

# Patent Litigation Reform Legislation in the 114<sup>th</sup> Congress

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## Summary

This report describes how current patent litigation reform legislation would change existing patent law to address the perceived problems caused by entities that engage in patent litigation tactics that have been criticized as abusive or deceptive. The bills introduced in the 114<sup>th</sup> Congress include the Innovation Act (H.R. 9), Protecting American Talent and Entrepreneurship Act (PATENT) Act (S. 1137), Demand Letter Transparency Act of 2015 (H.R. 1896), Targeting Rogue and Opaque Letters (TROL) Act (H.R. 2045), and the Support Technology and Research for Our Nation's Growth (STRONG) Patents Act of 2015 (S. 632). The legislation includes the following changes to the patent system:

**Heightened Pleading Requirements:** The Innovation Act and the PATENT Act would require parties alleging patent infringement in a civil action to include in the court pleadings specified details concerning each claim of each patent infringed, and the acts of the alleged infringer.

**Limits on Discovery:** During hearings relating to patent claim construction, the Innovation Act proposes to limit discovery “to information necessary for the court to determine the meaning of the terms used in the patent claim.” The PATENT Act proposes limitations on discovery pending the resolution of certain motions.

**Transparency of Patent Ownership:** The Innovation Act and the PATENT Act would require plaintiffs in patent cases to disclose to the United States Patent and Trademark Office (USPTO), the court, and all adverse parties information relating to entities that own or have a financial interest in the patent.

**Customer-Suit Exception:** The Innovation Act and the PATENT Act would allow a court to stay litigation against a customer of a product that contains allegedly infringing technologies, if the manufacturer of the product is a party to the same or other action on the same patent and other requirements are satisfied.

**Shifting of Attorney Fees:** The Innovation Act would require a district court to award attorney fees to a prevailing party in patent cases, unless the court finds that the nonprevailing party's position and conduct “were reasonably justified in law and fact or that special circumstances ... make an award unjust.” The PATENT Act would require the prevailing party to make a motion to the court to determine whether the nonprevailing party's position and conduct were “objectively reasonable”; if they were not, then the court must award reasonable attorney fees to the prevailing party unless there are special circumstances that would make an award unjust.

**Fee Recovery:** The Innovation Act would establish mandatory joinder rules when the nonprevailing party alleging infringement is unable to pay the fee award and other expenses. The PATENT Act would allow a defendant to submit a statement early in the litigation claiming that plaintiff's primary business is the assertion and enforcement of patents; the plaintiff would then need to certify that it has sufficient funds to satisfy any potential award of attorney fees that may be assessed, and to identify (and provide notice to) any “interested parties” that could be held accountable for the award if the plaintiffs are unable to pay it.

**Demand Letters:** Several bills propose various approaches to address demand letters. The STRONG Patents Act and the TROL Act would impose specific enforcement and content requirements for demand letters. The Innovation Act expresses the sense of Congress that

purposely evasive demand letters are abusing the patent system in a manner contrary to public policy. The Demand Letter Transparency Act proposes both disclosure and content requirements directed towards “abusive” demand letter practices, and the PATENT Act focuses on pre-suit notifications.

**Post-Grant Review Reforms:** The Innovation Act and the STRONG Patents Act would mandate that the Patent Trial and Appeal Board, in inter partes review (IPR) and post-grant review (PGR) proceedings, follow the same claim construction standard used by district courts. In addition, the Innovation Act and the PATENT Act would narrow the estoppel effect arising from a PGR. The STRONG Patents Act would heighten the standing requirements for persons wanting to initiate a PGR or IPR. The STRONG Patents Act would also require the IPR/PGR petitioner to prove unpatentability of a patent claim by “clear and convincing evidence.”

**Elimination of USPTO Fee Diversion:** The STRONG Patents Act would permit the USPTO to spend all fee revenue that it collects without further appropriation action or fiscal year limitation.

**Assistance for Small Businesses:** The Innovation Act, STRONG Patents Act, and the PATENT Act contain provisions designed to help small businesses that participate in the patent system either as patent owners or as defendants.

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## Introduction<sup>1</sup>

Congress has shown significant interest in altering the current patent system in response to concerns about entities that engage in patent litigation tactics that have been criticized as abusive or deceptive. Many congressional hearings on the topic of patent litigation abuse have been held in the 114<sup>th</sup> and 113<sup>th</sup> Congresses,<sup>2</sup> and several legislative proposals have been introduced;<sup>3</sup> one bill in the 113<sup>th</sup> Congress, H.R. 3309, the Innovation Act, was passed by the House in December 2013. This report describes how the major provisions of current patent litigation reform legislation would change existing patent law to address the perceived problems in the patent litigation system.

<sup>1</sup> Portions of this report have been borrowed and adapted from CRS Report R42668, *An Overview of the “Patent Trolls” Debate*, by Brian T. Yeh and CRS Report R43321, *Patent Infringement Pleadings: An Analysis of Recent Proposals for Patent Reform*, by Emily M. Lanza.

<sup>2</sup> S. 1137, the “PATENT ACT” – *Finding Effective Solutions to Address Abusive Patent Practices: Hearing Before the Senate Judiciary Comm.*, 114<sup>th</sup> Cong. 1<sup>st</sup> Sess. (2015); H.R. \_\_, the *Targeting Rogue and Opaque Letters Act (TROL Act): Hearing Before the House Energy & Commerce Comm., Subcomm. on Commerce, Manufacturing, and Trade*, 114<sup>th</sup> Cong. 1<sup>st</sup> Sess. (2015); *Patent Reform: Protecting American Innovators and Job Creators from Abusive Patent Litigation: Hearing Before the House Judiciary Comm., Subcomm. on Courts, Intellectual Property and Internet*, 114<sup>th</sup> Cong. 1<sup>st</sup> Sess. (2015); *The Impact of Abusive Patent Litigation Practices on the American Economy: Hearing Before the Senate Judiciary Comm.*, 114<sup>th</sup> Cong. 1<sup>st</sup> Sess. (2015); *Patent Reform: Protecting Innovation and Entrepreneurship: Hearing Before the Senate Comm. on Small Business & Entrepreneurship*, 114<sup>th</sup> Cong. 1<sup>st</sup> Sess. (2015); *Trolling for a Solution: Ending Abusive Patent Demand Letters: Hearing Before the House Energy & Commerce Comm., Subcomm. on Commerce, Manufacturing, and Trade*, 113<sup>th</sup> Cong. 2d Sess. (2014); H.R. 3309, the “Innovation Act.” *Hearing Before the House Judiciary Comm.*, 113<sup>th</sup> Cong., 1<sup>st</sup> Sess. (2013); *Protecting Small Businesses and Promoting Innovation by Limiting Patent Troll Abuse: Hearing Before the Senate Judiciary Comm.*, 113<sup>th</sup> Cong., 1<sup>st</sup> Sess. (2013); *The Impact of Patent Assertion Entities on Innovation and the Economy: Hearing Before the House Energy and Commerce Comm., Subcomm. on Oversight and Investigations*, 113<sup>th</sup> Cong., 1<sup>st</sup> Sess. (2013); *Demand Letters and Consumer Protection: Examining Deceptive Practices by Patent Assertion Entities: Hearing Before the Senate Commerce, Science, & Transportation Comm., Subcomm. on Consumer Protection, Product Safety, and Insurance*, 113<sup>th</sup> Cong., 1<sup>st</sup> Sess. (2013); *Abusive Patent Litigation: The Issues Impacting American Competitiveness and Job Creation at the International Trade Commission and Beyond: Hearing Before the House Judiciary Comm., Subcomm. on Courts, Intellectual Property, and the Internet*, 113<sup>th</sup> Cong., 1<sup>st</sup> Sess. (2013); *Abusive Patent Litigation: The Impact on American Innovation & Jobs, and Potential Solutions: Hearing Before the House Judiciary Comm., Subcomm. on Courts, Intellectual Property, and the Internet*, 113<sup>th</sup> Cong., 1<sup>st</sup> Sess. (2013).

<sup>3</sup> In the 114<sup>th</sup> Congress, introduced legislation includes the Innovation Act (H.R. 9), Protecting American Talent and Entrepreneurship Act (PATENT) Act (S. 1137), Demand Letter Transparency Act of 2015 (H.R. 1896), Targeting Rogue and Opaque Letters (TROL) Act (H.R. 2045), and the Support Technology and Research for Our Nation’s Growth (STRONG) Patents Act of 2015 (S. 632). In the 113<sup>th</sup> Congress, legislation that was introduced but not enacted included the following: the Innovation Act (H.R. 3309), Transparency in Assertion of Patents Act (S. 2049), the Patent Transparency and Improvements Act of 2013 (S. 1720), the Patent Abuse Reduction Act of 2013 (S. 1013), the Patent Litigation Integrity Act of 2013 (S. 1612), the Demand Letter Transparency Act of 2013 (H.R. 3540), Patent Litigation and Innovation Act of 2013 (H.R. 2639), End of Anonymous Patents Act (H.R. 2024), and the Saving High-Tech Innovators from Egregious Legal Disputes (SHIELD) Act of 2013 (H.R. 845).

# Background

## Patent Law Fundamentals

According to Section 101 of the Patent Act, one who “invents or discovers any new and useful process, machine, manufacture, or any composition of matter, or any new and useful improvement thereof, may obtain a patent therefore, subject to the conditions and requirements of this title.”<sup>4</sup> Thus, in order for an invention to qualify for patent protection, it must fall within one of the four statutory categories of patent-eligible subject matter: processes, machines, manufactures, and compositions of matter. However, the U.S. Supreme Court has articulated certain limits to Section 101 of the Patent Act, stating that “laws of nature, natural phenomena, and abstract ideas” may not be patented.<sup>5</sup>

The U.S. Patent and Trademark Office (USPTO) issues a patent to an inventor after USPTO examiners approve the submitted patent application for an allegedly new invention.<sup>6</sup> An application for a patent consists of two primary parts: (1) a “specification,” which is a written description of the invention enabling those skilled in the art to practice the invention, and (2) one or more claims that define the scope of the subject matter which the applicant regards as his invention.<sup>7</sup> Therefore, these claims define the scope of the patentee’s rights under the patent.<sup>8</sup>

Before a patent may be granted, the USPTO examiners must find that the new invention satisfies several substantive requirements that are set forth in the Patent Act.<sup>9</sup> For example, one of the statutory requirements for patentability of an invention is “novelty.”<sup>10</sup> For an invention to be considered “novel,” the subject matter must be different than, and not be wholly “anticipated” by, the so-called “prior art,” or public domain materials such as publications and other patents. Another statutory requirement is that the subject matter of an alleged invention must be “nonobvious” at the time of its creation. A patent claim is invalid if “the differences between the subject matter sought to be patented and the prior art<sup>11</sup> are such that the subject matter as a whole would have been obvious at the time the invention was made to a person having ordinary skill in the art to which said subject matter pertains.”<sup>12</sup> Finally, the invention must also be “useful,” which means that the invention provides a “significant and presently available,” “well-defined and particular benefit to the public.”<sup>13</sup>

<sup>4</sup> 35 U.S.C. § 101.

<sup>5</sup> *Diamond v. Diehr*, 450 U.S. 175, 185 (1981).

<sup>6</sup> 35 U.S.C. § 131.

<sup>7</sup> *Id.* § 112.

<sup>8</sup> 3-8 DONALD S. CHISUM, CHISUM ON PATENTS § 8.01 (2006).

<sup>9</sup> 35 U.S.C. §§ 102, 103(a).

<sup>10</sup> *Id.* § 102.

<sup>11</sup> “Prior art” is a legal term of art that refers to the materials (usually called “references” in patent law) that comprise the available knowledge regarding the subject matter of the invention sought to be patented, such as other issued patents, publications, and evidence of actual uses or sales of the technology. ROGER SCHECHTER & JOHN THOMAS, PRINCIPLES OF PATENT LAW 4-1 (2d ed. 2004).

<sup>12</sup> 35 U.S.C. § 103(a).

<sup>13</sup> *In re Fischer*, 421 F.3d 1365, 1371 (Fed. Cir. 2005).

The Patent Act grants patent holders the exclusive right to exclude others from making, using, offering for sale, or selling their patented invention throughout the United States, or importing the invention into the United States.<sup>14</sup> Whoever performs any one of these five acts during the term of the invention's patent, without the patent holder's authorization, is liable for infringement.<sup>15</sup> A patent holder may file a civil action against an alleged infringer in order to enjoin him from further infringing acts (by securing an injunction, also referred to as injunctive relief).<sup>16</sup> The patent statute also provides federal courts with discretion to award damages to the patent holder that are "adequate to compensate for the infringement, but in no event less than a reasonable royalty for the use made of the invention by the infringer."<sup>17</sup> The usual term of patent protection is 20 years from the date the patent application is filed.<sup>18</sup> At the end of that period, others may use the invention without regard to the expired patent.

Because the Patent Act expressly provides that "patents shall have the attributes of personal property,"<sup>19</sup> patent holders may sell their patent rights in a legal transfer called an "assignment."<sup>20</sup> Alternatively, patent holders may grant others a "license" to exercise one of the five statutory patent rights.<sup>21</sup> A license is not a transfer of ownership of the patent, but rather is the patent holder's permission to another entity to use the invention in a limited way, typically in exchange for periodic royalty payments during the term of the patent.<sup>22</sup> A patent holder may grant to a licensee the right to practice the invention through a contract (typically known as a patent licensing agreement). The terms of the licensing agreement, however, may include conditions upon the grant of rights—for example, restricting the licensee from making the invention but allowing that party to sell it.<sup>23</sup> A licensee that performs an act that exceeds the scope of the license (through a violation of the limitations and conditions of the grant of rights) or refuses to comply with the terms of the license agreement (such as by refusing to pay the required royalties) is potentially liable to the patent holder for breach of contract as well as for patent infringement.<sup>24</sup>

The U.S. Court of Appeals for the Federal Circuit (Federal Circuit) is a specialized tribunal established by Congress that has exclusive appellate jurisdiction in patent cases.<sup>25</sup> Parties dissatisfied with the Federal Circuit's rulings may petition the U.S. Supreme Court to review the appellate court's decision. However, the Supreme Court is not required to entertain the appeal; it has discretion to decide whether to grant certiorari to review the case.<sup>26</sup>

<sup>14</sup> 35 U.S.C. §§ 154(a)(1), 271(a).

<sup>15</sup> *Id.* § 271(a).

<sup>16</sup> *Id.* § 283.

