rule Making*, 10 LANDSLIDE, no. 2, Nov.–Dec. 2017, at 9 [hereinafter Boundy, *Rule Making Primer*].
3. No. IPR2012-00027, Paper No. 26 (P.T.A.B. June 11, 2013), [https://www.uspto.gov/sites/default/files/ip/boards/bpai/decisions/inform/ipr2012-00027\\_idle\\_free\\_system\\_v\\_bergstrom\\_paper\\_26.pdf](https://www.uspto.gov/sites/default/files/ip/boards/bpai/decisions/inform/ipr2012-00027_idle_free_system_v_bergstrom_paper_26.pdf).
4. 37 C.F.R. § 42.80.
5. Changes to Implement Inter Partes Review Proceedings, Post-Grant Review Proceedings, and Transitional Program for Covered Business Method Patents, 77 Fed. Reg. 48,680 (Aug. 14, 2012) [hereinafter IPR/PGR Final Rule].
6. 77 Fed. Reg. 6868, 6875 (Feb. 9, 2012).
7. IPR/PGR Final Rule, *supra* note 5, at 48,690 (citing 35 U.S.C. §§ 316(d), 326(d)).
8. *Id.* at 48,697 (citing 35 U.S.C. §§ 316(e), 326(e)).
9. *Id.* at 48,690; *see also id.* at 48,706 (“Failure to comply with [any] requirement in the regulation may result in denial of the proposed amendment(s).”).
10. Office Patent Trial Practice Guide, 77 Fed. Reg. 48,756, 48,767 (Aug. 14, 2012).
11. Rules of Practice for Trials before the Patent Trial and Appeal Board and Judicial Review of Patent Trial and Appeal Board Decisions, 77 Fed. Reg. 48,612, 48,626 (Aug. 14, 2012).
12. *Idle Free Sys., Inc. v. Bergstrom, Inc.*, No. IPR2012-00027, Paper No. 26 (P.T.A.B. June 11, 2013), [https://www.uspto.gov/sites/default/files/ip/boards/bpai/decisions/inform/ipr2012-00027\\_idle\\_free\\_system\\_v\\_bergstrom\\_paper\\_26.pdf](https://www.uspto.gov/sites/default/files/ip/boards/bpai/decisions/inform/ipr2012-00027_idle_free_system_v_bergstrom_paper_26.pdf).
13. *Id.* at 6–7 (emphasis added).
14. An overview of these laws is given in Boundy, *Rule Making Primer*, *supra* note 2, at 10–13.
15. PATENT TRIAL & APPEAL BD., STANDARD OPERATING PROCEDURE 2 (REVISION 9) § IV (2014) [hereinafter SOP2 (REV. 9)], <https://www.uspto.gov/sites/default/files/documents/sop2-revision-9-dated-9-22-2014.pdf>.
16. 789 F.3d 1292 (Fed. Cir. 2015).
17. No. IPR2015-00040, Paper No. 42 (P.T.A.B. July 15, 2015), <https://www.uspto.gov/sites/default/files/documents/ipr2015-00040%20paper%2047%2020150715.pdf>.
18. *Id.* at 4.
19. “CBM” is the transitional program for “covered business method” patents. CBMs generally correspond to PGRs.
20. Amendments to the Rules of Practice for Trials before the Patent Trial and Appeal Board, 80 Fed. Reg. 50,720 (proposed Aug. 20, 2015); Amendments to the Rules of Practice for Trials before the Patent Trial and Appeal Board; Correction, 81 Fed. Reg. 24,702 (Apr. 27, 2016).
21. *Zodiac Pool Sys., Inc. v. Aqua Prods., Inc.*, No. IPR2013-00159, Paper No. 71, at 47 (P.T.A.B. Aug. 22, 2014).
22. *In re Aqua Prods., Inc.*, 823 F.3d 1369 (Fed. Cir. 2016).
23. *Aqua Prods., Inc. v. Matal*, 872 F.3d 1290 (Fed. Cir. 2017).
24. *Id.* at 1339.
25. *See generally* Boundy, *Rule Making Primer*, *supra* note 2.
26. *Chevron U.S.A., Inc. v. Nat. Res. Def. Council, Inc.*, 468 U.S. 837 (1984); *Auer v. Robbins*, 519 U.S. 452 (1997).
27. *Gonzales v. Oregon*, 546 U.S. 243, 255–56 (2006).
28. *Martin v. Occupational Safety & Health Review Comm’n*, 499 U.S. 144 (1991). Thus, the PTAB properly has jurisdiction to determine its own jurisdiction, *Ex parte* Lemoine, 46 U.S.P.Q.2d 1432, 1434 (B.P.A.I. 1995), but not to opine on issues delegated to the Director, *Ex parte* Youngpeter, No. 2009-6636, 2010 WL 3534507, at \*5 (B.P.A.I. Sept. 9, 2010) (unpublished).
29. *See* IPR/PGR Final Rule, *supra* note 5, at 48,690.
30. *Encino Motorcars, LLC v. Navarro*, 136 S. Ct. 2117, 2125 (2016) (in evaluating an interpretation under *Chevron* step two, applying the *State Farm* factors to conclude that the agency had not explained its rule adequately to warrant *Chevron* deference); *Michigan v. EPA*, 135 S. Ct. 2699, 2710 (2015) (in analyzing a regulation under *Chevron* step two, noting the “foundational principle . . . that a court may uphold agency action only on the grounds that the agency invoked when it took the action,” citing *SEC v. Chenery Corp.*, 318 U.S. 80, 87 (1943)). *Motor Vehicle Manufacturer’s Ass’n v. State Farm Mutual Insurance Co.*, 463 U.S. 29, 43, 48, 52 (1983), and *Chenery* are the oft-cited cases elaborating an agency’s obligation to explain its actions and criteria for evaluating “arbitrary and capricious.”
31. Likewise, *Microsoft Corp. v. Proxyconn, Inc.*, 789 F.3d 1292, 1307 (Fed. Cir. 2015), approves that *Idle Free* is not “inconsistent” with the statute. That view had some currency in earlier precedent but was clearly erroneous in 2017.
32. *E.g.*, *Gen. Dynamics Land Sys., Inc. v. Cline*, 540 U.S. 581, 600 (2004) (reasoning that “deference to [an agency’s] statutory interpretation is called for only when the devices of judicial construction have been tried and found to yield no clear sense of congressional intent”).
33. 416 U.S. 267, 294 (1974).
34. *NLRB v. Wyman-Gordon*, 394 U.S. 759, 764, 765–66 (1969) (reasoning that the NLRB may not gap-fill without APA notice and comment); *cf. Bell Aerospace*, 416 U.S. 267 (finding that the NLRB may interpret).
35. While the PRA is nominally limited to “answers to identical questions posed to, or identical reporting or recordkeeping requirements imposed on, ten or more persons,” the relevant implementing regulation, 5 C.F.R. § 1320.3(c)(4)(i), clarifies that the scope of coverage embraces “any recordkeeping, reporting, or disclosure

