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EXAMINING RECENT SUPREME COURT CASES IN THE PATENT ARENA

HEARING

BEFORE THE

SUBCOMMITTEE ON
COURTS, INTELLECTUAL PROPERTY,
AND THE INTERNET

OF THE

COMMITTEE ON THE JUDICIARY
HOUSE OF REPRESENTATIVES

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EXAMINING RECENT SUPREME COURT CASES IN THE PATENT ARENA

THURSDAY, FEBRUARY 12, 2015

HOUSE OF REPRESENTATIVES

SUBCOMMITTEE ON COURTS, INTELLECTUAL PROPERTY, AND THE INTERNET

COMMITTEE ON THE JUDICIARY

Washington, DC.

The Subcommittee met, pursuant to call, at 1:03 p.m., in room 2141, Rayburn Office Building, the Honorable Darrell E. Issa (Chairman of the Subcommittee) presiding.

Present: Representatives Issa, Goodlatte, Collins, Smith, Chabot, Forbes, Franks, Poe, Marino, Farenthold, Nadler, Conyers, Chu, Deutch, DelBene, Jeffries, Cicilline, and Johnson.

Staff present: (Majority) Vishal Amin, Senior Counsel; Eric Bagwell, Clerk; and (Minority) Jason Everett, Counsel.

Mr. ISSA. The Committee will come to order. Today's hearing is on examining recent Supreme Court cases in the patent arena. The Subcommittee's work on intellectual property reform and the likely passage in this Congress of an internet—I am sorry. I apologize. Of a patent——

Mr. NADLER. That was this morning.

Mr. ISSA. That was this morning. [Laughter.]

Of a patent reform legislation package as we did in the last Congress in the House brings us to the importance of updating our awareness of recent Supreme Court cases in the patent arena.

In 2011, the American Invents Act, or AIA, became the most substantial reform to U.S. patent law since the 1836 Patent Act. The AIA reestablished the U.S. patent system as a global standard. I was proud to be part of that effort, and I am proud today that we will continue our work to uphold the competitiveness of the American patent system.

While the AIA rewrote the underlying patent law and procedures at the WTO, several items were left out of that bill as is often the case in any long-awaited, and large, and comprehensive reform. These items, coupled with the growing threat posed by what all will admit at times is abusive patent litigation, require us to continue our work to improve the patent system by strengthening patent quality and promoting smarter and less expensive, if possible, patent litigation.

Last Congress, the Innovation Act passed this Committee by a vote of 33 to 5. And when it passed out of the House on a highly bipartisan basis, the vote was 325 to 95. I am confident that H.R. 9, the Innovation Act, will become law and will build on the work of the AIA to protect the American patent system.

Increasingly, Americans find innovation obstructed with attempts to enter the markets frequently shut down by well-funded patent trolls that often exploit loopholes in our patent system, bullying inventors and small business into frivolous lawsuits that amount to litigation extortion. Reforming the patent system, including costly patent litigation, is an economic issue, not a partisan one.

With billions of dollars and the state of American competitiveness at risk, reforms are not solely the responsibility of one branch of government. All three branches must work hard to craft and implement law that promotes our innovative economy. And we must recognize that the work is being done to address abusive patent litigation in all three branches of government. In addition to the court decisions, which we for the most part on a bipartisan basis welcome, we will examine today how they affect the judiciary, the PTO, and the PTO's recently announced new patent quality initiatives, including additional staff to focus purely on patent quality.

The PTO has issued updated guidance on patent eligibility in the wake of several related Supreme Court cases, and the PTO continues to operate three important post-grant proceedings, including AIA's Section 18 covered business method program, which I believe is absolutely essential to the future of patent quality and the effort to make sure litigation is appropriate, meaningful, and, in fact, done expeditiously, because ultimately a patent holder or a defendant who believes that they will be meritorious wants their day in court always at the fastest reasonable time.

As the House and Senate prepare to move forward on meaningful patent litigation reform to complement the PTO's work and the Court's decisions, opponents have recycled some of the same tired arguments used in the lead-up to the AIA. These opponents claim that the courts and the judiciary have completely solved the problem, and congressional attempts to end abusive litigation practices are wholly unnecessary.

Today's hearing will examine recent Supreme Court patent decisions, and we will learn about areas where progress has been made and areas where much more needs to be done. I am convinced that before we pack our bags and go home at the end of this session, we will, and I insist we will, have ensured the legislative branch of government does its part to stop litigation abuse from occurring in the first place. American innovation cannot afford to be held captive by frivolous litigation from weak or overly broad patents. We need to work together to ensure the American economy does not continue to suffer.

Before I turn the microphone over to the Ranking Member, I must add one small personal point. When I came to this Committee some 14 years ago, the greatest issue we seemed to have in front of us was the 40 percent reversal rate of court decisions leading to an effectively de novo response and high number of appeals to the Federal circuit. The lack of confidence that existed then was a

problem. I believe we have gone a long way in most districts to get it right earlier at the district court level.

There is more to be done, and our efforts on a bipartisan basis will be to do so, to make sure that we facilitate the judicial branch having the tools and the skills to decide properly. We cannot back up work that we should do to the courts. The courts at the district level cannot simply pass onto the Fed circuit, and the Fed circuit cannot simply end up at the Supreme Court. That is part of our requirement, to get decisions made at the lowest and earliest level that could be counted on by the inventors.

And with that, I recognize my colleague and Ranking Member, Mr. Nadler.

Mr. NADLER. Thank you, Mr. Chairman. I want to begin by congratulating you on your new position as Chairman of this Subcommittee, and I look forward to working with you on the many important issues we will consider in this Congress.

We got off to a good start by joining together as original co-sponsors of the Innovation Act, which Chairman Goodlatte introduced last week. The Innovation Act addresses a scourge of patent trolls which continue to burden businesses across the country with abusive patent litigation. Patent trolls stifle innovation, damage our economy, and injure legitimate businesses. Rather than inventing new products and technologies to benefit consumers and businesses, they merely invent new methods to drive up legal costs, which they use as a weapon to extort settlements from innocent defendants.

A smartphone can contain hundreds of patents on everything from touch screen technology, to cameras, to GPS mapping, and just as the saying goes, "There's an app for that." There's also a patent for that, and worse, we are finding that there is a patent troll for that, too. As a result, our successful American businesses are exposed to abusive litigation on the many patents it takes to build the tech products of today. Whether they spend the resources on developing new products or on fighting off frivolous claims depends in part on whether or not we are successful in passing legislation. Therefore, our work here is critical, not just to lawyers and inventors, but to all of us.

I have heard from countless businesses calling out for relief from patent trolls. They tell me that it can cost millions of dollars just to take one case through to trial. For small business, it can make more sense financially to settle even a totally bogus case early even if they would be assured of winning in the end. Unfortunately, this only encourages bad actors to keep filing case after case and gaining settlement after settlement.

While it is vital to ensure that legitimate patent holders are able to enforce their rights, we need to rein in those who seek to abuse the legal system. I supported the Innovation Act when it passed the House in December 2013 because I thought it struck a reasonable balance in addressing the patent troll problems without imposing too great a burden on plaintiffs. Since then, the Supreme Court has issued a number of patent-related opinions on issues ranging from fee shifting to patentability. Our hearing today will help us examine these decisions to determine how the patent landscape has

changed since the Innovation Act passed the House, and whether we need to make changes to account for these decisions.

Some critics of the bill argue that in light of these decisions, legislation is no longer needed at all. I think that overstates the case considerably, but I will be interested to hear from the witnesses today their thoughts on how the Court's decisions should inform congressional action. I am most concerned with the two fee-shifting cases, *Octane Fitness* and *Highmark*, which significantly lowered the standard which must be met before a court will award fees to the prevailing party under Section 285 of the Patent Act.

There is already evidence that courts in response to these decisions are awarding fees at a much higher rate, but we need to determine if this is a temporary phenomenon or evidence of a long-term trend. More to the point, have these cases curbed abusive litigation? Businesses have indicated to me that they continue to be threatened by patent trolls and that the problem shows no sign of abating.

I should note that I also have longstanding concerns about fee-shifting provisions, and the language contained in the bill is at the outer edge of what I can support. Keep in mind a person or a business can have a legally legitimate dispute regarding fact and law, and yet can still ultimately lose the case. They should not be punished for trying to protect their interests in court. Furthermore, we should not want to create a situation in which experienced corporate defendants with enormous resources and expert legal talent can bully injured plaintiffs into unfair settlements because of the risks, including especially the risk of being forced to bear not only their own legal costs, but the defendants' legal costs as well associated with losing a potentially successful case.

I would be interested to hear from the witnesses whether there are improvements that can be made to the fee-shifting provisions in the Innovation Act to deter patent trolls in light of the decisions by the Supreme Court. I will also want to hear how the Court's new standards on patentability, definiteness, standard of review for factual matters and claim construction, and induced infringement may impact future litigation.

With these important questions in mind, I look forward to the testimony of our witnesses, and yield back the balance of my time.

Mr. ISSA. I thank the gentleman. It is now my pleasure to recognize the author of the bill and the Chairman of the full Committee, the gentleman from Virginia, Mr. Goodlatte, for his opening statement.

Mr. GOODLATTE. Thank you, Mr. Chairman. I appreciate your holding this hearing. Addressing abusive patent litigation, particularly the reforms set out in the Innovation Act, are critical to our Nation's future economic competitiveness. Last week, I, along with a large bipartisan group of members, reintroduced the Innovation Act. This bill was the product of multiple discussion drafts and hearings, passing the House last Congress with more votes than the landmark America Invents Act of 2011.

But patent reform, just like many other issues, has its proponents and its critics. Those opposed to reform are bringing back the same refrains that were used during the lead up to the AIA saying that in the last year the courts and the judiciary have

solved the problem, and that the Innovation Act is unnecessary. We have heard this before, and though I believe that the Court has taken several positive steps in the right direction, their decisions cannot take the place of a clear, updated, and modernized statute.

In fact, many of the provisions in the Innovation Act do not necessarily lend themselves to being solved by case law, but by actual law, congressional legislation. Congress, the Federal courts, and the PTO must take the necessary steps to ensure that the patent system lives up to its constitutional underpinnings. And let me be clear about Congress' constitutional authority in this area. The Constitution grants Congress the power to create the Federal courts, and the Supreme Court has long recognized that the prescription of court procedure falls within the legislative function.

I welcome today's hearing to review the recent Supreme Court patent cases, and as we examine those cases, we must remember that our patent system is a unitary one. That means that the rules that we lay out in statute apply to all areas of technology and all types of businesses, large and small, and generally to all users of the patent system equally.

Thomas Jefferson could not have envisioned the innovations and inventions that were to unfold over the last two centuries and, in particular, over the last 20 years. But when he and our founding fathers crafted our patent system, they wrote these laws in a way so that they applied equally to all.

In that spirit, as we crafted the Innovation Act, we worked to ensure that its many provisions generally applied fairly and equally to all stakeholders. That means that we view patent trolling as an adjective that can apply to either party in a case if they engage in unreasonable or abusive tactics. That is also why good legislative practice should caution us against creating excessive carve-outs to cabin in provisions of the bill or other parts of patent law toward certain types of stakeholders. And we should make sure that the ideas that we put forth are well supported, and not just by those who happen to exempt themselves from its reach. We have a unitary patent system for a reason, and our system works best when the rules of the road apply to all.

The American patent system is designed to reward true invention and promote innovation. The USPTO must ensure that they take the task of ensuring strong patent quality seriously. On the patent quality front, I strongly believe that the PTO should not simply be in the business of granting patents and leaving the mess created for the courts and Congress to fix, but rather focus on strengthening the requirements for patent eligibility to reduce the overall number of weak or overly broad patents from entering the system. I am encouraged by the PTO's recent announcements in this space.

We must also remind ourselves that reforming our patent system is not a right or left issue. It is an economic issue, one that is bipartisan, one that will be bicameral, and one that will be signed into law. As we take these steps toward eliminating the abuses of our patent system, discouraging frivolous patent litigation, and keeping U.S. patent laws up to date, we will help fuel the engine of American innovation and creativity, creating new jobs and growing our economy.

Thank you, Mr. Chairman. I look forward to hearing from our witnesses today.

Mr. ISSA. I thank the gentleman. It is now my pleasure to introduce the Ranking Member of the full Committee, the gentleman from Michigan, Mr. Conyers.

Mr. CONYERS. Thank you, Mr. Chairman. I am glad you did not introduce me as the skeptical Member of the Committee, but there is some skepticism that still remains. But this hearing today provides an important opportunity to consider the impact of recent Supreme Court cases involving abusive patent litigation.

While allegations of abuse of patent litigation fed a clamor for drastic legislative reform, patent litigation rates in 2014 have dropped to levels last seen 5 or more years ago. So one of the first issues that I hope we assess is the impact of these Supreme Court decisions and whether they effectively have eliminated the need for one-size-fits-all fee-shifting legislation.

For example, the Court in *Octane Fitness* lowered the standard by which a court may award attorney fees under Section 285 of the Patent Act. And in *Highmark*, the Supreme Court increased the level of deference that an appellate court must give to a lower court's decision in awarding attorney's fees. As a result of these two cases, it is now much easier for prevailing parties to obtain attorney fees. In fact, courts have granted nearly half of all motions for attorney fees filed in patent cases since these two cases were rendered.

Given these developments, I believe it would be unwise for Congress to push additional fee-shifting legislation as the Federal courts assess the ramifications of these Supreme Court decisions. Legislative intervention at this time could create confusion and engender more rather than less litigation. So while I am not persuaded at this point in time that Congress must alter the current fee-shifting statute, I do encourage our witnesses to share their perspectives about how these two Supreme Court cases will affect patent litigation.

In addition to these two cases, there have been two other recent Supreme Court cases that may further decrease abuse litigation. The Supreme Court in *Alice* declared that abstract ideas could not be patented. And in Nautilus, the Supreme Court set a higher standard for certainty and specificity for patent claims. Because the two cases will make it easier to invalidate many vaguely worded software patents and business method patents, plaintiffs with such patents will have less incentive to file lawsuits. Most importantly, the Patent and Trademark Office will be less likely to grant such patents under the new standards.

So taken together, these decisions largely respond to concerns about how poor patent quality can lead to unnecessary patent litigation. And finally, it is my hope that this Committee will conduct further hearings that review the changing landscape affecting patents before we take any congressional action. In particular, we should examine what the Patent and Trademark Office, the Federal Trade Commission and the courts are doing to address abusive patent litigation.

We know, for instance, the Patent Office is working on enhancing patent quality, and still in the process of implementing the Amer-

ican Invents Act. The Federal Trade Commission is in the midst of conducting a study on abusive patent litigation behavior. In addition, several Federal district courts have adopted model discovery orders or discovery guidelines that limit discovery in patent lawsuits. Following the recommendations of the Judicial Conference, the Supreme Court will in the near future likely approve eliminating Rule 84 and its Form 18, which will lead to the higher pleading requirements of Twombly and Iqbal.

The Supreme Court is also expected to approve amendments to other rules of civil procedure that are aimed at achieving proportionality and discovery and early and active judicial case management. These revisions would apply to patent cases commenced on or after December 1, 2015. Cumulatively, these various efforts may address many of the concerns expressed during the debates last Congress on the need for the Innovation Act.

I have long said that I am prepared to respond to the problem of abusive patent litigation, but we must not do so in a vacuum, but in an environment cognizant of other ongoing developments, and we cannot do so in a way that inhibits or discourages the creative process that has been such a critical part of our Nation's economic success. Thank you, Mr. Chairman.

Mr. ISSA. Thank you, Mr. Conyers. It is now my pleasure to introduce the distinguished panel for today's hearing. For the witnesses, your written statements will be entered into the record in their entirety. And I would ask that you summarize any and all portions of that or independent remarks within roughly the 5 minutes. You will see the guideline lights in front of you. Please note yellow means get ready to stop, not continue well into red. If you do it, it will encourage those here on the dais to do the same thing when questioning occurs.

Before I introduce the witnesses formally, I would appreciate if all four of you would rise and take the Committee required oath, and please raise your right hands.

Do you solemnly swear or affirm that the testimony you are about to give will be the truth, the whole truth, and nothing but the truth?

[A chorus of ayes.]

Mr. ISSA. Thank you very much. Please be seated.

Our witnesses today include Mr. Herb Wamsley, executive director of the Intellectual Property Owners Association, better known as IPO; Mr. Krish Gupta, senior vice president and deputy general counsel at EMC Corporation, and I might note, an alumni of the Digital Corporation, one that I started my life in electronics involved with; Mr. Andrew Pincus, partner at Mayer Brown and former general counsel of the Commerce Department in the Clinton Administration; and Mr. Robert Taylor, counsel to the National Venture Capital Association. Again, as you begin speaking, your statements in their entirety will be placed in the record.

Mr. Wamsley?

TESTIMONY OF HERBERT C. WAMSLEY, EXECUTIVE DIRECTOR, INTELLECTUAL PROPERTY OWNERS ASSOCIATION, WASHINGTON, DC

Mr. WAMSLEY. Thank you, Mr. Chairman and Members of the Subcommittee. I appreciate the opportunity to be here today to speak on behalf of the Intellectual Property Owners Association, or IPO, a diverse association whose members include more than 200 companies and industries ranging from pharmaceuticals and biotechnology to electronics and information technology.

We strongly support eliminating abusive suits and litigation misconduct by all plaintiffs and defendants in patent litigation, large and small companies, independent inventors, universities, and others. We believe abuses can be eliminated without making it more difficult for patent owners to enforce valid patents. Now, the Supreme Court has decided seven cases since the House passed the Innovation Act in December 2013. I will comment briefly on six of those.

In *Octane Fitness*, which is the most significant of the cases as far as the Innovation Act is concerned, the Supreme Court lowered the standard for finding a case exceptional for purposes of awarding fees to a prevailing party. *Octane* also lowered the evidentiary burden for a party to establish entitlement to attorney's fees. In the companion case of attorney fee awards, *Highmark*, the Court raised the standard of review for appeals of attorney fee awards. The net effect of *Octane* and *Highmark* is to make it somewhat easier for a prevailing party to obtain attorney fees, but IPO still supports legislation on attorney fees.

The legislation should require an award of attorney fees to a prevailing party in every case unless the position and conduct of the non-prevailing party were objectively reasonable and substantially justified or exceptional circumstances make an award unjust. This presumptive fee shifting will be more effective than the *Octane* and *Highmark* decisions in deterring abusive litigation practices and will provide uniformity.

The *Octane* standard of awarding fees in cases that stand out from others lowers the bar, but *Octane* is likely to be subject to a wide range of district court interpretations. Legislation can require judges to shift fees when they otherwise may be less inclined to do so. Fee shifting may be the single most effective legislative measure for discouraging frivolous lawsuits and frivolous defenses.

In *Alice Corporation*, the Supreme Court revisited patent eligibility under Section 101 of the Patent Act. Unfortunately the test articulated by the Court in *Alice* is not clear. We believe it is too early to tell what long-term effect *Alice* will have on abusive behavior in patent litigation. Since the *Alice* decision, reports have suggested an increase in district court dismissals of suits on software-related and business method inventions.

Alice may strengthen the hand of defendants in frivolous suits. Defendants may be able to get suits dismissed for lack of patent eligibility at an early stage before costly discovery. However, unless clarified, *Alice* may have adverse effects on the incentive for innovation not only in software, but in other industries.

Three other cases have some effect on patent litigation. Nautilus adopted the new reasonable certainty standard for patent claims

that will make it easier for a defendant to challenge a vague patent as indefinite. This will deter some frivolous charge of infringement. Teva Pharmaceuticals held at the Federal circuit must apply a clear error standard to review factual findings in support of patent claim construction. The Teva framework better aligns with appellate review of patent claim construction, and Supreme Court precedent in the Federal Rules probably will have no effect on abusive suits. Limelight Networks will foreclose some patent suits based on an infringement inducement theory.

We advise the Subcommittee to continue to monitor the possible impact of the Supreme Court decisions as it considers the Innovation Act. As mentioned, we draw attention to the amendments to the Federal Rules of Civil Procedure. They are scheduled to take effect at the end of this year, which will heighten the pleading standards for patent infringement, and provide judges with some more discretion relating to discovery.

I will close by noting that the Patent and Trademark Office can help deter litigation abuses by ensuring that patents that are granted are of the highest possible quality and define the scope of rights. We support the USPTO's new patent quality initiative. I will be happy to answer any questions.

[The prepared statement of Mr. Wamsley follows:]

Statement of

HERBERT C. WAMSLEY

EXECUTIVE DIRECTOR

INTELLECTUAL PROPERTY OWNERS ASSOCIATION

Before the

HOUSE SUBCOMMITTEE ON COURTS, THE INTERNET, AND INTELLECTUAL PROPERTY

on

"EXAMINING RECENT SUPREME COURT CASES IN THE PATENT ARENA"

Thursday, February 12, 2015
1:00 p.m.

Intellectual Property Owners Association (IPO)

Mr. Chairman and Members of the Subcommittee:

My name is Herbert C. Wamsley. I appreciate the opportunity to be here today to speak on behalf of Intellectual Property Owners Association (IPO). I am the Executive Director of the association.

INTRODUCTION

IPO is a diverse association, representing members that include more than 200 companies in industries ranging from pharmaceuticals and biotechnology to electronics and information technology. We believe IP rights drive innovation, which creates economic prosperity. One of the principles adopted by our 50-member corporate board of directors is to promote improvements and eliminate abuses in the IP system. We want to eliminate abusive patent suits and litigation misconduct by all plaintiffs and defendants – large and small companies, independent inventors, universities, and others. At the same time, we do not want to make it more difficult for patent owners to enforce valid patents.

My comments are based on positions adopted by the IPO Board of Directors in *amicus* briefs filed in the U.S. Supreme Court and on legislation introduced in the last Congress. We are continuing to study the impact of recent developments and look forward to working with the subcommittee as litigation reform legislation moves forward.

HAVE SUPREME COURT PATENT DECISIONS ISSUED SINCE THE INNOVATION ACT PASSED THE HOUSE ALTERED THE NEED FOR PATENT LITIGATION REFORM LEGISLATION?

Since the U.S. House of Representatives passed the Innovation Act on December 5, 2013, the U.S. Supreme Court has rendered decisions that have altered the patent system. Cases have been decided involving the standard for determining attorney fee

awards and the standard of review for those determinations, patent eligibility, patent claim definiteness, the standard of review for district court claim construction, and induced infringement. I will discuss each of these cases and whether they might have affected the need for legislation.[1]

Octane Fitness, LLC v. Icon Health & Fitness, Inc.* and *Highmark, Inc. v. Allcare Health Management Systems, Inc.

35 U.S.C. § 285 provides that courts "in exceptional cases may award attorney fees to the prevailing party." The purpose of this and other fee shifting statutes is to prevent abuses of the legal system by deterring frivolous litigation. According to Federal Circuit precedents before *Octane*, the bringing or maintenance of a frivolous suit or frivolous arguments or misconduct during litigation was sufficient to form the basis of an exceptional case finding.[2] The position of the nonprevailing party, however, had to be objectively unreasonable and asserted in bad faith.[3]

At issue in *Octane* was the standard for determining when positions taken by nonprevailing parties in litigation should result in fee shifting under § 285.[4] In *Octane* the Supreme Court rejected the Federal Circuit two-part test, stating that "exceptional" means the case "stands out from others with respect to the substantive strength of a party's litigation position (considering both the governing law and the facts of the case) or the unreasonable manner in which the case was litigated."[5] *Octane* also lowered the evidentiary burden for parties to establish entitlement to attorney fees from a clear and

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[1] This testimony does not address *Medtronic Inc. v. Mirowski Family Ventures*, which involved the question of which party has the burden of proving infringement in declaratory judgment suits.
[2] *Beckman Instruments, Inc. v. LKB Produkter AB*, 892 F.2d 1547, 1551 (Fed. Cir. 1989) (citing *Standard Oil Co. v. American Cyanamid Co.*, 774 F.2d 448, 455 (Fed. Cir. 1985)).
[3] *See, e.g.*, *Brooks Furniture Mfg., Inc. v. Dutailier Int'l, Inc.*, 393 F.3d 1378, 1381 (Fed. Cir. 2005).
[4] *Octane Fitness, LLC v. Icon Health & Fitness, Inc.*, 572 U.S. ___, ___ (2014); 134 S. Ct. 1749, 1752-53.
[5] *Id.* at 1756.

convincing standard to a preponderance of the evidence standard.[6] The companion decision, *Highmark*, held that abuse of discretion, not *de novo* review, is the proper standard of review for all aspects of district court exceptional case determinations because the inquiry is "rooted in factual determinations."[7]

IPO supported the Supreme Court's holding in *Octane*.[8] Our *amicus* brief in the Supreme Court argued that whether a case is "exceptional" should turn only on the objective reasonableness of the position taken by the nonprevailing party and not on any subjective intent.[9] Despite the changes in the interpretation of § 285 on attorney fee awards in *Octane* and *Highmark* and reports that judges are awarding fees in higher numbers of cases after these decisions, we conclude that legislation is still needed. The existing statute still requires a case to be "exceptional" for an attorney fee award. *Octane* fails to provide a clear, objective test for lower courts to apply. It will require more lower court cases to determine the meaning of a case that "stands out from others." *Highmark* commits more discretion to district court judges by adopting the abuse of discretion review standard, which will require more time to achieve uniformity in the law. Some judges will not be inclined to award fees despite this lower standard.

Strong patent protection can stimulate the economy, driving investment in research and development and assuring the capital necessary to bring new products to market. The assertion of frivolous or nuisance claims or defenses, which serve neither the patent system itself nor the public interest, should never be tolerated.

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[6] *Id.* at 1758.
[7] *Highmark, Inc. v. Allcare Health Management Systems, Inc.*, 572 U. S. ___ (2014); 134 S. Ct. 1744, 1749.
[8] Brief of Intellectual Property Owners Association as Amicus Curiae in Support of Petitioner at 8, *Octane Fitness, LLC v. Icon Health & Fitness, Inc.*, 572 U.S. ___ (2014) (No. 12-1184).
[9] *Id.*

Intellectual Property Owners Association (IPO)

IPO still supports legislation that would provide for awarding fees to a prevailing party *unless* the position and conduct of the non-prevailing party were objectively reasonable and substantially justified or exceptional circumstances made an award unjust. In addition to addressing abuses, presumptive fee shifting will more effectively deter abusive litigation in the first place than simply relaxing the standard for discretionary fee shifting. Such legislation will promote consistency, uniformity, and predictability. Legislation will address abuses in jurisdictions where judges may be less inclined to award fees. Legislation can provide objective criteria for parties to avoid paying fees, which will provide a stronger deterrent to patent litigation abuse.

Alice Corp. v. CLS Bank

Alice unsettled the law on patent-eligible subject matter. The case addressed the patent eligibility of computer-implemented inventions under Section 101 of the Patent Act, upholding a Federal Circuit decision that Alice's patent claims were directed to an abstract idea, which is ineligible subject matter.[10]

35 U.S.C. § 101 defines patent eligible subject matter as encompassing any new and useful process, machine, manufacture, or composition of matter, or any new and useful improvement thereof. By judicial interpretation, patent eligible subject matter cannot include laws of nature, physical phenomena, and abstract ideas.[11] IPO's *amicus* brief to the Supreme Court argued that a computer-implemented invention involving an

[10] *Alice Corp. v. CLS Bank*, 572 U.S. ___, ___ (2014); 134 S.Ct. 2347, 2360.
[11] *See Alice* at 2354 (*citing Ass'n for Molecular Pathology v. Myriad Genetics, Inc.*, 569 U.S. ___, ___; 133 S. Ct. 2107; 186 L. Ed. 2d 124, 133 (2013)).

abstract idea was patent eligible if it described a specific, practical application of the idea.[12]

The Supreme Court held that courts must distinguish patents that claim the "building blocks" of human ingenuity, which are patent ineligible, from "those that integrate the building blocks into something more."[13] First, the court should determine whether claims are directed to a patent-ineligible concept.[14] Then the court should ask whether the claim's elements, considered individually and in combination, transform the nature of the claim into a patent-eligible application.[15] This step in the analysis has been described as searching for "an inventive concept" such that any resulting patent amounts to "significantly more" than a patent on only the ineligible concept.[16]

Alice did not articulate a clear test, and the "significantly more" inquiry may have confused the issue by conflating subject matter eligibility with the § 102 novelty and § 103 obviousness inquiries. This contributes to uncertainty and a lack of clarity and creates risk that the courts will apply *Alice* incorrectly. Post-*Alice* Federal Circuit opinions addressing patent eligibility of computer-implemented inventions have reached different outcomes. *DDR Holdings v. Hotels.com* upheld district court denial of Hotels.com's motion that DDR's claims were directed to patent-ineligible subject matter.[17] The claimed solution was rooted in computer-technology in order to overcome a problem specifically arising in the realm of computer networks.[18] *Ultramercial, Inc. v. Hulu, LLC* upheld district court dismissal of Ultramercial's infringement suit for failing

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[12] Brief of Intellectual Property Owners Association as Amicus Curiae in Support of Neither Party at 12-15, *Alice Corp. v. CLS Bank*, 572 U.S. ___ (2014) (No. 13-298).
[13] *Alice* at 2354.
[14] *Id.* at 2355.
[15] *Id.*
[16] *Id.*
[17] *DDR Holdings LLC. v. Hotels.com LP*, 773 F.3d 1245, 1249 (Fed. Cir. 2014).
[18] *Id. at 1257.*

to claim eligible subject matter.[19] Ultramercial claimed a method of providing copyrighted works over the Internet free in exchange for viewing advertising.[20] The problem of reconciling cases is likely to occur frequently at the USPTO and the district courts, which decide far more cases than the Federal Circuit.

The test for patent eligibility articulated in *Alice* is not limited to computer-implemented inventions. A Federal Circuit opinion issued in December in *In Re BRCA1- & BRCA2-Based Hereditary Cancer Test Patent Litig., Univ. of Utah Research Found. v. Ambry Genetics Corp.*, held that method claims related to the BRCA1 and BRCA2 genes were ineligible under the *Alice* framework as merely reciting "the patent-ineligible abstract idea of comparing BRCA sequences and determining the existence of alterations."[21]

We conclude that it is too early to tell what long-term effect *Alice* will have on deterring or decreasing abusive behaviors in patent litigation. *Alice* was decided only 6 months ago. Reports suggest a significant increase in district courts invalidating patents on software-related inventions as lacking eligible subject matter. However, there is too little data to say whether this is a trend or a temporary spike. Some say reports of the death of software patents have been greatly exaggerated. Reportedly, the USPTO has slowed-down issuance of business method patents and some medical diagnostic patents following *Alice*. Further, because the Supreme Court test is unclear, there is no assurance the USPTO and the courts are applying the case correctly.

Anecdotally, patent abusers are said to assert patents that are overly broad, which include patents directed to abstract ideas. Arguably *Alice*, by causing more patents to be

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[19] *Ultramercial,Inc. v. Hulu, LLC*, 772 F.3d 709, 711-12 (Fed. Cir. 2014).
[20] *Id.* at 714.
[21] 774 F.3d 755, ___ (Fed. Cir. 2014); 113 U.S.P.Q.2D (BNA) 1241, 1246.

invalid, could strengthen the power of defendants in frivolous suits. Defendants may be able to get suits dismissed before costly discovery and thus may not be as willing to settle.

It will take a while to determine the impact of *Alice*. The long-term effect will depend on how the lower courts, particularly the Federal Circuit, interpret and apply *Alice*. Courts have had problems for years with consistency and predictability in making determinations about patent eligibility. The lack of clarity in *Alice* makes it more difficult for innovators to determine when it is appropriate to invest in patent protection, and casts the shadow of uncertainty on all patents, even good ones.

Nautilus, Inc. v. Biosig Instruments, Inc.

35 U.S.C. § 112(b) requires patents to particularly point out and distinctly claim the subject matter the applicant regards as the invention. This is known as the "definiteness" requirement. Patent rights are property rights; their boundaries must be clear so the owner must know what he owns and others should know what they do not.[22]

Indefiniteness is one of the invalidity defenses.[23] An accused infringer can overcome the presumption of definiteness by showing "by clear and convincing evidence that a skilled artisan could not discern the boundaries of the claim based on the claim language, the specification, and the prosecution history, as well as her knowledge of the relevant art area."[24] IPO's *amicus* brief in the Supreme Court supported a "reasonable

[22] *Festo Corp. v. Shoketsi Kinzoku Kogyo Kabushiki Co.*, 535 U.S. 722, 730 (2002).
[23] 35 U.S.C. § 282(b)(3)(A).
[24] *Halliburton Energy Servs., Inc. v. M-I LLC*, 514 F.3d 1244, 1249-50 (Fed. Cir. 2008); *Microsoft Corp. v. i4i Ltd. P'ship*, 564 U.S. ___, ___ (2011); 131 S. Ct. 2238, 2242.

clarity" standard that would require claims to be reasonably understandable to a person having ordinary skill in the art in light of the specification and prosecution history.[25]

In *Nautilus* the Supreme Court adopted a reasonable certainty standard and overruled a Federal Circuit holding that an ambiguous claim was definite under § 112 as long as the ambiguity was not "insoluable."[26] The "insoluably ambiguous" standard failed to satisfy the definiteness requirement.[27] It was difficult to apply,[28] tolerated "some ambiguous claims but not others," [29] and failed to discourage applicants from obscuring the scope of claimed inventions.[30] The Supreme Court articulated a new test: a patent's claims, viewed in light of the specification and prosecution history, must inform those skilled in the art about scope of invention with "reasonable certainty."[31] Writing for the Court, Justice Ginsburg said that "to tolerate imprecision … would diminish the definiteness requirement's public-notice function and foster innovation-discouraging "zone of uncertainty."[32]

Post-*Nautilus* it should be easier for a defendant to challenge the validity of a vague patent. We conclude that *Nautilus* may have a long-term effect on abusive litigation. We cannot find evidence yet of a significant increase in patents invalidated for indefiniteness since *Nautilus*. The long-term impact will depend on how the lower courts apply *Nautilus*, and how the Federal Circuit resolves inconsistencies across jurisdictions. Claim definiteness is an area where the USPTO has an opportunity to have an impact by

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[25] Brief of Intellectual Property Owners Association as Amicus Curiae in Support of Neither Party at 9-12, *Nautilus, Inc. v. Biosig Instruments, Inc.*, 572 U.S. ___ (2014) (No. 13-369).
[26] *Nautilus,* 572 U.S. ___, ___ (2014); 134 S.Ct. 2120, 2124.
[27] *Id.*
[28] *See id.* at 2130.
[29] *Id.* at 2124.
[30] *See id.* at 2129.
[31] *Id.*
[32] *Id.* at 2130.

indicating how it will implement *Nautilus*, possibly by an undertaking similar to its efforts to address changes in the law on subject matter eligibility, where the Office published enhanced examination guidance for public comment, held public roundtables to solicit additional input, provided examiner training, and published updated examples.

Teva Pharmaceuticals USA, Inc. v. Sandoz, Inc.

Teva vacated a Federal Circuit indefinite patent claim ruling.[33] At issue was the proper standard of review for the district court's claim construction.[34]

Claim construction is a matter of law and until *Teva* it was always reviewed *de novo* by the Federal Circuit.[35] Federal Rule of Civil Procedure 52(a)(6) sets forth that findings of fact must not be set aside unless they are "clearly erroneous." In *Teva*, the Supreme Court held that the Federal Circuit must apply a "clear error," not *de novo*, standard of review of factual findings in support of claim construction (e.g., findings based on expert testimony).[36] When the court reviews only evidence intrinsic to the patent, i.e., the claims, specification and prosecution history, the court reviews that construction *de novo*.[37]

IPO's *amicus* brief supported the result reached in *Teva*, arguing that the ultimate conclusion of what a claim term means should remain reviewable *de novo* by the Federal Circuit.[38] Where a district court resolves questions of fact based on extrinsic evidence, we argued such factual findings should be afforded deference.[39]

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[33] *Teva Pharmaceuticals USA, Inc. v. Sandoz, Inc.*, 574 U.S. ___, ___ (2015); No. 13-854, slip op. at 16 (U.S. Jan. 20, 2015).
[34] *Id.* at 1.
[35] *See id.* at 5-6.
[36] *Id.* at 6.
[37] *Id.* at 11-12.
[38] Brief of Intellectual Property Owners Association as Amicus Curiae in Support of Neither Party at 2-3, *Teva Pharmaceuticals USA, Inc. v. Sandoz, Inc.*, 574 U.S.C. ___ (2015) (No. 13-854).
[39] *Id.* at 5-6.

Intellectual Property Owners Association (IPO)

While *Teva* applies broadly to all cases with claim construction review, we conclude that any effect this particular case may have on curbing abusive litigation will be minimal. The new framework better aligns appellate review of claim construction with Supreme Court precedent and the Federal Rules of Civil Procedure. The framework allows the Federal Circuit to benefit from the district courts' superior fact-finding position with respect to extrinsic evidence, while fostering consistent claim construction rulings.

Limelight Networks, Inc. v. Akamai Technologies, Inc.