<sup>17</sup> *Id.* § 284.

<sup>18</sup> *Id.* § 154(a)(2).

<sup>19</sup> *Id.* § 261.

<sup>20</sup> ROGER SCHECHTER & JOHN THOMAS, *PRINCIPLES OF PATENT LAW* § 11-1 (2d ed. 2004).

<sup>21</sup> A patent holder has the right to exclude others from making, using, offering for sale, or selling the invention throughout the United States, or importing the protected invention into the United States. 35 U.S.C. § 154(a)(1).

<sup>22</sup> SCHECHTER & THOMAS, *supra* footnote 20, § 11-1.

<sup>23</sup> *United States v. General Electric Co.*, 272 U.S. 476, 490 (1926).

<sup>24</sup> JOHN R. THOMAS, *PHARMACEUTICAL PATENT LAW* 427 (BNA Books 2005).

<sup>25</sup> 28 U.S.C. § 1295(a)(1).

<sup>26</sup> *Id.* § 1254(1).

Besides seeking legal relief for infringement in the federal courts, U.S. patent holders may also obtain an order from the U.S. International Trade Commission (ITC or Commission) preventing the importation of foreign goods that infringe their rights. The ITC is an independent, nonpartisan, quasi-judicial federal government agency responsible for investigating and arbitrating complaints of violations of Section 337 of the Tariff Act of 1930 (19 U.S.C. § 1337), which prohibits unfair methods of competition or other unfair acts in the importation of products into the United States. Section 337 also prohibits the importation of articles that infringe valid U.S. patents, copyrights, processes, trademarks, or protected design rights. (The majority of unfair competition acts asserted under Section 337 involve allegations of patent infringement.)<sup>27</sup> The ITC has the power to order several forms of prospective injunctive relief, including ordering the U.S. Customs and Border Protection (CBP) to stop imports from entering U.S. borders (an exclusion order), or issuing cease and desist orders that prohibit parties from distributing or selling infringing articles from existing U.S. inventory. However, unlike the federal courts, the ITC lacks the statutory authority to award monetary damages for patent infringement (past or future).

Although issued patents are presumed to be valid, accused infringers may assert in court that a patent is invalid or unenforceable on a number of grounds.<sup>28</sup> The accused infringer could raise this argument as an affirmative defense or counterclaim when sued for patent infringement. A party could also preemptively file a “declaratory judgment action”<sup>29</sup> against a patent owner to challenge a patent’s validity, if there is a case or controversy between them.<sup>30</sup>

However, the constitutionally based “case or controversy” requirement for federal judicial proceedings significantly limits the ability of members of the public to challenge the USPTO’s decision to grant a patent. Unless the patent holder becomes involved in an actual, continuing controversy with another person, that person cannot successfully request that a court determine whether the patent is valid or not. To address this perceived deficiency, Congress established several administrative procedures that are conducted by the USPTO’s Patent Trial and Appeal Board, or PTAB,<sup>31</sup> through which any interested person may challenge the validity of an issued patent. Three trial proceedings comprise the current system of administrative patent challenges: inter partes review (IPR), post-grant review (PGR), and the transitional post-grant review for covered business method patents (CBM). The three proceedings have different rules, timing, and eligibility requirements.<sup>32</sup> The proceedings may result in the confirmation of patentability of the

<sup>27</sup> Colleen V. Chien, *Patently Protectionist*, 50 WILLIAM & MARY L. REV. 63, 70 (2008) (patent cases comprise 85% of the ITC’s Section 337 docket). For more information about Section 337 proceedings, see CRS Report RS22880, *Intellectual Property Rights Protection and Enforcement: Section 337 of the Tariff Act of 1930*, by Shayerah Ilias Akhtar.

<sup>28</sup> 35 U.S.C. § 282.

<sup>29</sup> For more on declaratory judgment actions in patent cases, see CRS Report RL34156, *A Nonrepudiating Patent Licensee’s Right To Seek Declaratory Judgment of Invalidity or Noninfringement of the Licensed Patent: MedImmune v. Genentech*, by Brian T. Yeh.

<sup>30</sup> The requirement that an immediate, concrete dispute between the patent owner and another individual arises because the U.S. Constitution vests the federal courts with jurisdiction only where a “case or controversy” exists. U.S. CONST., Art. III, Sec. 2, cl. 1. A charge of patent infringement typically satisfies the “case or controversy” requirement. See *Prasco, LLC v. Medicis Pharm. Corp.*, 537 F.3d 1329 (Fed. Cir. 2008).

<sup>31</sup> The PTAB’s membership consists of the USPTO director, deputy director, the Commissioner for Patents, the Commissioner for Trademarks, and the administrative patent judges. 35 U.S.C. § 6(a).

<sup>32</sup> The USPTO provides a helpful chart that compares the major differences between the three administrative trials, in terms of (1) who may file a petition with the USPTO to institute the review; (2) when such a petition is allowed; (3) the estoppel provisions applicable to the review (to prevent individuals from making repetitive arguments during later (continued...))



original claims, an amended patent with narrower claims, or a declaration of patent invalidity.<sup>33</sup> A party dissatisfied with the PTAB's final written decision in an IPR, PGR, or CBM review may appeal directly to the Federal Circuit.

## Patent Assertion Entities<sup>34</sup>

"Patent assertion entities" are people or companies that do not develop, manufacture, or sell any product covered by the patents they own. The business model of a patent assertion entity (PAE) instead focuses on buying and asserting patents against companies that have already begun using and developing the patent, often without knowledge of the PAE's ownership of the patent.<sup>35</sup> PAEs emerged alongside the burgeoning tech industry around the turn of the 21<sup>st</sup> century and gained notoriety with lawsuits claiming exclusive ownership of such ubiquitous technologies as wireless email, digital video streaming, and the interactive web.<sup>36</sup> The vast majority of lawsuits brought by PAEs end in settlements because litigation is risky, costly, and disruptive for defendants, and PAEs often offer to settle for amounts well below litigation costs to make the business decision to settle an obvious one.<sup>37</sup> PAEs are frequently referred to as "patent trolls," after the villains of folklore known to lie in wait under bridges they did not build, then emerge from the smog to demand tolls from unsuspecting travelers.<sup>38</sup> The term "troll" is controversial because it is both pejorative and ambiguous, often used imprecisely for any opportunistic or unpopular patent holder.<sup>39</sup>

Critics of PAEs argue that they extort the patent system through litigation by extracting licensing fees or damage awards from companies that cannot afford the cost of litigation. Critics also argue that "patent trolling" deters innovation and discourages companies from seeking patents, and thus delivering new products to the market.<sup>40</sup> However, defenders of PAEs argue that they actually

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(...continued)

proceedings—either in federal court, the ITC, or in a USPTO administrative proceeding); (4) standards to trigger the review; (5) the standard to prove invalidity; (6) time limits for completing the review; and (7) the basis for challenging validity of the patent, *available at* [http://beta.uspto.gov/sites/default/files/ip/boards/bpai/aia\\_trial\\_comparison\\_chart.pptx](http://beta.uspto.gov/sites/default/files/ip/boards/bpai/aia_trial_comparison_chart.pptx).

<sup>33</sup> 35 U.S.C. §§ 318(b); 328(b).

<sup>34</sup> For comprehensive background information on these entities, *see* CRS Report R42668, *An Overview of the "Patent Trolls" Debate*, by Brian T. Yeh.

<sup>35</sup> FEDERAL TRADE COMMISSION, *THE EVOLVING IP MARKETPLACE: ALIGNING PATENT NOTICE AND REMEDIES WITH COMPETITION* 67-68 (2011).

<sup>36</sup> *See* Gerard N. Magliocca, *Blackberries and Barnyards: Patent Trolls and the Perils of Innovation*, 82 NOTRE DAME L. REV. 1809 (2007).

<sup>37</sup> John R. Allison, Mark A. Lemley & Joshua Walker, *Patent Quality and Settlement Among Repeat Patent Litigants*, 99 GEO. L.J. 677, 694 (2011).

<sup>38</sup> The term was coined at Intel in 2001 as a pithy label for litigants asserting patents that they owned but did not practice and which they typically acquired. An Intel Corporation vice president had been sued after referring to such litigants as "patent extortionists." *See* Joff Wild, *The Real Inventors of the Term "Patent Troll" Revealed*, IAM MAGAZINE, August 22, 2008, <http://iam-magazine.com/blog/detail.aspx?g=cff2afd3-c24e-42e5-aa68-a4b4e7524177>.

<sup>39</sup> *See, e.g.*, Ronald S. Katz et al., *Patent Trolls: A Selective Etymology*, IP LAW 360, March 20, 2008, [http://manatt.com/uploadedFiles/News\\_and\\_Events/Articles\\_By\\_Us/patentroll.pdf](http://manatt.com/uploadedFiles/News_and_Events/Articles_By_Us/patentroll.pdf); *see also* Jenna Greene, *Trolls? Patent Director Says the Term Isn't Helpful*, NAT'L LAW JOURNAL, Jan. 22, 2015 (quoting USPTO Director Michelle Lee: "I don't find the term [patent troll] helpful. It means different things to different people. We need to focus on behavior.").

<sup>40</sup> *See, e.g.*, James Bessen et al., *The Private and Social Costs of Patent Trolls*, REGULATION 26, 31-35 (2006).

promote invention by increasing the liquidity and managing the risk of investments in applied research and invention, as well as by compensating small inventors.<sup>41</sup> PAEs' strongest allies include universities and other nonpracticing entities that benefit from having PAEs as buyers for their patents and are not as vulnerable to lawsuits because they ordinarily do not make or sell anything that could be infringing.<sup>42</sup>

## Legislation in the 114<sup>th</sup> Congress

The remainder of this report discusses and analyzes the key provisions of legislative proposals that have been introduced in the 114<sup>th</sup> Congress related to patent litigation abuse. The subject matter of the patent law reforms is presented below in no particular order.

### Heightened Pleading Requirements

According to the Federal Rules of Civil Procedure, a complaint for patent infringement<sup>43</sup> must include four statements that assert jurisdiction, patent ownership, patent infringement by the defendant, and a demand for relief.<sup>44</sup> Plaintiffs typically rely upon the Federal Rules of Civil Procedure's Form 18 to structure their patent infringement complaint. Generally, the Federal Circuit has applied the "notice pleading standard" to patent infringement pleadings for the purpose of a motion to dismiss for failure to state a claim (a typical method by which a defendant may attempt to have a case dismissed at the beginning of the case). Under this standard, a court finds that the patent pleading statements contain sufficient particularity to survive a motion to dismiss for failure to state a claim if they notify parties of the general issues of the case. In *K-Tech Telecommunications v. Time Warner Cable*, the Federal Circuit held that the information required by the Federal Rules of Civil Procedure's Form 18 is sufficient for pleading a patent infringement claim as the form states a plausible claim and places the alleged infringer on notice.<sup>45</sup> Additionally, the Federal Circuit in *McZeal v. Sprint Nextel Corporation* found that a party does not need to describe the relationship between each element of the claim and the infringing device in a patent infringement complaint.<sup>46</sup> According to the court, specific information such as this "is something to be determined through discovery."<sup>47</sup>

The Innovation Act, H.R. 9, proposes additional heightened initial pleading requirements for an infringement claim, as compared to the current requirements under the Federal Rules of Civil Procedure's Form 18. Under these new requirements, a party alleging infringement in a complaint must include specific details regarding the following:

<sup>41</sup> See, e.g., Ron Epstein, *Debunking the 'Patent Troll' Myth*, BLOOMBERG BUSINESSWEEK, August 15, 2011, available at <http://www.businessweek.com/stories/2010-02-01/debunking-the-patent-troll-mythbusinessweek-business-news-stock-market-and-financial-advice>.

<sup>42</sup> See Mark A. Lemley, *Are Universities Patent Trolls?*, 18 FORDHAM INTELL. PROP. MEDIA & ENT. L.J. 611, 618 (2008).

<sup>43</sup> As previously discussed, patent infringement is the unauthorized making, using, offering for sale, selling, and importing of a patented invention. 35 U.S.C. § 271.

<sup>44</sup> Fed. R. Civ. P. Form 18.

<sup>45</sup> *K-Tech Telecommunications v. Time Warner Cable*, 714 F.3d 1278 (Fed. Cir. 2013).

<sup>46</sup> *McZeal v. Sprint Nextel Corp.*, 501 F.3d 1354, 1358 (Fed. Cir. 2007).

<sup>47</sup> *Id.*

- each claim of each patent allegedly infringed;
- for each claim of indirect infringement, the acts of the alleged indirect infringer that contribute to, or are inducing, a direct infringement;
- the principal business of the party alleging infringement;
- the authority of the party alleging infringement to assert each patent and the grounds for the court's jurisdiction;
- each complaint filed that asserts any of the same patents; and
- whether the patent is essential or has potential to become essential to a standard-setting body, as well as whether the United States or a foreign government has imposed any specific licensing requirements.<sup>48</sup>

Like the Innovation Act, the Senate's PATENT Act also proposes heightened pleading requirements, including such details as

- the identification of each patent allegedly infringed;
- the identification of each claim of each patent that is allegedly infringed;
- the identification (including the name, model number, or description) of the accused instrumentality that has allegedly infringed the patent;
- a description of how the accused instrumentality is allegedly infringing specific elements of the claim; and
- a description of the acts of the alleged infringer that allegedly contributed to or induced the direct infringement, for claims of indirect infringement.<sup>49</sup>

The PATENT Act would not require such details in the initial pleading as the authority of the party alleging infringement to assert each patent and the principal business of the party alleging infringement, as outlined in the House's Innovation Act. Instead, the Senate bill would require the patentee to disclose specific information to the court and each adverse party no later than 14 days after the filing of the pleading.<sup>50</sup> These disclosure requirements would cover the identity of the patent assignee(s), the right to enforce the patent at issue, any ultimate parent entity, and entities that would have a particular financial interest in the patent at issue.<sup>51</sup> The PATENT Act would also explicitly eliminate the Federal Rules of Civil Procedure's Form 18.<sup>52</sup>

Both the PATENT Act and the Innovation Act provide that if the information is not readily accessible, then the party may generally describe the information with an explanation of why such undisclosed information was not readily accessible.<sup>53</sup> Similarly, both bills also exempt from

<sup>48</sup> H.R. 9, § 3, *adding new* 35 U.S.C. § 281A.

<sup>49</sup> S. 1137, § 3, *adding new* 35 U.S.C. § 281A.

