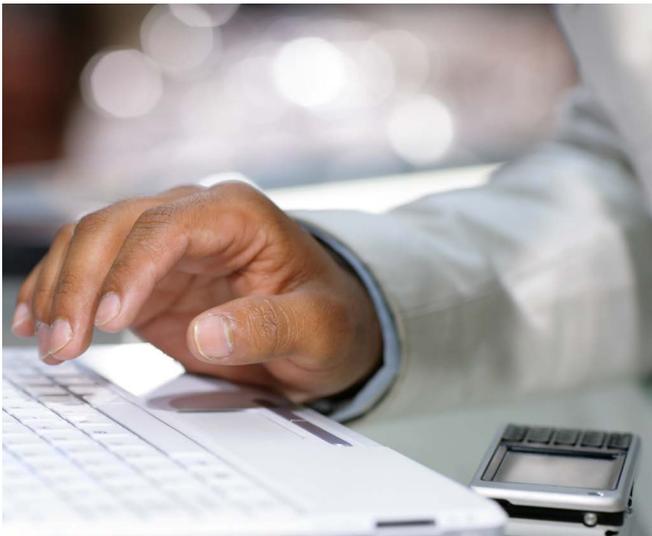


# The House Passes Substantive Patent Reform Aimed at So-Called Patent Trolls; Action in the Senate Awaits

by *Russell C. Petersen & Robert A. McFarlane*



Hanson Bridgett Technology Practice Group  
HANSONBRIDGETT.COM

## I. INTRODUCTION

Patent protection is enshrined in the U.S. Constitution, which grants Congress the power to “promote the progress of science and useful arts” by securing to inventors “the exclusive right to their discoveries” for a limited time. Today, many executives and attorneys working with technology companies believe that science and the useful arts are not promoted when entities who do not manufacture any products at all make it their business to sue the companies that do for patent infringement. These entities whose business models are founded solely on litigating and licensing patents are popularly termed patent trolls, or, less pejoratively, patent assertion entities (“PAEs”).

After a continuing spate of lawsuits filed by PAEs, the U.S. House of Representatives recently passed the “Innovation Act” that would make it more difficult for PAEs to prosecute infringement lawsuits. Numerous other bills are currently pending in Congress that also seek to address PAEs’ potentially abusive practices, such as sending voluminous and threatening demand letters, and it appears likely that some form of additional patent reform will emerge from Congress in 2014.

## II. THE FEDERAL GOVERNMENT RECENTLY PASSED THE AMERICA INVENTS ACT, BUT MANY NOW BELIEVE THAT THE LEGISLATION DIDN’T GO FAR ENOUGH TO CURB PAES

Congress passed the Leahy-Smith America Invents Act of 2011 (AIA) that represented the most wide-ranging modifications to the United States Patent system in half a century. The AIA included several provisions specifically intended to limit PAE activity, including the new process of *Inter Partes Review*, a proceeding within the U.S. Patent and Trademark Office that reviews the validity of an issued patent and that is designed to be quicker, cheaper and more efficient than protracted district court litigation. (35 U.S.C. §§ 321-329) Additionally, PAEs are no longer

permitted to file infringement actions naming dozens of unrelated companies for allegedly infringing the same patent. Instead, PAEs, as well as other plaintiffs, are now generally required to file separate lawsuits against each individual defendant, raising the cost and procedural burdens of engaging in wide-reaching infringement litigation. (*see* 35 U.S.C. § 299(a)(1) (excepting suits involving the same accused product or process)).

After enactment of the AIA, however, President Obama and many others believed the AIA did not go far enough to curtail PAEs. On February 14, 2013, President Obama observed:

The folks that you're talking about [PAEs] are a classic example; they don't actually produce anything themselves. They're just trying to essentially leverage and hijack somebody else's idea and see if they can extort some money out of them...[O]ur efforts at patent reform only went about halfway to where we need to go and what we need to do is pull together additional stakeholders and see if we can build some additional consensus on smarter patent laws.<sup>1</sup>

Because there appears to be consensus that additional reforms are needed, both the House and the Senate have been working on bills to further discourage litigation filed by PAEs.