The issue in *Limelight* was whether a defendant could be liable for inducing infringement of a patent under 35 U.S.C. § 271(b) when no one directly infringed the patent under § 271(a) or any other provision.[40] Supreme Court precedent requires that liability for inducement be predicated on direct infringement.[41] Earlier, in *Muniauction, Inc. v. Thomson Corp.*, the Federal Circuit held that direct infringement under § 271(a) requires all steps of a method patent to be attributable to a single party, either because the defendant actually performed the steps or because the defendant directed or controlled others who performed them.[42] Limelight was not liable for induced infringement even though Limelight provided directions to customers for performing the missing step of the patent claim.[43] IPO's *amicus* brief supported this outcome.[44]

We conclude that *Limelight* may foreclose some patent suits where different entities perform different steps of a method. Its impact will depend particularly on how

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[40] *Limelight Networks, Inc. v. Akamai Technologies, Inc.*, 572 U.S. ___ (2014); 134 S.Ct. 2111, 2115.
[41] *Aro Mfg. Co. v. Convertible Top Replacement Co.*, 365 U.S. 336, 341 (1961).
[42] 532 F. 3d. 1318, 1329-30 (Fed. Cir. 2008).
[43] *Limelight* at 2115-17.
[44] Brief of Intellectual Property Owners Association as Amicus Curiae in Support of Neither Party at 9-10, *Limelight Networks, Inc. v. Akamai Technologies, Inc.*, 572 U.S. ___ (2014) (No. 12-786).

courts analyze whether "direction or control" exists for purposes of direct infringement. The inquiry is likely to depend on a number of factors that will be different in each case, particularly given the opportunities for collaboration among companies.[45] Some facts to consider might include the closeness of the accused direct infringer and the third party that performed some of the steps of the claim, or the extent to which the relationship between the accused infringer and third party establishes the manner, timing, or other features that lead to the performance of the missing steps.[46]

Post-*Limelight* it will be more difficult to prove that a defendant is liable based on the induced infringement theory, and thus more difficult to sue on patents that require the completion of steps by a third party. Infringement will be foreclosed unless a plaintiff shows that a defendant exercises "control or direction" over end users. This might constrain the ability of patent owners to hold upstream suppliers or manufacturers liable for independent acts of downstream third-parties. The case might have implications for legislative proposals for stays of patent infringement suits against downstream suppliers or end users while litigation proceeds against manufacturers.

RELATED ISSUES

USPTO Must Issue Quality Patents

Some patents asserted in court should never have been issued by the USPTO. For many years IPO has supported improvements in USPTO administration to increase the quality of patent examination and speed up the processing of patent applications. A few specific measures likely to increase quality include upgrading IT systems for patent examiners, providing ongoing, timely examiner training on changes in the law and about

[45] *Id.* at 17.
[46] *Id.*

developments in technology, development and implementation of metrics to measure quality and, above all, to assure the issuance of patents that clearly define the scope of the rights they protect. We support the USPTO's new patent quality initiative for improving the reliability of patents and look forward to making suggestions to the USPTO about where we see room for improvements.

The USPTO Must Have Funding to Conduct High Quality, Timely Patent Examination

Our members all agree that the United States needs a fully-funded USPTO to keep our nation competitive, encourage innovation and create new jobs. User fees paid to the USPTO by patent and trademark applicants and owners are paid with the expectation that the money will be used to examine their applications and provide other services to them. However, close to $1 billion was sequestered or diverted to unrelated government programs between 1992 and 2013. This was one of the major causes of the large backlog of unexamined patent applications that the USPTO is still struggling with today.

The USPTO must have sufficient funds to hire and retain a nationwide workforce, and to train and supervise its workforce particularly to respond to emerging technologies and the evolution of case law. The patent system is a critical component of the U.S. economy and contributes greatly to U.S. leadership in innovation and technological advancement. It is imperative that the USPTO, which is fully funded by user fees and uses no taxpayer money, have full access to all of the user fees it collects. We urge Congress to revisit the issue of secure USPTO funding.

CONCLUSION

We continue to believe fee shifting legislation is needed despite the *Octane* and *Highmark* decisions, but the effects of the other decisions on frivolous litigation are more

difficult to assess. The number of new patent suits filed in U.S. district courts decreased substantially in 2014, from 6,107 new cases filed in 2013 to 5020 new cases filed in 2014.[47] While it is too early to conclude whether this is a trend or just a temporary lull, some speculate that this is a result of the cumulative effect of the recent Supreme Court patent decisions. Other factors, however, may be contributing to this decline in litigation. We recommend that the committee continue to monitor the possible impact of these Supreme Court decisions as it considers the scope of legislation to deter abusive litigation.

Another development since the House passed the Innovation Act may affect the patent landscape. Last year the U.S. Judicial Conference approved and forwarded to the Supreme Court for consideration proposed amendments to Federal Rules of Civil Procedure.[48] Among other changes, the new rules will delete Form 18 and thus heighten the pleading standard for patent infringement cases.[49] The new rules will also provide judges with more discretion and encouragement to more actively manage discovery, as well as enhanced guidance about when to shift fees with regard to discovery.[50] The new rules are scheduled to take effect December 1, 2015.[51] We suggest that the committee consider how these rule changes will affect patent litigation, with the goal of keeping patent law consistent with the rest of civil litigation to provide consistency, certainty, and predictability.

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[47] Docket Navigator Year in Review 2014 at 5 (*available at* http://home.docketnavigator.com/year-review).
[48] Press Release, Judicial Conference of the United States, Judicial Conference Receives Budget Update, Forwards Rules Package to Supreme Court (Sept. 16, 2014) (*available at* http://news.uscourts.gov/judicial-conference-receives-budget-update-forwards-rules-package-supreme-court).
[49] Memorandum from the Standing Committee on Rules of Practice and Procedure of the Judicial Conference of the United States B-4-11(June 14, 2014) (*available at* http://www.uscourts.gov/uscourts/RulesAndPolicies/rules/Reports/ST09-2014-add.pdf).
[50] *Id.* at B-19.
[51] Judicial Conference Press Release.

Intellectual Property Owners Association (IPO)

In addition to the recent case law and other considerations discussed above, we note that the changes made by the America Invents Act are difficult to discern so soon after the law's implementation. We urge the committee to consider the implications of the AIA's impact along with all other developments as it considers legislation to address abusive patent litigation practices.

It is crucial not to undermine strong patent rights by disturbing incentives undergirding the patent system. The law must deter frivolous litigation but must not penalize legitimate patent owners simply seeking to enforce their rights.

I will be happy to answer any questions.

* * *

Mr. ISSA. Thank you.
Mr. Gupta?

TESTIMONY OF KRISH GUPTA, SENIOR VICE PRESIDENT AND DEPUTY GENERAL COUNSEL, EMC CORPORATION, HOPKINTON, MA

Mr. GUPTA. Chairman Issa, Ranking Member Nadler, and Members of the Subcommittee, I am honored to testify today on the critical need for patent litigation reform.

EMC is a global leader in cloud computing. EMC and its affiliates hold more than 5,100 issued U.S. patents, and our portfolio is regularly recognized as one of the best in the information technology business. We support a strong patent system that protects and promotes innovation and one that cannot be exploited by abusive litigation tactics.

Since 2005, EMC has been sued by patent entities more than 35 times and has never been found to have infringed. Yet, defending those suits has been extremely expensive, costing $10 million in 2014 alone. And this does not include the substantial disruption to our business resulting from these frivolous lawsuits.

EMC is not alone in this regard. In 2014, more than 5,000 new patent lawsuits were filed. That is nearly twice as many as were filed only 4 years earlier when Congress passed the AIA. Most impartial observers agree abusive patent litigation harms innovation in all industries.

Some have suggested that recent decisions by the Supreme Court either reduce or negate the need for Congress to act. As a practitioner who spends most of his time on patent litigation matters, I disagree. Only Congress can comprehensively restore balance in the patent system. Let me walk through the Court's decisions that are most relevant to the issue of patent litigation reform, although I do not believe they offer an adequate solution.

In *Highmark* and *Octane*, the Court addressed the award of attorney's fees under Section 285 of the Patent Act, which currently limits the assessment of fees to exceptional cases. They loosened the standard by which courts evaluate what qualifies as an exceptional case while granting greater discretion to district courts to make this determination.

Highmark and *Octane* have had no meaningful impact. In the 9 months since these decisions, motions for fees have been granted in whole or in part only 4 percent more often than they were in the 2 years before these cases. Thus, fee shifting is still the exception rather than the rule. The Innovation Act would level the playing field by requiring that fees be awarded to the prevailing party unless the losing party's position is substantially justified or special circumstances make an award unjust. This provision will discourage the filing of frivolous suits and the use and abusive litigation tactics by imposing financial accountability in the patent system.

Next, I would like to turn to the Supreme Court's decisions in Iqbal and Twombly. In these cases, the Court addressed the level of specificity required in a complaint to include enough facts to plausibly suggest that the plaintiff is entitled to relief. With the Judicial Conference recently recommending the elimination of Form

18 for patent pleadings, it is expected that the Iqbal and Twombly standards will apply to all patent pleadings as well.

However, these cases do not set forth bright line rules necessary for patent cases and are bound to lead to variable outcomes. Many courts will undoubtedly continue to permit vague pleadings. The Innovation Act recognizes the need to provide uniform and clear pleading standards. This imposes no new burden on good faith plaintiffs who will have already conducted proper due diligence, but it will deter bad faith plaintiffs and will reduce costs for defendants by requiring the allegations to be made clear at the outset.

On discovery, there have been no Supreme Court developments regarding abusive tactics. We support provisions included in the Innovation Act that limit discovery before the Court issues its claim construction ruling. This would ensure that discovery is focused on claim construction issues that actually matter. By requiring the requesting party to cover the cost of unnecessary discovery, the Innovation Act will limit the extent to which discovery costs can be used as a bargaining chip to extort a settlement.

These three areas—fee shifting, pleading specificity, and discovery—require legislative intervention. The courts cannot bring about the comprehensive and prompt solution that Congress can structure while promoting consistency and predictability. The rampant proliferation of abusive patent litigation is a problem causing billions of dollars of costs that cry out for a legislative solution. We urge you to swiftly pass this legislation, and we stand prepared to help you in any way we can to bring a bill to the President's desk in short order.

Thank you, and I look forward to your questions.

[The prepared statement of Mr. Gupta follows:]

Committee on the Judiciary
Subcommittee on Courts, Intellectual Property, and the Internet
U.S. House of Representatives

Hearing
"Examining Recent Supreme Court Cases in the Patent Arena"

Testimony of Krish Gupta
Senior Vice President and Deputy General Counsel
EMC Corporation

February 12, 2015

EMC²

Testimony of Krish Gupta
EMC Corporation
Before the House Judiciary Committee
Subcommittee on Courts, Intellectual Property, and the Internet
February 12, 2015

Chairman Issa, Ranking Member Nadler, and Members of the Subcommittee, my name is Krish Gupta, and I am Senior Vice President and Deputy General Counsel for EMC Corporation (EMC). I had the honor and privilege of testifying before the Judiciary Committee in October, 2013, to express our support for patent legislation to curb abusive patent litigation. Since that time, the Supreme Court of the United States has issued a number of decisions that have provided some relief from certain abuses. I appreciate the opportunity to testify on the impact of these decisions on patent litigation and H.R. 9, the Innovation Act of 2015 ("Innovation Act"). EMC applauds the introduction of the bipartisan Innovation Act and believes strongly that these important legislative reforms continue to be necessary to protect the patent system and spur innovation and competition.

As background, I am a registered patent attorney with more than 20 years of experience in patent law. At EMC, I have worldwide responsibility for intellectual property (IP) law and technology licensing matters, including IP policy, patent and trademark prosecution, and IP litigation. I would like to thank you for the opportunity to discuss the importance of patents to EMC, the current state of the patent litigation system, and the continued and urgent need for the reforms enumerated in the Innovation Act. The Innovation Act is a major step forward toward curbing abusive patent litigation and making it possible for innovators to focus on developing the next new technology for the benefit of the American consumer and economy, rather than defending meritless lawsuits.

About EMC

EMC was founded in Newton, Massachusetts, in 1979. Today, EMC is a global leader in enabling businesses and service providers to transform their operations and deliver IT-as-a-Service. Through innovative products and services, EMC accelerates the journey to cloud computing, thereby helping businesses store, manage, protect, and analyze their most valuable asset—information—in a more agile, trusted, and cost-efficient way.

Since 2003, EMC has invested approximately $42 billion in research and development, as well as in acquisition of technologies that have revolutionized the world of information technology. EMC currently has an annual R&D investment of approximately $3 billion. These investments have enabled EMC to broaden our product portfolio, enter new market segments, and expand our market opportunity.

Headquartered in Hopkinton, Massachusetts, with additional concentrations of employees in California, North Carolina, Utah, and Washington State, we employ approximately 68,000

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people in 86 countries around the world. We rank 128th on the Fortune 500, based on 2014 revenues of $24.4 billion.

Importance of Patents to EMC

EMC's position of market leadership is the result of pioneering innovation, hard work, and substantial investment in new technologies. Innovation and intellectual property are our lifeblood, our keys to survival, and our future. We have a 36-year track record of anticipating future needs and building and acquiring technology solutions to solve problems in new and innovative ways.

EMC relies greatly on patents to establish and maintain our proprietary rights in our technology and products. EMC and its majority owned federated businesses hold more than 5,100 issued U.S. patents. EMC's patent portfolio is regularly recognized as one of the strongest and most impactful in the information technology business. In fact, the Wall Street Journal and the Patent Board recently ranked EMC as the 8th most innovative information technology company based on the quality and quantity of its patents.[1] These patents cover EMC's many innovations, including the hardware and software technologies used in our diverse products and offerings. In short, EMC is an advocate of a strong patent system; however, we want a system that protects and promotes innovation rather than inhibiting it, and a system that cannot be exploited by those who would use abusive tactics.

Abusive Patent Litigation is a Serious Problem

In 2014 alone, more than 5,000 new patent lawsuits were filed.[2] That is nearly twice as many as were filed only four years earlier.[3] The number of patent lawsuits filed last year was the third highest ever.[4] After adding in patent disputes filed in administrative agencies, the total number increases to more than 6,600 patent disputes—the second highest level in history.[5]

In 2011, litigation costs arising from cases filed by so-called "patent assertion entities" were estimated at $29 billion in direct out-of-pocket costs.[6] At that time, commentators

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[1] THE PATENT BOARD, http://www.patentboard.com/ (last visited February 9, 2015).
[2] *Unified Patent's 2014 Litigation Report*, UNIFIED PATENTS (January 8, 2015), http://unifiedpatents.com/2015/01/08/unified-patents-2014-litigation-report/.
[3] *Id.*
[4] *Id.*
[5] *2014 Patent Dispute Report and Analytics*, UNIFIED PATENTS (January 26, 2015), http://unifiedpatents.com/2015/01/26/2014-patent-dispute-report-and-analytics/.
[6] James E. Bessen & Michael J. Meurer, *The Direct Costs from NPE Disputes*, 99 CORNELL L. REV. 387 (2014), *available at* http://ssrn.com/abstract=2091210; *see also Litigations Over Time*, PATENT FREEDOM,

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estimated the total costs associated with abusive patent litigation at $80 billion per year,[7] and those numbers certainly have increased since then. Abusive patent litigation is a costly problem that is stifling American innovation and impeding job creation each and every day.

Small, medium, and large enterprises are all affected by abusive patent litigation. According to a 2013 survey, startup companies and venture capitalists overwhelmingly believe that the threat of patent litigation has a negative impact on their businesses.[8] Survey respondents cited monetary costs as well as distraction to management, engineers, and other employees. Respondents also described the human toll that these threats have taken on entrepreneurs, citing not only the impact on morale, but also the overall fear of losing a business. Further, the surveyed venture capitalists stated that if a company had an existing patent litigation threat against it, that fact could potentially be a major deterrent in deciding whether to invest. The survey succinctly summarized the responses on the impact of patent demands on startups: "[w]hen companies spend money protecting their intellectual property position, they are not expanding; and when companies spend time thinking about patent demands, they are not inventing."[9]

Other commentators echo this core conclusion: abusive patent litigation harms innovation.[10] While Congress hears a lot from large companies like EMC, in fact, the biggest impact is on small startup firms.[11] Most of the cases filed by abusive litigants target companies with revenues of less than $100 million a year.[12] A study conducted at the Massachusetts Institute of Technology concluded that frequent litigants caused a decline of $22 billion in venture investing over a five-year period.[13] A Rutgers University study concluded that small companies that were hit with abusive lawsuits significantly decreased their spending on research and development.[14] Likewise, researchers at Harvard University and the University of Texas found a substantial decline in research and development spending following protracted patent litigation initiated by patent assertion

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https://www.patentfreedom.com/about-npes/litigations/ (last visited February 8, 2015); Robin Feldman, Tom Ewing, & Sara Jeruss, *The AIA 500 Expanded: Effects of Patent Monetization Entities*, UC HASTINGS RESEARCH PAPER NO. 45, April 9, 2013, at 7, http://ssrn.com/abstract=2247195 (patent monetization entities filed 58.7 percent of patent lawsuits in 2012).

[7] James E. Bessen, Jennifer Ford & Michael J. Meurer, *The Private and Social Costs of Patent Trolls*, REGULATION, Winter 2011-2012, at 26.

[8] Robin Feldman, *Patent Demands & Startup Companies: The View from the Venture Capital Community*, UC HASTINGS RESEARCH PAPER NO. 75, October 28, 2013, http://ssrn.com/abstract=2346338.

[9] *Id.*

[10] James Bessen, *The Evidence Is In: Patent Trolls Do Hurt Innovation*, HARV. BUS. REV., July 2014, *available at* https://hbr.org/2014/07/the-evidence-is-in-patent-trolls-do-hurt-innovation.

[11] *Id.*

[12] *Id.*

[13] Catherine Tucker, *The Effect of Patent Litigation and Patent Assertion Entities on Entrepreneurial Activity*, MIT SLOAN SCHOOL WORKING PAPER 5095-14, June 22, 2014, at 31, http://ssrn.com/abstract=2457611.

[14] Roger Smeets, *Does Patent Litigation Reduce Corporate R&D? An Analysis of US Public Firms*, April 28, 2014, http://ssrn.com/abstract=2443048.

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entities.[15] The evidence is clear: frivolous and abusive patent litigation results in less innovation and less investment in cutting-edge technologies and companies.

We at EMC wholeheartedly agree with these conclusions. Public confidence in our nation's patent system suffers, justifiably, when that system allows low-quality patents to be asserted in litigation and allows abusive litigation practices to be used. Baseless patent litigation distracts innovators, preventing them from spending their time productively contributing to technological progress and to the economy.

The staggering costs of such abusive patent litigation are borne by innovative companies in all industries. While sixty-three percent of the patent lawsuits filed last year were in the high-tech field,[16] a recent article suggested that patent assertion entities may soon increase lawsuits targeting biotech and pharmaceutical companies.[17] In short, the patent system that was created to promote innovation, has, in far too many instances, actually had a detrimental impact on innovation by taking money and resources from those who innovate and handing it over to those who do not.

EMC's Experience

EMC is a frequent target of unscrupulous patentees with low-quality patents. Since 2005, EMC has faced unfounded patent lawsuits more than thirty five times, and has never been found to have infringed. As a matter of principle, EMC does not settle unmeritorious suits. To us, to do so would be tantamount to giving in to extortion. Yet defending against abusive litigation has cost us millions of dollars that could have been invested in growing our workforce or furthering innovation. In 2014 alone, EMC spent more than $10 million in defending frivolous patent actions.

Typically, at the outset of these cases, abusive patentees provide very little information about their allegations. EMC is forced to devote significant time, resources, and manpower to analyzing vague complaints that are directed at vast technology areas. This effort is needed because we must speculate about what will be the subject of the plaintiff's infringement argument. And in the process, we waste the time of our engineers—the driving force of our company—studying technical details of features that ultimately are not at issue in the case.

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[15] Lauren Cohen, Umit G. Gurun, and Scott Duke Kominers, *Patent Trolls: Evidence from Targeted Firms* HARVARD BUSINESS SCHOOL FINANCE WORKING PAPER NO. 15-002, August 7, 2014, http://ssrn.com/abstract=2464303.

[16] *Unified Patent's 2014 Litigation Report*, UNIFIED PATENTS (January 8, 2015), http://unifiedpatents.com/2015/01/08/unified-patents-2014-litigation-report/.

[17] Robin Feldman & W. Nicholson Price, *Patent Trolling — Why Bio & Pharmaceuticals Are at Risk*, UC HASTINGS RESEARCH PAPER NO. 93. Feb. 14, 2014, http://ssrn.com/abstract=2395987.

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At the beginning of a lawsuit, EMC spends between $100,000 and $150,000 per month in outside legal fees for routine administration of a patent suit. Once a case becomes more active with discovery, depositions, expert reports, and Markman hearings, the fees typically range from $150,000 to $300,000 per month, but can be even higher. Added to such costs are expenses for outside vendors, experts, and prior art searching, which may cost several hundred thousand dollars each.

Further, we often challenge the validity of low-quality patents through a Petition for Inter Partes Review (IPR). These petitions—highly beneficial proceedings introduced by the AIA—are filed with the Patent and Appeals Board of the U.S. Patent and Trademark Office, an expert agency that is often better situated to evaluate patent validity than a court. Although EMC is a great proponent of this new proceeding, an IPR can cost between $500,000 and $1,000,000 per patent. In instances in which the district court does not stay its proceedings, this expense may need to be borne simultaneously with the above-described litigation costs.

In total, we can easily spend several million dollars to reach a resolution on the merits of one case. Some plaintiffs use their leverage associated with these costs to extort unreasonable settlements. This tactic is especially effective against startups and small companies that may not have the capital for a robust defense. Indeed, some patentees negotiate scores of cost-of-litigation settlements with the majority of defendants, then simply dismiss the rest rather than proceeding with litigation. Although this tactic demonstrates the frivolous nature of the lawsuit, defendants rarely have any recourse against patentees who conduct no business aside from filing meritless cases.

Discovery is a major contributor to the overall cost of litigation. Discovery costs in intellectual property cases are almost 62 percent higher than in other cases.[18] In a case brought by a patent assertion entity, these discovery costs are borne almost exclusively by defendants. This sort of plaintiff typically has few documents and fewer employees. No matter how many discovery requests they are served, they can often simply produce all their documents in a single banker's box. There is a significant incentive for a patent assertion entity to drown a large company defendant in discovery requests, seeking to force its engineers, its IT department, and its legal staff to unearth tens of thousands of requested documents. Such discovery costs are particularly troubling because they are unpredictable. Judges across the country, abetted by the lack of uniform national patent rules, have very different views on the proper scope of discovery.

These burdens are unnecessary and unwarranted. According to one estimate, less than one document in ten thousand produced in discovery is actually introduced at trial.[19] Email appears even more rarely.[20] Yet despite the irrelevance of most documents produced in

[18] Chief Judge Randall B. Rader, *The State of Patent Litigation*, E.D. TEX. JUDICIAL CONFERENCE, Sept. 27, 2011, at 7, *available at* http://patentlyo.com/media/docs/2011/09/raderstateofpatentlit.pdf.
[19] *Id.* at 8.
[20] *Id.*

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discovery, some plaintiffs still use the threat of exorbitant discovery costs to increase the incentives to settle.

One of the lawsuits in which EMC is involved provides a compelling example of the need for reform. When this case was first filed, the complaint listed eight patents, with no explanation of which of the hundreds of claims in those patents were allegedly infringed. The complaint generically accused two large EMC product lines of infringing, with no designation of which specific models infringed, and no explanation of why any EMC product supposedly infringed, or which claims might be infringed.

Based on the limited information it had, EMC set to work investigating the plaintiff's allegations and preparing its defenses. But six months later, the plaintiff amended its complaint, adding three new patents and a third, separate EMC product line. The plaintiff still failed to identify any specific claims or any specific model numbers. EMC again diligently attempted to investigate the allegations, but the sheer number of claims and the lack of any explanation as to how the claims were allegedly infringed required enormous effort, involving hundreds of hours of potentially unnecessary analysis. It was not until eight months into the litigation that specific claims were identified and claim charts provided.

Then, a year and four months into the lawsuit, the plaintiff again tried to expand the case, asking the Court for permission to add new products and previously undisclosed claims. EMC should not have to litigate for more than a year, investing enormous sums of money for its defense, only to have the case fundamentally change direction again and again.

As a result of all this uncertainty, EMC has spent hundreds of thousands of dollars *per month* combating allegations that are a fast-moving target. If the plaintiff had identified its theory of the case from day one, EMC could have conducted its own investigation into infringement and validity in short order, spending a fraction of the time and expenses that it will be forced to incur. Instead, as is common in abusive patent litigations, the ever-changing allegations make it impossible to efficiently and effectively prepare a defense. This is by design and in the plaintiff's interest, as so many companies would prefer to settle for a fraction of the litigation cost and avoid the aggravation rather than continue to fight on these uneven terms.

Discovery represents a significant part of EMC's overall expenses in this case. The plaintiff has accused EMC products that are complex, refrigerator-sized storage systems that may cost up to $1 million or more. However, the alleged infringement is based solely on a relatively inexpensive commodity chipset that is supplied by a third party and embedded within the accused products. Thus, despite the narrow scope of the patent, EMC is forced to spend considerable money producing reams of technical and financial information that has nothing to do with the tiny chipset that is at the heart of the infringement allegations.

In short, the system as it exists today is highly skewed. Patentees who file frivolous cases can gain significant unfair leverage by increasing the risk and costs on the part of

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defendants. But, unless they are subject to counterclaims, they may share no part of the risk, and little part of the costs. Today, they are rarely held accountable for a defendant's attorneys' fees, even when the litigation they filed lacked any reasonable basis. The Innovation Act addresses these core issues and will ultimately change the system for the better.

Recent Supreme Court Cases and Related Developments

Some have suggested that recent decisions by the Supreme Court of the United States reduce the need for Congress to act. However, the great majority of small, medium and large entities that have been negatively impacted by abusive patent litigation know that much still needs to be done, and legislative action is required to address the core aspects of abusive litigation. That is, legislative action is required to secure the patent system so that it operates in the manner in which it was originally intended—to promote innovation. I will spend a few minutes summarizing the relevant recent cases, and will then explain why Congressional action is sorely needed to promote consistency and predictability.

Mayo. In 2012, in a case called *Mayo Collaborative Services v. Prometheus Laboratories*,[21] the Supreme Court addressed when one can patent medical processes. The Court held that if a patent is directed to a natural process that takes place in the human body—a so-called "law of nature"—it must also contain an "inventive concept" to be eligible for a patent. Tacking on routine or conventional steps, like taking measurements from blood, to the natural law cannot make it eligible.

Mayo demonstrated how the Court would scrutinize patents to make sure they are "eligible"—that is, to ensure they are directed to the subject matter that Congress intended for patenting, namely inventions that improve processes, machines, articles of manufacture, or compositions of matter, not natural laws, abstract ideas, or products of nature. But *Mayo* did not solve the problem of abusive patent litigation. Most bad-faith patent lawsuits did not involve the type of subject matter directly addressed by *Mayo*.

Myriad. Then, in 2013, in a case called *Association for Molecular Pathology v. Myriad Genetics*,[22] the Court built on its earlier decision, determining whether human DNA could be patented. The Court held that naturally occurring DNA, even isolated strands, could not be patented. However, artificial sequences of DNA can be patented because they are manmade.

As with *Mayo*, *Myriad* did not do much to solve the problem of abusive patent litigation. Whether you can patent DNA is an interesting question, but DNA patents are not an issue that affect most companies facing these baseless lawsuits.

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[21] *Mayo Collaborative Services v. Prometheus Laboratories, Inc.*, 132 S.Ct. 1289 (2012).
[22] *Association for Molecular Pathology v. Myriad*, 133 S.Ct. 2107 (2013).

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Limelight. Last June, the Supreme Court decided *Limelight Networks, Inc. v. Akamai Technology*,[23] a case relating to induced infringement of method claims. A method claim is a patent claim that sets forth steps to be performed rather than physical components of a patented machine. In a claim of induced infringement, the defendant is accused of encouraging someone else to infringe a patent. In *Limelight,* the Supreme Court confirmed that there can be no induced infringement unless there is direct infringement.

This decision simply returned the law to the way it was before the Federal Circuit's decision in this case. Furthermore, the decision involved only the narrow category of cases involving allegations of induced infringement of a method claim where there was no direct infringement. Therefore, *Limelight* did not have a substantial impact on baseless patent litigation.

Alice. In *Alice Corporation v. CLS Bank*,[24] also decided last June, the Court finally turned to the category of patents that abusive plaintiffs more often assert in patent litigation: patents on computer-implemented business ideas. The Court held that you cannot get a patent on a fundamental economic practice, like the idea of escrow, even if you limit your patent to escrow performed on a computer. Computers are so ubiquitous, the Court explained, that merely taking a longstanding idea and doing it on a computer is not truly inventive.

While *Alice* is helpful in some cases, it impacts only a small percentage of patents. Further, even patent cases that do not survive motions to dismiss under *Alice* run up enormous costs for defendants. Plaintiffs who file bad-faith litigation understand these costs, and can still coerce settlements out of defendant operating companies that would rather pay less to settle than to litigate.

Octane/Highmark. Last year, the Court decided two cases addressing when courts can award attorneys' fees to the prevailing party in patent litigation. Currently, Section 285 of the Patent Act says that even when a defendant wins, the defendant still must pay its own attorney's fees unless the defendant demonstrates that the case was "exceptional." In *Octane Fitness v. Icon Health & Fitness*,[25] the Supreme Court interpreted this provision to mean that fees are available in any case that "stands out from others." In *Highmark v. Allcare Health Management System,*[26] the Court held that district courts have great discretion in deciding whether to award fees. EMC filed amicus briefs in these cases urging the Court to make it easier for district courts to award fees, and these cases did loosen the prior standards applicable to deciding motions for fees. Unfortunately, as I will explain, these decisions have been only moderately successful in increasing the success rates of defendants who seek to recover their attorneys' fees when they are faced with baseless patent litigation.

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[23] *Limelight Networks, Inc. v. Akamai Technology*, 134 S.Ct. 2111 (2014).
[24] *Alice Corporation Pty. Ltd. v. CLS Bank Int'l*, 134 S.Ct. 2347 (2014).
[25] *Octane Fitness, LLC v. ICON Health & Fitness, Inc.*, 134 S.Ct. 1749 (2014).
[26] *Highmark, Inc. v. Allcare Health Mgmt. Sys., Inc.*, 134 S.Ct. 1744 (2014).

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Nautilus. In June of last year, the Court addressed how clear or "definite" patents must be in *Nautilus v. Biosig Instruments.*[27] The Court interpreted language in Section 112 of the Patent Act requiring that a patent "conclude with one more claims particularly pointing out and distinctly claiming the subject matter" of the invention as requiring the patent to provide "reasonable certainty" of what it covers. EMC filed an amicus brief in this case as well, successfully urging the Court to overrule the Federal Circuit's overly-narrow view of when a patent should be held invalid for indefiniteness. Nevertheless, since the Supreme Court issued this decision, few patent claims have actually been invalidated as a result of the new standard.

Teva. In its recent decision in *Teva Pharmaceuticals USA v. Sandor,*[28] the Court took a step backwards in its line of patent decisions, addressing the Federal Circuit's standard review of district court claim construction decisions. The Federal Circuit had always given a fresh look to such decisions, which enabled that court to ensure that a patent had been interpreted consistently across the district courts. But in January, the Supreme Court held that some aspects of a district court's claim construction decision would be reviewed with deference—that is, the Federal Circuit should allow district courts some leeway in interpreting patents, even if they get it wrong.

EMC filed an amicus brief in this case as well, warning that giving deference to a district court's claim construction decision would encourage abusive patent litigation. Patentees typically get to pick the district court in which they bring suit, and so they can shop for the forum most likely to interpret patents overly favorably. The Federal Circuit's fresh review of district court interpretations of a patent had put a small check on such forum shopping. Now unscrupulous patentees have an additional incentive to pick the district court most favorable to them, and that court's claim interpretation will be more insulated from Federal Circuit review.

***Twombly, Iqbal,* and Form 18.** In 2007 and 2009, the Court decided *Bell Atlantic v. Twombly*[29] and *Ashcroft v. Iqbal*[30], a pair of non-patent cases that increased, to a degree, the level of specificity required in a complaint by requiring the complaint to include enough facts to "plausibly" suggest that the plaintiff is entitled to relief.

Today, these cases do not directly apply to patent complaints that assert direct infringement (although they do apply where indirect infringement is alleged) because the Federal Rules of Civil Procedure include a sample form for patent infringement, Form 18, which requires less detail than is required by *Twombly* and *Iqbal.* Thus, today, a plaintiff need not fully identify the accused products; a plaintiff need not identify the asserted claims; and a plaintiff need not explain why it believes that the defendant infringes the asserted patent.

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[27] *Nautilus, Inc. v. Biosig Instruments, Inc.*, 134 S.Ct. 2120 (2014).
[28] *Teva Pharmaceuticals USA, Inc. v. Sandoz Inc.*, No. 13-854 (U.S. Jan. 20, 2015) (slip. op.).
[29] *Bell Atlantic Corp. v.* Twombly, 550 U.S. 544, 127 S.Ct. 1955 (2007).
[30] *Ashcroft v. Iqbal*, 556 U.S. 662, 129 S.Ct. 1937 (2009).

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In September, the Judicial Conference of the United States, which is a 26-member committee of judges that suggests changes to the Federal Rules of Civil Procedure to the Supreme Court, recommended abolishing certain model forms, including Form 18.[31]

The abrogation of Form 18 would be a positive development, as it would lead to courts applying the stricter standard of *Twombly* and *Iqbal* to patent cases. But these cases do not set forth bright-line rules, and there will inevitably be satellite litigation regarding whether or not a particular complaint satisfies the requirements of these cases. Different judges in different districts will come to different conclusions, leading to variable outcomes. Legislation is needed to provide uniform, clear national standards so that defendants may prepare their case from the outset.

Legislation is Needed

While helpful, recent developments in Supreme Court case law do not fully correct the core problems of patent litigation abuse. For example, they do not reduce the expense and burden of discovery. They do not require a patentee to initially disclose which claims of a patent it is asserting, which of the defendants' products it is accusing, or how the accused products supposedly infringe the patents. And these decisions do not make fee-shifting the default rule rather than the exception. I will address each of these issues in turn.

Discovery. No recent development has managed to turn the tide of the abusive discovery tactics that plague the meritless cases EMC faces on a daily basis. As I explained earlier, discovery is a significant weapon used to extort cost-of-litigation settlements in meritless cases. Abusive discovery tactics are particularly effective when used by non-practicing entities because they typically have few employees and few records or documents, and are generally not subject to counter suit.

The Innovation Act sensibly limits discovery before the court issues its claim construction ruling to only discovery that relates to claim construction issues. This will help prevent wasted effort by either eliminating the need for discovery entirely (where, for example, the court's claim construction order effectively resolves the case), or at minimum by focusing the parties on truly relevant discovery, which can only be known after the court has told the parties how the claims will be interpreted.

The Innovation Act further ensures that the technical discovery that does take place will be tailored to the issues that actually matter, and that the costs of inefficient "fishing

[31] *See Judicial Conference Receives Budget Update, Forwards Rule Package to Supreme Court*, UNITED STATES COURTS, September 16, 2014, http://news.uscourts.gov/judicial-conference-receives-budget-update-forwards-rules-package-supreme-court; Vin Gurrieri, *Judges Vote to Nix Rule Creating Patent Complaint Forms*, IP LAW 360, September 17, 2014, http://www.law360.com/articles/578149/judges-vote-to-nix-rule-creating-patent-complaint-forms.

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expeditions" will be borne by the party serving the discovery request. By requiring the requesting party to cover the costs of unnecessary discovery, the Innovation Act will limit the extent to which those who would abuse the litigation system can use discovery costs as a bargaining chip.

Pleading Specificity. Businesses like EMC require certainty and predictability. Uniform, clear national standards, such as those included in the Innovation Act, can only be provided by Congress, and are needed. And those standards should require a plaintiff to explain why it believes the defendant infringes, so that the defendant can actually investigate the allegations and prepare its case, rather than face ever-shifting theories of infringement.

The Innovation Act recognizes the need to provide uniform pleading requirements for patent infringement cases. The Act would require a patentee to set out in its complaint each asserted claim, each accused product, and an explanation of how each accused product supposedly infringes every asserted claim. This imposes no new burden on good-faith plaintiffs, who are required to have conducted due diligence and arrived at a tenable, good-faith theory of infringement before filing suit. The bill's heightened pleading requirement merely requires plaintiffs to disclose the results of their required analysis. The Act will have a real effect on those plaintiffs who file meritless, bad-faith lawsuits by making the lack of basis for the lawsuit apparent from the outset.

Fee-shifting. The Supreme Court's decisions in *Highmark* and *Octane* are welcome, but do not go far enough. Fundamental change is needed to stop the onslaught of frivolous patent cases companies have faced in recent years.

In the two years before these cases were decided, motions for fees were fully granted 18 percent of the time and granted in part 20 percent of the time. They were denied in full 62 percent of the time.[32] According to our analysis, in the nine months since the Supreme Court issued its decisions in *Highmark* and *Octane*, the grant rate has increased. In that period, motion for fees were fully granted 32 percent of the time and granted in part 10 percent of the time. The rate of full denials decreased marginally, from 62 percent to 58 percent. Viewed as a whole, more motions for fees have been granted in full and fewer have been granted in part. The number of denials has decreased, but not by very much.