<sup>50</sup> *Id.*, *adding new* 35 U.S.C. § 281B.

<sup>51</sup> *Id.*

<sup>52</sup> S. 1137, § 3.

<sup>53</sup> H.R. 9, § 3, *adding new* 35 U.S.C. § 281A; S. 1137, § 3, *adding new* 35 U.S.C. § 281A.

the proposed heightened pleading requirements any civil action that includes a claim for relief arising under Section 271(e)(2) of the current Patent Act relating to certain drug claims.<sup>54</sup>

Commentators have linked “patent trolls” together with the current patent pleading requirements for a patent infringement claim.<sup>55</sup> They have argued that the minimal information required in a patent infringement complaint encourages PAEs to initiate “frivolous” lawsuits that otherwise would not survive the initial pleading state under a more stringent standard. Proponents of these pleadings changes state that such heightened pleading requirements would force a plaintiff to consider the alleged infringement instrumentality more carefully and decide whether infringement has occurred before filing the suit.<sup>56</sup> Supporters of heightened pleading requirements also argue that “not providing the necessary information at the beginning of a case in the complaint slows down the litigation and makes it inefficient and expensive for both parties.”<sup>57</sup> Additionally, these proponents assert that heightened pleadings standards would not impose a greater burden on the plaintiff, who would develop a good-faith case, and providing such information at the early stages of litigation would improve efficiency and costs.<sup>58</sup> However, some commentators believe that the heightened pleading requirements would render patent enforcement impractical. According to these opponents, the plaintiff may not have the information available at this stage of litigation, as the discovery process typically reveals the information necessary to build a successful infringement claim.<sup>59</sup>

## Limits on Discovery and Cost-Shifting

The Federal Rules of Civil Procedure permit discovery<sup>60</sup> into any unprivileged matter that is relevant to the claim or defense of any party.<sup>61</sup> This broad definition leads to costly discovery in patent litigation.<sup>62</sup> During the discovery process, the court may decide to hold a “Markman hearing,”<sup>63</sup> during which a judge examines evidence concerning the parties’ disputes over the meaning and language of a patent claim that defines the boundaries of the invention. (Also referred to as “claim construction,” or the interpretation of a patent’s claims, this process largely determines the scope of the patent owner’s proprietary rights.) For these hearings, courts must

<sup>54</sup> The Innovation Act and the PATENT Act provide an exception to this disclosure requirement for civil actions that include a specific cause of action for patent infringement involving pharmaceutical drugs. The particular cause of action, established by the Hatch-Waxman Act and codified in 35 U.S.C. § 271(e)(2), allows a brand-name drug company to enforce its patents against a potential generic competitor at such time that the generic firm files an application (a so-called Abbreviated New Drug Application (ANDA)) with the Food and Drug Administration, seeking marketing approval. For more information on this provision, see CRS Report R42354, *Patent Infringement and Experimental Use Under the Hatch-Waxman Act: Current Issues*, by John R. Thomas.

<sup>55</sup> See, e.g., Patent Progress, *Common Sense Solutions to the Patent Control Problem*, at <http://www.patentprogress.org/patent-troll-reform/common-sense-solutions-to-the-patent-troll-problem/>.

<sup>56</sup> H.Rept. 113-279, at 23.

<sup>57</sup> *Id.*

<sup>58</sup> *Id.*

<sup>59</sup> See Edward R. Ergenzinger and Andrew R. Shores, “Here We Go Again: The Next Round of Legislative Patent Law Reform,” at <http://www.wardandsmith.com/articles/the-next-round-of-legislative-patent-law-reform>.

<sup>60</sup> Discovery is the process to gather information in preparation for trial.

<sup>61</sup> See Fed. R. Civ. P. 26.

<sup>62</sup> See Chief Judge Randall R. Rader, *The State of Patent Litigation*, Eastern District of Texas Bar Association Judicial Conference, Sept. 27, 2011.

<sup>63</sup> This type of hearing developed as the result of the U.S. Supreme Court decision in *Markman v. Westview Instruments, Inc.*, 517 U.S. 370 (1996).

consider volumes of evidence produced during discovery relating to many different aspects of claim construction including evidence regarding the definition, meaning, scope, and pertinent art of the claim.<sup>64</sup>

During hearings relating to patent claim construction, the Innovation Act proposes to limit discovery “to information necessary for the court to determine the meaning of the terms used in the patent claim.”<sup>65</sup> The bill would grant the courts with the discretion to permit discovery “in special circumstances” to prevent manifest injustice. Under H.R. 9, parties would also have the ability to consent to voluntary exclusion from these proposed limitations on discovery.

The Senate’s PATENT Act would require a court to stay discovery pending the resolution of preliminary motions including the motion to dismiss, the motion to transfer venue, and the motion to sever accused infringers.<sup>66</sup> The bill would provide a court with the discretion to allow limited discovery to resolve these motions or a motion for a preliminary injunction or to preserve evidence or otherwise prevent specific prejudice to a party, if the court would find that additional discovery is necessary.<sup>67</sup> Similar to the Innovation Act, the PATENT Act would also grant parties with the opportunity to exclude themselves voluntarily from these proposed limitations.

Supporters of these proposed limitations on discovery note that the technical nature and complexity of patent litigation inherently leads to the extensive document discovery, and correspondingly encourages frequent settlements to avoid this high cost.<sup>68</sup> These supporters have stated that the propensity towards settlements in patent litigation encourages PAEs to file infringement suits. Thus, supporters have also emphasized that specific limits on claim construction discovery, such as those proposed by the Innovation Act, would help the parties to focus “on truly relevant discovery” and to reduce “wasted efforts” during litigation over claim construction.<sup>69</sup> Critics of these discovery limitations argue that this approach may create further discovery by encouraging courts to separate claim construction analysis from its summary judgment decisionmaking.<sup>70</sup> Others have also raised concerns that the discovery limitation provision may cause “patent litigation in the overwhelming majority of patent cases [to] incur significant across-the-board delays and increased expense for all parties.”<sup>71</sup>

## Transparency of Patent Ownership<sup>72</sup>

Under current law, within a month after the filing of a civil action involving a patent, the clerks of the federal courts must provide written notice of the action to the USPTO director that describes

<sup>64</sup> See *Phillips v. AWH Corp.*, 415 F.3d 1303 (Fed. Cir. 2005).

<sup>65</sup> H.R. 9, § 3, *adding new* 35 U.S.C. § 299A.

<sup>66</sup> S. 1137, § 4, *adding new* 35 U.S.C. § 299B.

<sup>67</sup> *Id.*

<sup>68</sup> H.Rept. 113-279, at 9.

<sup>69</sup> *Id.* at 24.

<sup>70</sup> Dennis Crouch, “Patent Reform: Innovation Act of 2015,” Feb. 5, 2015, *available at* <http://patentlyo.com/patent/2015/02/patent-reform-innovation.html>.

<sup>71</sup> *The Impact of Abusive Patent Litigation Practices on the American Economy: Hearing Before the Senate Judiciary Comm.*, 114<sup>th</sup> Cong., 1<sup>st</sup> Sess. (2015) (Statement of Hans Sauer, Deputy General Counsel for Intellectual Property, Biotechnology Industry Organization).

<sup>72</sup> This topic is often referred to as the disclosure of the “real party-in-interest.”

the names and addresses of the parties, the name of the inventor, and the number of the patent upon which the action is based.<sup>73</sup> The USPTO director is then required to enter this information in the file of that patent.

Section 4 of the Innovation Act would amend this section of the Patent Act to impose specific disclosure requirements upon plaintiffs upon the filing of an initial complaint for patent infringement. (Similar to the exemption for the new pleading requirements, the Innovation Act's patent ownership disclosure requirement would not apply to any civil action that includes a cause of action for patent infringement under 35 U.S.C. § 271(e)(2).)<sup>74</sup> Upon the filing of an initial complaint for patent infringement, plaintiffs would be required to disclose to the USPTO, the court, and all adverse parties the following information relating to entities that own or have a financial interest in the patent:

1. the assignee(s) of the patent(s) involved in the case;
2. any entity with a right to sublicense or enforce the patent(s) at issue;
3. any entity, other than the plaintiff, that the plaintiff knows to have a financial interest<sup>75</sup> in the patent(s) at issue or in the plaintiff; and
4. the ultimate parent entity<sup>76</sup> of any assignee, or the entities identified in #2 and #3 above.

Section 4 of the Innovation Act would require the plaintiff to notify the USPTO of any changes in the identity of the assignee of the patent or the entities described above, within 90 days of such change.<sup>77</sup> Failure to comply with this ongoing duty of disclosure would result in the plaintiff being barred from recovering either enhanced damages or reasonable fees and other expenses incurred in connection with the infringement lawsuit (with respect to infringing activities occurring during the period of noncompliance), “unless the denial of such damages or fees would be manifestly unjust.”<sup>78</sup> In addition, the Innovation Act directs a court to award to a prevailing party accused of infringement any reasonable fees and other expenses that the party incurred to uncover the updated information about the assignee or entities, “unless such sanctions would be unjust.”<sup>79</sup>

Section 4 of the Innovation Act grants the USPTO director the power to issue regulations to establish a registration fee in order to recover the cost of administering the “disclosure of interests” requirement, which includes the costs to facilitate collection and maintenance of the

<sup>73</sup> 35 U.S.C. § 290.

<sup>74</sup> H.R. 9, § 4(a)(3), *adding new* 35 U.S.C. § 290(b)(2).

<sup>75</sup> The Innovation Act defines “financial interest” to mean (1) with regard to a patent, the right of a person to receive proceeds related to the assertion of the patent(s), and (2) with regard to the plaintiff, direct or indirect ownership or control by a person of more than 5% of such plaintiff. H.R. 9, § 4(a)(3), *adding new* 35 U.S.C. § 290(e)(1). However, the definition expressly excludes anyone who owns shares or other interests in a mutual or common investment fund (unless the person participates in the management of such fund) and also excludes the proprietary interest of a policyholder in a mutual insurance company or of a depositor in a mutual savings association, unless the outcome of the civil action could substantially affect the value of that proprietary interest.

<sup>76</sup> The Innovation Act defines “ultimate parent entity” by reference to 16 C.F.R. § 801.1(a)(3), which provides that the term “means an entity which is not controlled by any other entity.” H.R. 9, § 4(a)(3), *adding new* 35 U.S.C. § 290(e)(3).

<sup>77</sup> *Id.*, *adding new* 35 U.S.C. § 290(d)(1).

<sup>78</sup> *Id.*, *adding new* 35 U.S.C. § 290(d)(2)(A).

<sup>79</sup> *Id.*, *adding new* 35 U.S.C. § 290(d)(2)(B).



information submitted by plaintiffs and “to ensure the timely disclosure of such information to the public.”<sup>80</sup>

According to the sponsors of the Innovation Act, the amendments made by Section 4 “will ensure that patent trolls cannot hide behind a web of shell companies to avoid accountability for bringing frivolous litigation.”<sup>81</sup> However, a critic of this provision argued that it would be “needlessly burdensome” and that the required disclosure “could lead to the revelation of confidential financial and licensing agreements”;<sup>82</sup> furthermore, he noted that if such information is relevant to the litigation, “it is readily discoverable under current rules, with appropriate protective orders to maintain needed confidentiality.”<sup>83</sup>

The PATENT Act would require similar initial disclosures by a patentee in a patent infringement lawsuit as the Innovation Act.<sup>84</sup> Within 14 days of the patentee filing the pleading, the patentee would be required to notify the court and each adverse party of the following information:

1. The identity of each:
  - a. assignee of the patent(s) at issue, and any “ultimate parent entity”<sup>85</sup> thereof;
  - b. entity with a right to sublicense to unaffiliated entities or to enforce the patent(s) at issue, and any ultimate parent entity thereof;
  - c. any other entity that the patentee knows to have a financial interest<sup>86</sup> in the patent(s) at issue, or in the patentee (and any ultimate parent entity thereof); and
2. For each patent that the patentee alleges to be infringed:
  - a. a list of other complaints filed by the patentee in the three years before the filing of the action, as well as any other complaints filed in the United States (not by the patentee but that the patentee was aware of) that asserted the patent during the same three-year period;
  - b. a statement as to whether the patent is subject to certain licensing requirements (imposed by the federal government or by a standards development organization).<sup>87</sup>

<sup>80</sup> *Id.* § 4(c).

<sup>81</sup> *Press Release: Goodlatte, Defazio, Issa, Nadler, Smith, Lofgren, Eshoo Introduce Patent Litigation Reform Bill*, Feb. 5, 2015, available at <http://judiciary.house.gov/index.cfm/2015/2/goodlatte-defazio-issa-nadler-smith-lofgren-eshoo-introduce-patent-litigation-reform-bill>.

<sup>82</sup> Howard Klein, *Patent Law Reform—Proceed with Caution*, Law360.com, Mar. 9, 2015, at <http://www.law360.com/articles/626618/patent-law-reform-proceed-with-caution>.

<sup>83</sup> *Id.*

<sup>84</sup> S. 1137, § 3(b)(1), *adding new* 35 U.S.C. § 281B(b). However, unlike the Innovation Act, the PATENT Act would NOT create an exception to the patent ownership disclosure requirement for a civil action that includes a cause of action for patent infringement under 35 U.S.C. § 271(e)(2).

<sup>85</sup> The PATENT Act uses the same definition for “ultimate parent entity” as the Innovation Act.

<sup>86</sup> The PATENT Act defines the term “financial interest” in a similar fashion to the Innovation Act, except that S. 1137 would, with regard to the patentee, apply the term to persons who have “direct or indirect ownership or control” of more than 20% of the patentee (compared to the Innovation Act’s 5%).

<sup>87</sup> For more information about the promise of members of standard-setting organizations to license certain patented inventions to others on “fair, reasonable, and nondiscriminatory (FRAND) terms,” see CRS Report R42705, *Availability of Injunctive Relief for Standard-Essential Patent Holders*, by Brian T. Yeh.

The PATENT Act would allow the patentee to file such information under seal if the patentee considers the information to be confidential (such as the home addresses of any individuals);<sup>88</sup> the Innovation Act does not contain a similar provision.

Within a month of the disclosure of the information listed above, the patentee would be required to file the information described in #1 above with the USPTO.<sup>89</sup> However, unlike the Innovation Act, the PATENT Act does not appear to place upon the patentee an ongoing duty of disclosure of such information to the USPTO.