### III. THE HOUSE PASSES THE INNOVATION ACT

Most recently, the House passed the Innovation Act on December 6, 2013, by bipartisan vote of 325-91, and the bill has now been referred to the Senate Judiciary Committee. The Innovation Act includes several amendments that would significantly impact the conduct of patent litigation. Indeed, the stated goal of the Chairman of the Judiciary Committee, Rep. Goodlatte, for passing the law was to “address the abusive practices” of “patent trolls.”<sup>2</sup> Some of the most notable proposed reforms include:

**Heightened pleading requirements.** Currently, patent complaints are bare-boned documents that contain little if any detail regarding the alleged infringement. They are easy and inexpensive to file and provide minimal information to the accused infringer. Under the Innovation Act, an infringement complaint would be required to include an identification of each patent claim allegedly infringed, each accused instrumentality, and a detailed description of how each limitation of each claim is met by the accused instrumentality. Innovation Act, § 3(a). These requirements are intended to discourage the filing of unfounded infringement suits.

**Attorney-fees to the prevailing party.** Under current rules, attorneys' fees are awarded only in rare instances where infringement litigation is (1) brought in bad faith and (2) objectively baseless. In contrast, the Innovation act would require courts to award attorneys' fees to the prevailing party “unless the court finds that the position and conduct of the nonprevailing party . . . were reasonably justified in law and fact or that special circumstances make an award unjust.” *Id.*, § 3(b). This fee-shifting provision would almost certainly reduce the number of PAE suits of questionable merit.

<sup>1</sup> See *Patent Assertion and U.S. Innovation*, Executive Office of the President, p. 2 (June 2011); viewed at [http://www.white-house.gov/sites/default/files/docs/patent\\_report.pdf](http://www.white-house.gov/sites/default/files/docs/patent_report.pdf) on December 3, 2013.

<sup>2</sup> See *House Passes Innovation Act to Make Reforms to our Patent System*, House Judiciary Committee Press Release (December 5, 2013); viewed at <http://judiciary.house.gov/news/2013/12052013.html> on December 12, 2013.

**Limited discovery.** Under current practice, extraordinarily expensive discovery commences early in almost all patent infringement litigations. The Innovation Act would limit discovery to the narrow issues relating to claim construction until the Court construes the patent claims at issue, *id.* § 3(d), thereby postponing the expense of extensive discovery until after the potentially dispositive claim construction process.

**Transparency of Ownership.** Currently, companies accused of infringing patents held by PAEs have difficulty determining who ultimately owns the patent and who controls the litigation. Under the Innovation Act, patent holders would be required to disclose the ownership of and financial interests in either the patents at issue as well as their “ultimate parent entity,” *id.* § 4(b), thereby providing transparency regarding the ownership of widely-asserted patents.

**Stay for Customer Suits.** PAEs often pursue simultaneous litigation against the manufacturer of an accused product and their customers, driving up both the litigation expense and the settlement value. Under the Innovation Act, if both a manufacturer and its customer are sued for infringing the same patent, the customer suit would be stayed so long as the customer agrees to be bound by the results of that case. *Id.*, § 5(b).

Although there appears to be consensus that additional patent litigation reforms are needed, key actors are cautioning that further reforms should be approached with care so that well-meaning legislation does not end with unintended and undesirable consequences. Representatives Conyers and Watt released a statement prior to the House vote, calling the Innovation Act an improper “vehicle to pass far-ranging changes to the litigation system, such as limits on pleadings and discovery, and intrusive mandates on the court system.”<sup>3</sup> Representative Nadler, even while voting for the bill’s passage, asked the Senate “not [to] allow the House’s ‘loser pays’ provision into the final bill that we vote on in the conference report.”<sup>4</sup> The Federal Circuit Bar Association, an influential association of leading patent attorneys, wrote Chairman Goodlatte, cautioning that the current bill risked the unintended consequences not only for the adjudicatory process but also for innovation, economic recovery, and jobs.”<sup>5</sup>