Although at first glance, these statistics suggest that the rate of fully-granted motions for fees has increased after *Highmark* and *Octane,* in reality, that increase is largely isolated to the first three months after the Supreme Court issued its decisions. In those three months, motions for fees were fully granted 40 percent of the time, partially granted 10 percent of the time, and fully denied 50 percent of the time. But in the most recent three months, motions for fees have been fully granted only 24 percent of the time and partially granted 13 percent of the time, with full denials at 63 percent. In other words, in the most recent three months, the rate of full denials of attorneys' fees motions is about the same as it was

[32] *Docket Navigator Litigation Activity*, https://www.docketnavigator.com/stats (last updated Feb. 5, 2015).

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before the Supreme Court decided *Highmark* and *Octane*. As we can see, *Highmark* and *Octane* do not represent a panacea.

The upshot of this research is that fee-shifting is still the exception rather than the rule. For example, a judge on the Federal Circuit sitting as a district court judge by designation denied fees even though he found that the plaintiff's case "was certainly a weak one."[33] Critically, much is left to the discretion of district courts—discretion that is exercised very differently by different judges.

The Innovation Act would go further in leveling the playing field by requiring that fees be awarded to the prevailing party unless the losing party's position is substantially justified or special circumstances make an award unjust. We believe that this provision embodies the simplest way to discourage the filing of frivolous and abusive suits by imposing financial accountability in the patent system. Simply stated, some patent owners—especially non-practicing entities that are not generally subject to counter suits—have nothing to lose and everything to gain by filing suits, whether they have merit or not. Fee shifting would change that and bring some accountability to the system.

Congress is uniquely situated to make a real difference in these important areas. While the Supreme Court has been active in correcting some of the flaws in the patent system that frivolous litigants seek to exploit, the judiciary—even at the highest level—cannot bring about the comprehensive and prompt solution that Congress can structure. It takes time for a case to reach the Supreme Court and it only accepts for review a handful of IP cases each term. Congress on the other hand can enact comprehensive solutions in a single, coordinated approach, such as that outlined in the Innovation Act. The proliferation of abusive patent litigation is the kind of broad problem, causing billions of dollars in misdirected spending, that cries out for a legislative solution.

Conclusion

In conclusion, legislative action to address patent litigation abuses is necessary to restore confidence and balance in our patent system. The courts have made great strides, but the decisions are not sufficient to address all of the tactics associated with abusive patent litigation, including vague pleadings and discovery misconduct, which force many companies into settlement. Since I last appeared before the Judiciary Committee, EMC, its customers, and many similarly situated companies continue to be subject to frivolous litigation. The money spent on this frivolous litigation could be better invested in jobs and research and development. I must tell you, unfortunately, that I am certain that unless Congress acts, the problem will continue, unabated. The efforts undertaken by the Judiciary Committee and this Subcommittee are essential to the health of our patent system and the innovation of businesses in the United States.

[33] *Stragent LLC v. Intel Corp.*, Civ. No. 6-11-cv-00421, 2014 WL 6756304 (E.D. Tex. Aug. 6, 2014), at *5.

Mr. ISSA. Thank you. Mr. Pincus?

I would advise all of you that we will get through your statements, and once the vote is called at approximately 2:00, we will operate for 10 additional minutes and then anticipate a break for roughly two votes. So you will all be getting about a 30-minute break in about 30 minutes.

Mr. Pincus?

TESTIMONY OF ANDREW J. PINCUS, PARTNER, MAYER BROWN LLP, WASHINGTON, DC

Mr. PINCUS. Thank you, Mr. Chairman, Ranking Member Nadler, and Members of the Subcommittee. It is an honor to appear before you to discuss the Supreme Court's recent patent decisions, and, in particular, the impact of those decisions on the very serious problem of abusive patent litigation that this Committee in the House sought to address in the last Congress through passage of the Innovation Act.

The Supreme Court, of course, does not have free-floating policy authority to address concerns about patent litigation. Its responsibility is to interpret the statutory text when an issue is brought before it. So some of the Court's recent decisions have overturned Federal court rulings that promoted abusive litigation, but other of the Court's recent decisions are likely to have the opposite effect and actually increase the cost and complexity of patent cases. And as to some decisions, we actually do not yet know what the outcome will be.

For example, the Court's decision last year in the Nautilus case rejected a Federal circuit rule that had all but eliminated the patent max definiteness requirement, and the Supreme Court instead made clear that a claim is invalid if it fails to inform with reasonable certainty those skilled in the art about the scope of the invention. Reaffirming the definiteness requirement will help weed out some unjustified patents.

But in the Teva Pharmaceutical case, the Court's decision is likely to increase patent litigation costs and complexity. As the Committee knows, the key initial first step in patent litigation is construing the patent claim, and in doing that the Court can consider the language of the claims, the specifications, the prosecution record, as well as extrinsic evidence, including expert testimony. Claim construction is a task for the judge, and it takes place following a so-called Markman hearing at which the parties present all of the relevant evidence.

The Federal circuit had held that it reviewed all aspects of claim construction de novo, including the district court's determinations regarding extrinsic evidence, such as expert testimony. In Teva, the Supreme Court reversed and said that those factual determinations are subject to a clearly erroneous standard of review. Previously, introduction of expert testimony in the course of a Markman hearing while it occurred was rare, but Teva may be viewed by some district courts and some parties as an implicit endorsement of reliance upon expert testimony and other extrinsic evidence. And district courts may want to ground their decisions on those bases in order to limit the possibilities of reversal on appeal. So that may mean much more discovery and expert testimony at the beginning

of the case, which, of course, is going to make these cases even more complicated and even more costly than they already are.

The *Alice* case, as Mr. Wamsley said, involves the question of patentable subject matter. The Court had before it a patent claim that was troubling that basically said take this fundamental economic principle, do it on a computer, that is patentable. And the Court said, no, something significantly more is required, and the lower courts are now trying to flesh out what that "significantly more" is. Obviously there is a concern that that test not swallow up legitimate patent claims and not swallow up the other tests in the Patent Act that limit patentable. And we are going to have to see how that all plays out.

Most troubling, I think, from the perspective of reducing litigation abuse were the Court's decisions in the two attorney's fees cases, *Octane* and *Highmark*. They together give district courts more discretion, but the Supreme Court reaffirmed that the exceptional test, which is the language used in the current version of Section 285, which means that fee shifting is an option in only a small minority of cases because the case has to be exceptional, which by definition is going to be a very small group of cases.

So a defendant deciding whether to settle or fight a claim that the defendant views as abusive cannot count on the availability of fee shifting to offset the plaintiff's ability to inflict significant litigation costs through the litigation of the case. So the critical question I think is, how does that rational defendant view the ability to recovery attorney's fees if it decides to fight? And where the test is exceptional, that rational defendant has to say my ability to recover attorney's fees is going to be quite low. That is why a change along the lines of the Innovation Act really is essential.

So that ruling confirms the reality that the text of the Patent Act does not authorize the Supreme Court to address the principle factor producing abusive lawsuits, which is the ability of plaintiffs to inflict these huge asymmetric litigation costs on defendants while paying little themselves. That is what allows the coercion of unjustified settlements, and that is what congressional action is needed to address.

Thank you. I look forward to answering your questions.

[The prepared statement of Mr. Pincus follows:]

Statement of Andrew J. Pincus
Partner, Mayer Brown LLP

"Examining Recent Supreme Court Cases in the Patent Arena"

Hearing Before The Subcommittee on Courts,
Intellectual Property, and the Internet
Committee on the Judiciary
U.S. House of Representatives

February 12, 2015

Chairman Issa, Ranking Member Nadler, and members of the Subcommittee.

My name is Andrew Pincus, and I am a partner in the law firm Mayer Brown LLP. I am honored to appear before the Subcommittee today.

A significant part of my law practice focuses on Supreme Court and appellate litigation, including patent litigation. I participated in most of the Supreme Court's recent cases addressing patent issues. From 1997 to 2000, I served as the General Counsel of the United States Department of Commerce, where I was responsible for a number of intellectual property issues.

The Supreme Court's increased focus on patent issues over the past few years has been dramatic. In the ten years from the October 2000 Term through the October 2009 Term, the Court decided 11 patent cases; in the five Terms ending this June the Court will resolve 18 patent cases. The Court's increased attention to patent law is particularly noteworthy because the principal reason the Court grants review of statutory issues—the need to resolve conflicting decisions by different courts of appeals—can never arise in the patent context because of the exclusive jurisdiction exercised by the United States Court of Appeals for the Federal Circuit.

Why is the Supreme Court so concerned about patent law? Most likely because of a variety of factors:

- The increased importance of intellectual property in our knowledge-based economy;

- Changes in the nature of patent litigation—the increased cost of litigation and increased stakes; the assertion of claims by non-practicing entities; and clear evidence that the litigation system is being abused to coerce unjustified settlements;

- Concerns that judicially-created standards governing patent lawsuits are being exploited as a result of the changes in the nature of the litigation; and

- Significant evidence that the Federal Circuit's approach in interpreting the Patent Act differs significantly from the statutory construction principles that the Supreme Court uses to determine the meaning of laws enacted by Congress.

The Supreme Court, of course, does not have free-floating policy authority to address concerns about the patent litigation system—its responsibility is to interpret the statutory text when an issue is brought before it. Some of the Court's decisions have overturned Federal Circuit rulings that promoted abusive litigation. But other Supreme Court decisions have had the opposite effect, increasing the cost and complexity of patent cases. And the effect of some of the Court's decisions remains uncertain.

Most importantly, the text of the Patent Act does not authorize the Court to address the principal factor producing abusive lawsuits: the ability of plaintiffs to inflict huge litigation costs on defendants, while the plaintiffs pay relatively little themselves, even when the underlying claim is meritless—which enables plaintiffs to coerce unjustified settlements. Congressional action is needed to address this critical flaw in the current litigation system.

I. The Problem Of Abusive Patent Litigation

Everyone recognizes that a robust patent litigation system is necessary to ensure that inventors can capture an appropriate share of the value created by their inventions. But a substantial portion of modern patent litigation has little to do with securing appropriate compensation for actual infringement of valid patents. Instead, these lawsuits are brought to extract a cash settlement—not to win at trial. The plaintiff will assert either a patent that is exceptionally weak (and thus likely to be invalidated during the course of litigation) or a tenuous theory of patent infringement unlikely to withstand scrutiny. Plaintiffs bring these suits because very large asymmetrical litigation costs create heavy incentives for defendants to capitulate and settle the lawsuit at a cost that is invariably less than what it would take to defend the action. Plaintiffs therefore have a substantial incentive to assert claims regardless of the underlying merits, because the merits are not likely to be litigated to conclusion, and the plaintiff is likely to obtain a settlement payment that provides a significant profit over and above its cost of litigating the case.

Certainly there can be no doubt that patent litigation is enormously expensive, and the costs are growing. A 2011 survey by the American Intellectual Property Law Association found that the median cost of a medium-sized patent litigation is approximately $6 million dollars per party, double the cost reported in 2009 and four times the cost reported in 2001. Am. Intellectual Prop. Law Ass'n, Report of the Economic Survey 2011, at I-155 to I-156 (2011). These extraordinary expenses enable abusive litigation tactics. "[T]he greatest factor contributing to the existence of nuisance-value patent suits is the high cost of patent litigation." Ranganath Sudarshan, *Nuisance-Value Patent Suits: An Economic Model and Proposal*, 25 Santa Clara Computer & High Tech. L.J. 159, 172 (2009).

The asymmetries in patent litigation costs have three basic causes: **weak pleading standards** that permit a plaintiff to file suit with minimal investigation and no developed theory

of infringement; essentially **one-direction discovery**—the defendant will be forced to shoulder enormous discovery requests, whereas a plaintiff will generally be obliged to provide little or no discovery; and a **low likelihood that a victorious defendant will be able to recover its litigation costs**—because the Patent Act's fee-shifting provision maybe invoked only if a case is "exceptional" and because many plaintiffs would be unable to pay a fee award.

Asymmetrical discovery obligations. To begin with, the discovery costs in a patent dispute are massive and almost entirely one-sided. Abusive patent litigation is often brought by a shell corporation with no meaningful activities or assets other than the patents it asserts. And, in any event, a plaintiff's records are generally irrelevant to infringement contentions. But, particularly in light of broadly-framed infringement complaints, a patent plaintiff will typically seek access to a wide range of the defendant's product-development records, requiring a defendant to undertake time-consuming and costly searches through years of data. Unlike other types of litigation, moreover, dismissals in patent cases rarely occur prior to the *Markman* hearing, but pre-hearing discovery is often permitted and the *Markman* hearing itself inflicts costs on the defendant. This is exactly the kind of situation where "the threat of discovery expense will push cost-conscious defendants to settle even anemic cases before reaching those proceedings." *Bell Atl. Corp.* v. *Twombly*, 550 U.S. 544, 559 (2007).

Weak pleading standards. These enormous discovery costs are compounded by existing Federal Circuit standards that permit a patent lawsuit to proceed with minimal allegations. The Supreme Court has held that "[t]o survive a motion to dismiss, a complaint must contain sufficient factual matter, accepted as true, to 'state a claim to relief that is plausible on its face.'" *Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009) (quoting *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 570 (2007)). But the Federal Circuit expressly exempts patent suits from this pleading standard, holding that the patent plaintiff must allege only that it owns a patent and assert that the defendant is infringing that patent. No additional detail is required—such as *how* a defendant is infringing the patent, much less which particular patent claims are being asserted. As a result, plaintiffs can file meritless infringement suits in an effort to extract settlement value, and defendants have no ready recourse to a motion to dismiss for failure to state a claim—the tool that any other defendant would use in these circumstances.

No realistic possibility of fee-shifting. Lawyers representing patent plaintiffs often operate on contingency, requiring little or no up-front cost to the plaintiff, with the lawyer agreeing to share in any prospective recovery. Defendants, by contrast, must pay defense lawyers for their services on an ongoing basis. While Section 285 of the Patent Act permits a prevailing party to recover fees in "exceptional" cases, recent Supreme Court cases—which I discuss more fully below—make clear that a case is exceptional only if it is unusually weak. Moreover, because district courts now have substantial discretion to decide whether to award fees, district courts that signal a reluctance to shift fees will invariably attract greater proportions of future patent lawsuits from plaintiffs eager to avoid any risk of fee-shifting. Finally, even when a court does shift fees to a plaintiff, the shell-corporation structure of many abusive litigants precludes any meaningful recovery for the defendant. So long as the entity that owns the patent rights holds no other assets, patent plaintiffs can effectively render themselves judgment proof.

A recent White House report recognized that these asymmetries enable the filing of abusive claims. Patent owners may seek "to settle out of court for amounts that have not so much to do with the economic value of their patents or the probability that they have infringed;" rather, settlements are "affected more by the parties' relative opportunity costs of going to trial and attitudes towards risk." Executive Office of the President, *Patent Assertion & U.S. Innovation*, at 6 (2013), http://tinyurl.com/lvk6ajl. When parties face asymmetrical costs—such as when plaintiffs have lower costs than defendants—they may "have an incentive to drag out litigation, to increase pressure on defendants to settle the case." *Id.*

At bottom, the result is clear: a rational defendant will—absent a reliable fee-shifting mechanism—agree to settle a suit *whenever* the settlement offer is less than the cost to defend against the suit. Thus, it is basic economics that *whenever* a plaintiff's out-of-pocket expenses (i.e., the cost of acquiring the relevant patents, the filing fee, and cost of the plaintiff's lawyer) are less than the likely cost of a defense, an economically rational plaintiff will file suit, and an economically rational defendant will settle. *See* David Rosenberg & Steven Shavell, *A Model in Which Suits Are Brought for Their Nuisance Value*, 5 Int'l R. of L. & Econ. 3 (1985); Sudarshan, 25 Santa Clara Computer & High Tech. L.J. at 161-169. The current asymmetries thus permit plaintiffs to effectuate naked wealth transfers under the guise of patent litigation.

The impact of patent lawsuits "on smaller startups is particularly acute." *Patent Assertion & U.S. Innovation*, *supra*, at 10. One survey indicates that, over an approximately six-year period, roughly 66% of unique patent defendants are firms with annual revenue of less than $100 million. Colleen V. Chien, *Startups & Patent Trolls*, Santa Clara Univ. Legal Studies Research Paper No. 09-12, at 1-2 (Sept. 28, 2012). Forty percent of companies sued represented that the lawsuit caused a "significant operational impact," such as "delayed hiring or achievement of another milestone, change in the product, a pivot in business strategy, a shut-down business line or the entire business, and/or lost valuation." *Id.* at 2. Commentators have thus noted that "small companies—not tech giants—are the predominant targets" in certain abusive lawsuits. Brian J. Love & James C. Yoon, *Expanding Patent Law's Customer Suit Exception*, 93 B.U. L. Rev. 1605, 1611 (2013).

A recent survey of venture capitalists confirms this conclusion. Seventy percent of venture capitalists have portfolio companies that have received patent demands, and roughly one in three startup companies report receiving such demands. The overwhelming majority of venture capitalists and startup companies "report that patent demands had a significant impact on a company." Robin Feldman, *Patent Demands & Startup Companies: The View from the Venture Capital Community*, at 2.

II. Recent Supreme Court Decisions

Some of the Court's decisions in its last Term and during the Term now underway have eliminated legal rules that promoted abusive litigation. Yet other decisions—including an important decision this Term—will *increase* the cost of patent litigation, creating new opportunities for patent plaintiffs to extract settlements based on nothing more than the cost of defense that they can inflict simply by filing suit.

A. Steps by the Supreme Court that restore some balance to patent litigation.

In three different areas—standards for determining whether a patent is sufficiently definite, induced infringement, and so-called "divided" patent infringement—Supreme Court decisions will aid in deterring patent plaintiffs from employing certain abusive tactics.

Indefiniteness: *Nautilus.*

Section 112 of the Patent Act requires patent claims to, among other things, "particularly point[] out and distinctly claim[] the subject matter which the applicant regards as [the] invention." A patent claim that fails to provide sufficient definiteness is invalid; for example, the claim may not specify a particular result without explaining the steps necessary to achieve that result.

The question in *Nautilus, Inc. v. Biosig Instruments, Inc.*, 134 S. Ct. 2120 (2014), was whether the Federal Circuit was correct in holding that a patent claim fails the definiteness requirement "only when it is 'not amenable to construction' or 'insolubly ambiguous.'" This amorphous test significantly reduced the impact of the definiteness requirement by salvaging vague and highly ambiguous claims.

The Supreme Court rejected the Federal Circuit test, concluding instead that "a patent is invalid for indefiniteness if its claims, read in light of the specification delineating the patent, and the prosecution history, fail to inform, with reasonable certainty, those skilled in the art about the scope of the invention." *Id.* at 2124. By providing the lower courts with an appropriate, more restrictive standard for definiteness under Section 112, the Supreme Court's decision will enhance patent quality, an essential antidote to abusive patent litigation.

Induced Infringement: *Global-Tech Appliances.*

The Patent Act imposes liability on a person who induces another to infringe. 35 U.S.C. § 271(b). Inducement liability is important in a number of circumstances; it may, for example, provide a means to bring a patent infringement suit against manufacturers operating outside the United States, who sell products knowing that it will be used to infringe a patent within the United States. Inducement claims are also brought against companies that know their products will be used by customers in a way that infringes a patent. One common form of abusive patent claims is a lawsuit against the manufacturer of a component, asserting that the component supplier knew—or should have known—that its products would later be used by a *different* manufacturer in a way that infringes a patent.

It has long been established that an induced infringement claim requires a plaintiff to prove that a defendant acted with some degree of knowledge that its acts were inducing patent infringement. The Federal Circuit, however, had watered down this requirement, finding it sufficient for a plaintiff to demonstrate that a defendant was merely deliberately indifferent to the possibility of patent infringement.

In *Global-Tech Appliances, Inc. v. SEB S.A.*, 131 S. Ct. 2060, 2068 (2011), the Supreme Court reversed, holding that induced infringement turns on a showing that the defendant actually

knew "that the induced acts constitute patent infringement." Absent such knowledge—or the legal equivalent, that a defendant engaged in affirmative conduct to willfully blind itself to the relevant facts—induced infringement is not available. This holding eliminates the ability of plaintiffs to assert tenuous inducement theories against multiple stages of a manufacturing chain.

Commil USA, LLC v. Cisco Systems, Inc., No. 13-896, currently pending at the Supreme Court, poses an important issue subsequent to *Global-Tech*: whether a defendant's good-faith belief that a patent is invalid is a defense to patent infringement. Applying *Global-Tech*, the Federal Circuit held that such a good-faith belief *does* defeat the knowledge required for an induced infringement claim. But the federal government has taken the position that patent *validity* and patent *infringement* are two separate questions, meaning that a good-faith belief that a patent is invalid does *not* provide a defense to an induced infringement claim.

Affirming the result reached by the Federal Circuit—that a good-faith belief in invalidity *does* pose a defense to infringement—will aid in foreclosing low-merit, abusive patent suits. Indeed, what typically renders such lawsuits meritless is that the patent asserted is of exceptionally low quality. When a manufacturer has a reasonable basis to believe that a patent is invalid, it lacks the requisite knowledge that it is inducing others to infringe. If the Supreme Court were to agree with the government's contrary submission, it would embolden those who assert patents of dubious validity.

"Divided" Infringement: *Limelight Networks.*

Last Term, in *Limelight Networks, Inc. v. Akamai Technologies, Inc.*, 134 S. Ct. 2111 (2014), the Court confronted a different question with respect to induced infringement—whether a party may be held liable for inducing infringement when no single party completed every step of a method patent necessary for *direct* patent infringement. The *en banc* Federal Circuit had concluded that a defendant could be liable for induced infringement pursuant to Section 271(b) so long as the defendant carried out some steps constituting a method patent and encouraged others to complete the remaining steps, even if no one person or entity would be liable as a direct infringer. This decision provided an incentive for plaintiffs to cobble together tenuous theories of patent infringement, asserting that multiple different parties joined together to infringe a single method. The Supreme Court rejected the Federal Circuit approach, however, concluding that induced infringement turns on a demonstration that *direct* infringement occurred.

Attorneys' Fees: *Highmark & Octane.*

As mentioned above, Section 285 of the Patent Act provides that a court may require the losing party to pay the prevailing party's attorneys' fees only in an "exceptional" case. The Federal Circuit had interpreted the statute to mean that, absent unusual circumstances, a case could qualify as exceptional only if a defendant could show that a plaintiff brought a lawsuit in subjective bad faith *and* the litigation was objectively baseless.

In *Octane Fitness, LLC v. ICON Health & Fitness, Inc.*, 134 S. Ct. 1749, 1756 (2014), the Supreme Court held that this standard was too restrictive, concluding instead that a court must determine whether the case is one that "stands out from others with respect to the substantive strength of a party's litigating position … or the unreasonable manner in which the

case was litigated." At the same time, the Court concluded in *Highmark Inc. v. Allcare Health Mgmt. Sys., Inc.*, 134 S. Ct. 1744, 1746 (2014), that the Federal Circuit must defer to a district court's decision under Section 285, reviewing it only for abuse of discretion.

Octane and *Highmark* together give district courts more discretion to award fees. But the "exceptional" requirement in Section 285, the Supreme Court confirmed, means that fee shifting is an option only in a small minority of cases. A defendant deciding whether to settle or fight, therefore, cannot count on the availability of a mechanism to offset the plaintiff's ability to inflict significant litigation costs on defendants—which is the key characteristic of patent litigation that plaintiffs exploit to coerce settlement. A rational defendant therefore is still likely to view settlement as the economically sensible option.

B. Decisions *increasing* litigation costs.

On the other hand, some decisions of the Supreme Court will have the effect of increasing the costs of patent litigation and thereby creating greater leverage for plaintiffs to unfairly extract nuisance-value settlements.

Claim Construction: *Teva Pharmaceuticals.*

A critical step in virtually every patent dispute is interpreting the meaning of the words used in patent claims—such "claim construction" will often control whether a patent is valid (such as whether it is novel and non-obvious), as well as whether the defendant infringes the patent claims. To construe a patent claim, a court may consider the language of the patent claims themselves, the patent's specifications, and the prosecution record (all of which is referred to as "intrinsic" evidence) as well as certain "extrinsic" evidence, including expert testimony. Because claim construction is a task for a judge, it takes place following a so-called "*Markman* Hearing" at which the relevant evidence is put before the judge.

The Federal Circuit had long held that it reviews *all* aspects of claim construction *de novo*, including those "extrinsic" issues which turn on a resolution of factual disputes.

In *Teva Pharmaceuticals USA, Inc. v. Sandoz, Inc.*, 135 S. Ct. 831 (2015), the Supreme Court reversed, holding that Federal Rule of Civil Procedure 52(a)(6) requires a "clearly erroneous" standard of review with respect to such factual determinations by a district court. The Supreme Court seems to have been motivated, at least in part, by the Federal Circuit's high reversal rate of claim construction orders.

Teva Pharmaceuticals may, however, have a significant consequence on litigation costs. Previously, introduction of expert testimony in the course of a *Markman* hearing was relatively rare. Often, a case could complete the claim construction phase—and perhaps even reach a determination of non-infringement—*without* any need for expert testimony. But *Teva Pharmaceuticals* will likely be read by some district courts as an implicit endorsement of reliance upon expert testimony and other "extrinsic" evidence in the course of claim construction, as district courts may increasingly ground their claim construction orders in the resolution of factual disputes in order to insulate them from *de novo* review.

Following the Supreme Court's decision, parties are substantially rethinking the role of experts in *Markman* hearings. The likely outcome is that the "war of experts" will begin much earlier in patent litigation. The resulting increased costs will often inure to the benefit of patent plaintiffs, who will have yet another cost burden to exploit in order to increase the settlement pressure on the defendant.

Standard of Proof for Patent Invalidity: *Microsoft Corp. v. i4i Ltd. P'ship*.

The Supreme Court missed another opportunity to reduce the costs associated with patent litigation in *Microsoft Corp. v. i4i Ltd. P'ship*, 131 S. Ct. 2238 (2011). In the course of patent litigation, the defendant often challenges the asserted patent's validity; a litigant may contend, for example, that a patent is invalid because it lacks novelty or is obvious. In *i4i*, the Supreme Court agreed to review the standard of proof a party must satisfy in order to demonstrate, in the course of litigation, that a patent is invalid. In a divided opinion, the Supreme Court affirmed the approach long taken by a Federal Circuit—that a litigant must demonstrate a patent is invalid by "clear and convincing evidence."

The result of *i4i* is that there is a heavy thumb on the scale in favor of granted patents—even in circumstances, such as those present in *i4i*, where the prior art most relevant to the novelty or obviousness inquiry was never put before the PTO. Given that the scope of permissible prior art is enormous—an unpublished doctoral thesis available only in the library of Freiburg University was subsequently found to invalidate a granted patent (*In re Hall*, 781 F.2d 897, 899-900 (Fed. Cir. 1986))—the PTO often does not examine the most relevant prior art. This built-in advantage for the patent plaintiff creates enhanced risk for defendants who wish to defend against a patent claim, creating yet more pressure for defendants to settle dubious lawsuits.

C. The impact of some Supreme Court decisions is not yet clear.

The Supreme Court has also recently been active in defining the scope of subject matter that is patent eligible pursuant to Section 101 of the Patent Act. The Court has long held that certain subject matter—abstract ideas, laws of nature, and physical phenomena—are exempt from patent protection, because they constitute the basic building blocks of innovation.

Last year, in *Alice Corp. Pty. v. CLS Bank Int'l*, 134 S. Ct. 2347 (2014), the Supreme Court held ineligible claims directed to computer software for electronic, intermediated financial settlements. The Court concluded that the claims merely implemented, via computer, a long prevalent, fundamental economic practice. In other words, taking a basic business concept and saying "implement it on a computer" without any specificity regarding how to do so did not provide a sufficient limitation on the abstract idea to render it patent eligible.

In the aftermath of *Alice Corp.*, courts around the country are continuing to assess the scope of patentable subject matter as it relates to computer software. While it is likely too early to assess the full implications of *Alice Corp.*, a few lessons have emerged.

First, there is no serious doubt that software, as a general matter, is eligible for patent protection. Software innovation has provided a key engine of economic growth over the past

decade, the Supreme Court and Federal Circuit have upheld software patents, and no court has even suggested that software is outside the scope of the Patent Act. Instead, the critical question is how precisely to calibrate protections for software innovation.

Second, the lower courts are finding application of the Supreme Court's eligibility test very challenging in practice. The Court stated that although an abstract idea or law of nature itself cannot be patented, the practical application of such an idea or law will generally be patentable. Unfortunately, the Court did not provide clear guidance on how to distinguish between an idea and its application, stating only that the invention must add enough to the abstract idea to ensure that it amounts to "significantly more" than the idea itself. Currently, there is little consensus in the lower courts regarding what is necessary to satisfy this "significantly more" standard, but several potential approaches have emerged. Perhaps the most promising focuses on evaluating the extent that a software innovation enhances the functioning of a computer system. When a software innovation creates a solution to a particular technical problem—rather than just implementing an offline idea digitally—it is likely to satisfy the Section 101 requirement.

Third, although Section 101 plays a partial function in screening out weak and abusive patent suits, other requirements in the Patent Act—that a patent must be novel (Section 102), non-obvious (Section 103), and sufficiently definite (Section 112)—often will provide more appropriate and substantial protections for defendants against meritless patent suits. So, too, does an early and effective means for a defendant to demonstrate that it does not infringe the patent claims.

The Federal Circuit now has before it cases that will require the court to flesh out the standard adopted by the Supreme Court in *Alice*.

III. The Need For Congressional Reform

Although the Supreme Court has taken some steps to correct the imbalanced incentives in patent litigation, the courts are powerless to alter certain structural obstacles to restoring parity between patent plaintiffs and patent defendants. Action by Congress is necessary to address the asymmetries that drive abusive litigation. These reforms should include:

- **Addressing large and asymmetric discovery costs:** One of the most substantial asymmetries imposed by patent plaintiffs is forcing massive amounts of costly discovery early in a litigation. Currently, discovery often proceeds parallel to, or even in advance of, the district court's claim construction and its determination of dispositive motions—such as whether asserted patent claims are valid. But the court's resolution of claim construction and validity contentions often may conclude the lawsuit, obviating the need for discovery. Alternatively, the claim construction decision can significantly narrow the scope of the dispute, reducing the volume of discovery needed. Requiring discovery to proceed in stages, and permitting only limited discovery relating to the particular issue before the district, will reduce this cost burden. Another approach to consider is requiring the party seeking discovery to bear the costs of obtaining the information when its discovery requests range beyond the core issues in the case.

- **Tightening pleading standards:** Applying to patent cases the pleading standards that govern other categories of litigation will require plaintiffs to explain their theories of infringement. Not only does such a requirement force plaintiffs to undertake an appropriate pre-suit investigation, but specifying a clear theory of liability will reduce a defendant's cost of defending a suit by constraining the scope of discovery and making it easier for defendants to identify and rebut abusive claims.

- **Ensuring that judges have the power to utilize fee-shifting in appropriate cases:** Revising Section 285 to give judges the authority to impose fee-shifting on plaintiffs who institute abusive cases will give patent plaintiffs a strong monetary incentive to self-police the quality of the litigation that they initiate.

Thank you for the opportunity to appear before the Subcommittee. I look forward to answering your questions.

Mr. ISSA. Thank you.

Mr. Taylor? I think we cannot quite hear you yet.

TESTIMONY OF ROBERT P. TAYLOR, COUNSEL, NATIONAL VENTURE CAPITAL ASSOCIATION, WASHINGTON, DC

Mr. TAYLOR. I am Robert Taylor appearing for the National Venture Capital Association. NVCA represents approximately 400 venture capital firms that collectively account for the vast bulk of all venture capital invested in this country.

Let me stress three basic points. First, strong protection of intellectual property allows entrepreneurs and investors to assume the risks necessary to commercialize breakthrough technologies. Despite the fact that a few companies may not rely on patent protection, for the great majority of startups, patents are essential to their existence and survival.

Second, although people are justifiably offended by abuses of the legal system, it is important to ensure that efforts to correct that problem do not cause more damage to innovation than does the problem itself. NVCA strongly urges Congress to direct its efforts at improper behavior, not at the patent system. Innovation requires a healthy patent system, including the ability of innovators to enforce their patents without undue risk and expense.

Third, recent activity at the Supreme Court, the Federal Trade Commission, the Judicial Conference, and the Patent Office pursuant to the AIA has changed the patent landscape in important ways that already address most of the problems to which H.R. 9 is directed. As a result of these changes, new patent case filings dropped 18 percent between 2013 and 2014, and the full effect of those developments has yet to be felt.

Let me expand a little. For decades innovative new companies have been the most important source of job growth in this country. Creating a new company requires entrepreneurs willing to forego job security to pursue a vision for a better future. It requires investors willing to share that vision and to dedicate time and money to make it a reality. The process is fraught with considerable risk.

Several years ago I represented a small company that pioneered a revolutionary advance in minimally invasive surgery, surely the type of innovation we should encourage. As soon as that company showed its products to surgeons, however, large companies that sold surgical equipment began to copy the design, modify their own tools, and bundle their sales in ways that foreclosed my client from the market. The company spent nearly 5 years in scorched earth patent litigation with corporate giants to enforce its patents and stay in business, but ultimately it prevailed.

For the vast majority of innovative startups like that client, patents are the only way to ensure a return on investments sufficient to justify the risks involved. This group includes companies developing digital technologies that employ innovative hardware and software, energy companies, communication technologies, new polymers and metallurgical products, information technologies, medical devices, biologics, and pharmaceuticals.

My second point. H.R. 9 will make patent litigation more cumbersome, more expensive, and more risky for litigants on both sides. Importantly, this will impact smaller companies much more

than their larger and better-funded competitors, irrespective of which side each is on. And for innovators, the ability to enforce patents at reasonable cost and risk is an essential part of the patent right. Patents that companies cannot afford to enforce become nothing but wall decorations, and when incumbents perceive that a new entrant is unable to or unwilling to enforce its patents, the temptation to copy becomes irresistible. For venture capital firms themselves, the transparency and joinder provisions of H.R. 9 present serious problems.

My third point. My written testimony describes a number of actions by courts and Federal agencies that are creating a sea change in patent law that is already responding to much of what H.R. 9 targets. A series of Supreme Court decisions alone has made it much easier for companies to defend against meritless patent cases, including the ones that others have already referred to. Other changes are equally significant. The abolition of Form 18 is going to bring patent pleading in line with other Federal litigation. The FTC has taken on the challenge of abusive demand letters, and the AIA is having a major impact.

My closing point. The entrepreneurial drive to pursue new visions has been a bedrock feature of American culture for decades and has largely been responsible for our remarkable success as a Nation. The patent system is essential to protect the innovative spirit that pervades our national character. It would be tragic if this Congress, in the misguided belief that H.R. 9 will promote innovation, made it more risky and expensive for our most promising companies to protect themselves and their technology.

Thank you.

[The prepared statement of Mr. Taylor follows:]

Submission for the Record
Statement of Robert P. Taylor
House Subcommittee on the Courts, Intellectual Property, and the Internet
February 12, 2015

My name is Robert Taylor. I am the founder and owner of RPT Legal Strategies PC, an intellectual property consulting firm in San Francisco and Silicon Valley. For more than 30 years, I have been heavily involved in patent litigation, serving as lead trial and appellate counsel for both patent owners and companies accused of infringement. My clients have included companies of all sizes from Fortune 100 companies to start-ups, and my cases have dealt with a wide spectrum of technologies and industries. For the past 10 years, I also have counseled venture capital firms and many of the start-up companies in which they invest with respect to patent and litigation issues.

I am appearing here on behalf of the National Venture Capital Association ("NVCA"), which represents approximately 400 venture capital firms accounting for a large percentage of all venture capital invested in this country each year. NVCA wishes to express its thanks for an opportunity to be heard with respect to the pending patent legislation. One of NVCA's most important roles is to assist Congress in understanding how new legislation is likely to affect the venture capital industry, emerging growth companies, and the process of innovation in America.

Throughout the American economy, innovators large and small ranging from universities and non-profit foundations, to start-ups and small businesses, to manufacturing, technology, and life science companies, are critically dependent on patents to protect and recoup their investments of time, money, and other resources in research and development. These organizations understand that domestic job growth and our competitive advantage in the global economy depend on a strong patent system that creates incentives for invention and protects inventors from unfair copying and imitation by others.

Let me say frankly at the outset, we are concerned that H.R. 9, if enacted as written, will have a chilling effect on investment in patent intensive companies, which in turn will have a depressing effect on innovation in general. At the very least, the legislation will make it far more difficult, risky and expensive for emerging companies to enforce their patents, which is an essential part of the patent right. Equally important,

H.R. 9 also will raise the cost and risk confronting smaller companies trying to defend against patent litigation brought by their larger, incumbent competitors.

Many argue, correctly we believe, that much of the perceived need for legislation to address abusive litigation practices already is being dealt with effectively by the Supreme Court, U.S. Patent & Trademark Office ("PTO") and Federal Trade Commission (FTC), all of which are discussed in greater detail below. Nevertheless, if Congress still sees a need to address the problem of abusive behavior by certain patent litigants, NVCA strongly believes that any new legislation should focus on specific behavior, not on the procedural aspects of enforcing patents.

Innovation does not take place in a vacuum. It requires entrepreneurs willing to devote time and resources to pursue visions and new ideas. It requires investors willing to invest time and money in developing those innovative new ideas. Venture capitalists work closely with entrepreneurs and innovators to transform breakthrough ideas into emerging growth companies that drive U.S. job creation and economic growth. Almost all venture capital investing involves risk, and usually the more innovative and disruptive a breakthrough idea, the greater the risk facing those who would commercialize it. For thousands of companies across the United States, patents are the *only* way to ensure a return on investment sufficient to justify the risks involved in making such investments.