In addition, Section 10 of the PATENT Act would require that an assignment of all substantial rights in any issued patent (and the name of the assignee and the ultimate parent entity of the assignee) be recorded in the USPTO within the following time periods:

1. no later than the date on which the patent is issued; and
2. when any subsequent assignment is made that results in a change to the ultimate parent entity
  - a. no later than three months after such assignment is made; or,
  - b. in the case of an assignment made as part of a corporate acquisition, not later than six months after the closing date of such acquisition.<sup>90</sup>

The PATENT Act provides similar consequences as the Innovation Act for failure to comply with the duty to disclose this information to the USPTO: that is, the party asserting infringement of a patent would be denied the right to receive either enhanced damages or reasonable fees and other expenses incurred in connection with the infringement lawsuit (with respect to infringing activities occurring during the period of noncompliance).<sup>91</sup> Like the Innovation Act, the PATENT Act would also require a court to award to a prevailing accused infringer reasonable attorney fees and expenses incurred to discover the identity of any undisclosed entity that was required to be disclosed.<sup>92</sup> Under the PATENT Act, the USPTO Director would be given the same authority granted by the Innovation Act to establish fees to administer the process of collecting and maintaining the submitted assignment information.<sup>93</sup>

## Stays of Litigation Brought Against Infringing Customers

Under the Patent Act, anyone who “makes, *uses*, offers to sell, or sells any patented invention”<sup>94</sup> is potentially liable for patent infringement if such actions occur without the authority of the patent holder. Thus, the patent holder has the right to bring a lawsuit against not only the manufacturer or seller of products that incorporate allegedly infringing components, but also the customers who purchase and use those products.<sup>95</sup> Over the past few years, businesses (including

<sup>88</sup> *Id.*, adding new 35 U.S.C. § 281B(e).

<sup>89</sup> *Id.* § 3(b)(1), adding new 35 U.S.C. § 281B(d).

<sup>90</sup> *Id.* § 10(a), adding new 35 U.S.C. § 261(A)(b), (c).

<sup>91</sup> *Id.*, adding new 35 U.S.C. § 261(A)(d).

<sup>92</sup> *Id.*

<sup>93</sup> *Id.* § 10(b).

<sup>94</sup> 35 U.S.C. § 271(a) (emphasis added).

<sup>95</sup> See *Aro Mfg. Co., Inc. v. Convertible Top Replacement Co., Inc.*, 377 U.S. 476, 484 (1964) (explaining that “it has (continued...)”).



restaurants, retailers, and grocery stores) and individuals increasingly have faced charges of patent infringement for their use of certain equipment that contain technologies such as Wi-Fi, PDF scanning, email, and vehicle tracking.<sup>96</sup> A witness at a congressional hearing in 2013 described the situation as follows:

Another patent litigation practice that has been sharply criticized is the institution of suits against large numbers of assemblers, distributors or retailers rather than the original manufacturer or provider of the component or product alleged to infringe. This tactic takes advantage of the fact that such suits threaten defendants with the disruption of aspects of their businesses that are at best tangentially related to the invention which is the subject of the patent, and that each individual defendant has less motivation to litigate the issue to final conclusion than the manufacturer of the product at issue. The result can be to collect enormous sums as the result of a very large number of small settlements whose cumulative value far exceeds the amount that could have been recovered from the original manufacturer.<sup>97</sup>

The judicially created response to such customer lawsuits is the so-called “customer suit exception” doctrine, which allows courts to prioritize litigation against or brought by the manufacturer of infringing goods over a lawsuit by the patent owner against customers of the manufacturer in the interest of efficiency and judicial economy.<sup>98</sup> The doctrine permits a court to stay an earlier-filed action against a customer involving an infringement product pending the outcome of a later-filed declaratory judgment action brought by the manufacturer of the accused product. As explained by the First Circuit Court of Appeals (prior to the creation of the Federal Circuit), “At the root of the preference for a manufacturer’s declaratory judgment action is the recognition that, in reality, the manufacturer is the true defendant in the customer suit.... [I]t is a simple fact of life that a manufacturer must protect its customers, either as a matter of contract, or good business, or in order to avoid the damaging impact of an adverse ruling against its products.”<sup>99</sup> However, the doctrine “has long existed in a state of relative disuse” and the Federal Circuit has affirmed its application in only one case in the last three decades.<sup>100</sup>

Section 5 of the Innovation Act would codify a modified version of the customer suit exception by amending the Patent Act<sup>101</sup> to require a court to suspend or postpone litigation against a

(...continued)

often and clearly been held that unauthorized use, without more, constitutes infringement.”).

<sup>96</sup> See Colleen V. Chien & Edward Reines, *Why Technology Customers Are Being Sued en Masse for Patent Infringement & What Can Be Done* (Santa Clara Univ. Sch. of L. Legal Studies Research Papers Series, Working Paper No. 20-13, 2013), available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2318666](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2318666).

<sup>97</sup> *Abusive Patent Litigation: The Impact on American Innovation & Jobs, and Potential Solutions: Hearing Before the House Judiciary Comm., Subcomm. on Courts, Intellectual Property, and the Internet*, 113<sup>th</sup> Cong., 1<sup>st</sup> Sess. (2013) (Statement of Philip S. Johnson, Chief Intellectual Property Counsel, Johnson & Johnson, on behalf of the 21<sup>st</sup> Century Coalition for Patent Reform), at 7, available at [http://judiciary.house.gov/\\_files/hearings/113th/03142013\\_2/Johnson%2003142013.pdf](http://judiciary.house.gov/_files/hearings/113th/03142013_2/Johnson%2003142013.pdf).

<sup>98</sup> *Spread Spectrum Screening LLC v. Eastman Kodak Co.*, 657 F.3d 1349, 1357 (Fed. Cir. 2011).

<sup>99</sup> *Codex Corp. v. Milgo Electronic Corp.*, 553 F.2d 735 (1<sup>st</sup> Cir.), cert. denied, 434 U.S. 860 (1977).

<sup>100</sup> Brian J. Love and James C. Yoon, *Expanding Patent Law’s Customer Suit Exception*, 93 B.U. L. REV. 1605, 1614 (Oct. 2013), citing *Katz v. Lear Siegler, Inc.*, 909 F.2d 1459 (Fed. Cir. 1990).

<sup>101</sup> H.R. 9, § 5(a), replacing existing 35 U.S.C. § 296 that contains an unrelated provision that attempted to make state governments and state institutions liable for monetary damages in a patent infringement lawsuit. This provision that sought to abrogate a state’s Eleventh Amendment sovereign immunity has been invalidated by the Supreme Court in a 1999 decision, *Florida Prepaid v. College Savings Bank*, 527 U.S. 627 (1999). For more information on this issue, see CRS Report RL34593, *Infringement of Intellectual Property Rights and State Sovereign Immunity*, by Brian T. Yeh.

customer of a product or process that contains allegedly infringing technologies, if several requirements are satisfied.<sup>102</sup>

1. the manufacturer of the product and the customer consent to the stay of the action in writing;
2. the manufacturer is a party to the civil action or a separate action involving the same patent(s);
3. the customer agrees to be bound by the decisions of the court in the action involving the manufacturer, with respect to any issues that the customer and manufacturer have in common; and
4. the customer requests the court to stay the action no later than the later of (a) 120 days after the date on which the first pleading in the action is served (if such pleading specifically identifies the product or process that is the source of the customer's alleged infringement of the patent, and the pleading specifically explains how the product or process is alleged to infringe the patent), or (b) the date on which the first scheduling order in the case is entered.

The Innovation Act provides two limited exceptions to the manufacturer and customer's entitlement to a stay: (1) if the action involving the manufacturer will not resolve a major issue in the suit against the customer; or (2) if the stay unreasonably prejudices and would be manifestly unjust to the party seeking to lift the stay.<sup>103</sup> In addition, like the exemption for the new pleading and patent ownership disclosure requirements, the Innovation Act exempts from the customer suit stay provision any action that includes a cause of action for patent infringement under 35 U.S.C. § 271(e)(2).<sup>104</sup>

Though the stay provision would only postpone, and not terminate, a cause of action against the customer, supporters of the stay provision assert that “in the vast majority of cases, a suit involving the manufacturer will eliminate all potential infringement liability of the customer.”<sup>105</sup>

In testimony offered before the House Judiciary Committee in October 2013, former USPTO Director David Kappos argued that the Innovation Act's stay provision's definition of a “covered customer” is overbroad and may also have the potential for unintended consequences:

[A]s currently written the stay provision permits all parties in the product channel downstream of the first component part maker to escape infringement liability, including large commercial actors such as manufacturers combining procured components into value-added completed devices, as well as assemblers, and others not operating in the roles of “mere retailers” or “mere end users,” and certainly not operating in the roles of “mom and pop shops.” This unnecessarily devalues intellectual property and thus innovation by artificially limiting or even eliminating legitimate patentees' ability to protect their innovations. It also may leave an American innovator with no infringer at all to pursue where infringing manufacturers are located outside the reach of the US courts, such as overseas, or lack adequate assets to answer for infringement.<sup>106</sup>

<sup>102</sup> H.R. 9, § 5(a), *adding revised* 35 U.S.C. § 296(a)(1)-(4).

<sup>103</sup> *Id.*, *adding revised* 35 U.S.C. § 296(c).

<sup>104</sup> *Id.*, *adding revised* 35 U.S.C. § 296(d).

<sup>105</sup> H.Rept. 113-279, p. 30.

<sup>106</sup> H.R. 3309, the “Innovation Act:” *Hearing Before the House Judiciary Comm., 113<sup>th</sup> Cong., 1<sup>st</sup> Sess.* (2013) (continued...)

Others have raised similar concerns about stay provisions in patent litigation reform legislation that are “overly inclusive” by providing the benefit of a stay of a suit to “any and all downstream parties.”<sup>107</sup> One critic of the Innovation Act’s stay provision suggests that any bill providing for a stay of infringement suits against customers “limit eligibility of customer stays to retailers and end users who have not materially altered the product or process, or incorporated it into another product or process.”<sup>108</sup>

The PATENT Act includes a customer stay provision similar to that of the Innovation Act, although there are several important differences. First, in apparent response to concerns raised about the potentially overbroad applicability of the Innovation Act’s customer stay provision, the PATENT Act provides narrower definitions of “covered customer,” “retailer,” and “end user,”<sup>109</sup> as follows:

1. A “covered customer” is a retailer or end user who is accused of patent infringement based on sale or use of a product/process alleged to infringe a patent, if the retailer or end user did not materially modify such product/process for their own purposes.
2. An “end user” is a user of a product/process alleged to infringe a patent and also an affiliate of such an end user, but does not include an entity that manufactures (or causes the manufacture of) the product/process.
3. A “retailer” is an entity that generates its revenues mostly through sale of consumer goods or services, or an affiliate of such an entity, but does not include an entity that manufactures (or causes the manufacture of) the product/process alleged to infringe a patent.

Second, the PATENT Act would require a court to suspend or postpone litigation against a customer of a product or process that contains allegedly infringing technologies if

1. the manufacturer of the product/process alleged to infringe the patent is a party to the action or a separate federal court action involving the same patent(s) relating to the product/process;
2. the customer agrees to be bound by the issue decided in the action involving the manufacturer; and
3. the motion for the stay is filed after the first pleading in the action and the later of (a) 120 days or (b) the date on which the first scheduling order in the case is entered.<sup>110</sup>

(...continued)

(Statement of David J. Kappos, Former Under Secretary of Commerce for Intellectual Property and Director of the United States Patent and Trademark Office), at 7, available at [http://judiciary.house.gov/\\_files/hearings/113th/10292013/Kappos%20Testimony.pdf](http://judiciary.house.gov/_files/hearings/113th/10292013/Kappos%20Testimony.pdf).

<sup>107</sup> Thomas M. Susman and Robert O. Lindefield, *Re: S. 1720, the “Patent Transparency and Improvements Act of 2013,” and Related Bills*, Letter to Senate Judiciary Chairman Leahy and Ranking Member Grassley, Feb. 4, 2014, at 8, available at [http://www.americanbar.org/content/dam/aba/uncategorized/GAO/2014feb4\\_patentreformletters.authcheckdam.pdf](http://www.americanbar.org/content/dam/aba/uncategorized/GAO/2014feb4_patentreformletters.authcheckdam.pdf).

<sup>108</sup> *Id.* at 9.

<sup>109</sup> S. 1137, § 4, adding new 35 U.S.C. § 299A(a).

<sup>110</sup> *Id.*, adding new 35 U.S.C. § 299A(b).

Note that the Innovation Act would require that both the manufacturer and customer consent in writing to the stay, whereas such consent is not needed for a customer to obtain a stay under the PATENT Act. According to the sponsors of the legislation, this provision in the PATENT Act was intended “[t]o address concerns that manufacturer could prevent a stay from issuing by refusing to consent.”<sup>111</sup> However, the PATENT Act would require the consent of the manufacturer if the manufacturer had been made a party to the action on motion by the customer.<sup>112</sup> The PATENT Act contains the same provisions as the Innovation Act pertaining to situations in which a stay may be lifted: if the action involving the manufacturer will not resolve major issues in the suit against the customer, or the stay unreasonably prejudices or is manifestly unjust to the party seeking to lift the stay.<sup>113</sup> Also like the Innovation Act, the PATENT Act would exempt from the customer suit stay provision any action that includes a cause of action for patent infringement under 35 U.S.C. § 271(e)(2).<sup>114</sup>

## Shifting of Attorney Fees

For many years, patent cases were subject to the “American Rule,” under which “[e]ach litigant pays his own attorney fees, win or lose.”<sup>115</sup> Then in 1947, Congress enacted a fee-shifting provision that gave district courts the power to award attorney fees to the prevailing party in patent suits. The 1952 revision of the patent laws codified this provision at 35 U.S.C. § 285. This section of the Patent Act provides a court with the discretion to award “reasonable” attorney fees to the prevailing party (plaintiff or defendant) only “in exceptional cases.”

However, the Federal Circuit in its 2005 opinion, *Brooks Furniture Manufacturing, Inc. v. Dutilleul International, Inc.*,<sup>116</sup> established that courts may find an “exceptional case” under Section 285 in only two limited circumstances: (A) “when there has been some material inappropriate conduct” (during the litigation or in obtaining the patent from the USPTO) or (B) when the litigation is both (1) brought in subjective bad faith and (2) objectively baseless. In addition, *Brooks Furniture* held that the prevailing party must prove its entitlement to attorney fees by “clear and convincing evidence.”<sup>117</sup> In part due to this strict standard, federal judges have rarely award these fees.<sup>118</sup>

In April 2014, the Supreme Court in *Octane Fitness v. Icon Health & Fitness* unanimously overruled the Federal Circuit’s *Brooks Furniture* standard because the two-prong test “is unduly

<sup>111</sup> Section-by-Section Summary of the PATENT Act, at 2, available at <http://www.judiciary.senate.gov/imo/media/doc/Patents,%2004-29-15,%20PATENT%20Act%20-%20Short%20Section%20by%20Section.pdf>.