*Continued on page 64*



requirement contained in a rule of general applicability.”

36. *United States v. Picciotto*, 875 F.2d 345, 347 (D.C. Cir. 1989) (determining that a regulation permitting the Park Service to impose “additional reasonable conditions and . . . limitations” is an invalid attempt by the agency to “grant itself a valid exemption to the APA for all future regulations”).

37. *Aqua Prods., Inc. v. Matal*, 872 F.3d 1290, 1331–32 (Fed. Cir. 2017) (Moore, J., concurring).

38. *Id.* at 1355 (Hughes, J., dissenting).

39. *Id.* at 1364–67.

40. *Appalachian Power Co. v. EPA*, 208 F.3d 1015, 1019–20 (D.C. Cir. 2000); *see also* *Paralyzed Veterans of Am. v. D.C. Arena L.P.*, 117 F.3d 579, 584 (D.C. Cir. 1997), *overruled on other grounds by* *Perez v. Mortgage Bankers Ass’n*, 135 S. Ct. 1199 (2015).

41. *Christensen v. Harris County*, 529 U.S. 576, 588 (2000).

42. *Id.* (emphasis added) (citations omitted).

43. 44 U.S.C. § 3507(a).

44. *Id.* § 3512.

45. *OMB Control Number History*, OFFICE OF MGMT. & BUDGET, <https://www.reginfo.gov/public/do/PRAOMBHistory?ombControlNumber=0651-0069> (last visited Apr. 17, 2018).