NVCA recognizes that some companies have business models in which intellectual property, such as patents, does not play a particularly significant role. For many older and well-established companies, for example, their size alone may provide better protection for their markets and investments than do their patents. For thousands of other companies, however, patents are the only way to insure a return on investment sufficient to justify the risks involved. This group includes companies developing digital technologies that employ innovative hardware and/or software, energy technologies, communication technologies, new polymers and metallurgical materials, information technologies, medical devices, biologics and pharmaceuticals. For these companies, a highly structured and rigid approach to patent enforcement is likely to have unintended and unforeseeable consequences.

Enforceability is the essence of the patent right. A patent that cannot or will not be enforced is useless. A patent that others believe will not be enforced has no deterrent

effect on imitation of innovative products by incumbents. In this light, making it more difficult and costly to enforce patents in order to combat abusive litigation will have the unintended consequence of diminishing—if not extinguishing—the only true incentive that thousands of innovators presently have to invest the necessary time, money and other resources needed to create a new company from scratch. Put differently, the patent-backed right to own and profit from innovative ideas has been a major driving force for the American economy for 200 years, and that right requires that valid patents be fully enforceable in court at reasonable expense and without undue risk to the patent owner or its investors.

The Resurgence of Patent Cases at the Supreme Court.

In recent years, the Supreme Court has rekindled its interest in patent law. After a period of relative neglect following the 1982 creation of the Court of Appeals for the Federal Circuit, the Supreme Court in the last few years has begun tackling some of the most important issues defining the patent system. We are only halfway through the present decade and the Court already has decided more patent cases since 2010 than in the entire 1980s and 1990s combined.[1] The Court heard six patent cases last year and will hear more this year. The Court has plainly recognized the important role that patents play in our technological driven economy.

As a result of Supreme Court's decisions and the America Invents Act that became law in 2011, the patent landscape looks far different today than it did five years ago or even last year. New patent case filings in 2014 dropped 18 percent from 2013, as the full impact of judicial decisions and administrative developments began to be felt.

Fee Shifting.

Perhaps the most significant rulings of the past year were the two Supreme Court decisions in *Octane Fitness v. iCON Health & Fitness*[2] and *Highmark v. Allcare Health*

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[1] Dennis Crouch, Supreme Court Patent Cases per Decade, http://patentlyo.com/patent/2014/07/supreme-patent-decade.html.

[2] 134 S.Ct. 1749 (2014).

Management System[3], wherein the Court construed Section 285 of the Patent Act and allowed prevailing parties in patent litigation to recover their costs and their lawyer and expert witness fees from the losing party. In the two rulings, the Supreme Court was critical of the restrictive approach to fee shifting taken by the Federal Circuit, particularly in cases where the district judge had made a determination that the prevailing party seeking fees had met the existing statutory standard for what constitutes an "exceptional case."

The Supreme Court held that whether to shift fees under Section 285 is a matter that resides in the sound discretion of the district judge and is reviewable by the Federal Circuit only for abuse of discretion, not the *de novo* review the Federal Circuit had been using. Further, the Court held – contrary to the Federal Circuit rule – that a prevailing party need not establish its entitlement to fees by "clear and convincing" evidence, but only by a "preponderance of the evidence," a significantly reduced burden to meet in this context.

Finally, and perhaps most importantly, the Supreme Court overturned the Federal Circuit rule that a case is exceptional only if the position of the nonprevailing party is both objectively and subjectively baseless, holding instead that a "totality of circumstances" test should be used to determine exceptionality. The Court held that the baselessness tests were too rigid and that district judges should have the discretion to award fees in a case that simply "stands out" from other case in terms of its substantive strength.

These rulings have already had a significant impact on the use of fee shifting to force the parties in patent litigation to take positions that have some probability of success. It is likely to have particular impact in cases where nonpracticing entities attempt to assert weak or frivolous patents.

Patent-Eligible Subject Matter.

One of the major complaints about patent litigation affecting the business community has centered on the large number of so-called "business method" patents in

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[3] 134 S.Ct. 1744 (2014).

which the claimed "invention" was no more than the use of a computer to carry out a long established commercial practice. In *Alice Corporation v. CLS Bank*[4], the Court held that a computer implementation of a well-established commercial practice is not patentable. The case involved a patent claiming a computerized method for settling financial transactions using a stakeholder. The decision casts considerable doubt on the validity of dozens of business method patents that were issued by the PTO during the last 15 years.

In the aftermath of *Alice Corp.*, there has also been a significant increase in the number of patents that have been invalidated in the lower court for lack of patent-eligible subject matter. In the four months following the *Alice Corp.* decision, 18 federal court rulings have relied on that decision to decide patentability cases, and in 14 of such cases (*i.e.*, 78 percent), the court invalidated the patent claim in question.[5] Moreover, the lower courts appear to be reading *Alice Corp.* to hold that subject matter eligibility can decided at an early stage of litigation, without the need for costly discovery or claim construction.[6]

We are already seeing evidence of this. In 2014, more than a dozen motions to dismiss and motions for judgment on the pleadings were granted finding that the patents-in-suit were not directed to patent-eligible subject matter. Such motions are being granted in districts across the country, including such traditionally plaintiff-friendly venues as the Eastern District of Texas. Therefore, a motion for an early determination that a patent is not directed to patentable subject matter will likely prove to be a powerful new tool to dispose quickly and cheaply of meritless, abusive lawsuits.

Nor is *Alice Corp.* the only effort by the Supreme Court to narrow the range of subject matter that may be patented. Three other cases since 2004 have also dealt with patent eligibility, each of them narrowing the scope of what is patentable: *Bilski v.*

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[4] 134 S.Ct. 2347 (2014).

[5] B. McCall, Lessons from 4 Months of Post-Alice Decisions, LAW360, Oct. 31, 2014, available at http://www.law360.com/articles/590465/lessons-from-4-months-of-post-alice-decisions.

[6] *See I/P Engine, Inc. v. AOL Inc.*, 576 Fed. App'x 982, 996 (Fed. Cir. 2014) (Mayer, J. concurring).

Kappos[7], *Mayo Collaborative Services v. Prometheus Laboratories, Inc.*[8], and *Association for Molecular Pathology v. Myriad Genetics, Inc.*[9] *Bilski* was another business method patent involving the use of computers to hedge risk; the Court held that the method was not patentable subject matter. In *Myriad*, the Court held that naturally occurring DNA sequences are not patentable. In *Mayo*, the Court held that a diagnostic process that merely measured the human body's response to a drug was ineligible for patent protection.

Collectively, these cases are refocusing the entire federal judiciary on the basic objective of the patent system to protect specific categories of subject matter and nothing else. They are having a clear impact on the types of patent cases that are likely to be brought in the future.

Indefiniteness.

Another significant complaint that defendants have raised about patents in recent years has been that the claims are vague and therefore the "invention" was too difficult to identify. In *Nautilus, Inc. v. Biosig Instruments, Inc.*[10], the Supreme Court addressed the proper test for determining whether claim language is "indefinite" to the point that it fails to satisfy 35 U.S.C. § 112, ¶ 2. That statutory provision requires a patent owner to set forth claims that "particularly point out and distinctly claim" the invention, thus requiring patent applicants to differentiate their own inventions from the prior art and from the public domain so that members of the public are properly apprised as to what areas of endeavor are foreclosed by the patent.

Prior to the ruling in *Nautilus,* the Federal Circuit provided that a claim is indefinite only if it is "not amenable to construction" or "insolubly ambiguous."[11] The Supreme Court, in a unanimous opinion, held that such test does not adequately inform the public as to the boundaries of a patent claim. Noting that a patent draftsman may

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[7] 561 U.S. 593 (2010).

[8] 132 S.Ct. 1289 (2012).

[9] 133 S. Ct. 2107 (2013).

[10] 134 S. Ct. 2120 (2014).

[11] *Datamize, LLC v. Plumtree Software, Inc.*, 417 F.3d 1342, 1347 (Fed. Cir. 2005).

have a compelling incentive to write claims that are ambiguous and that the draftsman also is in the best position to avoid such ambiguities, the Court held that patent claims will be held invalid for indefiniteness if persons skilled in the art, after reading the patent specification and the claims, is unable to know with reasonable certainty what the invention is.

Nautilus will have a significant impact on the ability of patent owners to assert casually that a product or service is covered by a patent merely because a claim can be read in that fashion without regard to what it actually was intended to cover. Equally important is that *Nautilus*, when combined with the fee-shifting rules laid out in *Octane* and *Highmark*, will make it far more risky for patent owners to take absurd positions in litigation merely to promote unfair settlements.

Pleading Standards.

Notice pleading has been the normal practice in this country for decades. A complaint was required to put the defendant on notice of the general nature of the claims asserted and little else. An answer to a complaint needed only to apprise the plaintiff of the general nature of defenses likely to be asserted. Independently of patent litigation, that practice is being replaced with a more demanding form of complaint and answer. In *Bell Atlantic Corp. v. Twombly*[12] and *Ashcroft v. Iqbal*,[13] the Supreme Court imposed a higher pleading standard in most civil cases. A complaint "must contain sufficient factual matter ... to 'state a claim to relief that is plausible on its face.'"[14]

The Federal Circuit has held that *Twombly* and *Iqbal* do not apply to cases alleging only direct patent infringement,[15] reasoning that Form 18 appended to the Federal Rules of Civil Procedure is controlling. Form 18 requires little more than that the plaintiff identify the patents-in-suit and a broad category of products that are alleged

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[12] 550 U.S. 544 (2007).

[13] 556 U.S. 662 (2009).

[14] *Iqbal*, 556 U.S. at 678 (quoting *Twombly*, 550 U.S. at 556).

[15] *R&L Carriers v. Driver Tech LLC*, 681 F.3d 1323 (Fed. Cir. 2012).

to infringe.[16] The Federal Circuit has, however, expressed its disapproval of Form 18 and has urged its removal from the Federal Rules. In response, the Judicial Conference has proposed amendments to the Federal Rules that would do so. The amendments are currently pending before the Supreme Court. The amended rules, assuming they are approved, will take effect in December, at which point *Twombly* and *Iqbal* will apply to all patent cases.

***Inter Partes* Review (IPR) Under the America Invents Act.**

Another of the complaints about patent litigation is the high cost of getting to a final resolution, which is particularly significant where the patent is ultimately held to be invalid in light of prior art that was not before the PTO. An alternative procedure for determining patent validity in such cases was created by the Leahy-Smith America Invents Act (AIA), which became law in late 2011. The *inter partes* review procedure allows a challenger to contest the validity of a patent within the PTO, which is a much faster and cheaper way to test its validity than doing so in court. Although the AIA took a couple of years for full implementation, its impact is now clear and significant. Since its implementation in 2013, more than 2400 IPR petitions have been filed. The PTO has initiated a review in approximately 80 percent of the cases where one was requested. Among the cases that reached a merits decision, the PTO has rejected some or all of the challenged claims approximately 75 percent of the time.

IPR reviews have greatly reduced the burdens on courts. When a defendant files an IPR petition against a patent that has been asserted in litigation and the PTO agrees to initiate a review, the district court will often stay the case, depending on the stage of the litigation. Regardless of outcome, the *inter partes* review will usually simplify the issues for trial. If the patent claims are rejected on review, then the IPR may dispose of the litigation entirely. Moreover, where the claims survive the review, the petitioner is estopped from further challenging the invalidity of the patent at trial on any ground that was raised or reasonably could have been raised as part of the IPR.[17]

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[16] Fed. R. Civ. P. Form 18.

[17] *See* 35 U.S.C. § 315(e)(2).

Inter partes review has proven to be especially effective against nonpracticing entities, because such proceedings are faster and far cheaper than litigation to get resolution of the same essential issues a court would otherwise decide. *Inter partes* review is therefore an effective means for an accused infringer to defend itself against an abusive lawsuit.

Federal Trade Commission and Demand Letters

Another complaint that surfaces about the current state of patent litigation is that some patent owners have sent abusive or deceptive letters to companies that they believe are infringing their patent rights. The FTC and some state attorneys general have weighed into this practice, using the power of their offices protect small businesses and consumers from what they consider to be improper practices.

Abusive demand letters is one area where additional legislation may be useful. The Targeting Rogue and Abusive Letters (TROL) Act, which passed the House Energy and Commerce Subcommittee on Commerce, Manufacturing, and Trade in July, would strengthen FTC and state authority to combat abusive demand letters.

Conclusion.

Innovation has been a fundamental driving force for the American economy for decades, but at no time has this been truer than in the past 25 or 30 years – a period in which our economy has literally exploded with innovative machines, tools, chemicals, drugs, medical devices and procedures, forms of communication and much, much more. It is no coincidence that this most dynamic period in the growth of American economic strength has occurred at a time when respect for patents and patent enforcement was at its highest point in nearly a century. Patents are critical to innovation in many industries and a company's ability to enforce its patents at reasonable expense and risk is an essential element of such rights.

If this Congress chooses to move forward with legislation, NVCA hopes it will bear in mind the strong correlation between patents and investment so that innovative start-ups and emerging companies in all sectors of our economy will continue to thrive. In assessing the need for legislation, we encourage Congress to consider carefully the impact of recent developments in the federal courts, at the PTO and at the Federal Trade

Commission, all of which collectively have reduced significantly the number of new patent cases and promise to reduce them even further as the full impact of those developments begins to be felt. NVCA looks forward to working with this Committee and other members of the Congress on any such legislation.

Mr. ISSA. Thank you. I will now recognize myself for a 5-minute round of questioning. Mr. Taylor, what was the name of the company that spent 5 years trying to defend its right, ultimately prevailed?

Mr. TAYLOR. I was not involved for the full 5 years. The company was Applied Medical Systems.

Mr. ISSA. They have my sympathies because, in fact, the clod slow difficult system to enforce your patents is exactly what this bill is intending to fix.

Mr. Gupta, in the case of a major part of this legislation, the heightened pleading was followed by the early Markman in order to discover what the patent is and provide both sides a good faith understanding of what the patent really means and how it might apply to the product in question. Does that, in your opinion, and I will go to each of you, get you to many resolutions, some unclogging of the system, and ultimately an opportunity for people who in good faith want to end up with an ultimate outcome, to get there at lower cost?

Mr. GUPTA. Thank you, Mr. Chairman. Yes, I agree——

Mr. ISSA. I love it when someone says "yes" first. Please.

Mr. GUPTA. The Innovation Act, in my mind, has balanced provisions that are designed to make the litigation process much more efficient than it is today. We are in court today in a Markman hearing. The plaintiff asserted eight patents against us, accusing two major product lines. The complaint did not identify any of the hundreds of claims involved in the patents, did not identify any model numbers. 3 months later, they added three additional patents to bring it up 11 patents, another product, no model numbers. 8 months into the litigation, they gave us some claim charts and some claims. 12 months into the litigation, they attempted to add even more claims that were not announced previously and new products, and the Markman was about a month after. They attempted to add new claims again.

So it is an extremely cumbersome process for defendants when plaintiffs do not identify exactly what product, what claims, and how the infringement is being argued. And, more importantly, the imbalances in discovery are so severe that defendants often are left with two choices: one, either get extorted or settle, or take it all the way to the end, spend millions, and still not really win because they are out of pocket several hundred million dollars.

Mr. ISSA. And I appreciate that, and I want to go to Mr. Wamsley, too. But in a nutshell, having practiced as a patent holder and a defendant as a manufacturer, the one thing I know that I hope I get a yes from all of you on is, in a perfect world the pleadings tell what the infringement is if it is available to be defined. And if it is not available to be defined, at least sufficient for why you believe in good faith that there is a patent infringement, and an early Markman with discovery related to that.

Is that not the goal of everyone who has a valid patent that they truly believe has been infringed, or a defendant who truly believes they do not fall within the proper meaning of the patent? Is there anyone that disagrees with that?

Mr. TAYLOR. May I just address that, Mr. Chairman?

Mr. ISSA. As long as you are brief because I did describe your opening statement in my opening statement.

Mr. TAYLOR. Okay. Yes, I think in an ideal world you would like the pleadings to disclose as much as possible. It is often the case, however, and this is not just true of patent litigation, it is true of virtually all litigation. The plaintiff at the outset of a trial or outside of a case does not know all the facts it needs to put together a full trial brief.

Mr. ISSA. Okay. Well, let me follow up on that because I think that is extremely important having been the plaintiff. If you do not know there is patent infringement, then where do you get the right to go on a fishing expedition to see if you can find one?

Mr. TAYLOR. No lawyer today in light of——

Mr. ISSA. That was a question that requires an answer related to if, and I will go to Mr. Pincus because I have not gone to him yet. If you do not know there is patent infringement, what in any part of the law allows you to begin having Mr. Gupta's company spend money because you want to go on a fishing expedition because your patent on a swimming pool might apply to an array of disk drives?

Mr. TAYLOR. I do not think—oh, I am sorry.

Mr. PINCUS. I think that is exactly right, Mr. Chairman. I think you certainly should know which claims of your patents are infringed and what the infringing articles are, and I think that is the critical issue.

Mr. ISSA. And should you not know your accuser's true identity, particularly if you are being sued by a shell corporation? That is my closing question because I know Mr. Taylor objected to that.

Mr. PINCUS. I think you should know that as well, and I think that is why regardless of Iqbal and Twombly, the Innovation Act's specific requirements are so appropriate because if I were a patent plaintiff, I would not want to wait for 5 years for Iqbal and Twombly's application to patent infringement cases to be——

Mr. ISSA. Thank you. Mr. Wamsley, very quickly because my time has expired, if you have something to add.

Mr. WAMSLEY. Well, Mr. Chairman, I agree with your description of how it should work in a perfect world, and we support heightened pleading standards in principle. When we looked at this in the last Congress, we did it through a recommendation to amend Form 18 to specifically require identification of one or more claims, and explain how the latest infringing instrumentality infringed those claims. Now the Judicial Conference has gone to the Twombly/Iqbal standard, that may produce the same result, but we do not know yet.

Mr. ISSA. I look forward to finding out. Mr. Nadler is recognized for his questions.

Mr. NADLER. Thank you. I would like to ask Mr. Taylor to comment on the question that you did not get a chance to answer from the Chairman. I never liked the Iqbal or Twombly decisions, and I, in fact, introduced legislation to overturn them, which unfortunately has never passed because if you have a good reason to believe it is a general tort, the defendant is more likely to have the specific knowledge of the evidence.

But, Mr. Taylor, in patent, is that applicable? Should you not know if your patent is being infringed or how it is being infringed? Should you not be able to describe the provision of patent that is being infringed?

Mr. TAYLOR. Congressman, at least in the courts I have been practicing in for most of the last 35 years, lawyers before they will file a complaint are subject to Rule 11, which requires that you have a reasonable basis for believing that the factual allegations in the complaint are true. And I do not know any responsible lawyer that will file a case simply hoping that they can prove infringement. We go to great lengths sometimes——

Mr. NADLER. So then Iqbal is okay.

Mr. TAYLOR. I did not hear you.

Mr. NADLER. So then Iqbal is correct.

Mr. TAYLOR. Iqbal, it does not authorize people to make factual assertions in complaints for which the lawyers don't have some factual or some reasonable basis for believing them to be true. That is Rule 11 of the Federal Rules, and it is a seriously applied rule.

Mr. NADLER. But in a patent, is it not generally the case that if you are filing a patent infringement claim, you should have probably more specific knowledge in some tort case or whatever about what in your patent is being infringed allegedly?

Mr. TAYLOR. That is generally the case, and most responsible plaintiffs will take an accused's product and they will have it reversed engineered or they will analyze it. They will make every effort to determine whether the elements of a claim in the patent are all present, and in the process it is a little more difficult sometimes to find out.

Mr. NADLER. Thank you. Mr. Wamsley, in light of *Octane Fitness* and *Highmark*, do you believe we still need legislation on these subjects? And if so, why?

Mr. WAMSLEY. Yes, Mr. Nadler, we believe that legislation is still needed——

Mr. NADLER. Because?

Mr. WAMSLEY [continuing]. While *Octane* and *Highmark* are a step forward, the tests set forth by the Supreme Court in *Octane* that attorney's fees could be awarded in cases that stand out, it is broadly worded language.

Mr. NADLER. Too vague?

Mr. WAMSLEY. And we believe there is a spectrum of interpretations of that by the district court, and it is better to nail a brighter line in legislation.

Mr. NADLER. Thank you. Mr. Taylor, could you comment on the same question?

Mr. TAYLOR. I think that what we ought to do is wait for a while to see how the lower courts are going to apply the *Highmark* and *Octane* cases. I am not sure I agree that it is better to have a presumptive shifting of fees and for the following reason. At least from the perspective of the venture capital world, a small company that has been sued by a larger competitor is looking at two kinds of liability, liability for the infringement, and if you tack on attorney's fees as a presumption, that simply increases the ante. It raises the bogey, and that works distinctly to the advantage of larger companies to the detriment of smaller companies.

Mr. NADLER. And, Mr. Taylor, you say that the lower courts appear to be reading *Alice* to hold that subject matter eligibility can be decided in early stage of litigation without the need for costly discovery or claim correction. Mr. Taylor said that.

Mr. TAYLOR. Yes, sir.

Mr. NADLER. And that would seem to imply that we do not need legislation on that point.

Mr. TAYLOR. I certainly would suggest that we wait to see what the implications of *Alice*——

Mr. NADLER. And who would disagree with that on that point and why, of the other witnesses? Mr. Wamsley?

Mr. WAMSLEY. Well, Mr. Nadler, I would say that we may need legislation on *Alice*.

Mr. NADLER. We do not know yet.

Mr. WAMSLEY. But on clarifying *Alice*, the U.S. Patent and Trademark Office is now going through a public procedure to clarify.

Mr. NADLER. Thank you. Last question because my time is running out. Mr. Taylor, you said in your testimony that legislation should focus on specific behavior, not on the procedural aspects of enforcing patents. How would you accomplish this? What would you do?

Mr. TAYLOR. Well, the specific behavior, what we are trying to deal with here is what people consider to be abusive behavior by litigants. The courts already have a vast amount of power to deal with abusive behavior. And currently, I think the National Venture Capital Association would say that little is needed in connection with this, although, as noted in our statement, we do support the TROL Act, enactment of the act that would increase the power of the Federal Trade Commission to deal with abusive and deceptive demand letters.

Mr. NADLER. Thank you. My time has expired.

Mr. ISSA. I thank the gentleman. We now go to the Chairman of the full Committee, the author of the bill, the gentleman from Virginia, Mr. Goodlatte.

Mr. GOODLATTE. Thank you, Mr. Chairman. Mr. Taylor, on that last point, that is exactly what we are doing. I mean, we are providing for fee shifting, but in very precise circumstances, only when there is no reasonable basis in law or fact for asserting the claim, whether it is by a plaintiff or a defendant. When you translate that to the small startups that your companies invest in, they already are facing that right now. And when they get that claim, they are facing a multimillion dollar bill to defend their claim right now, or to assert it if they feel that some company, a bigger one, is going to do that, with no prospect—no prospect whatsoever—for recovery of that large loss.

So many of them choose to simply not fight it, and that is a reason why they are less successful in getting off the ground. So this predatory environment that they operate in is made, I think, worse by the fact that they have no prospect of anybody determining whether predatory actions took place in the first place, so I do not follow your reasoning there at all. I think this will be a big help, and many startups have told me just that, that it will be a big help to stop these kinds of predatory actions taking place against them.

Mr. TAYLOR. Some of the lawyers who represent non-practicing entity plaintiffs have told me that fee shifting is not going to affect their behavior at all.

Mr. GOODLATTE. Well, that does not explain why they are working very hard against this bill, I can tell you that.

Mr. TAYLOR. In my view, having been on both sides of lots of patent cases, I see the presumptive shifting of fees as an argument that allows the plaintiff to say to the defendant you owe me $100,000——

Mr. GOODLATTE. It is not presumptive shifting of fees. There is no presumptive shifting of fees in this law. It is only a shifting of fees when the Court finds that there was no reasonable basis in law or in fact for that to take place. So this constant assertion that there is going to be rampant fee shifting in patent cases after the passage of this law is incorrect.

What will happen, though, is there will be much greater certainty about when that fee shifting would take place. So you and your clients will be able to determine whether or not they have a good patent defense or a good claim to assert against somebody else and know much more likely than they do now what is going to happen because of the discovery process, the requirements when you file the case. And I think also importantly to know under what circumstances they should assert a defense and when they should not, because if they are not being reasonable, then darn right, they should not assert the defense. But if they are, this creates greater certainty than this morass of lawsuits.

So let me just say, and the elephant in the room here is that it is generally very rare for the Supreme Court to take up patent cases. But with all the recent Supreme Court decisions, it really looks like the Court has taken the Federal circuit to task. No judge wants to be reversed on appeal, especially not an appeal court judge that sits on a court with exclusive jurisdiction.

I will start with you, Mr. Wamsley. Do you think that the Federal circuit is getting the message, or do you foresee that the Supreme Court is having to just keep taking up more cases? Is this the new normal for the patent world, and is it good for the patent world to rely upon and wait on the next Supreme Court decision rather than to have some statutory certainty that is carefully negotiated, and takes into account all of these cases that have come down the line, but does not wait on that next decision around the corner, says here based upon experience and based upon what we have seen is some certainty in the law?

Mr. WAMSLEY. Well, Mr. Goodlatte, I would say the Federal circuits are certainly reading the Supreme Court decisions, and I believe recent decisions in some of the cases following *Alice*, for example, show that although there is still some inconsistency. And *Alice* is a case where the Supreme Court may have to come back to it again.

On fee shifting, I think the Federal circuit will follow. There was a case argued last week, according to the IP press, at the Federal circuit where, according to press accounts anyway, it sounded like the Federal circuit was inclined toward fee shifting.

Mr. GOODLATTE. Mr. Gupta?

Mr. GUPTA. Thank you, Mr. Chairman. In certain areas, the Supreme Court cannot provide the sort of consistent balanced solution that Congress can. And as I pointed out, for example, in the area of abusive discovery, there is no Court guidance and there are no Court decisions to help us. And in the area of pleading specificity, which is really important, you know, reliance on Iqbal and Twombly is not going to solve the problem because Iqbal and Twombly do not provide the kind of bright lines that we need in a specialized area like patent litigation.

Mr. GOODLATTE. Mr. Pincus?

Mr. WAMSLEY. Mr. Chairman, could I just——

Mr. GOODLATTE. I am already 30 seconds over. It is going to be up to that Chairman.

Mr. WAMSLEY. Could I just complete my last response?

Mr. ISSA. If the Chairman would like to let you have time, I would ask additional time.

Mr. GOODLATTE. We will hear from Mr. Pincus and then we can go back.

Mr. WAMSLEY. I would just like to say that no matter how strong the Federal circuit supports fee shifting, we think legislation is still needed because the way the statute is worded right now, only Congress can strike the balance that you want.

Mr. GOODLATTE. Thank you. Mr. Pincus?

Mr. PINCUS. Well, the Federal circuit had a bad year. There were six cases, and it did not get a single vote, so it was sort of 0 and 54 and a bad year for the Federal circuit, and I think that was a message that the Supreme Court was trying to send. But I think the problem is that the Supreme Court cannot rewrite the fee-shifting law to make the standard less mushy and clearer along the lines of what you were saying in terms of people's ability to anticipate how it will be applied and take that into account into their decisions. And that is something that only Congress can do.

The same with pleadings. Iqbal and Twombly can apply, and maybe in 10 years we will know how it applies to patent infringement actions. But there are some pretty clear rules that Congress could specify right now that would be great for both plaintiffs and defendants so they would know what is needed to get into court, and that would be that.

Mr. ISSA. Thank you. We now recognize the Ranking Member for up to 7 minutes depending upon how fast he wants to run to the vote. I would advise all Members this will be the last question before we recess for the vote.

Mr. CONYERS. Thank you so much. Let me ask, Mr. Taylor, with your background, counsel in venture capital firms who invest in patent owning businesses, how would the pending legislation impact the decisions venture capitalists make in investing?

Mr. TAYLOR. One of the provisions that we are most concerned about is the so-called joinder provisions, which are not clearly written, and read as if a venture capital firm that owns a majority share in a patent plaintiff would be on the hook for attorney's fees in the event a court were deciding to award that. Most venture capital investments are made, and that is the end of the money until they decide to make a new one, and to impose on the investors a responsibility for the actions of some of their companies. Piercing

the corporate veil, as it were, is something that is going to have a serious deterrent effect on venture capital investment.

Mr. CONYERS. How would this impact small investments and startups?

Mr. TAYLOR. Well, almost all venture capital investment is in entrepreneurial companies, innovative companies that are in either startup mode or not very far along from that.

Mr. CONYERS. All right. And my last question is to Mr. Wamsley. How has fee diversion impacted on USPTO's effort to ensure high quality patent examination?

Mr. WAMSLEY. There has been a serious adverse effect from fee diversion over the years. Going back over a period of years, more than $1 billion has been diverted to unrelated government programs or sequestered, and studies have shown that this is a principle reason for the backlog of cases to be examined. And we believe that more resources are also needed to improve quality, and so we would urge Congress when it has an opportunity to revisit the issue of guaranteeing secure funding for the PTO.

Mr. CONYERS. Do the other three witnesses generally agree with that response?

Mr. PINCUS. That diversion is a bad thing, absolutely.

Mr. GUPTA. Yes.

Mr. CONYERS. Thank you, Mr. Chairman.

Mr. ISSA. Thank you. I would advise all Members of the Subcommittee that we will return immediately after this series of two votes. So the first two Members back will begin the process. We stand in recess.

[Recess.]

Mr. ISSA. Could I ask you all to please take your seats? We are going to start again in a moment. The Committee will come to order. Is the gentleman from Texas prepared?

Mr. FARENTHOLD. I am always prepared.

Mr. ISSA. The gentleman is recognized.

Mr. FARENTHOLD. Thank you very much, Mr. Chairman. Mr. Gupta, I would like to touch briefly on a related issue, namely the rise of patent litigation before the ITC. I think it is important we do something about the rising tide of litigation in the Federal judiciary and the fact that we are moving over into concurrent tracks with litigation in the ITC. We have got to keep in mind that any reforms we do with respect to what happens in the judiciary may also roll over into the ITC.

My fear is that the trolls will use the ITC to pressure litigants to settle rather than face the cost of defending in that venue. We have already seen patent assertion entities starting to play the same game in the ITC that we are seeing in the Court, bringing suit against the customers or technology companies. To that end, I would like to ask you, is it your understanding that PAEs have additional leverage at the ITC and are actually in a better position to make settlements than in Federal courts?

Mr. GUPTA. Thank you, Congressman, for that question. It is concerning to us that the ITC is being used by patent assertion entities to essentially have dual litigation at times. The ITC is best able to deal with foreign knockoffs that come into our country, but to have an American entity litigate against another American com-

pany, particularly when the accusation is probably directed to some small component that might have in the supply chain originated outside the country appears to be not the most efficient use of the ITC. And I agree, and I share your concern.

Mr. FARENTHOLD. Thank you very much. Let us kind of shift to a different topic. In your written testimony you talk about the Teva Pharmaceuticals case and the potential of providing unscrupulous patentees with an incentive to pick the district court most favorable to them. Knowing their claim interpretation will be insulated from de novo review in the Federal circuit. I am wondering what you think about the impact of striking the broadest reasonable interpretation standard will be on current litigation environments in light of that decision.

I am especially interested given the decision in, what is it, the Cuozzo Speed Technologies this week holding that applying the broadest reasonable interpretation standard reduces the possibility that after a patent is granted, claims may be interpreted as giving broader coverage than justified.

Mr. GUPTA. We believe that the BRI standard is appropriate for IPRs and reviews post-grant. We have had several patents of ours challenged through the IPR proceedings, and we have challenged others as well. And we think that the Patent Office should be allowed to use the broadest reasonable interpretation standard when it looks at those patent claims.

Mr. FARENTHOLD. All right, thank you. Mr. Taylor, I believe in response to Mr. Nadler's question, I think you referred to "good plaintiffs," and I think that is not what we are after in this. I think our concerns are the bad actors who are using the expensive litigation to force settlements in questionable claims and the like. So I have no problem with, I guess, the term "good plaintiffs" with good cases coming, and I think we are drafting that such that we are going to preserve that. It is the bad actors we are going to get after.

But I am also a little interested, you know, based on your testimony, it kind of seems like it may be a little bit in conflict with NVCA's membership. There is a survey I think that said by and large they are harmed by patent trolls and supportive of reform. Why are you generally opposed to this litigation if some of your members or the majority of your members are having a problem?

Mr. TAYLOR. The only study I have seen is one that sampled a very small section of venture capital firms, and certainly does not represent the center of gravity of the NVCA. I have been working with the NVCA board now for almost a year on this issue, and trying to help people understand what the statute would say and how it would affect their businesses. And the positions that I am setting forth here today are the positions of the National Venture Capital Association.

Mr. FARENTHOLD. Thank you very much. And with the Chairman's permission and the consent of the Committee, I have a letter from Engine Advocacy titled, "Startup Investors Nationwide Support Broad Patent Reform," that I would like entered into the record.

Mr. ISSA. Without objection, so ordered.

[The information referred to follows:]

Startup Investors Nationwide Support Broad Patent Reform

6 November 2013

Dear Congress:

Each year, we invest hundreds of millions of dollars in software and information technology businesses and emerging mobile technologies. Together with other investors, we commit more than $1 billion annually in angel and venture capital that ensures continuing growth of young, high-tech companies employing 1.4 million people. Collectively, we have invested in companies such as Netflix, Twitter, Facebook, Dropbox, Palantir, Kickstarter, and countless other technologies that power American businesses everywhere. We are the fuel in America's startup economy engine.

We write to urge comprehensive legislation to address the troubling growth and success of the patent troll business model. Young, innovative companies are increasingly threatened and targeted by patent troll lawsuits. In fact, the majority of companies targeted by patent trolls have less than $10 million in revenue. And while big companies paid the lion's share of the $29 billion of direct costs resulting from patent troll activities in 2011, the costs borne by small companies are a proportionately larger share of their revenues.

As a result, Congress and the Administration are considering multiple reform proposals. None alone will fix the problem, but together they will make a substantial dent in what one famous troll recently called "a new industry."

Successful legislation should make it harder to be a patent troll, and easier for targeted businesses to protect and defend themselves. Legislation should:

- Make it easier to efficiently review patents at the Patent Office, as an alternative to litigation.
- Increase transparency by requiring patent trolls to specify, in complaints and demand letters, which patent and what claims are infringed, and specifically how the offending product or technology infringes.
- Limit the scope of expensive litigation discovery.
- Require patent trolls to pay legal fees and other costs incurred by prevailing defendants.
- Protect end users of technology (e.g., wi-fi, printers and scanners, and APIs) from being liable for infringements by technology providers.

Our Founders did not intend to incentivize patent trolling in the Constitution -- nor did Congress intend the Patent Act to promote this industry. Comprehensive legislation to reduce abusive patent litigation will make the patent troll business model less attractive, and will protect software, mobile and information technology entrepreneurs. In turn, our digital economy will continue to grow and so will our national economy.

The undersigned:

Gil Bickel
St. Louis Arch Angels
St. Louis, MO

David Bradbury
Vermont Center for Emerging Technologies
Burlington, VT

Glen Bressner
Originate Ventures
Bethlehem, PA

Brad Burnham
Union Square Ventures
New York, NY

Jeff Bussgang
Flybridge Capital
Boston, MA

Steve Case
Revolution Capital
Washington, DC

Jeff Clavier
SoftTechVC
Palo Alto, CA

Ron Conway
SV Angel
San Francisco, CA

Mark Cuban
Investor in over 70 startups
Dallas, TX

Peter Esperago
Cultivation Capital
St. Louis, MO

Brad Feld
Foundry Group
Boulder, CO

Nicole Glaros
Techstars
Boulder, CO and New York, NY

David Gold
Access Venture Partners
Westminster, CO

Greg Gottesman
Madrona Venture Group
Seattle, WA

Paul Graham
Y Combinator
Mountain View, CA

Bill Gurley
Benchmark Capital
Menlo Park, CA

Reid Hoffman
Greylock Partners
Menlo Park, CA

Kirk Holland
Access Venture Partners
Westminster, CO

Len Jordan
Madrona Venture Group
Seattle, WA

Scott Levine
iSelect Fund
Clayton, MO

John Lilly
Greylock Partners
Menlo Park, CA

Trevor Loy
Flywheel Ventures
Albuquerque and Sante Fe, NM

Chris Marks
High Country Venture
Boulder, CO

Dan Marriott
Stripes Group
New York, NY

Matt McCall
Pritzker Venture Capital Group
Chicago, IL and Los Angeles, CA

Jim McKelvey
Cultivation Capital
St. Louis, MO

Andrew McLaughlin
BetaWorks
New York, NY

Josh Mendelsohn
Hangar
San Francisco, CA

Jason Mendelsohn
Foundry Group
Boulder, CO

Michael Neril
Webb Investment Network
San Francisco, CA

Charlie O'Donnell
Brooklyn Bridge Ventures
New York, NY

Alexis Ohanian
Angel Investor
New York, NY

Bijan Sabet
Spark Capital
Boston, MA

Devin Talbott
Enlightenment Capital
Washington, DC

Brett Topche
MentorTech Ventures
Philadelphia, PA

Jorge M. Torres
Silas Capital
New York, NY

Hunter Walk
Homebrew
San Francisco, CA

David Weekly
Startup Founder and Angel Investor
Palo Alto, CA

Fred Wilson
Union Square Ventures
New York, NY

Engine

Application Developers Alliance

Mr. FARENTHOLD. And I timed that almost perfectly. I will yield back——

Mr. ISSA. Would the gentleman yield?