<sup>112</sup> S. 1137, § 4, adding new 35 U.S.C. § 299A(c).

<sup>113</sup> *Id.*, adding new 35 U.S.C. § 299A(d).

<sup>114</sup> *Id.*, adding new 35 U.S.C. § 299A(b).

<sup>115</sup> *Marx v. General Revenue Corp.*, 133 S. Ct. 1166, 1175 (2013); see also *Alyeska Pipeline Service Co. v. Wilderness Society*, 421 U.S. 240, 247-53 (1975) (explaining that “[i]n the United States, the prevailing litigant is ordinarily not entitled to collect a reasonable attorneys’ fee from the loser.”).

<sup>116</sup> *Brooks Furniture Mfg., Inc. v. Dutilleul Intern., Inc.*, 393 F.3d 1378 (Fed. Cir. 2005) (overruled by *Octane Fitness, LLC v. ICON Health & Fitness, Inc.*, No. 12-1184, slip op. (2014)).

<sup>117</sup> *Id.* at 1382.

<sup>118</sup> See Randall R. Rader et al., *Make Patent Trolls Pay in Court*, N.Y. TIMES, June 4, 2013, available at [http://www.nytimes.com/2013/06/05/opinion/make-patent-trolls-pay-in-court.html?\\_r=0](http://www.nytimes.com/2013/06/05/opinion/make-patent-trolls-pay-in-court.html?_r=0) (noting that “fees were shifted under Section 285 in only 20 out of nearly 3,000 patent cases filed in 2011.”).

rigid, and it impermissibly encumbers the statutory grant of discretion to district courts.”<sup>119</sup> Instead, the Court adopted a more lenient standard, holding “that an ‘exceptional’ case is simply 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.”<sup>120</sup> The Court explained that district courts must make the Section 285 determination by considering the “totality of the circumstances.”<sup>121</sup> The Court also rejected the Federal Circuit’s requirement that prevailing parties establish their entitlement to legal fees by “clear and convincing evidence” and instead embraced a “preponderance of the evidence” standard.<sup>122</sup> In a companion case decided the same day as *Octane Fitness*, the Supreme Court in *Highmark v. Allcare Health Management*<sup>123</sup> rejected the Federal Circuit’s position that a district court’s “exceptional case” determination is to be reviewed on appeal “de novo” and “without deference.” Instead, the Court held that the district court’s Section 285 determination must be reviewed on appeal under an abuse-of-discretion standard.<sup>124</sup>

By overruling the Federal Circuit’s restrictive interpretation of Section 285, *Octane Fitness* and *Highmark* provide district courts with greater discretion in deciding whether to award fees, thus likely increasing the number of patent cases in which attorney fees are shifted. Thus, in evaluating whether to award attorney fees, a court must first assess whether the case is “exceptional” in accordance with the standard announced in *Octane Fitness*, and if so, the court may (or may not) choose to award the fees. It is unclear the extent to which these recent Supreme Court decisions will impact the filing of patent infringement lawsuits by patent assertion entities, yet supporters of patent litigation reform express hope that the increased prospect of paying the other party’s litigation expenses could be a significant financial disincentive to PAEs’ litigation tactics.<sup>125</sup> However, some observers predict that *Octane Fitness* and *Highmark* will not have a significant impact on PAEs because fee-shifting will remain limited:

[R]ecent Supreme Court cases ... 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.<sup>126</sup>

<sup>119</sup> *Octane Fitness, LLC v. ICON Health & Fitness, Inc.*, No. 12-1184, slip op. at 1 (2014).

<sup>120</sup> *Id.* at 7.

<sup>121</sup> *Id.* at 8.

<sup>122</sup> *Id.* at 11.

<sup>123</sup> *Highmark Inc. v. Allcare Health Mgmt.Sys.*, No. 12-1163, slip. op. (2014).

<sup>124</sup> *Id.* at 5.

<sup>125</sup> Daniel Fisher, *Patent Trolls Face Higher Risks As Supreme Court Loosens Fee-Shifting Rule*, Forbes, April 29, 2014, at <http://www.forbes.com/sites/danielfisher/2014/04/29/patent-trolls-face-higher-risks-as-supreme-court-loosens-fee-shifting-rule/>.

<sup>126</sup> *Examining Recent Supreme Court Cases in the Patent Area: Hearing Before the House Judiciary Comm., Subcomm. on Courts, Intellectual Property, and the Internet*, 114<sup>th</sup> Cong., 1<sup>st</sup> Sess. (2015) (Statement of Andrew J. Pincus, Partner, Mayer Brown LLP), at 3, available at [http://judiciary.house.gov/\\_cache/files/43c13fd8-8287-4a3f-b172-67a0b37d236f/02.12.15-pincus-testimony.pdf](http://judiciary.house.gov/_cache/files/43c13fd8-8287-4a3f-b172-67a0b37d236f/02.12.15-pincus-testimony.pdf).

Section 3(b) of the Innovation Act would amend Section 285 to require a court, in any patent case, to award attorney fees to a prevailing party (plaintiff or defendant), *unless* the court finds that either

1. the nonprevailing party's position and conduct are "reasonably justified in law and fact"<sup>127</sup> or
2. there are "special circumstances (such as severe economic hardship to a named inventor) [that] make an award unjust."<sup>128</sup>

Although not explicitly stated by the legislation, the nonprevailing party would appear to have the burden of production and persuasion in proving the existence of either of these exceptions in order to rebut the presumption of an award of attorney fees. Supporters of the Innovation Act's fee-shifting provision believe that "allowing more liberal shifting of attorney fees against losing parties would reduce the frequency of such nuisance settlements, and would allow more defendants to challenge patents that are invalid or that have been asserted beyond what their claims reasonably allow."<sup>129</sup> On the other hand, those wary of fee-shifting provisions are concerned that they may benefit wealthy corporate parties to the disadvantage of individual inventors. They assert that "[a] 'loser pays' provision will deter patent holders from pursuing meritorious patent infringement claims and protects institutional defendants with enormous resources who can use the risk of fee-shifting to force inventors into accepting unfair settlements or dismissing their legitimate claims."<sup>130</sup>

The Support Technology and Research for Our Nation's Growth (STRONG) Patents Act of 2015 (S. 632) does not include a fee-shifting provision; instead, Section 101 of S. 632 (the "findings" section) asserts that the Supreme Court's *Octane Fitness* and *Highmark* rulings "significantly reduced the burden on an alleged infringer to recover attorney fees from the patent owner, and increased the incidence of fees shifted to the losing party."<sup>131</sup>

Section 7(a) of the PATENT Act expresses a "sense of Congress that, in patent cases, reasonable attorney fees should be paid by a nonprevailing party whose litigation position or conduct is not objectively reasonable."<sup>132</sup> Unlike the Innovation Act's creation of a presumption of an award of attorney fees, Section 7(b) of the PATENT Act would require the prevailing party to make a motion for the fees, thereby placing the burden of production and persuasion on the prevailing party to show that the nonprevailing party's litigation position or conduct was not objectively reasonable. Specifically, the PATENT Act would amend 35 U.S.C. § 285 to provide that, upon motion by a prevailing party, the court must determine whether the position of the nonprevailing party was "objectively reasonable in law and fact, and whether the conduct of the nonprevailing party was objectively reasonable." If the court finds that the nonprevailing party's position and conduct does not satisfy these standards, the court must award reasonable attorney fees to the prevailing party, unless special circumstances would make an award unjust.<sup>133</sup> Some practitioners

<sup>127</sup> H.R. 9, § 3(b), *adding revised* 35 U.S.C. § 285(a).

<sup>128</sup> *Id.*

<sup>129</sup> H.Rept. 113-279, at 21.

<sup>130</sup> *Id.* at 107 (quoting a letter from the American Association for Justice).

<sup>131</sup> S. 632, § 101(12).

<sup>132</sup> S. 1137, § 7(a).

<sup>133</sup> S. 1137, § 7(b), *adding revised* 35 U.S.C. § 285(a).



believe that the Innovation Act's fee-shifting provision "would likely require fee awards in more cases than" the PATENT Act's comparable provision.<sup>134</sup>

Unlike the Innovation Act, the PATENT Act would exempt from the fee-shifting provision any action that includes a cause of action for patent infringement under 35 U.S.C. § 271(e)(2).<sup>135</sup>

## Recovery of Fee Awards from Interested Parties

The Federal Rules of Civil Procedure outline when a person must and may join as a party in litigation. Under Rule 19, a person must join as a party if, in the person's absence, the court would be unable to accord complete relief among existing parties, the person is unable to protect an interest, or a present party would be subject to a substantial risk of incurring multiple obligations.<sup>136</sup> Under Rule 20, a person may join as a plaintiff if all the plaintiffs could claim a right to relief for injuries arising from the same occurrence or transaction.<sup>137</sup> Likewise, persons may be joined as defendants if any right to relief is asserted against them jointly, severally, or in the alternative with respect to or arising out of the same transaction or occurrence.<sup>138</sup> The Patent Act outlines more specific joinder requirements for a patent civil action. Under the Patent Act, a party may join a patent civil action as a defendant (accused infringer) only if any right to relief is asserted against the parties jointly and severally,<sup>139</sup> or arises out of the same transaction relating to the making, using, importing into the United States, offering for sale, or selling of the same accused product/process.<sup>140</sup> All defendants in the action must share the same questions of fact for joinder to occur.<sup>141</sup> Joinder cannot occur if "based solely on allegations that they each have infringed the patent or patents in suit."<sup>142</sup>

Section 3(c) of the Innovation Act would establish mandatory joinder rules when the nonprevailing party alleging infringement is unable to pay the fee award ordered by the court and other expenses. Thus, this provision would require a court presiding over a patent case to grant a defendant's motion to join an "interested party," "if such defending party shows that the plaintiff has no substantial interest in the patent or patents at issue other than asserting such patent claim in litigation."<sup>143</sup> An "interested party" subject to this joinder provision would include a party that is a patent assignee, has a right to enforce or sublicense the patent, or has a direct financial interest in the patent, such as the right to any part of a damage award or licensing revenue. The bill would exclude as an "interested party" legal counsel retained on a contingency fee basis or an individual

<sup>134</sup> Ryan Davis, *4 Differences in the House and Senate Patent Troll Bills*, Law360.com, April 30, 2015 (citing the views of several patent litigators).

<sup>135</sup> S. 1137, § 7(b), *adding revised* 35 U.S.C. § 285(d)(1). However, the PATENT Act would permit a court, in exceptional cases, to award reasonable attorney fees to the prevailing party in a civil action that includes a claim for relief arising under Section 271(e). *Id.*, *adding revised* 35 U.S.C. § 285(d)(2).

<sup>136</sup> Fed. R. Civ. P. 19.

<sup>137</sup> Fed. R. Civ. P. 20.

<sup>138</sup> *Id.*

<sup>139</sup> Joint and several liability occurs when two or more people are found liable, and the plaintiff may collect the entire judgment from any one of the parties or from any and all of the parties in various amounts until the judgment is paid in full. *See* Black's Law Dictionary, 2d. ed.

<sup>140</sup> 35 U.S.C. § 299(a).

<sup>141</sup> *Id.*

<sup>142</sup> *Id.* § 299(b).

<sup>143</sup> H.R. 9, § 3(c), *adding new* 35 U.S.C. § 299(d)(1).

“whose sole financial interest in the patent or patents at issue is ownership of an equity interest in the party alleging infringement, unless such person has the right or ability to influence, direct or control the civil action.”<sup>144</sup>

The Innovation Act would grant the court with the *discretion* to deny a motion to join if the interested party is not subject to service of process, or if the joinder would deprive the court of subject matter jurisdiction or render the venue improper.<sup>145</sup> The Innovation Act would *require* a court to deny a motion to join an interested party if the party did not receive “timely notice” of being identified as an interested party.<sup>146</sup> (The Innovation Act defines “timely notice” to mean actual notice, provided within 30 days after the party was identified in the plaintiff’s initial disclosure regarding entities that have financial interests in the patent, that the party may be liable for paying an award of fees if the plaintiff is unable to pay it.<sup>147</sup>)

A court would also be required to deny a motion to join an interested party if the interested party, within 30 days after receiving the notice described above, renounces in writing and with notice to the court and parties to the action, any ownership, right, or direct financial interest in the patent at issue.<sup>148</sup>

The Innovation Act would provide a court with discretionary authority to make an “interested party” who was joined under Section 3(c) of the act liable for any part of the award of attorney fees that the nonprevailing party is unable to pay.<sup>149</sup>

Mandatory joinder provisions, including that proposed by the Innovation Act, respond to the alleged lack of transparency regarding PAEs or the absence of financial resources held by some PAEs and their corresponding inability to pay fees to a prevailing defendant. Proponents of this proposed provision state that mandatory joinder would encourage greater transparency by granting patent defendants with further knowledge regarding all the parties who may have an interest in the litigation beyond the PAE “shell company.”<sup>150</sup> Proponents of the joinder provision also argue that such a change would allow prevailing defendants to seek a greater financial award against PAEs, who may not have extensive financial resources, by permitting the defendants to seek financial recovery against additional parties.<sup>151</sup> Opponents of this provision argue that the mandatory joinder of third parties is “one-sided” and may restrict the ability of patent owners to enforce their patents.<sup>152</sup> Some have stated that joinder provisions such as the one proposed by the Innovation Act may harm business relationships that arise through licensing by forcing parties to

<sup>144</sup> *Id.*, adding new 35 U.S.C. § 299(d)(4).

<sup>145</sup> *Id.*, adding new 35 U.S.C. § 299(d)(2)(A).

<sup>146</sup> *Id.*, adding new 35 U.S.C. § 299(d)(2)(B)(i).

<sup>147</sup> *Id.*, adding new 35 U.S.C. § 299(d)(3).

<sup>148</sup> *Id.*, adding new 35 U.S.C. § 299(d)(2)(B)(ii).

<sup>149</sup> H.R. 9, § 3(b), adding revised 35 U.S.C. § 285(b).