#### IV. THE SENATE’S RECENT BILL FOCUSES ON DEMAND LETTERS SENT BY PATENT ASSERTION ENTITIES

On December 17, 2013, shortly after the House passed the Innovation Act, the Senate Judiciary Committee held a hearing entitled “Protecting Small Businesses and Promoting Innovation by Limiting Patent Troll Abuse.” The Committee and several witnesses discussed the Senate’s pending patent reform bill, the Patent Transparency and Improvements Act of 2013 (S.1720) (“PTIA”).

The PTIA is more narrowly focused than the Innovation Act. While it does include provisions on transparency in ownership and stays for customer suits [PTIA §§ 3, 4], it does not include a loser pays provision, it does not raise the pleading standards, and it does not limit discovery during infringement suits. Instead, the core of the PTIA is in its target against abusive patent demand letters. PAEs often send these letters to dozens or even hundreds of companies threatening expensive litigation unless the targets agree to pay for a license to the patents. The PTIA makes clear

<sup>3</sup> <http://democrats.judiciary.house.gov/press-release/conyers-watt-goodlatte%E2%80%99s-manager%E2%80%99s-amendment-will-harm-patent-system>, viewed on December 3, 2013.

<sup>4</sup> Cong. Rec. – House, H7513 (Dec. 5, 2013).

<sup>5</sup> *Letter to Chairman Goodlatte*, Federal Circuit Bar Association (December 3, 2013).

that engaging in the widespread practice of sending fraudulent or materially misleading demand letters asserting patent infringement is an unfair and deceptive trade practice that falls within the Federal Trade Commission’s purview. The PTIA would require that any demand letter include a statement of (A) the patent asserter’s identity; (B) the patent being asserted; and (C) the reasons for the assertion. PTIA, § 5.

**V. CONCLUSION**

Although there have been numerous attempts over the past decade to reform U.S. patent statutes, the topic has never reached the level of attention it is now receiving in the popular and business presses. Consequently, companies that are advocating for PAEs to be further limited are likely to see relief in the near future. Since the clauses regarding transparency in ownership and stays for customer suits are largely consistent between both Rep. Goodlatte’s and Sen. Leahy’s bills now pending, they are likely to come out intact. A law targeting abusive demand letters also would seem popular. Finally, there is no doubt that changing the patent system to a loser pays model would cause potential plaintiffs to think twice before bringing a lawsuit. A genuine concern, however, is that such a change will prevent small plaintiffs from filing meritorious suits against large corporations and minimize meritorious contingency litigation. This clause is by far the most controversial, and the patent bar will be closely following the Senate’s treatment of these proposals.

If you have any questions about these decisions or other technology law issues, please contact:



**Russell C. Petersen**  
415-995-5816  
russ.petersen@hansonbridgett.com



**Robert A. McFarlane**  
415-995-5072  
rmcfarlane@hansonbridgett.com

**SAN FRANCISCO**

425 Market Street, 26th floor  
San Francisco, CA 94105  
TEL 415-777-3200  
FAX 415-541-9366

**NORTH BAY**

Wood Island  
80 E. Sir Francis Drake Blvd., Ste. 3E  
Larkspur, CA 94939  
TEL 415-925-8400  
TEL 707-546-9000  
FAX 415-925-8409

**SACRAMENTO**

500 Capitol Mall, Ste. 1500  
Sacramento, CA 95814  
TEL 916-442-3333  
FAX 916-442-2348

**SILICON VALLEY**

950 Tower Lane, Ste. 925  
Foster City, CA 94404  
TEL 650-349-4440  
FAX 650-349-4443

**EAST BAY**

1676 N. California Blvd., Ste. 620  
Walnut Creek, CA 94596  
TEL 925-746-8460  
FAX 925-746-8490