Mr. FARENTHOLD. I will.

Mr. ISSA. Mr. Taylor, would you provide transparency as to your members' statuses because it really is now a question of, you said you have been trying to convince your board to support opposition to the legislation. Do we have transparency for the 400 companies that are involved in yours to figure out how many of them support your position in light of the fact that it does appear as though there may be some doubt as to whether there is a formal process on a board and transparency?

Mr. TAYLOR. It is a large organization, and I am not certain how much of it is public. I have been dealing basically with the staff and with the board of directors, so I am not sure I can answer the question.

Mr. ISSA. Okay. I will take that as a no. [Laughter.]

With that, we go to the gentlelady from California, Ms. Chu.

Ms. CHU. Mr. Gupta, we have been talking quite a bit about the fee-shifting cases of the *Octane* and *Highmark* cases. You argue that these cases did not go far enough in deterring the filing of frivolous patent cases that companies both large and small have faced. You provide some statistics that can be helpful to us in evaluating how we should legislate in this area.

Why do you think that the rate of fully-granted motions increased shortly after the first 3 months of the Court decisions and then slowed in the last 3 months? Do you think this trend will continue?

Mr. GUPTA. Thank you, Congresswoman. You know, we have only had 9 months of data since *Highmark* and *Octane*, so it is hard to really speculate as to why it has been trending down. But the point I want to make is that *Highmark* and *Octane*, based on the data that we have right now, have not really had a meaningful impact. And I really believe that to get abusive litigation to slow down the abusive tactics, the plan or the proposal that is in the Innovation Act is a thoughtful bipartisan approach that I think will make a serious, you know, or have a serious impact on bad actors in court.

Ms. CHU. And can you tell us about the type of cases in which the defendant is being awarded fees since *Octane* and *Highmark*? Do they appear to be troll type suits, or is there no real pattern?

Mr. GUPTA. I do not know that I can generalize. We have a couple of motions pending ourselves where we have asked the court to grant us our fees, and we are waiting to see how the court will act, but I do not have a general sense. I think based on the data we have seen that the numbers generally seem to be evenly split between defendants and plaintiffs in terms of fee recovery, but not necessarily whether it is a NPE litigation or not.

Ms. CHU. And also in the Nautilus decision, the Supreme Court addressed how definite or clear a patent must be. The Court established a new test which requires that the patent provide reasonable certainty of what it covers. You have stated that it would be easier for a defendant to challenge the validity of a vague patent given the decision. Could you explain why it would be easier for the de-

fendant and what long-term effects do you think the decision will have on abusive patent litigation?

Mr. GUPTA. Certainly. We often find that patentees will attempt to really stretch the meaning or the meets and bounds of a patent in litigation downstream. Sometimes a patent 10, 12 years old, covering technology that was dated, they will attempt to stretch it to cover new developments in technology. And we think that this decision in Nautilus will allow us as defendants to be able to argue that Section 112 requirements were not met by the patentee, particularly in light of claim construction orders.

If the judge grants a claim construction order that is really broad and the plaintiff pushes for that broad construction, I think it will be easier for defendants downstream to then show that that claim construction is simply not supported by what is in the specification, but it is too early to tell. We also have one motion pending before a district court arguing that certain claims are invalid in light of Nautilus, but we do not have a ruling yet.

Ms. CHU. Okay. Mr. Pincus, what do these Supreme Court cases not address? And by that I mean what are the provisions in the Innovation Act that are still necessary despite the court decisions?

Mr. PINCUS. Well, they obviously do not address at all pleadings. The patent specific decisions. Obviously the changes that will be made in the Federal Rules striking Rule 84 and the forms will have some effect on pleading, but the Supreme Court has not addressed it. And as I said earlier, I think the Congress has an opportunity to put specified clear rules of the road for pleading rather than leave it to the courts to flesh out what Iqbal and Twombly mean in the pleading context, which will take a few years and could leave people uncertain about what the rules are. So pleading is one area.

Discovery is another area not addressed at all. The asymmetrical discovery costs which really are one of the critical drivers of the litigation, nothing done there. And with respect to the attorney's fees, although *Highmark* and *Octane* do address the issue, the problem is that because the current language of the statute is what it is, the Court could not interpret that language to provide the kind of guidance that is really necessary so that somebody making the decision, do I fight this case because I have a reasonable chance to get my fees back, or should I settle because I cannot be sure, and so fighting it will end up costing me more. The current statute does not do that.

The other problem with the current statute and the Court's decision in *Highmark* with respect to deference is at least when we are concerned about abuse by plaintiffs, plaintiffs pick the forum. And if a district judge indicates or members of a district court indicate that they are going to be tough on fees under a murky standard, it is pretty easy for the plaintiff to say, well, I am going to go somewhere else where this murky standard is getting a better interpretation. If Congress makes the rules of the road clearer, that kind of disparity is much less likely to develop.

Ms. CHU. Thank you. I yield back.

Mr. ISSA. I thank the gentlelady. We will now go to the gentleman from Georgia's 9th District, Mr. Collins.

Mr. COLLINS. Thank you, Mr. Chairman, and I am pleased to be starting back here. I am pleased to be on this Committee with you

and also the Chairman as Vice-Chair of this Committee because this is very important to me. It is something I worked hard in my first term, and look forward to working even more so in our second term. As we look forward to working with this Committee on intellectual property, obviously patents are a vital part of the system. So I want to thank the Chairman Goodlatte for holding this hearing and reintroducing the Innovation Act.

It is important for Congress to look for ways to eliminate frivolous and abusive litigation. We need to unclog the system to ensure that true innovators are given fair opportunity to enforce their patent rights, a right that our founders explicitly provided for in the Constitution. Last year, I had some serious concerns with the direction of some patent reform proposals, especially those that attempted to expand and extend the CBM program.

These types of proposals are unsettling because they discriminate against a particular type of technology rather than focus on the real problem, the bad behavior that occurs all too often during patent litigation. So I am grateful to the Chairman that the CBM issue is not a part of the Innovation Act. Having it in would certainly undermine my ability to support the bill in Committee and on the House floor. Now we can focus on moving forward legislation that eliminates and stops bad actors and improves our patent system.

But also before we start, this is my question. It was on something, Mr. Taylor, that you brought up, and I believe if we have it. Okay, if you would look at the screen. In your testimony, after your testimony I took your testimony and I went to your website, which is now on the screen. And on the first page under "research" tab, there was a study listed by Robin Feldman, and I am going to read just a few lines before turning to my questions. In the paper it said, "A study conducted on the topic of patent demands against venture back startups. The study was conducted through the members of the National Venture Capital Association."

[The information referred to follows:]

NATIONAL VENTURE CAPITAL ASSOCIATION

Funding innovation. Empowering entrepreneurs.

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RESEARCH
ECOSYSTEM
RESOURCES
MEMBER PORTAL

Research / Stats & Studies

STATS & STUDIES

NVCA underwrites, encourages and publicizes research on issues important to venture capital and the entrepreneurial ecosystem. Below are some examples of our most recent projects:

Patent Demands & Startup Companies: The View from the Venture Capital Community

NVCA partnered Robin Feldman, Professor Law and Director of the Institute for Innovation Law at University of California Hastings, to study the impact of patent demands against venture-backed startup companies. The study found that venture capitalists and startup CEOs overwhelming believe that patent demands have a negative impact on the venture-backed community, with all or most of those assertions coming from entities whose core activity involves licensing or litigating patents.

Download the Study

It said, and quoting from this report, it says, "74 percent of venture capitalists and 58 percent of startup companies report that patent demand had a significant impact on a company." The next one it said, "According to the vast majority of both venture capitalists and startup companies, the cost of preparing for and defending against patent demands exceeded $50,000 per company with a number of companies reporting costs in the millions of dollars."

When asked whether they see patent assertion as a positive for startups in the startup community, 72 percent of venture capitalists disagree. We might have an insight into why you are having trouble getting people to disagree with this bill.

Mr. Gupta, thank you. I appreciated listening to your testimony. I have heard from some groups that the Innovation Act will actually devalue property rights by diminishing the ability for parties to license their patents and defend them in court. How would you respond to that claim?

Mr. GUPTA. I completely disagree with that characterization. The Patent Act was designed to promote innovation and to promote art and sciences, and the true value of a patent really goes to the claims and the invention that those claims describe. I think a reformed system makes patents stronger. It provides companies like us, who rely on our R&D investment to protect our innovations, to know that we can actually enforce our patents in a meaningful way and protect the investments we have made.

The suggestion or the logic that somehow a patent is devalued if a patent holder cannot plead imprecisely and bury the other side with discovery requests, and do so with impunity knowing that at the end of the day they have no downside and they can walk away if they are not able to extort settlements from people, is just flawed.

Mr. COLLINS. And I think the thing that I have mentioned so many times in this Committee, and I think proposing this whole issue of patent, copyright, and others, that really strong protections, they actually increase and encourage innovation, and do not detract from it, whether it be venture capital or anything else. You want to invest in something that you know that you are at least protected to the extent you can be in a free market from an abusive system like we have now.

Mr. Pincus, I really like your expertise in this intellectual property area, and I think it is not only important we improve our patent system, but we also improve other aspects of the country's intellectual property policy. I am particularly interested to make sure that America still contains the highest standards really in the world. All too often we see our trade secrets stolen out of our factories here in the United States and then end up on a plane to a foreign competitor. I also want to improve the system to protect America's inventors, which is why I supported the Committee's trade secret legislation last year.

Can you talk about the intersection of patents and trade secrets? I am also interested in your perspective on any current improvements that we could make to our current trade secrets policy.

Mr. PINCUS. Yes, thank you, Congressman. As you know, sometimes for various reasons companies have very important, and significant, and valuable intellectual property that they either do not

want to patent or cannot patent, but is valuable and is confidential to them. And the question is how does the law protect that? Trade secret law has traditionally been the means of doing that, and as you know, trade secret law has traditionally been the domain of the States. But I think increasingly we have realized that in the global environment in which we find ourselves now, that there are holes in that protection, and something at the Federal level that puts forth clear rules of the road is really essential to ensuring that American companies can protect those trade secrets effectively.

Mr. COLLINS. I appreciate it. You will be hearing more from me on that in the weeks coming. Mr. Chairman, I yield back and appreciate that time.

Mr. ISSA. We now go to the gentlelady from Washington One, someone who is familiar with intellectual property, Ms. DelBene.

Ms. DELBENE. Thank you, Mr. Chairman, and thanks to all of our witnesses for taking the time to be with us today.

I know there has been a lot of close attention paid to the Supreme Court cases on Section 101, and, Mr. Wamsley, in your testimony, you stated that the lack of clarity in the *Alice* case makes it more difficult for innovators to determine when it is appropriate to invest in patent protection and cast a shadow of uncertainty on all patents, even good ones. And so, I wondered if you would elaborate a little bit more on that statement and what your concerns are with respect to the *Alice* case.

Mr. WAMSLEY. Thank you for the question, Congresswoman. Yes, we feel there is a great uncertainty caused by *Alice* currently, and the *Alice* case concerned a computer-related invention. But recently the Federal circuit extended the abstract idea test in a case involving the University of Utah even to a biosciences invention.

So I think right now with the level of uncertainty we have, people who are making R&D decisions in companies, at least computer implemented inventions, pharmaceuticals, cases that involve processes of all kinds, are wondering whether they are in the patent eligible area, even if they have what they think is a practical application for what might involve abstract process. So we think there is an urgent need to clarify this. Now, there was an earlier question about whether we need legislation. I would not urge legislation tomorrow, but if the courts are unsuccessful in clarifying this, I think that ultimately Congress needs to look at the adverse effect on the incentives for R&D.

Ms. DELBENE. Thank you.

Mr. TAYLOR. Could I offer just a footnote to that? It is important to remember that one of the purposes of the patent system is to encourage disclosure of inventions. And to the extent people conduct research and develop technology that they are not confident they can patent, or in the case of what we have been talking about this afternoon, not confident that they can reasonably enforce their patents, the tendency will be to protect it by trade secrets. And it is my strong sense right now, given some of these cases from the Supreme Court and given the pendency of this legislation, that companies are making that decision and opting to go the trade secret route for more of their technology that they used to try patenting.

Ms. DELBENE. Thank you. Many supporters of the Innovation Act have complained that they are being sued by shell companies with few assets to pay attorney's fees even if they are awarded. And according to the American Intellectual Property Law Association, the average cost of defending a patent suit with a million to $25 million, at risk is about $2.5 million, and the cost of defending patent suits with more than $25 million, at risk is over $5 million. And we know that there has been targeting obviously of startups that are particularly vulnerable.

So I guess I will ask you, Mr. Gupta, what do you see as the best way to deal with abusive litigation by shell companies in particular when they have a lot to gain and not a lot to lose under the current system? And do you think the Innovation Act will address that issue?

Mr. GUPTA. Thank you for the question, Congresswoman. I think the Innovation Act has a provision that requires people who have a financial interest in the litigation be joined. I think it is an important requirement. We are often sued by shell companies who are very thinly capitalized, and so even if you get an award, they are judgment proof essentially.

And by the way, my company, EMC, is a member of the National Venture Capital Association. We have a venture arm. We invest several hundred million dollars in venture funding. We are not concerned that as a VC that one of the companies we are investing is somehow going to be joined in a patent suit because we do not invest in companies whose primary business is to sue people with their patents.

And in the past 15 years, we have acquired 96 companies and spent $18-plus billion in acquisitions, primarily of venture-backed companies. And I can assure you that when I talk to the CEOs and the entrepreneurs who started these companies, they are very concerned about abusive patent litigation, and they are very concerned about how much of their funding they are having to spend on defending these demands versus hiring an engineer developing the technology that they want to perfect.

And so, I really think, you know, requiring joinder of folks who are funding the abusive practices is a very important step, and I believe that this bill has the right types of provisions for that.

Ms. DELBENE. Thank you. Thanks. I yield back, Mr. Chairman.

Mr. ISSA. Thank you. Anecdotally, Mr. Gupta, I would assume that you are not in support of your association's position here today.

Mr. GUPTA. Absolutely not.

Mr. ISSA. Just checking. The gentleman from Virginia, Mr. Forbes.

Mr. FORBES. Thank you, Mr. Chairman, and, gentlemen, thank you so much for taking the time to share your expertise with us today. I apologize that some of us have had to be in and out for votes. So it is not my desire to reopen a line of questioning that perhaps has been asked and answered, but I do want to make sure I am getting clarity.

And, Mr. Taylor, in response to what I heard the Chairman ask you, as I read your written statement and heard your oral presentation today, you accentuated the fact that you had 400 members,

I believe, in your association. But it would not be fair to conclude that your position today represents the position of those 400 members. Would that be fair to say?

Mr. TAYLOR. I think it is fair to say that the position we have tried to develop represents the center of gravity of that organization. I cannot tell you that all——

Mr. FORBES. Let's look at the center of gravity then, is Cisco one of your members?

Mr. TAYLOR. Say again?

Mr. FORBES. Is Cisco one of your members?

Mr. TAYLOR. Of the National Venture Capital Association? I do not know.

Mr. FORBES. They are I think. And do know their position on this?

Mr. TAYLOR. I do.

Mr. FORBES. And they are for the Innovation Act, are they not?

Mr. TAYLOR. They are.

Mr. FORBES. How about Google? Are they one of your members?

Mr. TAYLOR. I do not know the answer to that.

Mr. FORBES. Do you know their position on this act?

Mr. TAYLOR. I do.

Mr. FORBES. And they are for the act, are they not?

Mr. TAYLOR. Correct.

Mr. FORBES. Dell, do you know whether they are one of your members?

Mr. TAYLOR. I do not know.

Mr. FORBES. And do you know their position on the act?

Mr. TAYLOR. I am not sure I do.

Mr. FORBES. EMC, you look down the panel. You know their position. Are they one of your members?

Mr. TAYLOR. Yes.

Mr. FORBES. Are they one of your members?

Mr. TAYLOR. According to Mr. Gupta they are, and I have nothing to refute that.

Mr. FORBES. Okay. Intel, are they one of your members?

Mr. TAYLOR. I do not know, but I think they are.

Mr. FORBES. Do you know their position?

Mr. TAYLOR. I assume they are in favor of this bill.

Mr. FORBES. Micron, are they one of your members?

Mr. TAYLOR. I do not know.

Mr. FORBES. Do you know their position?

Mr. TAYLOR. No.

Mr. FORBES. Motorola, are they one of your members?

Mr. TAYLOR. The piece that is owned by Google. I do not know the——

Mr. FORBES. Do you know their position?

Mr. TAYLOR. I do not.

Mr. FORBES. How about Salesforce, are they one of your members?

Mr. TAYLOR. I do not know.

Mr. FORBES. Verizon?

Mr. TAYLOR. I do not know the answer to that either.

Mr. FORBES. So then basically you are not sure which of your members are for the Innovation Act or against the Innovation Act as you testified today. Fair assumption?

Mr. TAYLOR. That is fair except that I would say that all of the companies you identified are very large corporations. And the concern I have expressed is that for small innovative companies, and they were once small innovative companies I might add.

Mr. FORBES. And I think that would be fair, but I think it would be also fair to say that there is a large segment of your members that would be against your position today. Is that fair to say?

Mr. TAYLOR. Let me say this a different way. The members of NVCA that I have talked to have often not known enough about this legislation——

Mr. FORBES. So all these large companies you either have not talked to them or you feel that they just are not well-informed enough to have an informed opinion on whether they support the Innovation Act or not.

Mr. TAYLOR. I have had no reason to talk to the large companies. Their position has been clear since before I took this——

Mr. FORBES. Thank you. Mr. Gupta, can you help me with this? We have heard from stakeholders that the discovery proposals would actually make litigation longer and more expensive. As a litigator and practitioner who spends much of your time in court, do you agree with this statement? And if so, why or why not?

Mr. GUPTA. Thank you for the question, Congressman. I do not agree with that. I think if we streamline discovery to focus discovery early on to claim construction and Markman issues, and expedite Markman hearings and defer non-Markman related discovery to later, we will end up streamlining and speeding up the process immensely. We will de-clutter our courts to give them more time to handle substantive motions.

We will end up saving a lot of time, and mindless discovery, and expert reports for both plaintiffs and defendants, and bring a lot more focus to the litigation process, and make it a whole lot more efficient.

Mr. FORBES. And just a follow-up question, Mr. Gupta. We have heard claims that the number of cases are on the decline with estimates as much as a 40 percent drop, negating the need for Congress to act. Can you just respond to those numbers?

Mr. GUPTA. The fact of the matter is we still had over 5,000 patent cases filed, and I believe that is twice as many since the AIA was enacted, on an annual basis, and that is a lot of patent litigation.

Mr. FORBES. Thank you all so much for being here. Mr. Chairman, I yield back.

Mr. ISSA. Would the gentleman yield his remaining time?

Mr. FORBES. I would be glad to yield to the Chairman.

Mr. ISSA. So if can characterize, Mr. Taylor, what I think your testimony is, small companies within your group that you are not naming here today oppose the act based on your explaining it to them, and large companies, some of which have been named and more will be placed in the record, support the act, but because they are large, they do not count. You are still speaking on behalf of the

venture capital firm that you head. Is that correct? Or venture capital association you head?

Mr. TAYLOR. I have not heard any dissent from members of the National Venture Capital Association with respect to the positions, and they have been widely publicized within the organization.

Mr. ISSA. Okay. Then I ask unanimous consent that the members of the NVCA from the website be placed in the record, a partial list including Seagate, IBM, Johnson and Johnson, KPG, Morgan Stanley, Nike, DuPont, General Motors, Google, SoftBank, the owners of Sprint, EMC, of course, Delphi, Dell Corporation, USAA, the large fraternal association of former military personnel, Tyco, Verizon, et cetera.

Without objection, so ordered.

[The information referred to follows:]

Funding innovation. Empowering entrepreneurs.

MEMBERS

From Boston to Silicon Valley, NVCA has a diverse membership base of venture capital firms and corporate venture groups that work with America's entrepreneurial community to transform groundbreaking ideas into high-growth companies. Please visit our membership page (http://nvca.org/about-nvca/become-member/) if you are interested in exploring all the benefits that come with membership to NVCA.

.406 Ventures (http://www.406ventures.com/)

500 Startups, LP (http://500.co/)

5AM Ventures (http://5amventures.com/)

ABB Technology Ventures (http://www.abb.us/cawp/abbzh254/9cefb344ae2fbf87c1257918002f0b4c.aspx)

Abbott Capital Management, LLC (http://www.abbottcapital.com)

ABS Capital Partners (http://www.abscapital.com/)

Accel Partners (http://www.accel.com)

Acero Capital (http://www.acerovc.com)

Adams Capital Management, Inc. (http://www.acm.com)

Adams Street Partners, L.L.C. (http://www.adamsstreetpartners.com/)

Advantage Capital Partners (http://www.advantagecap.com)

Allegis Capital (http://www.allegiscapital.com)

Alloy Ventures (http://www.alloyventures.com%20)

Alsop Louie Partners (http://www.alsop-louie.com)

Alta Partners (http://www.altapartners.com)

Altira Group LLC (http://www.altiragroup.com)

Altos Ventures (http://www.altosventures.com)

Amgen Ventures (http://www.amgen.com)

Andreessen Horowitz (http://www.a16z.com)

Antares Capital Corporation (http://www.antarescapital.com)

Aperture Venture Partners, LLC (http://www.aperturevp.com)

Applied Ventures, LLC (http://www.appliedmaterials.com/company/applied-ventures)

Arboretum Ventures (http://www.arboretumvc.com)

ARCH Venture Partners (http://www.archventure.com)

Artiman Ventures (http://www.artiman.com/)

Aretê Corporation (http://www.arete-microgen.com)

Ascension Health Ventures, L.L.C. (http://www.ascensionventures.org)

Ascent Venture Partners (http://www.ascentvp.com/)

Asset Management Company (http://www.assetman.com/)

ATA Ventures (http://www.ataventures.com/)

ATEL Ventures, Inc. (http://www.atel.com/ventures/)

Atlas Venture (http://www.atlasventure.com)

August Capital (http://www.augustcap.com/)

Austin Ventures (http://www.austinventures.com)

Avalon Ventures (http://www.avalon-ventures.com/)

Azure Capital Partners (http://www.azurecap.com)

Bain Capital Ventures (http://www.baincapitalventures.com/)

Baird Venture Partners (http://www.bairdcapital.com/funds/venture-capital-funds.aspx)

Baker Hughes

Ballast Point Ventures (http://www.ballastpointventures.com/)

Battery Ventures (http://www.battery.com/)

Baxter Healthcare Corporation (http://www.baxter.com/about_baxter/.../baxter_ventures/)

BBVA New Ventures (http://www.bbvaventures.com)

Beecken Petty O'Keefe & Company (http://www.bpoc.com)

Ben Franklin Technology Partners (http://www.benfranklin.org)

Benchmark (http://www.benchmark.com)

Beringea L.L.C (http://www.beringea.com)

Bessemer Venture Partners (http://www.bvp.com/)

BioAdvance-Biotechnology Greenhouse of Southeastern Pennsylvania (http://www.bioadvance.com)

BioGenerator (http://www.biogenerator.org)

Blackrock-Private Equity Partners (http://www.blackrock.com/equity-dividend)

BlueCross BlueShield Venture Partners (http://www.bcbsvp.com/)

BlueRun Ventures (http://www.brv.com/)

BNY Mellon (http://www.bnymellon.com)

Borealis Ventures (http://www.borealisventures.com/)

Boston Millennia Partners (http://www.bostonmillenniapartners.com)

Bowery Capital (http://www.bowerycap.com/)

Braemar Energy Ventures (http://www.braemarenergy.com/)

Canaan Partners (http://www.canaan.com)

Cardinal Partners (http://www.cardinalpartners.com/)

Catalyst Investors (http://www.catalystinvestors.com)

Catamount Ventures (http://www.catamountventures.com)

Cayuga Venture Fund (http://www.cvf.biz/)

Charles River Ventures (http://www.crv.com)

Chevron Technology Ventures (http://www.chevron.com/ctv/)

CincyTechUSA (http://www.cincytechusa.com)

Cintrifuse (http://www.cintrifuse.com)

Cisco Investments (http://www.cisco%20investments.com)

CIT GAP Funds (http://www.cit.org/service-lines/cit-gap-funds)

Citigroup (http://www.ventures.citi.com)

City Light Capital (http://www.citylightcap.com)

Claremont Creek Ventures (http://www.claremont.com)

Claritas Capital (http://www.claritas%20capital.com)

Clarus Ventures, LLC (http://www.clarusventures.com)

Columbia Capital (http://www.colcap.com)

CommonAngels (http://www.commonangels.com)

Compass Venture Partners L.P. (http://www.compasstechpartner.com)

Connecticut Innovations, Inc. (http://www.ctinnocations.com)

ConocoPhillips Technology Ventures (http://www.conocophillips.com/what-we-do/innovating/technology-ventures/Pages/venture-capital.aspx)

Contour Venture Partners (http://www.contourventures.com/)

Coronis Medical Ventures (http://www.coronismedical.com)

Correlation Ventures (http://www.correlationvc.com/)

Cottonwood Capital Partners (http://www.cottonwoodtechnologygroup.com/)

Cross Atlantic Capital Partners (http://www.xacp.com/)

Cross Creek Capital (http://www.crosscreekadvisors.com/)

Crosslink Capital (http://www.crosslinkcapital.com)

Cue Ball Capital (http://www.cueball.com)

Cultivian Ventures, LLC (http://www.cultivian.com)

Dace Ventures (http://www.daceventures.com)

DAG Ventures (http://www.dagventures.com)

Davis, Tuttle Venture Partners (http://www.davistuttle.com)

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DCM (http://www.dcm.com)

Deerfield Management Company LP (http://www.deerfield.com)

DEFTA PARTNERS (http://www.defta%20partners.com)

Dell Ventures (http://www.dell.com/learn/us/en/uscorp1/dell-ventures)

Delphi Ventures (http://www.delphiventures.com)

Detroit Venture Partners (http://www.detroitventurepartners.com)

Disruption Corp. (http://www.disruption.vc/)

Divergent Venture Partners (http://www.divergentvc.com/)

Domain Associates, L.L.C. (http://www.domainvc.com/)

Draper Fisher Jurvetson (http://www.dfj.com/)

Draper Richards, L.P. (http://www.draperrichards.com/)

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Edison Ventures (http://www.edisonpartner.com/)

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EMC (http://www.emc.com/corporate/emc-ventures/index.htm)

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Foundry Group (http://www.foundrygroup.com)

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Fulcrum Equity Partners (http://www.fulcrumep.com/)

FundersClub Management (http://www.fundersclub.com)

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Hercules Technology Growth Capital, Inc (http://www.htgc.com)

Highland Capital Partners (http://www.hcp.com)

Hina Group Fund (http://www.hinagroup.com/index.html)

HLM Venture Partners (http://www.hlmvp.com)

Hopen Life Science Ventures (http://www.hopenls.com/)

IBM Venture Capital Group (http://www.ibm.com/venturecapitalgroup/)

IDG Ventures SF (http://www.idgvusa.com)

Illumina Ventures (http://www.illumina.com)

Innovate Partners (http://www.innovatepartnersllc.com)

Innovation Ventures, L.P. (http://www.innovationcapital.com)

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JAFCO Ventures (http://www.jafco.com)

JK&B Capital (http://www.jkbcapital.com/)

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Johnson & Johnson Development Corporation (http://www.jjdevcorp.com)

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Jumpstart, Inc. (http://www.jumpstartinc..com)

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Kinetic Ventures, L.L.C. (http://www.kineticventures.com)

Kleiner Perkins Caufield & Byers (http://www.kpcb.com/)

KPG Ventures (http://www.kpgventures.com)

Lambda Fund Management, Inc. (http://www.lambdafund.com)

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Lauder Partners (http://www.lauderpartners.com)

Lee Munder Capital Group (http://www.leemunder.com)

Legacy Venture (http://www.legacyventure.com)

Level Equity (http://www.levelequity.com)

Levensohn Venture Partners (http://www.levp.com)

LG Innovation Ventures (http://www.collaborateandinnovate.com)

Liberty Mutual (http://www.liberty%20mutual.com)

Life Sciences Greenhouse of Central PA (http://www.lsgpa.com)

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Lightstone Ventures (http://www.lightstonevc.com)

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Lumira Capital (http://www.lumiracapital.com)

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Maveron, LLC (http://www.maveron.com)

Mayfield Fund (http://www.mayfield.com)

Mayo Clinic Ventures (http://www.ventures.mayoclinic.org)

Mediphase Venture Partners, L.P. (http://www.medipaseventure.com)

Menlo Ventures (http://www.menloventures.com)

Mercato Partners (http://www.mercatopartners.com)

Merck Global Health Innovation Fund, LLC (http://www.merck.com/ghi)

Mercury Fund (http://www.mercuryfund.com)

Meritech Capital Partners (http://www.meritechcapital.com)

Michigan eLab (http://michiganelab.com/)

Micron Ventures (http://www.micron.com/about/company-info/ventures)

Milestone Venture Partners (http://www.milestonevp.com)

Mitsui & Co. Global Investment, Inc. (http://www.mitsui-global.com/en/)

Mohr Davidow (http://www.mdv.com)

Montreux Equity Partners (http://www.mepvc.com)

Moore Venture Partners, LP (http://www.moorevp.com)

Morgan Stanley Expansion Capital (http://www.morganstanley.com/institutional/expansion-capital/)

Morgenthaler (http://www.morgenthaler.com)

Motorola Solutions Venture Capital (http://www.motorolasolutions.com/US-EN/About/Company+Overview/Motorola+Solutions+Venture+Capital)

MPM Capital (http://www.mpmcapital.com)

Needham Capital Partners (http://www.needham.com)

NETCIRQ (http://www.netcirq.com)

New Atlantic Ventures (http://www.navfund.com)

New Enterprise Associates (http://www.nea.com)

New Leaf Venture Partners, LLC (http://www.nlvpartners.com)

New Venture Partners LLC (http://www.nvpllc.com)

NewSpring Capital (http://www.newspring.com)

NGEN Partners L.L.C (http://www.ngenpartners.com)

Nike Inc. (http://www.nikefuellab.com/)

Noro-Moseley Partners (http://www.noromoseley.com)

North Bridge Venture Partners and Growth Equity (http://www.nbvp.com)

Northern Light Development Corporation (http://www.nlvc.com)

Northwood Ventures (http://www.northwoodventures.com)

Norwest Venture Partners (http://www.nvp.com)

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Novartis Venture Fund (http://www.venturefund.noartis.com)

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Pfizer Venture Capital (http://www.pfizer.com/partnering/areas_of_interest/venture_investments)

Pine Brook Partners (http://www.pinebrookparners.com/)

Pittsburgh Life Science Greenhouse (http://www.plsg.com/)

Point Judith Capital (http://www.point.com/pjc/)

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Pritzker Group Venture Capital (http://www.pritzkergroup.com/venture-capital/)

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PTV Sciences (http://ptvhc.com/)

Quaker Partners (http://www.quakerpartners.com/)

Qualcomm Ventures (http://www.qualcommventures.com/)

QuestMark Partners (http://www.questm.com/)

Radius Ventures, L.L.C. (http://www.radius%20ventures.com/)

Redhills Ventures LLC (http://www.redhillsventures.com/)

Redpoint Ventures (http://www.redpoint.com/)

Relay Ventures (http://www.relayventures.com)

Research Corporation Technologies (http://www.rctech.com/)

Rho Capital Partners, Inc. (http://www.rho.com/)

Ridgewood Capital (http://www.ridgewoodcapital.com/)

River Cities Capital Funds (http://www.rccf.com/)

River Street Management, LLC (http://www.riverstreetmgt.com/)

RiverVest Venture Partners (http://www.rivervest.com/)

Rocket Ventures (http://www.rocketventures.org/)

Rogers Venture Partners (http://www.rogersvp.com/)

RRE Ventures (http://www.rre.com/)

RUSNANO USA, Inc. (http://www.rvc-usa.com/partners.html)

S.R. One, Limited (http://www.rone.com/)

S3 Ventures (http://www.s3vc.com/)

SABIC Ventures (http://www.sabic.com/ventures/)

Safeguard Scientifics, Inc. (http://www.safeguard.com/)

Salesforce (http://www.salesforce.com)

Sanderling Ventures (http://www.sanderling.com/)

SanDisk Ventures (http://www.sandisk.com/about-sandisk/corporate/ventures/)

Santé Ventures (http://www.santéventures.com)

Sapphire Ventures (http://www.svi35.com/)

Scale Venture Partners (http://www.scalevp.com/)

Schlumberger Technology Corporation (http://www.slb.com/)

Seagate (http://www.seagate.com/)

Second Alpha Partners (http://www.secondalpha.com/)

Second Century Ventures (http://www.secondcenturyventures.com/)

Sequoia Capital (http://www.sequoiacap.com/)

SeventySix Capital (http://www.seventysixcapital.com/)

Shasta Ventures (http://www.shastaventures.com)

Shell Technology Ventures (http://www.shell.com/global/future-energy/innovation/innovate-with-shell/shell-technology-ventures.html)

Siemens Venture Capital (http://finance.siemens.com/financialservices/venturecapital/pages/venture_capital.aspx)

Sierra Ventures (http://www.sierraventures.com)

Sigma Partners (http://www.sigmapartners.com)

Sigma Prime Ventures (http://www.sigmaprime.com/)

Sigma West (http://www.sigmawest.com)

Silver Lake Kraftwerk (http://www.silverlake.com/)

Slater Technology Fund (http://www.slaterfund.com/)

Sofinnova Ventures (http://www.sofinnova.com)

SOFTBANK Capital (http://www.softbank.com)

SoftTech VC (http://www.softtechvc.com)

Split Rock Partners (http://www.splitrock.com/)

SRI International (http://www.sri.com)

StarVest Partners, L.P. (http://www.starvestpartners.com)

Steamboat Ventures (http://www.steamboatvc.com)

Summit Partners (http://www.summitpartners.com)

SunBridge Partners (http://www.sunbridgepartners.com)

Sutter Hill Ventures (http://www.shv.com/)

SV Life Sciences Advisers, LLC (http://www.svlsa.com/)

SVB Capital (http://www.svb.com/svbcapital/)

Syngenta Ventures (http://www.syngenta.com/global/corporate/en/about-syngenta/Pages/syngenta-ventures.aspx)

Tahoma Ventures (http://www.johnives.com)

TDF Ventures (http://www.tdfventures.com)

Technology Crossover Ventures (http://www.tcv.com/)

Tenaya Capital (http://www.tenayacapital.com/)

The Coca-Cola Company Venturing and Emerging Brands Unit (http://www.vebatcoke.com/)

The Dow Chemical Company (http://www.dow.com/)

The Ohio Tech Angels (http://www.ohiotechangels.com/)

The Vertical Group (http://www.vertical-group.com/)

Third Rock Ventures LLC (http://www.thirdrockventures.com/)

Thomas, McNerney & Partners L.L.C. (http://www.tm-partner.com/)

Top Tier Capital (http://www.toptiercp.com/)

Trailblazer Capital (http://www.trailblazercap.com/)

TransLink Capital (http://www.translinkcapital.com/)

Trident Capital (http://www.tridentcap.com/)

Trillium Group, LLC (http://www.trillium-group.com/)

Trinity Ventures (http://www.trinityventures.com/)

True Ventures (http://www.trueventures.com/)

Tyco (TYC) (http://www.tyco.com)

U.S. Venture Partners (http://www.usvp.com/)

Upfront Ventures (http://www.upfront.com)

UPS Strategic Enterprise Fund (http://www.ups.com/sef/)

USAA (http://www.usaa.com)

Vantage Partners, L.L.C. (http://www.vantagepartners.com/)

VantagePoint Capital Partners (http://www.vpcp.com/)

Velocity Venture Capital (http://www.velocityvc.com/)

Venrock (http://www.venrock.com)

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Verge (http://www.vergefund.com/)

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Versant Ventures (http://www.versantventures.com)

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Virginia Capital Partners (http://www.vacapital.com/)

Walden International (http://www.waldenintl.com/usa/index.aspx)

Walgreens (http://www.walgreens.com/topic/well-ventures/well-ventures-info.jsp)

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Wellington Financial (http://www.wellingtonfund.com)

Western Digital Capital, Inc. (http://www.wdc.com/)

Western Technology Investment (http://www.westerntech.com)

Weston Presidio (http://www.westonpresidio.com)

Willowridge Partners, Inc. (http://www.willowridge.com)

Wing (http://www.wing.vc/)

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Mr. ISSA. Who is next? Mr. Cicilline, thank you for coming back. You are now recognized.

Mr. CICILLINE. Thank you, Mr. Chairman. Thank you to the witnesses for this very useful hearing. And, you know, I think it strikes me that it matters a lot how you look at the implications of both these Supreme Court decisions you have discussed and the proposed legislation depending on whether you are a plaintiff or defendant, whether you are defending a patent or being a defendant in a patent litigation action.