<sup>150</sup> *Hearing on H.R. 3309 Innovation Act Before the House Committee on the Judiciary, Subcommittee on Courts, Intellectual Property, and the Internet*, 113<sup>th</sup> Cong., 1<sup>st</sup> Sess., (2013) (Statement of Kevin T. Kramer, Vice President and Deputy General Counsel for Intellectual Property, on behalf of Yahoo! Inc.).

<sup>151</sup> *Protecting Small Businesses and Promoting Innovation by Limiting Patent Troll Abuse: Hearing Before the Senate Judiciary Comm.*, 113<sup>th</sup> Cong., 1<sup>st</sup> Sess. (2013) (Statement of Philip S. Johnson, Chief Intellectual Property Counsel, Johnson & Johnson).

<sup>152</sup> *The Impact of Abusive Patent Litigation Practices on the American Economy: Hearing Before the Senate Judiciary Comm.*, 114<sup>th</sup> Cong., 1<sup>st</sup> Sess. (2015) (Statement of Hans Sauer, Ph.D., Deputy General Counsel for Intellectual Property, on behalf of Biotechnology Industry Organization).



join in order to pay damages and other fees.<sup>153</sup> Opponents also contend that joinder in this context for the purposes of fee-shifting raises constitutional concerns as the provision would create standing for parties that would otherwise not have standing.<sup>154</sup> Specifically, the opponents point to the scenario where “a defendant may join [as] a third-party at the end of the case for the purposes of fee-shifting, but the third-party had no standing to assert or defend themselves during the course of the legal proceedings.”<sup>155</sup>

The PATENT Act contains a mechanism for recovering fee awards from interested parties that differs from the Innovation Act. First, the PATENT Act’s recovery of award provision would require the defendant to file (no later than 14 days before a scheduling conference is to be held or a scheduling order is due) an initial statement expressing the good faith belief that the primary business of the plaintiff is the assertion and enforcement of patents (or the licensing that results from it).<sup>156</sup> Within 45 days of being served with such an initial statement, the plaintiff would then be required to file a certification that<sup>157</sup>

1. the party will have sufficient funds to pay for any potential award of reasonable attorney fees;
2. the party’s primary business is not the assertion and enforcement of patents (or the licensing that results from it);
3. the identity of “interested parties,” if any; or
4. it has no such interested parties.

The PATENT Act defines “interested party” for purposes of this section concerning the recovery of fees, to mean a person who has a substantial financial interest related to the proceeds from any settlement, license, or damages award resulting from the enforcement of the patent in the action.<sup>158</sup> However, the term does NOT include any of the following: (A) an attorney or law firm providing legal representation in the action if the sole basis for its financial interest in the action arises from compensation related to the provision of legal representation; (B) a person who has assigned all right, title, and interest in a patent, except for passive receipt of income to an institution of higher education or a nonprofit technology transfer organization affiliated with the institution; and (C) a person who would otherwise meet the definition of an interested party but whose financial interest is based solely on an equity or security interest that had been initially established when the party alleging infringement’s primary business was not the assertion and enforcement of patents (or the licensing resulting from it).<sup>159</sup> The PATENT Act would place an ongoing duty on the plaintiff to update its certification within 30 days after a material change to any of the information provided within it.<sup>160</sup> Prior to filing the certification, the plaintiff must provide each identified interested party “actual notice in writing by service of notice in any district where the interested party may be found,” in order to establish jurisdiction over the interested party for the sole purpose of enforcing an award of attorney fees, “consistent with the

<sup>153</sup> *Id.*

<sup>154</sup> H.Rept. 113-279, p. 109.

<sup>155</sup> *Id.*

<sup>156</sup> S. 1137, § 7(b), *adding revised* 35 U.S.C. § 285(c)(1)(A).

<sup>157</sup> *Id.*, *adding revised* 35 U.S.C. § 285(c)(1)(B).

<sup>158</sup> *Id.*, *adding revised* 35 U.S.C. § 285(c)(2)(A),

<sup>159</sup> *Id.*, *adding revised* 35 U.S.C. § 285(c)(2)(B), (C), and (D).

<sup>160</sup> *Id.*, *adding revised* 35 U.S.C. § 285(c)(1)(B).

Constitution of the United States.”<sup>161</sup> The notice must identify the action, the parties, the patents at issue, and the interest qualifying the party to be an interested party. The notice must also inform the recipient that the recipient may be held accountable for any award of attorney fees (or a portion thereof) resulting from the action in the event the plaintiff cannot satisfy the full amount of such award, unless the recipient submits a statement to the court and parties in the action, within 120 days of receiving the notice, that renounces its interest related to the enforcement of the patent.<sup>162</sup> The PATENT Act would make any interested parties who are timely served with this notice potentially liable to pay any attorney fees, or portion thereof, awarded by the court, in the event that the party alleging infringement cannot satisfy the full amount of the award.<sup>163</sup> However, interested parties would not be accountable if “a true and correct certification” is filed with the court that the plaintiff will have sufficient funds to pay for any potential award of reasonable attorney fees, or that the party’s primary business is not the assertion and enforcement of patents (or the licensing that results from it).<sup>164</sup>

The PATENT Act grants an interested party the right to intervene in the action for purposes of contesting its identification as an interested party or its liability for attorney fees.<sup>165</sup> A court may, in the interest of justice, exempt from award recovery any party identified as an interested party. Finally, the PATENT Act would create a statutory exception to the applicability of the award recovery provision for any institution of higher education (as defined in 20 U.S.C. § 1001(a), or under equivalent laws in foreign jurisdictions), or a non-profit technology transfer organization whose primary purpose is to facilitate the commercialization of technologies developed by one or more institutions of higher education.<sup>166</sup> These entities must file with the court a certification that they qualify for this exception and provide notice to the parties in the action.

## Demand Letters

A patent demand letter is a letter sent by a patent-holder to a company or an individual accusing the recipient of patent infringement. The letters tend to demand that the alleged infringer take a specific action such as ceasing the infringing action or agreeing to a licensing arrangement. A patentee may use demand letters to prove willfulness in a patent infringement lawsuit, a high bar after recent court decisions. In the 2007 case, *In re Seagate Technology*, the Federal Circuit established a two-pronged test for willful infringement in a patent case. First, the patentee must show, by clear and convincing evidence, “that the infringer acted despite an objectively high likelihood that its actions constituted infringement of a valid patent.”<sup>167</sup> Then the patentee must prove “subjective recklessness,” which means that the accused infringer knew or should have known the risk of infringement.<sup>168</sup> A detailed demand letter, including a summary of the alleged patent infringement, helps to establish that the recipient/alleged infringer has the high degree of knowledge to meet this standard. Current law, however, does not dictate any specific content requirements or level of detail for demand letters.

<sup>161</sup> *Id.*, adding revised 35 U.S.C. § 285(c)(1)(C).

<sup>162</sup> *Id.*

<sup>163</sup> *Id.*, adding revised 35 U.S.C. § 285(c)(1)(D).

<sup>164</sup> *Id.*

<sup>165</sup> *Id.*, adding revised 35 U.S.C. § 285(c)(1)(G).

<sup>166</sup> *Id.*, adding revised 35 U.S.C. § 285(c)(1)(F).

<sup>167</sup> *In re Seagate Technology*, 497 F.3d 1360, 1371 (Fed. Cir. 2007).

<sup>168</sup> *Id.* at 1371-72.

The Innovation Act states that it is the “sense of Congress” that “it is an abuse of the patent system and against public policy for a party to send out purposely evasive demand letters to end users alleging patent infringement.”<sup>169</sup> H.R. 9 also states that any claimant asserting willful infringement may not rely on demand letters as notification of infringement unless the letter identifies with particularity the asserted patent, the product or process accused, and the ultimate parent entity of the claimant, and explains how the product or process infringes to the extent possible.<sup>170</sup>

H.R. 1896, the “Demand Letter Transparency Act of 2015,” outlines both content and disclosure requirements for demand letters. The bill would require any entity that sends 20 or more demand letters during any 365-day period to submit to the USPTO a disclosure identifying

- the patent, including a confirmation that the entity that sent the letter is the owner of the patent and is the last recorded entity in USPTO records for purposes of assignment, grant, or conveyance;
- the entity that has the right to license the patent or the name of the exclusive licensee;
- each entity asserting a claim with regard to the patent;
- each obligation to license the patent and the financial terms at which such patent has been licensed;
- the ultimate parent entity of such entity;
- the number of recipients of the letter;
- any case that has been filed by such entity relating to such patent; and
- any ex parte review or inter partes review of such patent.<sup>171</sup>

In order to enforce these proposed disclosure requirements, H.R. 1896 would permit a court in a patent infringement or validity action brought by an entity that does not meet such USPTO disclosure requirements to sanction such entity for an amount to be awarded to the adverse party to cover any costs incurred as a result of such violation.<sup>172</sup> The bill would exempt from these disclosure requirements original or joint inventors, institutions of higher education, and technology transfer organizations facilitating the commercialization of technology developed by institutions of higher education.<sup>173</sup>

In addition to the disclosure requirements, the Demand Letter Transparency Act of 2015 would require any demand letter sent to another entity to include specified information concerning

- each claim of each patent allegedly infringed, including each accused instrumentality;
- each party alleging infringement;

<sup>169</sup> H.R. 9, § 3.

<sup>170</sup> *Id.*

<sup>171</sup> H.R. 1896, § 2, *adding new* 35 U.S.C. § 263.

<sup>172</sup> *Id.*

<sup>173</sup> *Id.*

- the direct infringement for each claim alleged to have been infringed indirectly;
- the principal business of the party alleging infringement;
- each complaint filed that asserts or asserted any of the same patents, each case filed by such entity, and any ex parte or inter partes review for each patent;
- whether the patent is subject to any licensing term or pricing commitments;
- owners, co-owners, assignees, or exclusive licensees of the patent;
- any person who has a legal right to enforce the patent;
- any person with a direct financial interest in the outcome of the action; and
- how the recipient can access the USPTO demand letter database.<sup>174</sup>

Under the House’s TROL Act<sup>175</sup> and the Senate’s STRONG Patents Act,<sup>176</sup> a demand letter would qualify as an “unfair or deceptive act or practice” under the Federal Trade Commission Act<sup>177</sup> if the sender states or represents *wrongly* and *in bad faith* that

- the sender is a person with the right to license and enforce the patent;
- a civil action asserting a claim of infringement has been filed against the recipient;
- a civil action asserting a claim of infringement has been filed against other persons;
- legal action for infringement of the patent will be taken against the recipient;
- the sender is the exclusive licensee of the patent;
- persons other than the recipient purchased a license for the patent asserted in the letter;
- persons other than the recipient purchased an unrelated license and it is not identified as such;
- an investigation of the recipient’s infringement occurred.<sup>178</sup>

The TROL Act and the STRONG Patents Act also would consider demand letters as unfair practices if the sender in bad faith seeks compensation for

- a patent that is held to be unenforceable or invalid in a final determination;
- activities taken by the recipient after expiration of the asserted patent;
- activity of the recipient that the sender knew was authorized by a person with the right to license the patent.<sup>179</sup>

<sup>174</sup> H.R. 1896, § 3, *adding new* 35 U.S.C. § 264. H.R. 1896, § 2 also would require the USPTO to establish a demand letter database that is publicly accessible and searchable.

<sup>175</sup> H.R. 2014.

<sup>176</sup> S. 632.

<sup>177</sup> 15 U.S.C. § 45(a)(1).

<sup>178</sup> S. 632, § 202.

Demand letters would also qualify as unfair practices under the TROL Act and the STRONG Patents Act if the sender fails to include

- the identity of the person including the name of the parent entity unless such person is a public company and the name of the public company is identified;
- an identification of at least one patent allegedly infringed;
- an identification of at least one product or service of the recipient infringing the identified patent;
- a name and contact information of a person the recipient may contact about the assertions or claims.<sup>180</sup>

Under both the TROL Act and the STRONG Patents Act, the Federal Trade Commission would enforce any violations of the provisions above.<sup>181</sup> This provision would also preempt any state law “expressly relating to the transmission or contents of communications relating to the assertion of patent rights.”<sup>182</sup>

The Senate’s PATENT Act addresses both abusive demand letters and demand letters sent as pre-suit notification. Section 9 of the Senate’s PATENT Act would impose civil penalties on a person who has engaged in widespread abusive demand letter practices and has committed an unfair or deceptive act within the meaning of Section 5 of the Federal Trade Commission Act.<sup>183</sup> This bill outlines abusive demand letter practices as communications that falsely represent judicial relief or threaten litigation, and contain assertions that lack a reasonable basis in law or fact because the person does not have the right to assert the patent, the patent has expired, the patent is unenforceable, or the person has falsely represented that an infringement has occurred.<sup>184</sup> Similar to the enforcement provision outlined in the Senate’s STRONG Patents Act, the Federal Trade Commission would enforce any violations of this particular provision. The Senate’s PATENT Act would also require pre-suit notice letters that accuse a party of infringement to identify each patent believed to be infringed, to identify the allegedly infringing product, to describe why the plaintiff believes each patent identified is infringed, and to identify the person who can rightfully enforce the patent, as well as additional information.<sup>185</sup> The bill also states that if the plaintiff is seeking to establish willful infringement, then he may not rely on evidence of pre-suit notification of infringement unless that evidence includes this information. Commentators often associate vague demand letters with PAEs using these letters for the sole purpose of extracting financial concessions.<sup>186</sup> Supporters of more stringent requirements for demand letters point to vague demand letters as impediments of innovation due to the financial costs relating to litigation or settlement that ultimately arise from receiving these types of communications and the resulting

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(...continued)

<sup>179</sup> *Id.*

<sup>180</sup> *Id.*

<sup>181</sup> *Id.* § 203.

<sup>182</sup> *Id.* § 204.

<sup>183</sup> S. 1137, § 9, *adding new* 35 U.S.C. § 299D.

<sup>184</sup> *Id.*

<sup>185</sup> *Id.* § 8, *adding new* 35 U.S.C. § 299C.