46. *Chocolate Mfrs. Ass’n of the U.S. v. Block*, 755 F.2d 1098, 1104 (4th Cir. 1985).

47. *Benedict v. Super Bakery, Inc.*, 665 F.3d 1263, 1267–68 (Fed. Cir. 2011) (“The PTO ‘comment’ is not stated in the rule as adopted; the Rule does not state [the PTO’s interpretation].”).

48. *Perez v. Mortgage Bankers Ass’n*, 135 S. Ct. 1199, 1206 (2015); *City of Idaho Falls v. FERC*, 629 F.3d 222, 227 (D.C. Cir. 2011).

49. *Michigan v. EPA*, 135 S. Ct. 2699 (2015).

50. West’s *U.S. Code Annotated* has no cases on the meaning of “indexed”—apparently no other agency has ever had the chutzpah to treat its nonprecedential opinions with similar precedential effect. However, it is a separate requirement than simple listing on the agency’s website and requires something more.

51. BD. OF PATENT APPEALS & INTERFERENCES, STANDARD OPERATING PROCEDURE 2 (REVISION 7) (2008), <https://web.archive.org/web/20080706035523/http://www.uspto.gov/web/offices/dcom/bpai/sop2.pdf>.

52. SOP2 (REV. 9), *supra* note 15, § IV(A).

53. *See, e.g.,* *Zodiac Pool Sys., Inc. v. Aqua Prods., Inc.*, No. IPR2013-00159, Paper No. 71, at 47 (P.T.A.B. Aug. 22, 2014); *HTC Corp. v. Advanced Audio Devices, LLC*, No. IPR2014-01154, Paper No. 40, at 40 (P.T.A.B. Dec. 29, 2015).

54. *In re Lowry*, 32 F.3d 1579, 1582–83 (Fed. Cir. 1994), states, “[t]he printed matter cases have no factual relevance where ‘the invention as defined by the claims requires that the information be processed not by the mind but by a machine, the computer,’” and any “printed matter” exception is confined to “arrangements of printed lines or characters, useful and intelligible only to the human mind.” The PTAB regularly cites “informative” opinions to overrule *Lowry* and apply an imaginary “nonfunctional descriptive matter” rule to computer-readable data.

55. Boundy, *Rule Making Primer*, *supra* note 2, at 54.

56. 5 U.S.C. § 552(a)(1)(C), (a)(2)(A).

57. Memorandum from David P. Ruschke, Chief Admin. Patent Judge, to Patent Trial & Appeal Board, Guidance on Motions to Amend in View of *Aqua Products* (Nov. 21, 2017), [https://www.uspto.gov/sites/default/files/documents/guidance\\_on\\_motions\\_to\\_amend\\_11\\_2017.pdf](https://www.uspto.gov/sites/default/files/documents/guidance_on_motions_to_amend_11_2017.pdf).

58. PTAB Trial Committee Meeting, AIPLA 2017 Annual Meeting (Oct. 19, 2017).

59. *Idle Free Sys., Inc. v. Bergstrom, Inc.*, No. IPR2012-00027, Paper No. 26, at 6 (P.T.A.B. June 11, 2013).

60. The requirement to “consult with members of the public” *in advance* of an NPRM is not literally in the text of the statute but arises out of the interdependencies between required steps. 44 U.S.C. § 3507(a)(1)(D)(ii)(V), (d)(1)(A); 5 C.F.R. §§ 1320.5(a)(3), .8(a)(4), .11(b). The *Rule Making Primer*, *supra* note 2, at 56 n.43, notes several letters explaining the USPTO’s persistent neglect of obligations under rulemaking laws.

61. The Regulatory Flexibility Act and PRA are briefly introduced at Boundy, *Rule Making Primer*, *supra* note 2, at 11–12.

62. OFFICE OF MGMT. & BUDGET, EXEC. OFFICE OF THE PRESIDENT, OMB BULL. NO. 07-02, FINAL BULLETIN FOR AGENCY GOOD GUIDANCE PRACTICES (2007), <https://obamawhitehouse.archives.gov/sites/default/files/omb/assets/omb/memoranda/fy2007/m07-07.pdf>.