So I think the goal here, at least from my perspective, is to have reforms which ensure that we have a strong patent system, but also ensure that we make the ability to resolve disagreements cost-efficient, fair, quick, and that we preserve the ability of small entrepreneurs, particularly who have maybe economic imbalance of power in the system to be able to protect their inventions and their discoveries.

So what I am wondering first is, should our focus be, you know, if the idea is how do we come to the quickest resolution or the quickest determination as to the validity of a claim. Shouldn't we direct our attention to the pleading and discovery phases where we can make improvements to help arrive at that determination in a fairer, faster, more transparent way? And I know the Supreme Court decisions do not focus on those, but does the panel think that is an area we should focus on where there is the greatest opportunity to eliminate the abuse that we are intending to eliminate?

Mr. TAYLOR. Who did you want to answer that? Well, let me take a first stab at it.

Mr. CICILLINE. Yes, Mr. Taylor.

Mr. TAYLOR. It is always the case when a lawsuit is filed that the defendant will sit down with the patent and ask its lawyers to locate whatever prior art they can. Often the defendant will have the better prior art and to assess the strength of the claims, and if the claims are really genuinely not valid. I have had a number of situations in bringing prior art to the attention of the plaintiff and the case went away. It is one of those issues that you should be able to resolve early if you can.

One of the reasons for the AIA proceeding was to allow the litigants to get the validity issues out on the table. An AIA proceeding costs substantially less than trying to do it through a district judge and combative adversarial lawyers. And so, that is a partial answer to your question. I am not sure it is complete.

Mr. PINCUS. I think certainly those are two critical elements. I would not say they are the only ones, but I do think they are critical. I think at the pleading stage, I think everybody has agreed today that anybody filing a lawsuit should be able to identify the particular claims that they think are being infringed and the particular articles that are infringing. That seems pretty basic, and that is basically what the Innovation Act pleading provision requires.

And I think with respect to discovery, the critical question is staging the discovery to fit the part of the proceeding. Everybody should want to have the discovery, if there is any relating to the Markman proceeding, before the Markman proceeding. That then puts pressure on the judge to have to decide the Markman issue

right then, and then move to the next phase of the proceeding. You know what the patent means. Now, let's look at validity and infringement and get the relevant discovery with respect to that. So staging things in that way is quite sensible.

I think the other critical ingredient is something that levels the economic playing field because it still will be the case even if you make those changes that the costs of litigation are going to be asymmetric as it moves forward. And so, the question then is how do you incentivize a defendant to not settle a claim that he knows is pretty much abusive at the beginning when the settlement offer that is being made is less than——

Mr. CICILLINE. Okay, I take it back. I just have a few minutes left, 1 minute left. I just want to ask Mr. Wamsley, you said we should not act on *Alice*, legislate right away. And I am wondering whether or not it might make sense for us to see *Highmark* and *Octane*, how they play out, whether or not the Court may have actually solved at least that piece of the problem. Does it make some sense to give these decisions some time to be absorbed the Court?

And then secondly, I would just ask Mr. Taylor or any of the other panelists, what can we do to protect small investors who might be disadvantaged by some part of the Innovation Act? We want to deal with this issue of patent trolls in a serious way, but are there any suggestions you can make of things we should be looking at that will protect the small investors?

Mr. TAYLOR. Small investors?

Mr. CICILLINE. Small entrepreneurs?

Mr. TAYLOR. I think that protecting investors, it is terribly important to get rid of the joinder provisions that allows a prevailing defendant to turn to the owners of a company, pierce the corporate veil, and make the owners stand liable for attorney's fees. And the statute is capable of being read that way, although I think it is somewhat ambiguous. The concern we have is that it will be read that way. I think that provision is just anathema to encouraging venture capital investment.

Mr. CICILLINE. Thank you. I yield back, Mr. Chairman.

Mr. ISSA. Thank you. We now go to the gentleman from Pennsylvania, Mr. Marino.

Mr. MARINO. Thank you, Chairman. Mr. Taylor, let us talk a little bit about the venture capitalists. How widespread is the market in venture capitalism with regard to patent litigation?

Mr. TAYLOR. I do not think that for most venture-backed companies patent litigation to date has been a significant problem. The ones that I am aware of and the ones that I have actually personally dealt with have almost all been venture-backed companies being sued by larger competitors because they have got an innovative technology that the larger competitor sees an advantage to taking out.

Mr. MARINO. Would you agree with me that in most situations, those individuals investing in venture capitalists concerning patent litigation or any other investment pretty much know what is going on, what they are investing in?

Mr. TAYLOR. I think as a general proposition, yes.

Mr. MARINO. Okay. And you talk about piercing the corporate veil, which is an interesting point. But would you agree with me

that in order to pierce the corporate veil, the investors would have to know or should have known that there was unethical or even criminal activity taking place with the investors, with the principals who are running the investment?

Mr. TAYLOR. State laws differ with respect to the requirement for piercing the corporate veil, and there are a number of situations in which courts have done that. But in general, I can tell you that most investors assume if you are just buying stock in a company, you are not assuming any responsibility for a company's liabilities.

Mr. MARINO. I know you are right. It is something that could rear its ugly head, but not on a regular basis or highly unlikely. You have to show intent on the part of the investor that they were condoning, or allowing, or turning a blind eye to what was taking place with whom they gave money to invest.

Mr. TAYLOR. The way I read this legislation is that if someone has a financial interest, the owner of patent, and given the joinder rules, they are susceptible to being joined. That is one of the fundamental problems that surfaced when I first read it.

Mr. MARINO. Have you seen situations where that has occurred where investors were held liable because of activity on the part of the principles?

Mr. TAYLOR. Not to date.

Mr. MARINO. Okay. Let us talk a little bit also about courts. I clerked a long time ago for a Federal judge at least in my last year in law school and then as a prosecutor, U.S. attorney. I am very familiar with the Federal court system both in the criminal and the civil side. U.S. attorneys have responsibilities on the civil side to resolve cases as well.

And I found over the years and years of my experience that courts are just reluctant to award attorney's fees, to fee shift, even for egregious activity. I have been in court numerous times and showed clearly evidence that was purposely withheld or false statements were made, and the courts would not sanction or award fees. So what other way could this be handled other than re-legislating, among other things, that issue of awarding fees?

Mr. TAYLOR. Well, the mechanisms are in place for truly abusive and frivolous litigation already.

Mr. MARINO. I understand that, sir. They are there. You studied the Federal rules. I know the State rules at least in a couple of States. But the courts are just not doing it.

Mr. TAYLOR. I think Congress——

Mr. MARINO. Can you give an example of why they are not doing it?

Mr. TAYLOR. Since the *Octane* case was decided last summer, there have been 49 cases in which the prevailing party sought fees, and in 21 of those cases the court has awarded it, which I think is a different equation today than existed at the beginning of last year. There is a quotation from Justice Sotomayor from a copyright case, and she lists the kind of activities that should give rise to a fee award, and they include asserting frivolous positions.

Mr. PINCUS. Congressman, can I——

Mr. MARINO. Go ahead. Yes.

Mr. PINCUS. So here is the problem. In the real world, there is Rule 11, but the problem is very few people ever seek fees because

what they do in these cases is they decide it is cheaper to settle than fight. So the fee application never happens because the case is settled.

What you want people to do is stand up and say I am going to fight this because I think this fee standard gives me some reasonable belief that if I fight, I am not going to end up a net economic loser. And that is the critical change that has to be made is to get people willing to invest the time to fight, which will change all of the incentives in the action. I wonder if I could just——

Mr. MARINO. Well, that is going to be up to the Chairman because my time is well over.

Mr. ISSA. If on the subject of the question you want to complete your answer you may, but only that, please.

Mr. PINCUS. I will be very quick, Mr. Chairman. I know Mr. Taylor is very worried about this interested party provision. But I would just urge people to read the text of the Innovation Act, which is quite restrictive and specifically says that just having an economic interest in the company is not enough to make you an interested party.

Mr. MARINO. I would agree with that.

Mr. ISSA. Thank you. The gentleman from Florida, a fellow Michigan graduate, although I was down the street. I was at Siena where you at the big school, University of Michigan, Ann Arbor.

Mr. DEUTCH. I think we saw you in the stadium some Saturday afternoon.

Mr. ISSA. Well, that is because we did not have a football team. We had women's field hockey. The gentleman is recognized. [Laughter.]

Mr. DEUTCH. Thank you, Chairman Issa and Ranking Member Nadler, for holding this important hearing today. There is no question that we have got to address the real problem of patent trolls and truly fix the broken patent system. Any legislation that moves forward from this Committee has to strongly promote, not stymie, American innovation and ingenuity.

We have got to take into account the rights of inventors and small businesses, make it harder for patent trolls to take advantage of this system at the expense of legitimate practitioners and third parties. And if we fail to balance these goals, then we are going to hurt American businesses, weaken inventors, harm our universities, and seriously damage our economy.

I am personally committed—personally committed—to improving our patent system. That is why I introduced the End Anonymous Patents Act that would help end the secret system of patent ownership. I strongly support many provisions in this bill, including the new transparency rules and many others. But I genuinely worry that the legislation as currently drafted contains language that could actually weaken a patent holder's willingness and ability to protect their valid patent rights.

I am also concerned that the legislation fails to take into account the new and significant shift in the law that was the result of Supreme Court cases. That change in law and the change in the courthouses, Mr. Pincus, I would suggest is also the real world. These cases give district court judges significant and expansive discretion to award fees to a prevailing party, and they have more

than ever. I trust judges that know the facts intimately to properly exercise such good discretion rather than rigid rules set by Congress that cannot separate the innovative inventor from the patent troll.

And as much as I like H.R. 9, I am concerned that the loser pays attorney's fees provision in the bill may, in fact, deter patent holders from pursuing even meritorious patent infringement claims. I am worried that small businesses and independent inventors will be affected. Mr. Taylor, those are perhaps companies that you know best.

So I would ask after *Octane Fitness*—Mr. Taylor you just spoke about this. Now, you pointed out that judges have awarded fees in patent cases far more than they have before, so here is the real question I have. In light of all of the steps that have been taken by the PTO, by Congress, and now by the Supreme Court, Mr. Taylor, help me understand why it is necessary to place additional burdens on the individual who is seeking to defend his or her property right.

Mr. TAYLOR. I do not think you should be placing additional burdens on the person trying to defend his or her property, nor do I think we should be placing additional burdens on litigants who have been sued by larger competitors. Those are serious concerns. And I think the way you stated it, I would certainly subscribe to.

Mr. DEUTCH. Do the Supreme Court decisions make it harder for patent owners to file frivolous lawsuits? Does it make them think more in light of the decisions that have come down in what we have seen in Federal court?

Mr. TAYLOR. I think that the reason you have seen a drop off is patent owners are going back to the drawing board with their lawyers and seriously examining whether or not they are inviting a fee award at the end of a losing case rather than a settlement. But bear in mind, the bulk of these cases will continue to settle, and the fee award, by raising the risk to both sides, gives the plaintiff a very good argument to the defendant for why you ought to settle the case without taking it to trial.

Mr. DEUTCH. Now, you had said in your testimony, Mr. Taylor, that if the Innovation Act as written were to pass, it would have a chilling effect on investment and patent-intensive companies. Can you just expand on that? And I apologize if you have already, but I had two other hearings.

Mr. TAYLOR. Well, I think for all the reasons we have been talking about, I think the fee-shifting proposal is going to make it more difficult and certainly make it riskier. I believe the fee-shifting proposal is going to raise the expense. I think that the pleading requirements are going to raise the expense because what will happen as a practical matter is I file a complaint, and you are the defendant, and you come in and say, hey, look, Congress has listed 20 things here that you have to comply with in order to file a valid complaint.

And I am going to say to the Judge, well, I think I have done them all, Your Honor. And then there is going to be a motion filed as to a number of those points that is going to be $30,000 or $40,000 per side just to resolve whether the complaint is any good.

Mr. DEUTCH. I only have a few seconds left. Can you describe some of the types of companies that might be affected in that way?

Mr. TAYLOR. Companies in the energy business who depend terribly on their patents, biotechnology companies, pharmaceutical companies, medical device companies. The medical device companies are particularly vulnerable because a medical device takes a lot of development time. It is so easily copied. And unlike pharmaceuticals, the FDA process for clearance of a medical device if you have got another device on the market is quite simple.

And so, for medical device developers, unless they can protect their patents, they are dead in the water, and the larger companies are watching the marketplace. They spot the new technology, new trends. And it is not uncommon for medical devices quickly to be copied by their larger competitors.

Mr. DEUTCH. Thank you, Mr. Chairman. Yield back.

Mr. ISSA. You are most welcome from one Michigan kid to another. Sort of Michigan.

We now go to a man who understands State court law, Judge Poe.

Mr. POE. Thank the Chairman. Thank you all for being here. Yes, it is true. I did serve as a district judge in Texas for 22 years, but it is a fact universally that most cases settle. Civil cases, criminal cases, big cases, little cases, traffic cases, most of them settle. Is that not a truism in our court system, State and Federal? Anyone disagree with that?

[Nonverbal response.]

Mr. POE. Most cases do not go to trial. They settle somewhere early on. They settle on the steps of the courthouse. They settle when they see who the judge is. They settle eventually. It is a universal issue about litigation and the cost of litigation when someone decides to sue another one. How much is it going to cost and who is going to pay for that? This a discussion that has been going on since before any of us probably were lawyers.

It seems to me that public policy, we want people to be able to go to court if they can if they have what they believe to be a legitimate case of some kind. And if they win, great. If they lose, there is always the theory or threat, well, I have lost, now I have got to pay, and I do not have the money to pay.

Let us talk about this issue of patent trolls, use the definition, whatever you prefer. Would not what would happen is, and let us take the new legislation. Mandatory to the judges, you got to impose these fees. Patent trolls are not going to be paying those fees, are they? The judge finds it is a frivolous lawsuit. These patent troll companies, they just go out of business and start another business. Is that not what is going to happen? It is a question. If any of you want to answer it, it is fine.

Mr. TAYLOR. I do not know exactly how that is going to play out. What I do think, though is that the courts have today the mechanisms to put in place assurances that that will not happen. The courts had, for example, what we may see is the attorney's fee issue does not have to wait until the end of the case. And indeed what I am told by some of my friends who are representing people actively today in litigation is there is already posturing going on among the lawyers to set up the fee issue at the end of a case.

And if you are dealing with a genuinely impecunious plaintiff and it has no real party interest, and there are mechanisms already in the Federal rules for finding out who the party-in-interest is. And it is not very many real parties-in-interests that are completely impecunious. The judge is in a position to make rules that either make them streamline the case to the point that it can be afforded, or make some kind of a presentation or representation——

Mr. POE. That was not my question. Is that going to be the end game, they are just going to re-incorporate under another name? Anybody else want to weigh in on this? I have one other question, too. Go ahead.

Mr. GUPTA. If I may, Congressman. I think the Reform Act's provision dealing with ensuring that people who are funding the enterprise and funding the entities who are acquiring patents just to sue people is a thoughtful solution to that issue. If you peel behind sort of the actors who are funding a lot of this, there are a lot of common players. I think I have seen research that said more than 60 percent of troll actions are really initiated, are funded by a very small group of companies.

And so, I think the reason that patent lawsuits settle as much as they do is because patent litigation is very expensive, and small companies in particular. And I have data that I have cited from MIT and Harvard, very recent studies, saying that they are really impacted negatively when they have to deal with patent suits rather than spending their resources in creating technology.

Mr. POE. I understand. That is what some of them say, and I do not necessarily disagree with them. My other question is, having been a judge, of course, I think the trier of fact or the person who gets to hear the whole case is in a pretty good position to make some decisions about attorney's fees, if you will. I agree with that philosophy. Except for the statistics mentioned by Mr. Taylor, why have Federal judges been reluctant to order fees since they can already do it? They have the discretion. Why do they not do it?

Mr. TAYLOR. Prior to the decisions of the Supreme Court in *Octane* and *Highmark*, there had been in place for at least a decade Federal circuit decisional law that made it essentially impossible for the prevailing party, a prevailing defendant particularly, to recover attorney's fees. And the message one gets from the two decisions written by Justice Sotomayor is that we, the Supreme Court, reject that approach. We think the district judge, as you just stated, is in a way better position than the Court of Appeals to decide whether or not there is a reason to shift fees. And we are going to entrust that issue to the discretion of the judge. The Federal circuit may no longer review it de novo. The Federal circuit is required to review it.

Mr. POE. Let me interrupt because I am out of time.

Mr. ISSA. Yes, you are.

Mr. POE. If the Chairman would let me ask the question?

Mr. ISSA. Without objection.

Mr. POE. Look, the district judge who hears the whole case but early reversed the decision of the district judge if there is an abuse of discretion as it is under some other types of law.

Mr. TAYLOR. Correct.

Mr. POE. Would that be a fair analysis——

Mr. TAYLOR. Yes.

Mr. POE [continuing]. Of something that maybe we should consider?

Mr. TAYLOR. That is what the decision in *Highmark* and *Octane* specifically state.

Mr. POE. I understand. I yield back.

Mr. ISSA. I thank the gentleman for yielding back. I would remind all the witnesses that we do allow significant revise and extend in order to comment further on some of the specifics where a question could not be fully answered. So it is not full amicus, but we certainly would look forward to your further comments.

We now go to the gentleman from Brooklyn, Mr. Jeffries.

Mr. JEFFRIES. Thank you, Mr. Chair, and I thank Ranking Member Nadler as well, and thank the witnesses for your presence and your testimony here today.

I want to explore this issue of trying to help through the Innovation Act startup companies, tech entrepreneurs, young inventors, and others, the small inventor, which is of particular importance to me. The Chairman noted that I am from Brooklyn. We have a growing technology and innovation economy filled with tech entrepreneur startup companies, new inventors.

And, you know, Mr. Taylor, you seem to indicate in your testimony that in your view, the Innovation Act would hurt these entities. But in speaking to some tech entrepreneurs and some small startup companies, who have had experiences with patent trolls, one of the concerns that they face is that because there is such an imbalance right now, and abusive litigation is not being decided on the merits, which it should be, but is being decided on the basis of the expensive cost of litigating to the very end.

Even if you believe that the case being brought is invalid, would not the Innovation Act in its effort to restore this litigation balance so that people can make decisions based on the merits of the claim, actually help the tech entrepreneur, the startup company, and the young inventor?

Mr. TAYLOR. I do not believe that that would be the case, and the reason is that the way in which the bill is structured, the enhanced pleading requirement is going to raise the cost of getting the court even to have the initial pleadings in place. The fee-shifting provision is going to become an amount of money that the defendant has to take into account as what it is facing by way of risk at the end of the case. And it is going to create more pressure on the defendant to settle than exists today.

I agree with you. Today the cost of litigation is prohibitive, and it is particularly prohibitive for small companies. But I do not think this bill gets rid of that.

Mr. JEFFRIES. Now, in terms of the enhanced pleading, I would note that when the Private Securities Litigation Reform action or Act was passed, I think, in the late 1990's, which put in enhanced pleading as it relates to securities litigation, there was a view amongst many that this would hurt the ability of the small individual investor, the individual plaintiff, the type of person that I am concerned with—I was not in Congress at the time—to actually bring actions holding big companies responsible for financial impro-

priety. But that, in fact, has not been the case, notwithstanding the enhanced pleading. And that is in a much broader context, the securities litigation, than the specialized area of patent litigation.

So on the fee-shifting point, however, I am very interested in because I am sensitive to the concern as it relates to separation of powers, one that I think the Judiciary Committee should take seriously, that the House of Representatives should take seriously, in terms of us being a co-equal branch of government. And at the end of the day, you know, the Supreme Court and the courts at the circuit level and the district court level should be separate and co-equal and have a capacity to determine how matters should proceed through the judiciary, though Congress has the authority to do it.

That said, in the post-*Octane* environment, you made mention of the fact that courts now appear more willing to shift fees. Is that correct? So what I am trying to understand is since the Court said the previous standard, which I believe was objectively unreasonable and asserted in bad faith, was not the standard that should be applied in determining whether this was an exceptional circumstance. And that we have now got a standard where we have shifted the burden to say that the court shall award fees unless the case was reasonably justified in law and fact.

It is not clear to me that there is a lot of space between the enhanced Supreme Court directive and the attorney's fees provision that is in this bill. And I would be interested in, you know, your observation, Mr. Pincus, and the observation of Mr. Taylor if time permits.

Mr. PINCUS. I think the difference is the Supreme Court's standard is basically sort of a Gestalt standard, right? They say it is exceptional and the district court can consider all relevant factors in deciding whether or not it is exceptional. And so, I think the problem is in terms of both getting some uniformity across district courts and also in terms of having a standard that people can anticipate how it might be applied in a particular case, that is not really a very helpful test.

And I think the testimony that is in the Innovation Act focuses the district judge on some key factors. One is, as you say, reasonable in law and fact, and then the countervailing consideration about whether special circumstances, and it specifically says such a severe economic hardship to an inventor. So specifically saying if this is going to hurt a small inventor, do not do it, I think focus the district judge on the key factors in a way that the current law does not because it sort of says look at everything and make this decision.

Mr. JEFFRIES. Thank you.

Mr. ISSA. Okay. Seeing no further questions for our witnesses, I want to thank you for your testimony here today. I want to thank you for your candor. And, again, to the extent that you want to give us additional information either to be placed in the record, that would have to be within 5 legislative days. So without objection, all Members and our witnesses shall have 5 legislative days in which to submit additional written questions for the witnesses or additional materials for the record. Anything coming in after that will still be disseminated to all the Members of the Committee.

We stand adjourned.
[Whereupon, at 3:43 p.m., the Subcommittee was adjourned.]

APPENDIX

Material Submitted for the Hearing Record

UNITED *for*
PATENT REFORM

Statement for the Record

Submitted to the United States House of Representatives Judiciary Subcommittee on Courts, Intellectual Property and the Internet

Hearing on Examining Recent Supreme Court Cases in the Patent Arena

February 12, 2015

www.unitedforpatentreform.com

Introduction

The members of United for Patent Reform are a broad and diverse group of Main Street, high tech, and manufacturing , companies—from internet service providers to home builders, brick-and-morter retail stores to wi-fi technology providers—that all share two essential goals: to give real meaning to the constitutional recognition that intellectual property is protected in order to "promote the progress of science and the useful arts" and to fight back against abusive litigation tactics that undermine that aim. Our nation's courts provide a critical forum for protecting patent rights, and thus for ensuring that we continue to reward the innovation that has long made the United States the envy of the globe. But in recent years, those who abuse the patent system through litigation have become more energetic, more predatory, and more successful as they take advantage of the costs and uncertainties of federal litigation to leverage settlements and accommodations to which they have, in fairness, no right.

While patent trolls are wreaking havoc on American businesses large and small, there are some who say recent Supreme Court rulings have solved all our patent problems and there is no more need for patent reform legislation. Nothing could be further from the truth. Patent trolls continue their assault on American businesses, and the need for patent reform is greater now than ever. Many who have long opposed any patent reform pointed to the temporary drop in lawsuit filings after the *CLS Bank vs. Alice* decision and declared "mission accomplished." Not surprisingly though, after an initial decline in lawsuits, since November of 2013, patent suits have once again spiked up and remain at historic highs.

Contrary to our opponents' rhetoric, even after the recent Supreme Court rulings, patent trolls are still filing the majority of these lawsuits and continuing to rob businesses of critical resources and to drain billions of dollars from our economy. Patent litigation reform is about stopping patent troll's lucrative business model of sending vague demand letters and using

overly broad patents to file lawsuits and get shakedown settlements. The Supreme Court's recent decisions did nothing to stop these practices. Only Congress can pass the comprehensive reform needed to put abusive patent trolls out of business for good. The recent introduction of the Innovation Act is a strong first step to making that a reality.

Our patent system is strong, and is being made stronger through recent reforms and efforts by the Patent and Trademark Office and by Congress and by the courts. But the abuses of our litigation system cry out for correction, and United for Patent Reform has championed seven straightforward reforms that will make efficient and effective changes, without harming the value of patents, but curtailing the possibilities of manipulating the litigation of those patents to unfair advantage.

Stopping Abusive Demand Letters

Patent trolls use so-called "Demand Letters" to target small and medium sized businesses. Rather than going to the trouble and expense of filing an actual lawsuit, a patent troll will simply send a letter to a legitimate business—sometimes to dozens or even hundreds of businesses at once—claiming the business has infringed a patent held by the troll. The only solution, the troll will usually say, is a quick cash payoff.

These letters are typically mass produced form letters that have little or no facts about what alleged infringement has supposedly occurred. The letters often fail to identify the patent supposedly being infringed or what the business being sued has done to infringe it. The letters always include a threat of costly lawsuits to follow if a payment to "settle" the matter is not soon made.

The infringement alleged by the demand letter is often based on the business' use of a commercial product, like a printer, a wi-fi router, or a software program that the business buys from a commercial vendor to use in its day-to-day operations. Most small and medium sized

businesses who receive demand letters face only bad choices: they know they have likely done nothing wrong, but they either must pay the troll; hire an expensive lawyer just to get advice about what to do; or fight the troll in court, where "winning" can often cost many times more than just paying the original settlement offer in the demand letter.

Congress should act to protect innocent business from this abuse. Someone accused of infringing a patent in a demand letter must be told at least the basic facts supporting that accusation. Congress should clarify that transmittal of a demand letter that fails to give genuine notice of the alleged infringement is a fraudulent act.

Making Trolls Explain Their Claims

Trolls often file threadbare complaints based on no investigation with only boilerplate recitals in the hope that discovery will uncover a plausible claim or that the burden and expense of responding will coerce defendants into a quick settlement. Under current law, the trolls are not required to identify the patent that they claim is infringed, the product or process that allegedly infringes that patent, or why the troll believes that the infringement in occurring.

These lax rules allow patent trolls to file tens and even hundreds of cookie-cutter lawsuits that include no real details about the claim. The troll's hope is that during the discovery phase of the trial, it might uncover a plausible claim or that the burden and expense of responding to the discovery request will coerce the troll's target into a quick cash settlement.

A legitimate business hit with a barebones infringement suit cannot judge the merits of the suit, accurately determine its legal exposure, prepare an answer, design a defense strategy, or decide which documents need to be collected and produced. In these vague, poorly designed cases, discovery evolves into unfettered and expensive fishing exposition in which the burden is disproportionately borne by the defendant.

Congress should put an end to this abusive practice by ensuring that defendants in

infringement suits are given genuine notice of the claims against them. The law should state that a claim alleging patent infringement does not state a plausible claim for relief—and therefore must be dismissed—unless it identifies: (1) the patent allegedly infringed, (2) the allegedly infringing product or process; (3) how the product infringes the patent; and (4) and party having a financial interest in any recovery.

Protecting Innocent End Users

Traditional discussions about patent litigation focused on two parties: a patent holder and the manufacturer of a product that allegedly infringes the patent holder's patent. But today, patent trolls are increasingly targeting a third party—the alleging infringing product's end users—by suing them for patent infringement or demanding extortionate settlement payments simply for using an off-the -shelf product in their day-to-day businesses.

End users of a product differ from the product's manufacturer in several critical ways that make patent lawsuits against them particularly attractive to trolls looking for quick settlements. First, end users often lack familiarity with patent litigation. They don't know how to judge the merits of a patent troll's legal threat or accurately measure the merit of a patent lawsuit filed against them. Second, they usually lack the same level of technical sophistication as the product manufacturer. Most end users operate in non-technical industries and lack technical expertise with the patented subject matter. They tend to be "Main Street" businesses like retail stores, restaurants, hotels, non-profits, public agencies, Realtors, homebuilders, and small manufacturers. Finally, most end users have no stake in the determination of the patent's infringement or validity. The patented technology is usually ancillary to the end user's business, which often leads them to avoid the costs and risk of litigation by settling even meritless claims. All three of these factors make end users particularly vulnerable to patent trolls.

Congress should ensure that when a product manufacturer and end user are both involved

in infringement actions involving the same products and patents, the courts will stay claims against the end users and proceed first with the claims against the product manufacturer.

Defining the Case before Full Discovery

To decide the meaning of the asserted patent claims, patent cases incorporate a unique procedure—a *Markman* or claim construction ruling—during which the judge rules on the appropriate meaning of key words and phrases in the patent claims. The court's claim construction ruling often resolves or significantly narrows the scope of the case. Requiring patent trolls to explain and judges to decide what a patent means at the beginning of a case will drive early resolutions, preserve scarce judicial resources, and avoid unnecessary and expensive discovery for the parties.

Staying discovery not necessary to the construction of the claim language until the district court issues its *Markman* decision will force courts to conduct early claim construction, which reduces patent trolls' ability to extract settlements. Trolls often attempt to stretch patent claims far beyond the original invention to support demands for expansive, broad-ranging discovery. Because broad discovery is tremendously expensive and burdensome for the defendant, it is cheaper and easier for many defendants to simply settle with the trolls rather than defend the claim. Determining the scope of the patent right before full discovery stops this practice. Many trolls will drop their case when their specious claim constructions are rejected, and if not, an early *Markman* decision allows courts to consider summary judgment motions and promotes settlement. Even when early case resolution is not possible, early *Markman* decisions narrow and focus discovery, lowering overall costs for all parties.

When a ruling relating to the construction of the patent claims asserted in a complaint is required, Congress should ensure efficient patent litigation by requiring courts to limit discovery to only that information necessary for the court to construe each asserted patent claim until the

claim construction ruling has issued.

Stopping Discovery Abuses

Patent litigation is notoriously expensive. A large portion of that expense comes from the costly discovery process by which the parties disclose of all relevant facts and documents to the other side prior to trial.

When patent trolls sue companies for patent infringement, there is often a dramatic imbalance in the discovery process. Because trolls don't make anything, they have few documents to produce, so their own discovery costs are minimal. They have every incentive, however, to make discovery as expensive and burdensome for their targets as possible by making expansive discovery requests. This, in fact, is a part of the patent troll business model: Patent trolls try to drive-up expenses, and impose them as early as possible in the legal process, by seeking expanded discovery on their targets in order to force a quick cash settlement.

In truth, only a small number of documents produced in litigation are ever relevant to determining liability for patent infringement and most of those would fall within the category of "core documents." To level the discovery playing field, we believe that Congress should mandate that the party seeking discovery beyond core documents pays for the costs associate with the expanded discovery. This will deter unreasonable discovery demands and make litigation more efficient. The parties would still be able to obtain the documents they need, but trolls will not be able to exploit the discovery process to force innocent parties to pay settlements just to avoid crushing legal fees.

Making Abusive Trolls Pay

Patent trolls will often file dozens, and in some cases, hundreds of lawsuits in a single day even though they know the cases have little or no merit. This behavior wastes the judiciary's time and impose tremendous costs on the businesses they sue. Trolls leverage the significant

expense of patent litigation to force defendants to settle to avoid the millions of dollars required to defend a suit. Even *successfully* defending against a meritless patent suit can cost over $1 million in legal fees for a small business and an average of over $6 million for a larger company.

Given how costly it is to go to court, many defendants, even those who know they have not committed any patent infringement, simply choose to settle the case. The inequities in current law force legitimate businesses to choose the lesser of two evils and pay the trolls because fighting the suits is too expensive. This structural imbalance makes the patent troll business model profitable and attractive.

Congress should fix this imbalance by passing legislation to require the winning parties in *truly frivolous* patent cases to be awarded reasonable fees and expenses by the losing party. Because many patent trolls are intentionally designed to be asset-free to avoid this very sort of responsibility, such legislation must also include fee recovery mechanisms, to assure that well-funded backers of abusive shell entity plaintiffs do not escape accountability. This solution would reduce the significant cost leverage that trolls currently enjoy without hindering the ability of patent owners to bring legitimate infringement suits. Moreover, although the proposed reform presumptively awards fees to the prevailing party, it also gives courts discretion to not award fees when the patent owner's position and conduct are substantially justified.

Enhance and Preserve Less Expensive Administrative Alternatives

Our coalition supports balanced possible legislative reforms to eliminate or minimize the incentives that encourage patent trolls to engage in abusive litigation, but no part of those reforms should undermine the existing laws and administrative procedures meant to prevent abuse of the patent system. Foremost among those are the existing procedures for efficiently and fairly challenging questionable patents before the PTO. Any revision of the patent laws must be careful to enhance or maintain, rather than diminish, the PTO's existing procedures for

preventing litigation abuses.

The PTO's implementing rules for the America Invents Act specifically require that the Patent Trial and Appeal Board use the broadest reasonable interpretation (or "BRI") standard when performing claim construction. Thus, the patent system currently maintains two claim construction standards: (1) the BRI standard applied by the PTO; and (2) the narrower *Phillips* standard used by federal courts to determine infringement and invalidity. These parallel standards must be maintained because they eliminate the possibility that a claim, once issued by the PTO, will be interpreted more broadly in the courts than it was before the PTO or can be justified by the underlying application. In addition, the BRI standard serves a public notice purpose of informing potential infringers of the broadest scope of the claims, outside of which there would be no infringement. Congress should preserve the BRI standard as the PTO.

The America Invents Act also introduced an important new post-grant review procedure within the PTO allowing a petitioner to challenge the validity of one or more claims of a recently issued patent. This new administrative, adversarial proceeding acts as an efficient, low-cost alternative to district court litigation. However, the Act also included an estoppel provision providing that the petitioner cannot assert in a later civil action that the challenged claims are invalid "on any ground that the petitioner raised or reasonably could have raised during that post-grant review." Although the inclusion of the expansive "or reasonably could have been raised" language is widely attributed (including by the Act's sponsors) to a scrivener's error made by the legislative staff charged with making technical corrections when the bill was reported by the House Judiciary Committee, it is now law. As written, this provision is both overly broad and vague: Too broad because if the petitioner loses, it forfeits nearly all of its rights to challenge the patent in federal court; and too vague because what a petitioner "reasonably could have raised"

before the PTO remains undefined and unknown. Congress should strike the "reasonably could have raised" language from the text to return the law to its original intent: a means of preventing challengers of patent claims from getting more than one bite at an apple on the same issue.

Conclusion

United for Patent Reform is confident that these changes, all of which simply reflect the realities of effective and efficient patent litigation, will serve to preserve the value of good patents while limiting opportunistic litigation abuse. Although the recent Supreme Court cases made modest and narrow improvements to U.S. patent law, those cases did little to stop patent trolls' lucrative business model of asserting meritless patents and extorting shakedown settlements. Only Congress can pass the multi-faceted reform needed to put them out of business for good. United for Patent Reform stands ready to assist the Congress and its Members in making these proposals a reality.

Submitted Statement for the Record of

Charles Duan
Director, Patent Reform Project
Public Knowledge

Before the
Subcommittee on Courts, Intellectual Property, and the Internet
of the
Committee on the Judiciary
House of Representatives

Hearing on
Examining Recent Supreme Court Cases in the Patent Arena

February 12, 2015

EXAMINING RECENT SUPREME COURT CASES IN THE PATENT ARENA

STATEMENT OF CHARLES DUAN
DIRECTOR, PATENT REFORM PROJECT, PUBLIC KNOWLEDGE

CHAIRMAN ISSA, RANKING MEMBER NADLER, AND MEMBERS OF THE SUBCOMMITTEE:

Thank you for providing me with the opportunity to submit the following testimony for the record of this hearing on recent Supreme Court patent cases.

Public Knowledge is a non-profit organization dedicated to preserving the openness of the Internet and the public's access to knowledge, promoting creativity through balanced intellectual property rights, and upholding and protecting the rights of consumers to use innovative technology lawfully. As part of this mission, Public Knowledge advocates on behalf of the public interest for a balanced patent system, particularly with respect to new and emerging technologies.

In light of these purposes, Public Knowledge has played an active part in the patent cases before the Supreme Court over the past few months. We filed *amicus curiae* briefs in many of those cases, including *Alice Corp. Pty. Ltd. v. CLS Bank International*,[1] *Nautilus, Inc. v. Biosig Instruments, Inc.*,[2] *Octane Fitness, LLC v. Icon Health & Fitness, Inc.*,[3] and *WildTangent, Inc. v. Ultramercial, LLC*,[4] in which we presented the public interest in maintaining a balanced patent system. Furthermore, we have participated closely in discussions on how the decisions in those cases are to be interpreted and implemented, through

[1]Brief of Public Knowledge and the Application Developers Alliance as Amici Curiae in Support of Respondents, *Alice Corp. Pty. Ltd. v. CLS Bank Int'l*, 134 S. Ct. 2347 (Feb. 26, 2014) (No. 13-298) [hereinafter Public Knowledge *Alice* Brief], *available at* https://www.publicknowledge.org/assets/uploads/blog/13-298_bsac_Public_Knowledge_and_the_Application_Developers_Alliance.pdf.

[2]Brief of Public Knowledge and the Electronic Frontier Foundation as *Amici Curiae* in Support of Petitioner, *Nautilus, Inc. v. Biosig Instruments, Inc.*, 134 S. Ct. 2120 (Oct. 23, 2013) (No. 13-369) [hereinafter Public Knowledge *Nautilus* Brief], *available at* https://www.publicknowledge.org/files/pk-nautilus-brief.pdf.

[3]Brief of *Amici Curiae* Electronic Frontier Foundation, Application Developers Alliance, Engine Advocacy, and Public Knowledge in Support of Petitioner, *Octane Fitness, LLC v. Icon Health & Fitness, Inc.*, 134 S. Ct. 1749 (Dec. 9, 2013) (No. 12-1184) [hereinafter Public Knowledge *Octane Fitness* Brief], *available at* https://www.eff.org/files/2013/12/09/octane_v_icon_eff_amicus_brief.pdf.