<sup>186</sup> *See, e.g.,* Brian Fung, “Patent reform advocates are launching a ‘super-coalition’ to whack patent trolls,” *Washington Post*, Jan. 14, 2015.

impact on small businesses that cannot afford such costs.<sup>187</sup> Supporters also claim that placing more content-based requirements on demand letters would encourage patent owners to target specific infringers more carefully and likewise, would allow alleged infringers to have a clearer understanding of the infringement claims.<sup>188</sup> Critics of patent legislation have argued, however, that the legislation itself is not sufficiently tailored towards letters sent by PAEs, and additional requirements for patent letters may make “it more difficult for patent owners to communicate with potential licensees and alleged infringers even when those communications are in good faith.”<sup>189</sup>

## Post-Grant Review Reforms

The Leahy-Smith America Invents Act (AIA)<sup>190</sup> established a new administrative proceeding conducted by the USPTO’s Patent Trial and Appeal Board (PTAB) called a “post grant review” (PGR). In this proceeding, petitioners may challenge the validity of an issued patent based on any ground of patentability.<sup>191</sup> A petition to initiate a PGR must be filed within nine months of the date of patent grant.<sup>192</sup> To initiate a PGR, the petitioner must present information that, if not rebutted, would demonstrate that it is “more likely than not that at least one of the claims” is unpatentable.<sup>193</sup> A PGR must be completed within a year of its commencement, with an extension of six months possible for good cause shown.<sup>194</sup>

## Claim Construction Standard

The AIA is silent on what claim construction standard is appropriate in post-grant proceedings conducted by the PTAB. Pursuant to authority granted by the AIA, the USPTO promulgated a regulation in August 2012<sup>195</sup> that provided the following standard for instituting post-grant review as well as regulating proceedings after such institution: “[a] claim in an unexpired patent shall be given its broadest reasonable construction in light of the specification of the patent in which it appears.”<sup>196</sup> In a case issued in February 2015 involving a challenge to the USPTO’s rulemaking authority to promulgate this regulation, a divided panel of the Federal Circuit upheld the PTAB’s use of the “broadest reasonable interpretation” (BRI) standard in claim construction.<sup>197</sup> The appellate court noted that the USPTO has long applied the BRI standard in a variety of

<sup>187</sup> *Trolling for a Solution: Ending Abusive Patent Demand Letters: Hearing Before the House Energy & Commerce Comm., Subcomm. on Commerce, Manufacturing, and Trade*, 113<sup>th</sup> Cong. 2d Sess. (2014) (Statement of Mark Chandler, Senior Vice President and Chief Compliance Officer, on behalf of Cisco Systems Incorporated).

<sup>188</sup> *Id.*

<sup>189</sup> Gene Quinn & Steve Brachmann, “Demand Letter Legislation Must be Narrowly Tailored,” March 4, 2015, available at <http://www.ipwatchdog.com/2015/03/04/demand-letter-legislation-must-be-narrowly-tailored/id=55365/>.

<sup>190</sup> P.L. 112-29. For more information on this law, see CRS Report R42014, *The Leahy-Smith America Invents Act: Innovation Issues*, by John R. Thomas.

<sup>191</sup> 35 U.S.C. § 321(b).

<sup>192</sup> *Id.* § 321(c).

<sup>193</sup> *Id.* § 324(a).

<sup>194</sup> *Id.* § 326(a)(11).

<sup>195</sup> USPTO, *Changes to Implement Inter Partes Review Proceedings, Post-Grant Review Proceedings, and Transitional Program for Covered Business Method*, 77 Fed. Reg. 48680 (Aug. 14, 2012) (final rule).

<sup>196</sup> 37 C.F.R. § 42.100(b).

<sup>197</sup> *In re Cuozzo Speed Technologies LLC*, 778 F.3d 1271 (Fed. Cir. 2015).

proceedings, including initial examinations, interferences, and reissue and reexamination proceedings.<sup>198</sup> The Federal Circuit explained that by applying the BRI standard, the USPTO “reduce[s] the possibility that, after the patent is granted, the claims may be interpreted as giving broader coverage than is justified.”<sup>199</sup> The appellate court stated that “Congress is presumed to legislate against the background of existing law where Congress in enacting legislation is aware of the prevailing rule,”<sup>200</sup> and concluded that “Congress implicitly adopted the broadest reasonable interpretation standard in enacting the AIA.”<sup>201</sup>

Section 9 of the Innovation Act would legislatively overrule the Federal Circuit’s recent decision regarding the use of the BRI standard in post-grant proceedings. Instead, the Innovation Act would require that the PTAB, in inter partes review (IPR) and PGR proceedings, use the same claim construction standard that is applied by federal courts; that is, the PTAB would need to construe a patent claim “in accordance with the ordinary and customary meaning of such claim as understood by one of ordinary skill in the art and the prosecution history pertaining to the patent.”<sup>202</sup> The Innovation Act would also require the PTAB to consider prior claim construction by a court in a civil action in which the patent owner was a party.<sup>203</sup>

Sections 102 and 103 of the STRONG Patents Act contain similar amendments regarding the claim construction standard to be used in IPR and PGR proceedings. The PATENT Act does not include a provision that would alter the existing claim construction standard.

Former USPTO Director David Kappos has observed that currently, “the speed mandated for post-grant procedures is leading to greater interaction between court interpretations and USPTO interpretations of the same patent claims, and having the USPTO apply a different standard than the courts [for claim construction] is leading, and will continue to lead, to conflicting decisions.”<sup>204</sup> However, he notes that there are valid arguments for retaining the broader standard for post-grant proceedings, such as that the BRI standard “requires patentees to define their claims clearly over the prior art during proceedings” before the USPTO.<sup>205</sup>

Others have asserted that changing the claim construction standard in IPR and PGR from BRI to “ordinary and customary meaning” would be a positive benefit to patent owners who feel that the BRI standard makes it easier to invalidate their patents in the AIA-established post-grant reviews than in federal courts.<sup>206</sup>

<sup>198</sup> *Id.* at \*16.

<sup>199</sup> *Id.* at \*17 (quoting *In re Prater*, 415 F.2d 1393, 1396 (CCPA 1981)).

<sup>200</sup> *Id.* at \*17.

<sup>201</sup> *Id.* at \*21.

<sup>202</sup> H.R. 9, § 9, adding new 35 U.S.C. § 316(a)(14)(A).

<sup>203</sup> *Id.*, adding new 35 U.S.C. § 316(a)(14)(B).

<sup>204</sup> H.R. 3309, the “Innovation Act,” *Hearing Before the House Judiciary Comm., 113<sup>th</sup> Cong., 1<sup>st</sup> Sess.* (2013) (Statement of David J. Kappos, Former Under Secretary of Commerce for Intellectual Property and Director of the United States Patent and Trademark Office), at 8.

<sup>205</sup> *Id.*

<sup>206</sup> Ryan Davis, *Innovation Act Would Revamp AIA Reviews to Shield Patents*, Law360.com, Feb. 10, 2015 (explaining that “[c]onstruing the claims of a patent in an AIA review broadly means that significantly more prior art can be used to invalidate the patent than would be available in district court. A majority of AIA final decisions to date have invalidated at least some claims of the patent.”).



### ***Estoppel Effect of Unsuccessful Challenges in PGR and IPR Proceedings***

An individual who commences a PGR proceeding, along with anyone who has a legal interest in the patent, are barred from raising in a later civil action issues that they raised in the administrative review of the validity of a patent claim—as well as any issue that “reasonably could have been raised” during the PGR.<sup>207</sup> Section 9 of the Innovation Act and Section 14(a) of the PATENT Act would narrow the estoppel effect arising from a PGR by removing the phrase “or reasonably could have raised” in the statute.<sup>208</sup> Thus, this provision would effectively permit parties to later assert in a civil action that a patent claim is invalid on any ground that the party “reasonably could have raised” during the PGR. The purpose of this change is apparently to correct an “inadvertent scrivener’s error” made in drafting the AIA.<sup>209</sup>

### ***Presumption of Validity and Burdens of Proof***

The AIA provided that in an IPR or PGR proceeding, “the petitioner shall have the burden of proving a proposition of unpatentability by a preponderance of the evidence.”<sup>210</sup> Sections 102(c) and 103(c) of the STRONG Patents Act would amend existing law to provide a presumption of validity to a previously issued claim that is challenged during an IPR or PGR proceeding.<sup>211</sup> These sections of the legislation would also heighten the evidentiary standard for proving unpatentability of a previously issued claim, requiring that the IPR or PGR petitioner prove such unpatentability “by clear and convincing evidence.”<sup>212</sup>

### ***Standing***

Sections 102(d) and 103(d) of the STRONG Patents Act would provide more stringent standing requirements for persons wanting to initiate a PGR or IPR. The legislation provides that in order to have standing to file a petition with the USPTO to institute an IPR,<sup>213</sup> a person, or a real party in interest or privy of the person, must show a reasonable possibility of being sued for, or charged with,<sup>214</sup> infringement of the patent. The STRONG Patents Act adjusts the standing requirement

<sup>207</sup> 35 U.S.C. § 325(e).

<sup>208</sup> H.R. 9, § 9(a), *amending* 35 U.S.C. § 325(e)(2); S. 1137, § 14(a).

<sup>209</sup> See Colleen Chien and Eric Goldman, *In its Rush to Fix Patent Reform, Congress Didn’t Fix Its Biggest Error*, Forbes.com, Jan. 2, 2013; *see also* 158 Cong.Rec. S8517 (daily ed. Dec. 28, 2012) (statement of Senator Leahy) (“Regrettably, the legislation passed today does not include one technical correction that would improve the law by restoring Congress’s intent for the post-grant estoppel provision of the America Invents Act. Chairman Smith recently described certain language contained in that provision as an ‘inadvertent scrivener’s error.’ As written, it unintentionally creates a higher threshold of estoppel than was in the legislation that passed the Senate 95-5, or that was intended by the House, according to Chairman Smith’s statement. I hope we will soon address this issue so that the law accurately reflects Congress’s intent.”).

<sup>210</sup> 35 U.S.C. §§ 316(e), 326(e).

<sup>211</sup> S. 632, § 102(c), *adding revised* 35 U.S.C. § 316(e)(1); S. 632, § 103(c), *adding revised* 35 U.S.C. § 326(e)(1).

<sup>212</sup> *Id.* § 102(c), *adding revised* 35 U.S.C. § 316(e)(2); S. 632, § 103(c), *adding revised* 35 U.S.C. § 326(e)(2).

<sup>213</sup> *Id.* § 102(d), *adding new* 35 U.S.C. § 311(d)(2).

<sup>214</sup> The STRONG Patents Act defines the term “charged with infringement,” for purposes of this standing provision, to mean “a real and substantial controversy regarding infringement of a patent exists such that the petitioner would have standing to bring a declaratory judgment action in Federal court.” S. 632, § 102(d), *adding new* 35 U.S.C. § 311(d)(1).



slightly for instituting a PGR:<sup>215</sup> a person, or a real party in interest or privy of the person, must demonstrate

1. a reasonable possibility of being sued for, or charged with, infringement of the patent; or
2. a competitive harm related to the validity of the patent.

## Ending Diversion of USPTO Fees

The USPTO is funded entirely by fees it charges to patent and trademark applicants, as well as other entities that interact with the agency.<sup>216</sup> However, the amounts received as fees by the USPTO must still be appropriated by Congress in order for the funds to be available to the agency for obligation or expenditure.<sup>217</sup> Yet over the past 25 years, Congress has often not allocated all of the fees that the USPTO has collected towards the operation of that agency. It has been estimated that, since 1999, over \$1 billion in USPTO fee revenue has been withheld from the USPTO and directed towards unrelated government programs and operations.<sup>218</sup>

The America Invents Act (AIA) that was enacted in 2011 made several changes to the handling of fees collected by the USPTO. Under the AIA, the use of fees generated is still subject to the appropriations process, whereby Congress provides the budget authority for the USPTO to spend these fees. To address the issue of fees withheld from the office in the past, the AIA created within the Treasury a “Patent and Trademark Fee Reserve Fund” into which fee collections above that “appropriated by the Office for that fiscal year” are to be placed.<sup>219</sup> These funds are to be available to the USPTO “to the extent and in the amounts provided in appropriations Acts” and may only be used for the work of the USPTO.<sup>220</sup> However, the USPTO must still obtain congressional authority to use these “excess” funds.

Some argue that USPTO fee diversion is the “single most important problem facing our patent system today” because “continuing fee diversion constitute[s] a tax on innovation and undermine[s] efforts of the USPTO to reduce its backlog [of pending patent applications].”<sup>221</sup>

The STRONG Patents Act would put an end to USPTO fee diversion.<sup>222</sup> Section 107(a) of S. 632 would establish within the U.S. Treasury a revolving fund<sup>223</sup> called the “United States Patent and

<sup>215</sup> S. 632, §103(d), *adding new* 35 U.S.C. § 321(d)(2).

<sup>216</sup> See *Figueroa v. United States*, 466 F.3d 1023, 1027-28 (Fed. Cir. 2006). The USPTO became fully user-fee funded as a result of P.L. 101-508, the Omnibus Budget Reconciliation Act (OBRA) of 1990. For more information about USPTO’s funding structure, see CRS Report RS20906, *U.S. Patent and Trademark Office Appropriations Process: A Brief Explanation*, by Glenn J. McLoughlin.

<sup>217</sup> In the absence of an appropriation making fees collected by an agency available to that agency, the collected fees are placed in the general fund of the Treasury as miscellaneous receipts, unless otherwise directed. See Government Accountability Office (GAO), Office of the General Counsel, 3 Principles of Federal Appropriations Law 1-12 (2004) (citing 31 U.S.C. § 3302(b)).

<sup>218</sup> See Intellectual Property Owners, *USPTO Funding*, at <http://www.ipo.org/index.php/advocacy/hot-topics/uspto-funding/>.

<sup>219</sup> 35 U.S.C. § 42(c)(2).

<sup>220</sup> *Id.*

<sup>221</sup> H.Rept. 113-279, p. 104.

<sup>222</sup> A bill introduced in the House, the Innovation Protection Act (H.R. 1832), would similarly end USPTO fee diversion. However, this legislation does not contain provisions unrelated to the funding of the USPTO.

Trademark Office Innovation Promotion Fund” (Fund). Any fees collected by the USPTO would be deposited into this Fund and would be available to the USPTO Director until they are expended.<sup>224</sup> The amounts in the Fund would be available, without fiscal year limitation, to pay for all expenses of the USPTO, including all administrative and operating expenses that the office incurs.<sup>225</sup>

## Provisions Concerning Small Businesses

The patent reform litigation legislation introduced in the 114<sup>th</sup> Congress contains several provisions designed to help small businesses that are involved in the patent system either as patent owners or as defendants in infringement lawsuits.

### *Innovation Act and the PATENT Act*

Section 7(a) of the Innovation Act and Section 12 of the PATENT Act would require the USPTO director to develop educational resources for small businesses with respect to their “concerns arising from patent infringement.”<sup>226</sup> Furthermore, the Innovation Act would require that the USPTO’s existing small business patent outreach programs, as well as relevant offices at the Small Business Administration and the Minority Business Development Agency, provide education and awareness on abusive patent litigation practices.<sup>227</sup> Section 7(b) of the Innovation Act and Section 12(b) of the PATENT Act would require the USPTO to create and maintain a “user-friendly” section of its official website, in which the public can find information about patent cases that have been filed in federal court and information about the patent at issue (including the disclosures regarding patent ownership that are mandated by the Innovation Act and PATENT Act). Neither bill authorizes or provides additional appropriations to pay for these initiatives; rather, they are to be implemented using existing agency resources.

Section 8(g) of the Innovation Act would require the USPTO director, in consultation with several heads of relevant agencies and interested parties, to conduct a study that examines the economic impact of the Innovation Act on the ability of individuals and small businesses owned by women, veterans, and minorities to enforce their patent rights. STRONG Patents Act

Section 111 of the STRONG Patents Act would require the Small Business Administration to produce a report that analyzes the impact of patent ownership by small businesses (those that are independently owned and operated and which are not dominant in their field of operation) and patent infringement actions against small businesses. In addition, the STRONG Patents Act would require the Director of the Administrative Office of the United States to designate at least six U.S. district courts (that are already participating in the patent cases pilot program) “for the purpose of that program to address special issues raised in patent infringement suits against individuals or

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(...continued)

<sup>223</sup> S. 632, § 107(a)(4), *adding revised* 35 U.S.C. § 42(d)(2).

<sup>224</sup> *Id.* § 107(a)(2), *adding revised* 35 U.S.C. § 42(c)(1).

<sup>225</sup> *Id.* § 107(a)(4), *adding revised* 35 U.S.C. § 42(d)(4).

<sup>226</sup> H.R. 9, § 7(a)(1); S. 1137, § 12(a)(1).

<sup>227</sup> *Id.* § 7(a)(2); S. 1137, § 12(a)(2).

small business concerns.”<sup>228</sup> These specially designated courts would be required to expedite cases in which an individual or small business concern is accused of patent infringement.<sup>229</sup>

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<sup>228</sup> S. 632, § 111(c)(1).

<sup>229</sup> *Id.* § 111(c)(2).

**Table I. Patent Litigation Reform Legislation in the 114<sup>th</sup> Congress**

	<b>H.R. 9 Innovation Act</b>	<b>S. 1137 PATENT Act</b>	<b>S. 632 STRONG Patents Act</b>	<b>H.R. 1896 Demand Letter Transparency Act</b>	<b>H.R. 2045 TROL ACT</b>
<b>Pleading Requirement</b>	Proposed pleading requirements to include: each patent claim, acts of alleged infringer, principal business of plaintiff, authority to assert patent  General description where information is not available	Proposed pleading requirements to include: each patent claim, accused instrumentality, description of infringement  General description where information is not available	n/a	n/a	n/a
<b>Limits on Discovery</b>	ANDA suit exception  Proposed discovery limitations prior to claim construction to information necessary to construe claims  Court may allow discovery to prevent injustice  Parties may consent to exclusion from limitation	ANDA suit exception  Proposed discovery limitations to ruling on motions to dismiss, transfer venue, and sever accused infringers to information necessary to resolve those motions  Court may allow discovery to preserve evidence or prevent prejudice to party  Parties may consent to exclusion from limitation	n/a	n/a	n/a

	<b>H.R. 9 Innovation Act</b>	<b>S. 1137 PATENT Act</b>	<b>S. 632 STRONG Patents Act</b>	<b>H.R. 1896 Demand Letter Transparency Act</b>	<b>H.R. 2045 TROL ACT</b>
<b>Transparency of Patent Ownership</b>	<p>Upon filing of initial complaint for infringement, plaintiff must disclose to USPTO, court, and all adverse parties:</p> <ul style="list-style-type: none"> <li>• Assignee(s) of the patent</li> <li>• Entities with right to sublicense or enforce patent</li> <li>• Entities with financial interest in the patent (right to receive proceeds related to patent assertion) or in the plaintiff (direct or indirect ownership/control of more than 5% of the plaintiff)</li> </ul> <p>Ultimate parent entities (UPE) of the above entities (UPE is an entity not controlled by any other entity)</p> <p>Plaintiff has an ongoing duty to notify USPTO of any changes in the above</p> <p>Failure to comply with ongoing duty of disclosure means the plaintiff may not recover treble damages or reasonable fees during period of noncompliance; court may award fees to prevailing party for expenses incurred to uncover the updated information</p> <p>ANDA suit exception</p>	<p>Within 14 days of filing the complaint, plaintiff must notify court and adverse parties of:</p> <ul style="list-style-type: none"> <li>• Assignee(s)</li> <li>• Entities with right to sublicense or enforce patent</li> <li>• Entities with financial interest in the patent or in the plaintiff (direct or indirect ownership/control of &gt; 20% of the plaintiff)</li> <li>• UPE of the above</li> <li>• List of other complaints filed in prior 3 years asserting the patent</li> <li>• Any licensing requirements that patent is subject to</li> </ul> <p>Patentee may file this information under seal if confidential</p> <p>Patentee must file information regarding identity of entities with USPTO but no ongoing duty to update the information</p> <p>Assignment of all substantial rights in issued patent (and name of assignee and UPE) must be recorded in USPTO upon grant of patent and whenever subsequent assignments are made</p> <p>Same consequences as Innovation Act for failure to comply with duty to disclose assignment/UPE information to USPTO</p> <p>NO ANDA suit exception</p>	n/a	n/a	n/a

	<b>H.R. 9 Innovation Act</b>	<b>S. 1137 PATENT Act</b>	<b>S. 632 STRONG Patents Act</b>	<b>H.R. 1896 Demand Letter Transparency Act</b>	<b>H.R. 2045 TROL ACT</b>
<b>Stays of Customer- Suits</b>	<p>Court required to suspend/postpone litigation against customer if:</p> <ul style="list-style-type: none"> <li>• manufacturer and customer consent to the stay in writing</li> <li>• manufacturer is party to the civil action or in a separate action involving the patent</li> <li>• customer agrees to be bound by issues decided against the manufacturer</li> <li>• customer requests stay within the later of: 120 days after first pleading is served, or the first scheduling order in the case</li> </ul> <p>Stay may be lifted if suit against manufacturer will not resolve major issue in suit against customer or if stay unreasonably prejudices or is manifestly unjust to the party seeking to lift it</p> <p>ANDA suit exception</p>	<p>Court required to suspend/postpone litigation against customer if:</p> <ul style="list-style-type: none"> <li>• manufacturer is party to the civil action or in a separate action involving the patent</li> <li>• customer agrees to be bound by issues decided against the manufacturer</li> <li>• Consent of the manufacturer to the stay is needed only if manufacturer was made a party to the action on motion by the customer</li> <li>• customer requests stay within the later of: 120 days after first pleading is served, or the first scheduling order in the case</li> </ul> <p>Defines “customer” as a retailer or end user who has not materially modified the product/process alleged to infringe the patent</p> <p>Defines “end user” and “retailer” to exclude entities that manufacture the product/process at issue</p> <p>Same criteria as the Innovation Act for lift of the stay</p> <p>ANDA suit exception</p>	n/a	n/a	n/a

	<b>H.R. 9 Innovation Act</b>	<b>S. 1137 PATENT Act</b>	<b>S. 632 STRONG Patents Act</b>	<b>H.R. 1896 Demand Letter Transparency Act</b>	<b>H.R. 2045 TROL ACT</b>
<b>Shifting of Attorney Fees</b>	<p>Requires a court to award attorney fees to prevailing party unless court finds that either:</p> <ul style="list-style-type: none"> <li>• nonprevailing party's litigation position and conduct are "reasonably justified in law and fact" or</li> <li>• special circumstances exist that make an award unjust</li> </ul> <p>NO ANDA suit exception</p>	<p>On motion of the prevailing party, court must determine whether the the nonprevailing party's position was "objectively reasonable in law and fact" and whether its conduct was "objectively reasonable"</p> <ul style="list-style-type: none"> <li>• If they were not, court must award reasonable attorney fees to prevailing party unless special circumstances exist that make an award unjust</li> </ul> <p>ANDA suit exception</p>	n/a	n/a	n/a

	<b>H.R. 9 Innovation Act</b>	<b>S. 1137 PATENT Act</b>	<b>S. 632 STRONG Patents Act</b>	<b>H.R. 1896 Demand Letter Transparency Act</b>	<b>H.R. 2045 TROL ACT</b>
<b>Attorney Fee Recovery</b>	<p>If nonprevailing party is unable to pay attorney fee award, upon motion by prevailing party, court shall join an interested party to pay if prevailing party shows that nonprevailing party has no substantial interest in the case other than asserting the patent</p> <p>Court may deny motion to join interested party if:</p> <ul style="list-style-type: none"> <li>interested party is not subject to service of process</li> <li>joinder would deprive court of subject matter jurisdiction or make venue improper</li> </ul> <p>Court must deny motion to join interested party if:</p> <ul style="list-style-type: none"> <li>party did not receive timely notice of being identified as an interested party</li> <li>interested party renounces in writing and with notice to the court and parties, any ownership, right, or direct financial interest in the patent</li> </ul> <p>Joined interested parties may be required by the court to pay any unsatisfied portion of the fee award</p>	<p>No later than 2 weeks before scheduling conference is held, defendant may file initial statement expressing good faith belief that the plaintiff's primary business is asserting/enforcing patents</p> <p>Plaintiff must file a certification within 45 days of the defendant's initial statement that includes:</p> <ul style="list-style-type: none"> <li>that the party has sufficient funds to pay for any potential fee award,</li> <li>that the party's primary business is not asserting/enforcing patents,</li> <li>identity of interested parties, or</li> <li>no such interested parties exist</li> </ul> <p>Plaintiff must provide interested parties notice that the party may be held accountable to pay for an award of attorney fees if the plaintiff cannot satisfy the full amount of the award</p> <p>Interested parties may avoid financial liability by renouncing their interest related to enforcement of the patent, within 120 days of receipt of actual notice described above</p> <p>Interested parties have right to intervene in the action to contest its identification as an interested party or their liability for attorney fees</p> <p>Court may exempt interested party from liability in the interest of justice</p> <p>Exceptions for: universities, non-profit tech transfer organizations, and ANDA suits</p>	n/a	n/a	n/a



	<b>H.R. 9 Innovation Act</b>	<b>S. 1137 PATENT Act</b>	<b>S. 632 STRONG Patents Act</b>	<b>H.R. 1896 Demand Letter Transparency Act</b>	<b>H.R. 2045 TROL ACT</b>
<b>Demand Letters</b>	“Sense of Congress” that action including litigation stemming from purposely evasive demand letter should be considered fraudulent or deceptive practice	<p>Party may not rely on evidence of pre-suit notification to establish willful infringement unless communication contains specific information</p> <p>Defines widespread demand letter abuse as violation of FTC Act</p>	Defines a demand letter as an unfair or deceptive practice under FTC Act if wrongly and in bad faith misrepresents specific details	<p>Entity that sends 20 or more demand letters per year must disclose specific information to USPTO</p> <p>Demand letters must include specific information relating to the patent claim allegedly infringed and the party alleging infringement</p>	Defines a demand letter as a unfair or deceptive practice under FTC Act if wrongly and in bad faith misrepresents specific details

	<b>H.R. 9 Innovation Act</b>	<b>S. 1137 PATENT Act</b>	<b>S. 632 STRONG Patents Act</b>	<b>H.R. 1896 Demand Letter Transparency Act</b>	<b>H.R. 2045 TROL ACT</b>
<b>Post-Grant Review Reforms</b>	<p>Requires the Patent Trial and Appeal Board (PTAB), in inter partes review (IPR) and post-grant review (PGR) proceedings, to follow the same claim construction standard used by district courts</p> <p>Narrows the estoppel effect arising from a PGR by allowing a PGR petitioner to raise in a later civil action issues (with respect to the validity of a patent claim) that they “reasonably could have raised” during the PGR</p>	<p>Narrows the estoppel effect arising from a PGR by allowing a PGR petitioner to raise in a later civil action issues (with respect to the validity of a patent claim) that they “reasonably could have raised” during the PGR</p>	<p>Requires the PTAB, in IPR and PGR proceedings, to follow the same claim construction standard used by district courts</p> <p>Provides a presumption of validity to a previously issued claim that is challenged during an IPR or PGR proceeding</p> <p>Requires IPR/PGR petitioner to prove unpatentability of a previously issued claim “by clear and convincing evidence” (existing law is “preponderance of the evidence”)</p> <p>Provides more stringent standing requirements for IPR/PGR petitioner</p>	n/a	n/a
<b>Elimination of USPTO Fee Diversion</b>	n/a	n/a	<p>Establishes a revolving fund in which fees collected by USPTO would be deposited; such fees would be available to USPTO until expended</p>	n/a	n/a

	<b>H.R. 9 Innovation Act</b>	<b>S. 1137 PATENT Act</b>	<b>S. 632 STRONG Patents Act</b>	<b>H.R. 1896 Demand Letter Transparency Act</b>	<b>H.R. 2045 TROL ACT</b>
<b>Small Business</b>	<p>Requires USPTO director to develop educational resources for small businesses with respect to their “concerns arising from patent infringement”</p> <p>Requires USPTO and other federal agencies to provide, through existing small business outreach programs, education and awareness on abusive litigation practices</p> <p>Requires USPTO to create and maintain a “user-friendly” section of its website in which the public may find information about filed patent cases and the patents at issue in those cases</p> <p>Requires USPTO director to conduct a study examining the economic impact of the Innovation Act on the ability of individuals and small businesses owned by women, veterans, and minorities to enforce their patent rights</p>	<p>Requires USPTO director to develop educational resources for small businesses with respect to their “concerns arising from patent infringement”</p> <p>Requires USPTO to create and maintain a “user-friendly” section of its website in which the public may find information about filed patent cases and the patents at issue in those cases</p>	<p>Requires Small Business Administration to produce a report analyzing the impact of patent ownership by small businesses and patent infringement actions against small businesses</p> <p>Requires Director of the Administrative Office to designate at least six district courts to address special issues raised in patent infringement suits against individuals or small business concerns; such courts would be required to expedite cases in which an individual or small business concern is accused of patent infringement</p>	n/a	n/a

**Source:** Congressional Research Service.

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