[4]Brief of Amicus Curiae Public Knowledge in Support of Petitioner, *WildTangent, Inc. v. Ultramercial, LLC*, 134 S. Ct. 2870 (Sept. 23, 2013) (No. 13-255), *available at* https://www.publicknowledge.org/files/wildtangent-v-ultramercial-pk-amicus.pdf.

two appellate court *amicus* briefs,[5] comments on the USPTO's *Alice* guidance to patent examiners,[6] an empirical research article,[7] published commentary and opinion pieces,[8] and panel discussions.[9]

Briefly, the statement below makes the following three points:

1. **Patent law must be balanced and crafted to serve the public interest, because abusive patent litigation is the direct result of unbalanced patent law.** The Constitution mandates that patents must promote innovation and progress, and specifically warns that excessive patent protection will have the opposite effect. Unfortunately, patent law today has lost sight of this important goal, often making it too easy to obtain an overbroad patent on ordinary, noninventive ideas, and making it too easy to use those patents as a weapon against small businesses, consumers, and the economy in general.

2. **The Supreme Court's decisions reflect a careful attempt to restore that balance.** The Court frequently invokes the principle that patent law must be calibrated to provide a sufficient incentive for inventors to invent, but also to ensure a degree

[5]Brief of *Amicus Curiae* Public Knowledge in Support of Defendant-Appellee, *Ultramercial, Inc. v. Hulu, LLC*, 772 F.3d 709 (Fed. Cir. Aug. 28, 2014) (No. 10-1544), *available at* https://www.publicknowledge.org/assets/uploads/documents/brief-ultramercial-cafc-supp.pdf; Brief of Amici Curiae Application Developers Alliance, Computer and Communications Industry Association, Electronic Frontier Foundation, Engine Advocacy, National Restaurant Association, and Public Knowledge in Support of Defendant-Appellee Bravo Media, LLC, *DietGoal Innovations LLC v. Bravo Media LLC*, No. 14-1631 (Fed. Cir. Nov. 24, 2014), *available at* https://www.eff.org/files/2014/11/25/14-1631_dietgoal_amicus_final.pdf.

[6]Charles Duan & Joseph Savage, *Comments of Public Knowledge on Examination Instruction and Guidance Pertaining to Patent-Eligible Subject Matter* (USPTO July 31, 2014), http://www.uspto.gov/sites/default/files/patents/law/comments/al-a-publicknowledge20140731.pdf.

[7]Tristan Gray–Le Coz & Charles Duan, *Apply It to the USPTO: Review of the Implementation of Alice v. CLS Bank in Patent Examination*, 2014 PATENTLY-O PAT. L.J. 1, http://patentlyo.com/media/2014/11/GrayLeCozDuan.pdf.

[8]*E.g.*, Charles Duan, *A Definite Problem of Patent Law: Nautilus v. Biosig Instruments*, JURIST PROF. COMMENT. (May 7, 2014), http://jurist.org/hotline/2014/05/charles-duan-patents-natilus.php; Charles Duan, *Would You Like a Patent Lawsuit with Your Meal?*, ROLL CALL (Dec. 18, 2014), http://www.rollcall.com/news/would_you_like_a_patent_lawsuit_with_your_meal_commentary-238838-1.html (discussing *Alice Corp. Pty. Ltd. v. CLS Bank International*, 134 S. Ct. 2347 (2014)).

[9]*E.g.*, *Supreme Court Series:* Nautilus, Inc. v. Biosig Instruments, Inc., PROGRAM ON INFORMATION JUSTICE AND INTELLECTUAL PROPERTY, AMERICAN UNIVERSITY WASHINGTON COLLEGE OF LAW (Apr. 28, 2014) (panel discussion), http://www.pijip.org/events/nautilus/.

of freedom for the public so that future innovations may occur. All of the decisions of the Court have strived to implement this principle. In particular, the *Alice* decision is not a dilution of patent rights, as some critics have called it. Rather, it is a return to the crucial first principles of patent law, that a balanced patent system requires basic, fundamental ideas to be free for everyone to use, lest ownership of such basic ideas blockade further innovation.

3. **Patent reform is a multifaceted effort, and Congress must play a role even in view of the Supreme Court decisions.** In particular, while Congress has tended to focus on process issues of how patents are used and litigated, the Court's decisions have dealt more with the substance of what subject matter is patentable and how patents are to be interpreted. Neither is sufficient to fully repair the patent system, but both are necessary and urgently needed.

Further general information on patent reform issues generally may be found at Public Knowledge's whitepaper, *A Five Part Plan for Patent Reform.*[10]

I. The Present Plague of Patent Abuse Derives from a Misbalancing of the Patent System

The patent system is in crisis. Abusers take advantage of questionable patents on basic ordinary technologies—ones that you and I use every day, such as scanners[11] and Wi-Fi[12]—turning those patents into weapons for threatening businesses big and small. Such abuses have cost our economy billions of dollars,[13] have destroyed small startups and com-

[10] Charles Duan, Pub. Knowledge, A Five Part Plan for Patent Reform (2014), *available at* https://www.publicknowledge.org/documents/a-five-part-plan-for-patent-reform.

[11] *See, e.g.*, Joe Mullin, *Patent Trolls Want $1,000—for Using Scanners*, Ars Technica (Jan. 2, 2013), http://arstechnica.com/tech-policy/2013/01/patent-trolls-want-1000-for-using-scanners/.

[12] *See* John Ribeiro, *Cisco Reaches Agreement with Innovatio over Wi-Fi Patents*, PCWorld (Feb. 7, 2014), http://www.pcworld.com/article/2095700/cisco-reaches-agreement-with-innovatio-over-wifi-patents.html.

[13] *See* James Bessen et al., *The Private and Social Costs of Patent Trolls*, Regulation, Winter 2011–2012, at 26, http://object.cato.org/sites/cato.org/files/serials/files/regulation/2012/5/v34n4-1.pdf.

panies,[14] and have kept valuable innovations and technologies out of the hands of American consumers.[15] And with the rapid growth of computers, the Internet, and emerging technologies such as 3D printing,[16] the problem of abusive patent assertion has rapidly grown as well, developing into an entire industry of so-called Patent Assertion Entities.[17]

This crisis of patents is unfortunate because patents are not intended to impede innovation and growth—patents are intended for the exact opposite. The purpose of our patent system is enshrined in the Constitution: "to promote the Progress of Science and the useful Arts."[18] But to promote that progress, the patent system must be delicately balanced. While patent protection can certainly incentivize new inventions, "sometimes too much patent protection can impede . . . the constitutional objective."[19] Finding that right balance is difficult, but it is not impossible. So despite the naysayers who refuse to reform a troubled patent system, professing that patent abuse is the unavoidable[20]—or, worse yet, *desirable*[21]—effect of patent law, I believe that effective patent reform can bring our system in line with those constitutional ideals of promoting progress, by carefully striking a "balance between the interest in motivating innovation and enlightenment . . .

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[14] *See* COLLEEN V. CHIEN, NEW AM. FOUND., PATENT ASSERTION AND STARTUP INNOVATION 17 fig.3 (2013), http://www.newamerica.net/publications/policy/patent_assertion_and_startup_innovation.

[15] *See id.* at 18 (quoting interview with investor describing one of its investments) ("The company develops and sells novel therapeutic medical devices to treat patients in pain. The suit by the NPE will result in the company changing its hiring and commercialization plans to deal with the suit, or worse the current suit may put company out of business." (internal quotations and alterations omitted)).

[16] *See* MICHAEL WEINBERG, PUB. KNOWLEDGE, IT WILL BE AWESOME IF THEY DON'T SCREW IT UP: 3D PRINTING, INTELLECTUAL PROPERTY, AND THE FIGHT OVER THE NEXT GREAT DISRUPTIVE TECHNOLOGY 7–8 (2010), *available at* https://www.publicknowledge.org/files/docs/3DPrintingPaperPublicKnowledge.pdf.

[17] *See, e.g.*, EXECUTIVE OFFICE OF THE PRESIDENT, PATENT ASSERTION AND U.S. INNOVATION 5 (2013), *available at* http://www.whitehouse.gov/sites/default/files/docs/patent_report.pdf.

[18] U.S. CONST. art. I, § 8, cl. 8.

[19] *Lab. Corp. of Am. Holdings v. Metabolite Labs., Inc.*, 548 U.S. 124, 126–27 (2006) (Breyer, J., dissenting from dismissal of certiorari) (emphasis in original).

[20] *See* Stephen Haber & Ross Levine, *The Myth Of the Wicked Patent Troll*, INNOVATION ALLIANCE (June 29, 2014), http://innovationalliance.net/patent-news/wall-street-journal-myth-wicked-patent-troll/ (describing 60% increase in patent litigation as "reflect[ing] a healthy, dynamic economy").

[21] *See* Adam Mossoff, *Thomas Edison Was a "Patent Troll"*, SLATE: HISTORY OF INNOVATION (May 19, 2014), http://www.slate.com/articles/technology/history_of_innovation/2014/05/thomas_edison_charles_goodyear_and_elias_howe_jr_were_patent_trolls.html (describing so-called "patent trolls" as "essential to how the patent system has been a driver of America's innovation economy for more than two centuries").

and the interest in avoiding monopolies that unnecessarily stifle competition."[22]

And every branch of the United States government agrees, for every branch of the United States government has sought to play its part in rebalancing that patent system. Congress, with support of the Administration, has introduced legislation to "level the playing field" for patent litigation.[23] The U.S. Patent and Trademark Office has embarked on numerous initiatives to improve patent quality, because, as Acting Director Michelle Lee said, fixing the patent system is "about maintaining the public's faith that the benefits of patents outweigh their costs to society."[24] And, critically, the Supreme Court has taken a handful of patent cases on questions of what matter ought to be patentable and how the substantive rules of patent law ought to be applied.

The common threads among these diverse efforts at patent reform are twofold: first, a recognition that the patent system has gone awry and requires repair, and second, an aim to center patent policy at a balanced position that promotes the progress of science and the useful arts. These themes are reiterated time and time again in the Supreme Court's decisions, and it is to a selection of the most important of those recent decisions that I now turn.

II. The Supreme Court's Patent Decisions Uniformly Reflect the Criticality of a Balanced Patent System Serving the Public Interest

The following is a summary of key patent cases decided by the Supreme Court in 2014. As will be seen, the common theme throughout all the decisions is a focus on maintaining a balanced patent system dedicated to the public interest.

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[22] *Pfaff v. Wells Elecs., Inc.*, 525 U.S. 55, 63 (1998).

[23] *See* Innovation Act, H.R. 3309, 113th Cong. (2013); House Comm. on the Judiciary, 113th Cong., *The Innovation Act Will Level the Playing Field for Small Businesses and Start-Ups* (Nov. 20, 2013), http://content.govdelivery.com/attachments/USHRC/2013/12/02/file_attachments/255001/%2528Courtesy%2Bof%2Bthe%2BJudiciary%2BCommittee%2529%2BHR%2B3309%2BHandout%2B-%2BSmall%2BBusiness.pdf; Press Release, Office of the Press Sec'y, The White House, *Fact Sheet—Executive Actions: Answering the President's Call to Strengthen Our Patent System and Foster Innovation* (Feb. 20, 2014), http://www.whitehouse.gov/the-press-office/2014/02/20/fact-sheet-executive-actions-answering-president-s-call-strengthen-our-p.

[24] Michelle K. Lee, Deputy Under Sec'y of Commerce for Intellectual Prop., *Speaking Truth to Patents: The Case for a Better Patent System, Remarks at Stanford Law School* (June 26, 2014), http://www.uspto.gov/about-us/news-updates/speaking-truth-patents-case-better-patent-system.

A. *Alice Corp. Pty. Ltd. v. CLS Bank International*: Protecting the Common Idea from Exclusive Monopoly

Among the Supreme Court's decisions on patents, *Alice* was undoubtedly the most widely discussed and the most controversial. Scholars, reporters, and attorneys debated how the case would affect software companies and patent abusers.[25] Given this spirited debate over the decision, one would imagine that it was a complex case dealing with highly technical aspects of law. But, in fact, *Alice* was actually a very simple case.

The question in *Alice* was whether basic, simple ideas are patentable simply because they are done on a computer rather than, say, by pencil and paper. The Supreme Court said they are not.

Public Knowledge's *amici curiae* brief,[26] filed together with the Application Developers Alliance, clearly illustrates this point of how the patent at issue was just a basic idea run on a computer. The patent itself, of course, did not make this clear, confusingly setting forth the patent's claims, the part of the patent text where the inventor defines the invention, in 200-word-long sentences, set forth in full in the footnote.[27] But, as our brief

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[25] *See, e.g.*, Julie Samuels, *The Supreme Court Gets Tech Right With This Software Patent Ruling*, Slate: Future Tense (June 20, 2014), http://www.slate.com/articles/technology/future_tense/2014/06/alice_v_cls_bank_supreme_court_gets_software_patent_ruling_right.html; Richard H. Stern, Alice v. CLS Bank: *Are US Business-Method and Software Patents Doomed? Part 1*, IEEE Micro, Sept./Oct. 2014, at 64.

[26] Public Knowledge *Alice* Brief, *supra* note 1.

[27] *See id.* app. B, at 8a–9a. The claim printed there reads:

A data processing system to enable the exchange of an obligation between parties, the system comprising:
a communications controller,
a first party device, coupled to said communications controller,
a data storage unit having stored therein
(a) information about a first account for a first party, independent from a second account maintained by a first exchange institution, and
(b) information about a third account for a second party, independent from a fourth account maintained by a second exchange institution; and
a computer, coupled to said data storage unit and said communications controller, that is configured to
(a) receive a transaction from said first party device via said communications controller;
(b) electronically adjust said first account and said third account in order to effect an exchange obligation arising from said transaction between said first party and said second party after ensuring that said first party and/or said second party have adequate value in said first account and/or said third account, respectively; and
(c) generate an instruction to said first exchange institution and/or said second exchange institution to adjust said second account and/or said fourth account in accordance with the adjustment of said first account and/or said third account, wherein said instruction being an irrevocable, time invariant obligation placed on said first exchange institution and/or said second exchange institution.

showed, those two hundred words did not define a complex or intricate technology. They did not define an "invention" in the ordinary sense of that word.

Those 200-word sentences defined nothing more than the idea of using a computer to exchange money through a broker.[28]

The patented idea was so simple, in fact, that we were able to write a program to do all the steps of that money exchange—in just seven lines of computer code, shown in the footnote.[29] For comparison, the seven lines of code are shorter than the ten-minute homework problems from my college introductory Computer Science textbooks. Based on this showing, we argued that the patent could not pass muster because it described nothing more than a basic idea run on a computer.

The Supreme Court agreed. In a unanimous decision, Justice Thomas began with the rule that "[l]aws of nature, natural phenomena, and abstract ideas are not patentable."[30] These categories are outside the realm of patent, he said, because a balanced patent law must "not inhibit further discovery by improperly tying up the future use of these building blocks of human ingenuity."[31] In other words, certain ideas are so basic and fundamental that to allow such ideas to be tied up in patents would prevent future ideas from being discovered, thus frustrating the constitutional premise of having patents promote progress.

Furthermore, the Court decided that simply running one of those basic ideas on an ordinary computer did not merit a patent either. Because computers are a "wholly generic" technology, and "[g]iven the ubiquity of computers," the Court concluded that a

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[28] *See id.* at 9.

[29] *Id.* at 6–7. The full code reads as follows:

```
10 LET account1 = 200.00
20 LET account3 = 300.00
30 INPUT "Value to exchange for transaction"; exchange
40 IF account1 < exchange THEN PRINT "Inadequate value" : STOP
50 account1 = account1 − exchange
60 account3 = account3 + exchange
70 PRINT "Instruction to 1st institution: adjust 2nd account by "; −exchange
```

[30] *Alice Corp. Pty. Ltd. v. CLS Bank Int'l*, 134 S. Ct. 2347, 2354 (2014).

[31] *Id.*

patent on a computer running a basic idea was no better than a patent on the basic idea itself.[32]

Alice thus clearly represents the Supreme Court's effort to develop well balanced patent jurisprudence based on the public interest. The very justification behind the Court's ban on patents on basic, fundamental ideas is that the public interest requires such ideas, being "the basic tools of scientific and technological work," be free for all to use.[33] A patent on such a basic idea "might tend to impede innovation more than it would tend to promote it, thereby thwarting the primary object of the patent laws."[34] Furthermore, the Court repeatedly expressed concern about strict rules that would "make patent eligibility depend simply on the draftsman's art," because these principles of maintaining the freedom of basic ideas should not be easily thwarted by clever lawyering.[35]

Thus, *Alice* represents a strong shift toward a more balanced patent system, spearheaded by the Supreme Court. It is thus surprising to me that some, particularly patent attorneys, have called the Supreme Court "Public Enemy Number One for Patent Owners."[36] In fact, the Court's decisions are based wholly on championing the public interest, removing loopholes that permitted patents on ideas never meant for ownership, ensuring that the public retains access to "what is free for all to use."[37]

B. *Nautilus, Inc. v. Biosig Instruments, Inc.*: Ensuring that Patents Make Sense

Part of the difficulty with *Alice* stemmed from the fact that a simple idea about money brokering was masked in 200 words of complex patent language. This broader problem, of patents being unnecessarily difficult to understand, is well recognized to be a

[32] *Id.* at 2358.
[33] *Id.* at 2354 (quoting *Ass'n for Molecular Pathology v. Myriad Genetics, Inc.*, 133 S. Ct. 2107, 2116 (2013)).
[34] *Id.* (quoting *Mayo Collaborative Servs. v. Prometheus Labs., Inc.*, 132 S. Ct. 1289, 1923 (2012)).
[35] *Id.* at 2360 (quoting *Parker v. Flook*, 437 U.S. 584, 593 (1978)).
[36] Gene Quinn, *SCOTUS: Public Enemy Number One for Patent Owners*, IP Watchdog (Oct. 2, 2014), http://www.ipwatchdog.com/2014/10/02/scotus-public-enemy-number-one-for-patent-owners/id.
[37] *Bonito Boats, Inc. v. Thunder Craft Boats, Inc.*, 489 U.S. 141, 151 (1989).

major contributor to patent abuse.[38] The Supreme Court sought to curb that sort of abuse in the *Nautilus* case.

Public Knowledge and the Electronic Frontier Foundation filed an *amici curiae* brief arguing that patents must clearly define what infringes and what does not, because "ambiguous patent claims would create a 'zone of uncertainty' . . . and thereby 'discourage invention.' "[39] We analogized patent claims on inventions to title claims on land:

> A developer wishes to build a hotel by a highway, and is searching the records of deeds for a prospective plot of land. The search reveals a recordation of an easement stating in part, "the western boundary is in a *spaced relationship* with the highway."
>
> What can the developer do? "Spaced relationship" could mean a foot from the highway, or a yard, or a mile. The developer could guess at the meaning, but a wrong guess could render the entire investment in building the hotel a waste. Should the case be brought to court, different judges or juries could reasonably disagree on the meaning. Worse yet, when the easement owner sues the developer, the owner will have the benefit of hindsight in making his argument for interpreting the property claim, but the developer has no such benefit when choosing where to build the hotel. The cards are stacked against the developer, a deadweight loss for the hotel business and for the economy at large.
>
> . . . .
>
> Such ambiguous descriptions of the metes and bounds of real property would never be tolerated, but for years the Federal Circuit has tolerated equally ambiguous descriptions of the metes and bounds of patents. Indeed, the term "spaced relationship," so clearly improper in the hypothetical example above, is the exact term held "definite" by that court in the present case.[40]

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[38] *See* Bessen et al., *supra* note 13, at 34 (tracing how patents with "fuzzy boundaries" have created "a business opportunity based on acquiring patents that can be read to cover existing technologies and asserting those patents"); FED. TRADE COMM'N, THE EVOLVING IP MARKETPLACE: ALIGNING PATENT NOTICE AND REMEDIES WITH COMPETITION 85 (2011) (noting stakeholder comments that the patent system "generally creates 'an incentive to be as vague and ambiguous as you can with your claims' and to 'defer clarity at all costs.' "); PHIL GOLDBERG, PROGRESSIVE POLICY INST., STUMPING PATENT TROLLS ON THE BRIDGE TO INNOVATION 3 (2013) (citing "vague or expansive terms" in patents as one of "three cross winds" creating a flood of patent litigation); David Segal, *Has Patent, Will Sue: An Alert to Corporate America*, NEW YORK TIMES, July 14, 2013, BU1 ("But as long as the [patent] system exists, [noted patent assertor Erich] Spangenberg is going to exploit its ambiguities and pokiness for all it's worth."); JAMES BESSEN & MICHAEL J. MEURER, PATENT FAILURE: HOW JUDGES, BUREAUCRATS, AND LAWYERS PUT INNOVATORS AT RISK 164 (2008) ("The evidence suggests . . . that the deterioration of the notice function might be the central factor fueling the growth in patent litigation").

[39] Public Knowledge *Nautilus* Brief, *supra* note 2, at 5 (quoting *United Carbon Co. v. Binney & Smith Co.*, 317 U.S. 228, 236 (1942)).

[40] *Id.* at 2–3.

We thus argued that the Supreme Court should set a high bar for clarity of patents, requiring that a patent applicant "provide clear and unambiguous claim language describing the scope of his or her invention."[41] Such unambiguous claims "serve the public interest by ensuring that patents are kept within their legitimate scope," we wrote.[42]

The Supreme Court agreed. Writing for a unanimous Court, Justice Ginsburg initially noted that the decision was controlled by a need for a "delicate balance" of patent law.[43] Implementing that balance, the Court concluded that the law "mandates clarity, while recognizing that absolute precision is unattainable." Thus, the Court enunciated a standard that a patent's claims must "inform those skilled in the art about the scope of the invention with reasonable certainty."[44] Thus, just as our brief suggested, the Court applied the age-old principle of balancing patent holder interests against those of the public, to arrive at a threshold of patent clarity that would ultimately serve the public good of fair notice of the coverage of patents.

C. *Octane Fitness, LLC v. Icon Health & Fitness, Inc.*: Keeping Abusive Patent Assertion at Bay

While *Alice* and *Nautilus* dealt with the content of patents, *Octane Fitness* and its companion case *Highmark Inc. v. Allcare Health Management System, Inc.*[45] related to the litigation process of asserting patents. Specifically, the cases considered a statutory provision, commonly known as a "fee shifting" provision, that provides that a court "in exceptional cases may award reasonable attorney fees to the prevailing party."[46]

This sort of fee shifting provision is long established[47] and important to patent cases because it serves as a check on overzealous patent assertion—again ensuring that the in-

[41] *Id.* at 21.

[42] *Id.* at 22.

[43] *Nautilus, Inc. v. Biosig Instruments, Inc.*, 134 S. Ct. 2120, 2128 (2014) (quoting *Festo Corp. v. Shoketsu Kinzoku Kogyo Kabushiki Co.*, 535 U.S. 722, 731 (2002)).

[44] *Id.* at 2129.

[45] *Highmark Inc. v. Allcare Health Mgmt. Sys., Inc.*, 134 S. Ct. 1744 (2014).

[46] 35 U.S.C. § 285 (2013).

[47] *See Octane Fitness, LLC v. Icon Health & Fitness, Inc.*, 134 S. Ct. 1749, 1753 (2014) (noting historical origins of § 285 dating back to 1946).

centives for patent assertion remain balanced between the interests of patent owners and the interests of the public. Indeed, the Court of Appeals for the Federal Circuit has applied that statutory fee shifting in a case where a patent owner "acted in bad faith by exploiting the high cost to defend complex litigation to extract a nuisance value settlement."[48]

However, as Public Knowledge and three other organizations argued, the Federal Circuit had misinterpreted that fee shifting law, making it too difficult for prevailing parties to obtain fees.[49] This undue difficulty, the burden of which primarily fell on the shoulders of patent lawsuit defendants, had the effect of facilitating the rise in abusive litigation that so plagues the patent system today.[50] As we argued:

> Commentators have rightfully laid blame for the rise in abusive patent litigation on many issues, such as dubious patent quality and the lack of transparency surrounding patent ownership. But *amici* find a significant concern drives much of the problem, particularly as it relates to the small businesses and startups it represents. That concern is the issue of this case: an inability to hold abusers accountable, due to an inappropriately high bar for attorney fee shifting, created by an overzealous Federal Circuit misinterpreting Section 285 of the Patent Act.
>
> Read correctly, that section deters abusive and frivolous litigation by protecting defendants through the recovery of attorneys' fees and costs. But the Federal Circuit's erroneous interpretation fails to provide any substantial promise—or even hope—of recovering those fees and costs in even the most egregious infringement cases.
>
> The consequence of the Federal Circuit's withering of Section 285 protection is the creation of an industry of patent abusers, decimating the very small businesses and startups that drive American innovation.[51]

To make the fee shifting statute effective in deterring abusive behavior, we urged the Court to adopt a standard whereby a defendant could have legal fees compensated in "objectively weak" cases or where the patent owner "uses the cost of defense as a weapon."[52]

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[48] *Eon-Net LP v. Flagstar Bancorp*, 653 F.3d 1314, 1327 (Fed. Cir. 2011).

[49] *See* Public Knowledge *Octane Fitness* Brief, *supra* note 3, at 7–8.

[50] *See id.* at 9 ("A potential defendant who faces a lawsuit with no hope of remuneration and the prospect of mounting legal bills or an escape route [of paying a settlement to a patent assertion entity] for a fraction of those bills will almost always chose the escape route even where that payment is not justified.").

[51] *Id.* at 4.

[52] *Id.* at 17 (capitalization altered).

Consistent with our arguments, the Supreme Court rejected the Federal Circuit's framework for fee shifting as being "unduly rigid."[53] Instead, the Court adopted a "totality of the circumstances" rule, permitting district courts to use their discretion to determine whether a case was "one that stands out from others with respect to the substantive strength of a party's litigating position (considering both the governing law and the facts of the case) or the unreasonable manner in which the case was litigated."[54]

Perhaps most noteworthy about the Supreme Court's decision in *Octane Fitness* is the uniform rejection of the Federal Circuit's justifications. *Octane Fitness* effectively overruled a Federal Circuit case known as *Brooks Furniture Manufacturing, Inc. v. Dutailier International, Inc.*, which had imposed that now-defunct higher bar for fee shifting.[55] The Court found three defects with *Brooks Furniture*. First, *Brooks Furniture* had derived its strict rule from Supreme Court precedent on the *Noerr-Pennington* doctrine on protecting the First Amendment right to petition.[56] But the Court rejected this analogy, saying that the need to protect patent owners from claims of legal fees was an order of magnitude off from the need to protect litigants' rights to access courts.[57] Second, *Octane Fitness* noted that the *Brooks Furniture* standard for fee shifting was so high, that it would be rendered superfluous.[58] Finally, the Supreme Court rejected the Federal Circuit's notion that entitlement to a fee shifting award must be proven by "clear and convincing evidence," on the grounds that no other fee shifting statute had ever been interpreted to require such a high showing of evidence.[59]

The discrepancy between *Brooks Furniture* and *Octane Fitness* reflects a larger trend of discrepancies between the Federal Circuit and the Supreme Court. The Federal Circuit's decisions, such as those in *Brooks Furniture*, have led some commentators to criticize the

[53] *Octane Fitness, LLC v. Icon Health & Fitness, Inc.*, 134 S. Ct. 1749, 1755 (2014).
[54] *Id.* at 1756.
[55] *See Brooks Furniture Mfg., Inc. v. Dutailier Int'l, Inc.*, 393 F.3d 1378, 1381 (Fed. Cir. 2005).
[56] *See Octane Fitness*, 134 S. Ct. at 1757.
[57] *See id.* at 1757–58.
[58] *See id.* at 1758.
[59] *See id.*

court for taking an unbalanced position favoring patent owners.[60] In contrast, as shown by the above discussion of *Octane Fitness*, *Alice*, and *Nautilus*, the Supreme Court strongly focuses on the constitutional requirement for a balanced patent system to arrive at and justify its decisions on patent law. And the other patent cases decided by the Supreme Court in its last Term, namely *Limelight Networks, Inc. v. Akamai Technologies, Inc.*[61] and *Medtronic, Inc. v. Mirowski Family Ventures, LLC*,[62] further reflect the Supreme Court's rejection of patent-friendly Federal Circuit decisions in favor of balanced, public-oriented rules of patent law.[63]

The Supreme Court's approach is the right one. Besides being mandated by the Constitution, it best serves the public interest in encouraging inventors with the reward of a patent while ensuring that the patent reward does not go so far as to actually undercut further innovators, small businesses, and ordinary consumers.

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[60] *See, e.g.*, Matthew D. Henry & John L. Turner, *The Court of Appeals for the Federal Circuit's Impact on Patent Litigation*, 35 J. LEGAL STUD. 85, 87 (2006) ("Not surprisingly, the CAFC has earned a reputation as a pro-patent court."); Eli Dourado, *The True Story of How the Patent Bar Captured a Court and Shrank the Intellectual Commons*, CATO UNBOUND (Sept. 8, 2014), http://www.cato-unbound.org/2014/09/08/eli-dourado/true-story-how-patent-bar-captured-court-shrank-intellectual-commons ("The consolidation of patent appeals into a single court also concentrated the benefits that pro-patent interests could get by lobbying to affect the judicial nomination and confirmation process."); Jeff Bleich & Josh Patashnik, *The Federal Circuit Under Fire*, SAN FRANCISCO ATTORNEY, Fall 2014, at 40, 41, *available at* http://www.mto.com/Templates/media/files/Reprints/Bleich%20%20Patashnik%20--%20Supreme%20Court%20Watch%20Fall%202014.pdf ("This continues a trend stretching back several years now, in which the Supreme Court has repeatedly rejected the Federal Circuit's patent-friendly approach in a range of cases . . . ."); Timothy B. Lee, *Obama Wants to Fix the Patent System. Here's a Crucial Reform He Overlooked*, WASHINGTON POST: THE SWITCH (Jan. 29, 2014), http://www.washingtonpost.com/blogs/the-switch/wp/2014/01/29/obama-wants-to-fix-the-patent-system-heres-a-crucial-reform-he-overlooked/ ("And the Supreme Court's repeated reversals of patent-friendly rulings suggest that the [Federal Circuit] is biased toward the interests of trolls and other patent holders.").

[61] *See Limelight Networks, Inc. v. Akamai Techs., Inc.*, 134 S. Ct. 2111, 2117 (2014) (rejecting Federal Circuit's novel indirect infringement theory as "fundamentally misunderstand[ing] what it means to infringe a method patent").

[62] *See Medtronic, Inc. v. Mirowski Family Ventures, LLC*, 134 S. Ct. 843, 851 (2014) (rejecting Federal Circuit's rule swapping burden of proof from patent owners to defendants, because "we see no convincing reason why burden of proof law should favor the patentee").

[63] *See generally* Robin Feldman, *Coming of Age for the Federal Circuit*, 18 GREEN BAG 2D 27 (2014), *available at* http://www.greenbag.org/v18n1/v18n1_articles_feldman.pdf (describing the contrary approaches of the Federal Circuit and the Supreme Court to patent law).

III. Legislative Patent Reform Must Move Forward, Because Congress Is Focusing on Different Aspects of the Patent System than the Supreme Court Decisions Address

Given that the Supreme Court has made substantial progress toward achieving a balanced patent system, members of Congress may ask what role remains for them to play in patent reform. Indeed, many of those entrenched in the patent status quo have claimed that congressional efforts are no longer needed, because the Supreme Court has taken care of patent reform.[64]

The answer is that there is still an enormous role for Congress to play in patent reform, because Congress and the courts are addressing different aspects of a very large set of systemic problems with the patent system. Specifically, Congress has primarily focused on *procedure* for using patents after they are issued, such as sending of patent demand letters,[65] litigation over patents,[66] and post-grant proceedings before the U.S. Patent and Trademark Office.[67] In contrast, the Supreme Court cases have primarily focused on the *substance* of what patents ought to properly exist and what those patents cover.[68]

It might seem that *Octane Fitness* is the exception because that case deals with litigation procedure. But in fact Congress is dealing with a different aspect of fee shifting than *Octane Fitness* contemplated. The Supreme Court decided only what the level of fee shifting should be, in the context of particular existing statutory language that fees shall be awarded in "exceptional" cases. But Congress has the opportunity to change the statutory

[64] *See, e.g.*, Richard Lloyd, *Patent Reform Delayed, Not Dead; Pause Could Mean Better Legislation, Says Market*, Innovation Alliance (May 22, 2014), http://innovationalliance.net/patent-news/intellectual-asset-management-patent-reform-delayed-dead-pause-mean-better-legislation-says-market-richard-lloyd/ ("The two recent decisions on fee shifting may have been the Supreme Court telling Congress to back off and let them deal with it." (quoting Anthony Hayes, Spherix)); Ashby Jones, *Patent Reform Bill Arises Again in Congress*, Wall Street Journal: Law Blog (Feb. 5, 2015), http://blogs.wsj.com/law/2015/02/05/patent-reform-bill-arises-again-in-congress/ ("A host of biotech companies and others—including Qualcomm Inc., Merck & Co., and Monsanto Co.—object to the bill, claiming recent other measures have adequately reined in the worst litigation abuses.").

[65] *See* Demand Letter Transparency Act, H.R. 3540, 113th Cong. (2013).

[66] *See* Innovation Act, H.R. 3309, 113th Cong. (2013); Patent Abuse Reduction Act, S. 1013, 113th Cong. (2013).

[67] *See* Patent Quality Improvement Act, S. 866, 113th Cong. (2013).

[68] *See Alice Corp. Pty. Ltd. v. CLS Bank Int'l*, 134 S. Ct. 2347 (2014); *Nautilus, Inc. v. Biosig Instruments, Inc.*, 134 S. Ct. 2120 (2014); *Limelight Networks, Inc. v. Akamai Techs., Inc.*, 134 S. Ct. 2111 (2014).

language to better fit the realities of patent litigation today, and it has the opportunity to devise new procedures under which courts will decide whether to shift fees. The Court was bound by the existing statutory language, but Congress, being free of that restriction, may apply all of its tools of policy expertise to crafting an improved law.

There is no question that the need for Congressional action on patent reform is urgent. As I explained previously, abuses of the patent system are growing in number, magnitude, and destructive effect on the economy. Without prompt action, our current patent system will continue to step further and further away from that ideal balance of patent law that best protects and benefits the American people, making it only more likely that patents will be abused and misused, making it only more difficult as time passes to return that patent law to solid footing.

As I have stated before: "There is no silver bullet to patent reform, and improving the patent system will require a long-term, multifaceted effort."[69] Congress has an important role to play in addressing that problem. A patent reform bill, the Innovation Act,[70] made substantial headway last year. I am encouraged to see it reintroduced, and I look forward to working with the Committee to craft a strong, effective bill that will maintain the necessary balance of patent law, protect the public interest, and promote the progress of science and the useful arts.

Thank you again for providing me with the opportunity to submit the foregoing written statement. If members of the Subcommittee have any follow-up questions, I am happy to provide further information as will be helpful.

[69]DUAN, *supra* note 10, at 2.
[70]H.R. 3309.

Patent troll targets crowdfunding startups — Innovation Act could stop that

Image Credit: mangostock/Shutterstock

February 10, 2015 6:00 PM
D.J. Paul, CFIRA and Julie Samuels, Engine

On Thursday, House Judiciary Chairman Bob Goodlatte (R-VA) re-introduced the Innovation Act, a bipartisan bill targeted at fixing the out-of-control patent troll problem.

This comes not a moment too soon, as patent trolls have begun to target one of the newest areas of innovation and job creation: the crowdfunding industry.

AlphaCap Ventures, an entity that claims to offer "strategic, operations, and financial advisory services in the United States" and whose website resolves to nothing, has so far sued at least

10 companies engaged in some form of crowdfunding. They accuse each company of infringing upon multiple patents (you can see one here) that allegedly cover the very basic workings of managing customer information as it relates to private equity and debt markets.

On its face, the AlphaCap cases look sadly typical. There's no evidence that AlphaCap has its own crowdfunding platform. Instead it appears to be using its patents as a tool of extortion against those who are actually creating something valuable for our economy.

Crowdfunding platforms have become an important part of the innovation economy, giving entrepreneurs unprecedented access to the capital they need to grow a business or launch a project. They're also beginning to democratize finance: Women are nearly four times more successful when crowdfunding than when raising funds through traditional means like venture capital.

Unfortunately, many of these platforms are small and young — the most popular targets for patent trolls. In fact, 55 percent of troll suits are filed against companies with revenues of less than $10 million.

Fortunately, the Innovation Act gives the startup community a chance to fight back against trolls. This bill won't stop patent holders from filing legitimate lawsuits, but it will give those unfairly targeted by trolls important tools to fight back. Among other things, it will require more transparency, shift costs of discovery — one of the most expensive costs of litigation — and shift legal fees when plaintiffs bring particularly baseless suits.

As the Innovation Act makes its way through Congress, it's sure to meet opposition from some of the same powerful special interests groups, namely trial lawyers and pharmaceutical companies, who thwarted previous attempts at patent reform as recently as last spring. That's why both startups and individuals who care about innovation need to make our voices heard in the weeks ahead. We need to send a message to members of both parties: Move quickly to support and pass this critical legislation.

For more insights from tech industry insiders,
explore VentureBeat's selection of recent guest posts.

Companies like AlphaCap have every legal right to own patents and file infringement actions based on those patents — that won't change with passage of patent reform. What will change is that defendants will be emboldened to fight back, righting a system that has been lopsided for too many years. After all, the patent system is meant to incentivize innovation, not hinder it.

Julie Samuels is executive director of Engine, a nonprofit that supports the growth of technology entrepreneurship through economic research, policy analysis, and advocacy on local and national issues.

D.J. Paul is member of the Securities and Exchange Commission's Advisory Committee on Small and Emerging Companies, and the co-chair of the Crowdfund Intermediary Regulatory Advocates (CFIRA). He is the founder of DJP&Co., a consulting firm within the investment crowdfunding space.

http://venturebeat.com/2015/02/10/patent-troll-targets-crowdfunding-startups-innovation-act-could-stop-that/?utm_campaign=naytev&utm_content=54db3d43e4b07fbd5f8f4112

Internet Association

February 12, 2015

The Honorable Darrell Issa
Chairman
Subcommittee on Courts, Intellectual Property, and the Internet
Committee on the Judiciary
U.S. House of Representatives
2138 Rayburn House Office Building
Washington, DC 20515

The Honorable Jerrold Nadler
Ranking Member
Subcommittee on Courts, Intellectual Property, and the Internet
Committee on the Judiciary
U.S. House of Representatives
2138 Rayburn House Office Building
Washington, DC 20515

Dear Chairman Issa and Ranking Member Nadler:

The Internet Association respectfully requests that this letter be submitted to the record for today's hearing entitled "Examining Recent Supreme Court Cases in the Patent Arena."

The Internet Association is the unified voice of the Internet economy, representing the interests of leading Internet companies[1] and their global community of users. We are dedicated to advancing public policy solutions to strengthen and protect Internet freedom, foster innovation and economic growth, and empower users. While the Internet Association represents many established Internet platforms, we also represent less established platforms, many of them recent start-ups seeking to build a business using limited resources. Even though our members differ in terms of size and scope, one thing they have in common is patent trolls who extort money from them in order to settle frivolous lawsuits. We share our concerns about patent trolls with highly regarded Internet venture capitalists, including Marc Andreessen and Mark Cuban[2], both of whom have extensive, first-hand experience of the negative and debilitating impact trolls have on start-up activity.

The questions raised by today's hearing are important ones, and the subcommittee should be commended for doing due diligence on procedural changes to the patent litigation landscape since the Innovation Act passed in December 2013.

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[1] The Internet Association's members include Airbnb, Amazon.com, AOL, auction.com, eBay, Etsy, Expedia, Facebook, Gilt, Google, Intuit, LinkedIn, Lyft, Monster Worldwide, Netflix, Pandora, Practice Fusion, Rackspace, reddit, salesforce.com, Sidecar, SurveyMonkey, TripAdvisor, Twitter, Yahoo!, Yelp, Uber and Zynga.
[2] *See, e.g.*, http://www.politico.com/magazine/story/2014/04/tame-the-trolls-105251_Page2.html#.VNzLb0s05Hg (Cuban); and https://twitter.com/pmarca/status/482395929626939392 (Andreessen).

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Here are some hard facts to consider[3]:

- Even in 2014, trolls accounted for 62% of all patent cases filed.
- Companies with less than $100 million in revenue accounted for more than 40% of total troll defendants added to cases in 2014.
- Trolls brought cases against 3,615 defendants in 2014; 1,078 of these companies were targeted for the first time in 2014 in a troll patent infringement case.
- Even if troll litigation dropped slightly from 2013 to 2014, it is important to consider that troll litigation reached a record high in 2013 after increasing through the past decade and skyrocketing over the past three years.
- Consequently, troll litigation rates remain six times higher in 2014 than they were in 2004.

Opponents of patent reform cite three significant recent Supreme Court cases to support their argument that Congress no longer needs to act to reform abusive patent litigation. These cases are *Alice Corp v. CLS Bank Intl*[4]; *Octane Fitness v. Icon Health & Fitness*[5]; and *Highmark Inc. v. Allcare Health Management Systems, Inc.*[6] While each of these cases, and some other developments outside of Congress, brought about incremental changes to patent litigation, none of them can or should be considered a silver bullet - or even a lead bullet, for that matter - when it comes to stopping abuse of the patent litigation system.

First, the Court's analysis in *Alice* applies to only a small subset of the patents asserted by trolls. The fact that courts have invalidated perhaps 20 patents since the *Alice* decision can hardly be considered a solution to the troll problem when thousands of suits are filed each year. More importantly, invoking *Alice* still requires defendants to litigate a case to the point where a judge will rule on the validity of the patent at issue. Reaching this juncture in patent litigation can generate millions of dollars in discovery costs, a price that the vast majority of defendants – even the IA's established members - simply cannot afford in every case filed against them.

Similarly, *Octane Fitness* and *Highmark* made incremental changes to the fee shifting standard in patent litigation cases, but as required by the current statute, the Court allowed fee shifting only in an "exceptional case," meaning one that is "rare" and "stands out." Unfortunately, meritless cases are all too prevalent in 2015 and yet troll litigation continues unabated in several Federal district courts. There is still no meaningful fee shifting deterrent, even in cases where both the facts and the abuse of the system are truly "exceptional." A stronger fee shifting standard that will be consistently applied to trolls is needed. As with *Alice*, it is also important to understand that any fee shifting standard only kicks in at the end of protracted and costly discovery – in other words after the damage has been done and the majority of defendants have settled a frivolous lawsuit.

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[3] See RPX Blog, *2014 NPE Litigation: New and Smaller Targets*, (Jan. 9, 2015), available at http://www.rpxcorp.com/rpx-blog/; Patent Freedom, *Litigations Over Time*, available at https://www.patentfreedom.com/about-npes/litigations/.
[4] 134 S. Ct. 2347 (2014).
[5] 134 S. Ct. 1749 (2014).
[6] 134 S. Ct. 1744 (2014).

Internet Association

Patent litigation reform remains as much a problem in need of a practical solution in 2015, as it was in 2013 when the Innovation Act passed in the House with overwhelming bipartisan support. The changes to the law brought about by the Supreme Court (which could be reversed or diluted in future cases) cannot be compared to the comprehensive and meaningful reform only Congress can implement. In particular, only Congress can recalibrate the key weapon in the patent trolls' arsenal: the ability to leverage asymmetrical litigation costs against defendants – whether those defendants are household names or struggling start ups - in order to coerce settlements of their meritless patent lawsuits. This weapon remained untouched by the Supreme Court in recent cases, allowing the troll business model to continue to thrive.

We thank you for your continued interest in this important issue and look forward to working with your subcommittee in the coming weeks and months to bring to an end abusive patent troll litigation.

Respectfully,

Michael Beckerman
President & CEO
Internet Association

Statement of the

National Retail Federation

National Council of Chain Restaurants

and

Shop.org

submitted to the

U.S. House of Representatives
Committee on Judiciary
Subcommittee on Courts, Intellectual Property, and the Internet

for its hearing on
"Examining Recent Supreme Court Cases in the Patent Arena"

held on

February 12, 2015

David French
Senior Vice President,
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On behalf of

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Chairman Issa, Ranking Member Nadler and members of the House Judiciary Subcommittee on Courts, Intellectual Property, and the Internet, on behalf of the National Retail Federation (NRF) and its communities the National Council of Chain Restaurants and Shop.org, I appreciate the opportunity to submit this written statement to the Committee in connection with its hearing entitled "Examining Recent Supreme Court Cases in the Patent Arena" held on February 12, 2015.

NRF is the world's largest retail trade association, representing discount and department stores, home goods and specialty stores, Main Street merchants, grocers, wholesalers, chain restaurants and Internet retailers from the United States and more than 45 countries. Retail is the nation's largest private sector employer, supporting one in four U.S. jobs – 42 million working Americans. Contributing $2.6 trillion to annual GDP, retail is a daily barometer for the nation's economy. Retailers create opportunities for life-long careers, strengthen communities, and play a critical role in driving innovation.

Retailers and Main Street Businesses are Significantly Impacted by Patent Troll Lawsuits

Members of the National Retail Federation appreciate the attention the Committee is paying to the issue of abusive patent litigation and its harmful effect on competitiveness and innovation. Many retailers are using capital resources to settle with or fight patent trolls' infringement claims that they would otherwise use to invest in their businesses, engage in their communities, and create jobs.

Retail, at its core, is a highly competitive industry, and many retailers are using innovative technology creatively to expand and grow their businesses. Patent trolls, who are not investing in technological innovation, providing jobs or giving back to their communities, employ tactics that cut at the heart of this growth and ingenuity.

In recent years, hundreds of retailers have contacted NRF about this issue because they have been, or are currently, the target of patent trolls' abusive litigation practices. The threat typically comes from firms whose business model is buying obscure patents that are about to expire and then either licensing the patents to retailers through the threat of litigation or filing lawsuits in an effort to force a settlement. Often retailers will choose to pay the licensing fee because patent litigation is prohibitively expensive.

Patent trolls sued more non-tech Main Street companies than tech companies in 2012.[1] Patent trolls employ a strategy that focuses on businesses such as retailers and restaurants because businesses that "use" technology, but don't manufacture it, are more numerous. One manufacturer or vendor may supply a product or service to thousands of retail end-users. Thus, there are many more entities from which to demand a royalty. End-user retailers are also easy prey because they lack the legal resources and in-house expertise to fight complex patent infringement claims. Compared to high tech companies, retailers typically operate on thin profit margins. Patent trolls, knowing that retailers lack technical expertise, retail stores operate on thin margins, and patent litigation is exorbitantly expensive, will often price a settlement demand

[1] Colleen Chien, "Patent Trolls by the Numbers," Patently-O, March 14, 2013. http://www.patentlyo.com/patent/2013/03/chien-patent-trolls.html

(which may still be in the millions) below the cost of litigating, effectively blackmailing a retailer into settlement. This is an abuse of the system.

Patent trolls assert infringement claims covering the use of technology in all areas of e-commerce and mobile retailing because their claims are based on broad concepts and general business methods (such as operating a retail business "online") rather than specific software innovations. This approach is especially damaging to retailers, who are embracing new technology and groundbreaking innovation to better serve their customers.

For example, MacroSolve Inc. has filed numerous suits related to violating U.S. Patent No. 7,822,816, which is a method patent covering the process that many businesses have used to develop their mobile apps. They have sued technology companies, service providers and end-users, including retailers. Over half of the defendants have settled, and the details have not been released. MacroSolve claims their patent covers thousands of apps as well as those yet to be developed.[2] This is of great concern to retail businesses, which increasingly rely on mobile apps as part of their omnichannel presence in the marketplace.

Trolls' claims not only affect e-commerce applications but also affect the operations of traditional "brick and mortar" retail stores. Some examples of the latter are claims that purport to cover the printing of receipts at cash registers, the sale of gift cards, and the connection of any device (such as a computer or printer) to an Ethernet network.

These cases rarely go to trial because the damages claims are so exorbitant, and the prospect of relief through litigation so time-consuming, that retailers make a business decision to settle, rather than litigate. It has been reported that trolls lose 92 percent of cases that proceed to merits judgments, but, as noted, it is infrequent that a defendant has the fortitude to litigate.[3] Smaller retailers may find themselves particularly ill-equipped legally or financially to defend themselves from abusive claims, and dealing with these claims certainly inhibits their ability to innovate and grow.

The exorbitant costs associated with seeing a court case through to final adjudication are startling for retailers, especially small businesses. We have heard from our members that they spend as much as one million dollars or more annually on patent troll-related expenses and settlement agreements. These expenditures and the employee hours diverted to fighting patent trolls are precious capital resources that retailers would rather reinvest in their businesses.

The recent case of *Soverain v. Newegg* demonstrates the many costly steps involved in litigating a patent case and the enormous economic impact that just one patent troll can wreak on an industry. Beginning in 2004 and continuing up through 2012, Soverain has filed numerous suits against dozens of retailers alleging that the basic check-out technology used by nearly all

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[2] Robert Evatt, "MacroSolve adds Wal-mart to list of patent lawsuits," Tulsa World, February 8, 2012. http://www.tulsaworld.com/site/printerfriendlystory.aspx?articleid=20120208_52_E1_Jsasat255194&PrintComments=1

[3] John R. Allison, Mark A. Lemley, and Joshua Walker, *Patent Quality and Settlement Among Repeat Patent Litigants*, 99 GEO. L.J. 677, 694 (2011).

websites infringe its patents[4]. One large retailer is reported to have settled the first suit for $40 million because of the fear of jury verdicts in that era in the Eastern District of Texas. Numerous other settlement amounts are unreported, but in a subsequent suit, an Eastern District of Texas jury awarded damages of almost $18 million against two other national brands.

In 2007 Soverain sued Newegg, which decided to fight back. The case went to trial three years later in April 2010 and resulted in a judgment of $2.5 million against Newegg. Newegg appealed to the Federal Circuit, and on January 14, 2013, more than five years after the suit against it was first instituted, it obtained a judgment in its favor, reversing the lower court judgment and declaring the patents invalid due to obviousness. Although Newegg has won, it took more than five years and millions of dollars in attorneys' fees.

The Newegg case is just one example of the broad infringement claims trolls are asserting against retailers. There are over one million software patents in the United States. Many software patents contain broad concepts dealing with Internet functionality and have extraordinarily vague claims.

Troll cases in federal district court have resulted in the waste of extensive judicial and party resources. NRF is concerned that, fueled by the *eBay* decision and certain portions of the America Invents Act (AIA) of 2011, these abuses will simply be replicated in short order at the ITC.[5] Accordingly, NRF believes that preventative steps should be taken so that this does not occur.

NRF Support for Patent Legislation

NRF is engaged in discussions with Members of the Committee and Congress to address the abusive litigation practices patent trolls utilize. Retailers support H.R. 9, The Innovation Act, which will help deter frivolous litigation brought by patent trolls if enacted.

In recent months, the Supreme Court has issued several rulings in patent infringement cases. While many of the rulings are helpful, Main Street businesses cannot afford to wait for the evolutionary process of court cases to play out. Additionally, despite helpful rulings, the patent trolls have simply adjusted their legal tactics and resumed targeting retailers, restaurants and thousands of other Main Street businesses.

Demand letters and new cases pile up while the court cases proceed. Retailers need certainty and clarity that only multi-pronged legislation, targeted at the asymmetry in the system that patent trolls exploit, will provide. Legislation should give Main Street businesses that certainty and clarity by making patent trolls explain their claims, protect innocent customers, make patent litigation more efficient, stop discovery abuses, make abusive trolls pay and allow for less expensive alternatives to litigation.

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[4] Joe Mullin, "How Newegg Crushed the "Shopping Cart" Patent Troll and Saved Online Retail" ArtsTechnica.com, January 27, 2013. http://arstechnica.com/tech-policy/2013/01/how-newegg-crushed-the-shopping-cart-patent-and-saved-online-retail/

[5] *eBay Inc. v. MercExchange, L.L.C.*, 547 U.S. 388 (2006).

Conclusion

By papering Main Street businesses, including retailers, with broad and vague demand letters and filing an endless series of lawsuits against retail end-users alleging the same patent infringement claims alleged against manufacturers and service providers of a particular device or technology, patent trolls are able to cast a very wide net that hauls in a lucrative catch. They have proven that many of the companies they target will settle given the extraordinarily high demands they make and the costs those companies know it will take to fight even the most frivolous of alleged claims.

Addressing this abusive and growing patent litigation problem with common sense reform will help release retailers from the controlling grip on their industry that patent trolls currently enjoy. Because the retail industry contributes $2.6 trillion to our nation's annual GDP, removing or even loosening this grip on retailers will allow innovation and growth to flourish, and undoubtedly benefit the overall U.S. economy.

Patent litigation reform is about stopping the lucrative business model used by patent trolls of asserting meritless patents and getting shakedown settlements. After each court ruling, patent trolls regroup and decide how best to adjust and continue their abusive tactics against retailers. Only Congress can pass reform needed to put them out of business for good.

NRF thanks the Committee for their extensive examination of the impact of abusive patent litigation and is happy to work with Members of the Committee to find effective solutions to curb abusive patent litigation.

February 19, 2015

Rep. Darrell Issa (R-CA)
Chairman, Subcommittee on Courts, Intellectual Property and the Internet
U.S House of Representatives
2269 Rayburn House Office Building
Washington, DC 20515

Dear Mr. Chairman,

Thank you once again for allowing the National Venture Capital Association's (NVCA) outside counsel to testify before the Subcommittee on Courts, Intellectual Property and the Internet to share NVCA's views on patent litigation reform. We ask that the following comments be submitted into the hearing record from the hearing on Thursday, February 12, 2015 at which Robert Taylor, Esq. testified on behalf of NVCA.

During the hearing, several members of the subcommittee asked Mr. Taylor a series of questions related to NVCA's membership and the positions of individual members on specific patent reform legislative measures. To be clear, Mr. Taylor was present at the hearing to testify as NVCA's outside counsel on behalf of the broader industry, not as a representative of individual NVCA member firms. I believe it's important to clarify that point for the record under the belief that this line of questioning may have led some to mistakenly believe that NVCA's membership is not fully aligned with NVCA's position on patent litigation reform.

As you know, it is not uncommon for large companies to belong to multiple trade associations, especially those that are active across multiple industries. Trade associations typically do not operate by unanimous consent but rather a general consensus approach when determining the appropriate position the organization will present to policymakers on behalf of its membership and broader industry. As the voice of the venture capital community, NVCA advocates for public policies that encourage innovation and reward long-term investment. With a diverse cross-section of nearly 400 member firms, ranging from small traditional venture capital firms to large corporate venture groups that invest across multiple industries and sectors, NVCA balances the views of its entire membership when deciding on a policy position.

Because venture capitalists have differing investment focuses—and as a result differing opinions of the right balance between the protection of plaintiffs and defendants in patent cases—reaching our position as an organization on the issue of patent reform was a long and judicious process. Our guiding principle throughout was based on the fact that venture capital

investing, at its core, is driven by a risk-reward assessment. That is, the greater the perceived risk of an investment, the greater must be the projected return to justify moving forward.

With that in mind, NVCA's overarching position on patent litigation reform is that any changes need to be considered carefully and approached in a measured manner, because almost any change is likely to alter the risk-reward equation in ways that affect individual companies and industries differently. That's been our position since reaching a consensus amongst our members last year and was the position Mr. Taylor accurately presented to the committee when he testified on behalf of NVCA last week.

While we may have some members who disagree in some respects with the positions of the organization, as President and CEO of NVCA, I can assure you that the views expressed by Mr. Taylor are consistent with NVCA's position on the issue of patent litigation reform generally, and more specifically, related to H.R. 9, the Innovation Act.

UC Hastings-NVCA Survey on Patent Assertion

During the hearing, several members of the subcommittee cited a survey conducted by UC Hastings and NVCA on patent assertion, and attempted to use the survey results to draw an inaccurate conclusion that NVCA's position on patent litigation reform is not a reflection of the views of its membership.

To clarify, on October 28, 2013, NVCA and Robin Feldman, Professor of Law and Director of the Institute for Innovation Law at University of California Hastings, released the findings of the survey, "Patent Demands & Startup Companies: The View from the Venture Capital Community." Among the many findings, the survey found that patent assertions impact various industry sectors unevenly, defending against patent assertions is costly, patent demands often impact business operations significantly and most VCs surveyed do not perceive patent assertion as a positive influence in the startup community.

In an October 28, 2013 press release announcing the survey results, then NVCA Senior Vice President of Federal Policy and Political Advocacy Jennifer Dowling said, "This study confirms what we've been hearing anecdotally from our members: the current patent system is working well for some portfolio companies, but not for others. The trend line, however, is not heading in the right direction. As more startups are targeted, more resources are devoted to litigation rather than to innovation. Balancing the need for reform with the need to maintain strong protection for patent-dependent start-ups will be a critical challenge."

As was the case then and remains the case now, the survey findings do not indicate a difference of opinion between NVCA's position on patent litigation reform and the issue of patent assertions. NVCA believes that abuses with patent assertions is a problem in need of attention; however, we also believe that any attempt to reform the system must maintain strong patent enforcement mechanisms for small startups that depend on them for their survival.

The Path Forward on Patent Litigation Reform

As was the case with H.R. 3309, which passed the House during the 113th Congress, NVCA is concerned that H.R. 9, if enacted as written, will have a chilling effect on investment in patent-intensive companies and it will make it far more difficult, risky and expensive for emerging companies to enforce their patents, an essential part of the patent right. Further, H.R. 9 will also raise the cost and risk confronting smaller companies trying to defend against patent litigation brought by their larger competitors.

Any congressional effort to address abusive patent litigation practices that has the effect of making patent enforcement more risky, difficult, and expensive will have a dramatic impact on small businesses and startups. Universities, medical device manufacturers, technology companies, and businesses of all shapes and sizes, from startups to Fortune 500 companies, are critically dependent on patents to protect investments of time, money, and other resources from both competition and imitation here and abroad. Especially for the thousands of venture-backed startup companies across a broad spectrum of industries, preservation of their ability to obtain and enforce patents is fundamental to survival.

It is critical for Congress to take a measured and targeted approach in determining what steps need to be taken to curb abusive patent enforcement and improve the patent system for the innovation ecosystem without undermining the legitimate assertion of the rights of patent owners. We believe consensus can be achieved on a range of issues, including enhancing transparency of patent ownership and enforcement, curtailing unfair or deceptive practices in the indiscriminate sending of patent licensing or settlement demand letters, and proper funding of the Patent Office to improve the overall quality of patents.

As a result of recent Supreme Court decisions and the Leahy-Smith America Invents Act passed in 2011, the patent landscape looks far different today than it did five years ago or even last year. New patent filings in 2014 dropped 18 percent from 2013, as the full impact of judicial decisions and administrative developments have only began to be felt. We believe it is important for Congress to consider this changing landscape and target reforms that address issues that are not already being addressed, including providing the Federal Trade Commission (FTC) the legal authority to challenge bad faith or deceitful demand letters sent out on a mass scale as well as providing full protection of user fees paid to the U.S. Patent and Trademark Office.

Conclusion

In spite of our concerns with H.R. 9, we strongly support the intent and stated purpose of patent litigation reform. We look forward to working with you and your colleagues to improve H.R. 9 as the process moves forward so that it protects and America's small startups and preserves the broader entrepreneurial ecosystem.

Bobby Franklin

President & CEO

Statement for the Record
House Judiciary Committee
Subcommittee on Courts, Intellectual Property, and the Internet
"Examining Recent Supreme Court Cases in the Patent Arena"

The *American Bankers Association; American Insurance Association; The Clearing House Payments Company L.L.C.; Credit Union National Association; Financial Services Roundtable; Independent Community Bankers of America; National Association of Federal Credit Unions; and National Association of Mutual Insurance Companies* appreciate the opportunity to submit this statement for the record in connection with the February 12, 2015, hearing before the House Committee on the Judiciary Subcommittee on Courts, Intellectual Property, and the Internet.

The Federal Circuit's 1998 decision in *State Street Bank & Trust Co. v. Signature Financial Group, Inc.*[1] created a flood of poor quality business method patents and a cottage industry of business method patent litigation.[2]

In response to the poor quality of business method patents, the federal judiciary has written numerous decisions attempting to reign in business method patents. The Supreme Court's recent decision in *Alice Corp. Pty. Ltd. v. CLS Bank Int'l* is arguably the most significant. In *Alice*, the Supreme Court established that a patent claim directed to an abstract idea implemented on a generic computer is not patentable subject matter under 35 U.S.C. § 101 (hereinafter "§ 101").[3]

As a result of *Alice,* there are a substantial number of business-method patents that are invalid under current law. [4]

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[1] 149 F.3d 1368.

[2] Douglas L. Price, *Assessing the Patentability of Financial Services and Products*, 3 J. High Tech. L. 141, 155 (2004) ("The fallout from *State Street* has created a gold-rush mentality toward patents and litigation in which companies ... gobble up patents on anything and everything ... . It is a mad rush to get as many dumb patents as possible."(citations and internal quotation marks omitted)); John R. Thomas, *The Patenting of the Liberal Professions*, 40 B.C. L. Rev. 1139, 1160 (1999) ("After *State Street*, it is hardly an exaggeration to say that if you can name it, you can claim it."); Krause, *supra* at 101 (*State Street* "opened up a world of unlimited possession to anyone quick enough to take a business method and put it to use via computer software before anyone else.").

[3] *Alice Corp. Pty. Ltd. v. CLS Bank Int'l*, 134 S. Ct. 2347, 189 L. Ed. 2d 296 (2014).

[4] *See, e.g.,* Professor Mark Lemley of Stanford Law School stated that "I don't think it's all software patents, but I guess what I would say is a majority of the software patents being litigated right now, I think, are invalid under Alice." (http://www.ipwatchdog.com/2014/09/04/the-ramifications-of-alice-a-conversation-with-mark-lemley/id=51023/). Erich Spangenberg, founder of IPNav, recently expressed his view that "the combination of the AIA and recent Supreme Court decisions, especially *Alice*, have had the effect of wiping out billions of dollars of value in patents, especially software patents. If some of the more recent 101 (what is patent eligible) decisions are upheld, we are only beginning to understand what Alice means." (http://www.ipnav.com/blog/erich-spangenbergs-patent-predictions-for-2015/). Professor David Hricik of Mercer University School of Law commented that "I've been reading a lot of law professor views, and several (if not many) think software patents are dead, or largely so. . . . My guess is *Alice* is going to cause us all to bang our heads, stub our toes, and wander through Wonderland for many years to come." (http://patentlyo.com/hricik/2014/06/which-mushroom-alice.html).

Currently, there are only two ways to get rid of business method patents that are invalid under § 101: (i) litigation in federal district court ("District Court") and (ii) the covered business method ("CBM") review proceedings before the United States Patent and Trademark Office's ("USPTO") Patent Trial and Appeal Board ("PTAB").

1. CBM Review is Substantially More Efficient than District Court Litigation for Disposing of Business Method Patents Now Invalid under *Alice*

Litigation over whether business method patents are invalid under *Alice* places a substantial monetary burden on U.S. courts and the U.S. economy. CBM is the only viable tool for quickly, efficiently and cost-effectively eliminating covered business method patents that are invalid under *Alice*. Without CBM, the federal judiciary is the only vehicle for the Supreme Court's direction in *Alice* to be applied to currently issued business method patents. *Inter Partes* Review ("IPR") does not allow for a determination as to whether the patent is invalid under § 101.[5] While Post-grant Review ("PGR") does allow review under § 101, PGR is not available for the more than 45,000 business method patents that have already issued.[6] Moreover, leaving the post-*Alice* clean up to the federal judiciary is contrary to Chairman Goodlatte's opening remarks: "On the patent quality front, I strongly believe that the PTO should not simply be in the business of granting patents and leaving the mess created for the courts and Congress to fix . . . ."

The efficiency of having an administrative proceeding to rule on the invalidity of business method patents under *Alice* is evidenced by the time and cost savings of CBM as compared to District Court litigation. CBM review proceedings are statutorily required to be complete within eighteen months.[7] In contrast, the median time to trial for patent litigation cases in District Court takes about 66% longer (thirty months total).[8] Moreover, an administrative review option has allowed District Courts to utilize stays to more efficiently manage judicial resources and reduce litigation costs. In fact, District Courts are staying about 70% of their cases in favor of CBM review.[9]

Not only are CBM reviews substantially faster, they are also much less expensive than District Court litigation. In 2013, companies spent over $4.7 billion in legal costs to defend

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[5] *See* 35 U.S.C. § 311(b) ("A petitioner in an inter partes review may request to cancel as unpatentable 1 or more claims of a patent only on a ground that could be raised under section 102 or 103 and only on the basis of prior art consisting of patents or printed publications.")

[6] *See* P.L. 112-29, § 6(f)(2)(A) (PGR shall only apply to patents issued under the first to file rules); 35 U.S.C. § 321(c) ("A petition for post-grant review may only be filed not later than the date that is 9 months after the date of the grant of patent or of the issuance of a reissue patent (as the case may be))."

[7] *See* P.L. 112-29, § 18(a)(1) (CBM "shall employ the standards and procedures of, a post-grant review"); 35 U.S.C. § 324(c); 35 U.S.C. §326(a)(11) (final decision must be made within 1 year of institution of proceeding).

[8] Chris Barry et al., *2014 Patent Litigation Study: As Case Volume Leaps, Damages Continue General Decline*, PricewaterhouseCoopers (July 2014) (available at http://www.pwc.com/en_US/us/forensic-services/publications/assets/2014-patent-litigation-study.pdf).

[9] *See* http://interpartesreviewblog.com/statistics-stays-view-ipr-cbm-proceedings/

against patent suits brought by non-practicing entities.[10] The median patent litigation cost for cases proceeding through trial range from $2,000,000 to $5,500,000 where the damages at-risk exceed $1,000,000.[11]

In stark contrast, the USPTO estimated that the cost of preparing a petition for CBM review to be about $61,000.[12] This is still extremely expensive for small financial institutions, especially when the PTO's filing fees and post-institution fees are considered. However, it remains much cheaper than the alternative of litigating in District Court. Furthermore, a typical budget for a patent suit in District Court is 600% more than that of an IPR, which mirrors the activities of a CBM proceeding.[13]

Because the onus for dealing with erroneously issued patents that are invalid under § 101 already falls on the shoulders of innocent businesses, it is critical to maintain CBM review as a faster, cheaper and more efficient alternative to District Court litigation.[14] Without CBM, there is no administrative proceeding in which to determine the validity of tens of thousands of issued business method patents under *Alice*.

A. CBM Review Has Proven Highly Effective At Evaluating Business Method Patent Invalidity Under § 101

Due to its benefits in terms of time, efficiency, and cost, CBM review has proven to be an effective and favored tool for challenging business method patents that are invalid under § 101. In 2014, the PTAB became the most chosen venue for patent disputes.[15] The success of CBM as a program is evidenced by the broad range of industries that have utilized CBM. Approximately 70% of CBM petitions have been filed by industries other than financial services.[16] Moreover, CBM has been widely embraced as an effective forum to assess invalidity

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[10] 2013 NPE Cost Report: High-Level Findings, RPX Corporation (available at http://www.rpxcorp.com/wp-content/uploads/2014/01/RPX-2013-NPE-Cost-Report—-High-level-Findings.pdf).

[11] AIPLA Report of the Economic Survey (2013).

[12] 77 Federal Register 28 (10 February 2012), p. 7086.

[13] *See* Tom Engellener, *Comparison of Federal Court, ITC, and USPTO Proceedings in IP Disputes*, January 2014 AIPLA MWI Meeting.

[14] Opponents of making CBM review permanent may argue that defendants can seek early dismissal on § 101 grounds under Rules 12(b)(6) or 12(c) of the Federal Rules of Civil Procedure. Given however, that District Courts may decide that construction of claim terms is required before determining whether the claims are directed to patentable subject matter under § 101, defendants may be forced to engage in costly preparation for District Court claim construction proceedings —including discovery pertaining to claim construction, written briefs, and an oral hearing —as well as unrelated written discovery and document production which often occur in advance of or in parallel with claim construction proceedings. *See, e.g.*, *StoneEagle Services, Inc. v. Pay-Plus Solutions, Inc.*, Case No. 9:13-cv-2240-T-33MAP, Dkt. No. 91 (M.D. Fla. Feb. 9, 2015); *Bancorp Servs., L.L.C. v. Sun Life Assur. Co. of Canada*, 687 F.3d 1266, 1273-1274 (Fed. Cir. 2012) ("We note, however, that it will ordinarily be desirable — and often necessary — to resolve claim construction disputes prior to a § 101 analysis, for the determination of patent eligibility requires a full understanding of the basic character of the claimed subject matter.").

[15] *See 2014 Patent Dispute Report and Analytics*, Unified Patents (available at http://unifiedpatents.com/2014-patent-dispute-report-and-analytics/).

[16] Based on a review of filed CBM petitions filed by December 31, 2014 and accessed through the PTAB's Patent Review Processing System (https://ptabtrials.uspto.gov/).

under § 101. Indeed, § 101 is the second most frequent grounds used in CBM for invalidation of business method patents.[17] In addition, the prevalence of § 101 challenges in CBM review proceedings demonstrates the continuing existence and assertion of business method patents that are invalid under § 101 and the demand for an administrative proceeding to resolve § 101 issues.

B. Keeping the CBM Program Is Necessary For An Effective Administrative Review of Patents Now Invalid Under *Alice*

CBM review is an efficient and effective means for dealing with a substantial pool of business method patents exposed by *Alice* as invalid under § 101. Pursuant to the sunset provision of the Leahy-Smith America Invents Act ("AIA"), however, CBM review is slated to cease existence in September 2020 with respect to new patent challenges.[18] Without CBM, there will be no administrative procedure in which to address these business method patents now invalid under *Alice*.

With the looming end to administrative review of business method patents based on *Alice*, there is tremendous incentive for holders of business method patents to simply delay assertion and thereby avoid invalidation of their patents through a CBM review proceeding. As September 2020 draws closer, the incentive for delaying assertion in this manner will continue to grow. Such gaming of the system is an unintended consequence of the sunset provision and one that drastically undermines the purpose for creating CBM review.

Letting CBM review proceedings lapse, which is the only available administrative procedure to review business method patents exposed as invalid by *Alice*, will impose a substantial burden on the U.S. court system and the U.S. economy. Accordingly, the existing CBM program should be made permanent.

C. CBM Review is a Critical Tool for Combating Abusive Demand Letters

Some of the most abusive demand letters allege infringement of business method patents. Recognizing the weakness in these patents, pre-AIA demand letter campaigns often sought settlements slightly less than the cost of litigation. The availability of CBM review has been a major disruptive force. Instead of seeking settlements at less than the cost of litigation, for which a typical budget is 600% more than that of a CBM proceeding, demand letter campaigns involving business method patents now often seek settlements that are less than the cost of a CBM proceeding. Now that a plethora of business method patents have been exposed by *Alice* as invalid under § 101, many campaigns have effectively gone out of business, while others have reduced their settlement expectations even lower.

Permitting the CBM program to expire would increase the viability of abusive demand letter campaigns asserting business method patents that are invalid under § 101. Without the availability of CBM review as a less expensive option for challenging business method patents

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[17] Based on a review of CBM decisions through October 30, 2014, § 101 (36%) trailed only obviousness under 35 U.S.C. § 101 (41%) as grounds for successful invalidation of claims in challenged patents.

[18] *See* 37 C.F.R. §42.300(d)

under § 101, the organizations running these abusive demand letter campaigns will be able to increase the range of their settlement demands about 600% (the difference in cost between CBM review and District Court litigation). Moreover, many targets of abusive demand letter campaigns are small-to-medium-sized businesses that cannot afford to engage in patent litigation in District Court and therefore, absent the availability of CBM review, would have no viable option to challenge an asserted business method patent under § 101.

Accordingly, it is critical that the existing CBM review program be made permanent so as to minimize the harmful effects of abusive demand letter campaigns.

D. CBM Has the Appropriate Safeguards Already Built In To Avoid Abuse While Efficiently Addressing The Effect of *Alice*

Preserving CBM review ensures that there is an efficient, cost-effective alternative to litigation for the review of business method patents exposed as invalid by *Alice*. Preserving CBM review will not subject patent holders to harassment or abuse.

There are numerous unique safeguards built into CBM review to prevent the harassment of patent holders and ensure that only those patents more likely than not to be invalidated are subject to review:

- Patents only become eligible for CBM review when the patent holder threatens or elects to pursue litigation. Only at that point can those parties charged with infringement of an eligible patent petition for review under CBM.
- CBM review requires meeting a high bar for review. A petitioner must establish that it is "more likely than not" that the patent is invalid in order to gain admission into the program.
- A petition for review under CBM can only be filed when PGR is not an option, meaning nine months after the issuance of the patent.
- Once a party charged with infringement files for declaratory judgment they are barred from petitioning for relief under CBM program.
- Petitioner in a CBM proceeding in which a final written decision is issued, is estopped from raising grounds of invalidity in a District Court proceeding that were raised in the CBM proceeding.
- There is no mandatory stay under CBM.
- CBM-eligible patents do not include patents for "technological inventions."
- Review under the CBM must be completed within one year from initiation of the review and not more than 18 months from the time the petition for review was filed.

2. Conclusion

As a result of the Supreme Court's decision in *Alice* there are a substantial number of business-method patents that are not valid under current law. CBM review is the only

administrative proceeding in which these patents can be evaluated under *Alice*. In the absence of CBM review, there is no viable option for challenging the validity of these patents on § 101 grounds other than costly and protracted litigation in District Court.

CBM review was established as a pilot program. It has proven highly efficient and highly effective at balancing the rights of patent holders against the need to ensure patent quality. Any effort at addressing abusive patent litigation should be built upon those aspects of the current patent review system that are working well. CBM review is a vital tool for efficiently challenging low quality patents. We urge that any patent legislation going forward make the existing CBM review program permanent. In addition, we urge Congress to give the Director of the Patent and Trademark Office discretion to waive the fees associated with the program for small institutions, as is included in section 9(d)(2) of H.R. 9. Thank you for the opportunity to submit this statement. We would be happy to answer any questions or discuss this issue further with members of the Committee.

Respectfully submitted,

American Bankers Association
American Insurance Association
The Clearing House Payments Company L.L.C.
Credit Union National Association
Financial Services Roundtable
Independent Community Bankers of America
National Association of Federal Credit Unions
National Association of Mutual Insurance Companies

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