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## Trolling for an NPE Solution

Jared A. Smith

Nicholas R. Transier

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## Trolling for an NPE Solution

By JARED A. SMITH\* AND NICHOLAS R. TRANSIER\*\*

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\* Jared Smith is a 2015 J.D. Candidate at the University of California, Hastings College of the Law. Prior to law school, Jared worked as a professional engineer at Raytheon along with Nick Transier, and later at Northrop Grumman. Jared received a Bachelor of Science in Industrial & Systems Engineering from the University of San Diego and a Master of Science in Systems Architecture & Engineering from the University of Southern California.

\*\* Nick Transier is a registered patent attorney and partner at EIP US LLP, where he focuses on intellectual property matters with an emphasis on patent litigation and prosecution. Nick received his J.D. with honors from The University of Texas School of Law. Before law school, Nick worked as a professional engineer at Lockheed Martin and Raytheon. Nick received a Bachelor of Science and a Master of Science in Systems Engineering from the University of Virginia.

## Foreword

This note was written and submitted for publication in March of 2014. The patent landscape has been dynamic (more like terrifying) since that time. In particular, the Supreme Court has issued landmark opinions changing the exceptional case standard under Section 285 (*Octane Fitness*) and changing the scope of the test for patentable subject matter under Section 101 (*Alice*). Consequently, this note has been selectively updated to reflect those changes.

### I. Introduction

Consider the following brief fact scenarios. First, a small-time inventor has a brilliant idea and the good sense to patent it, but cannot afford to start a business, so instead licenses the patent to a company who then uses the technology with great success. Second, a university conducts research that is ultimately patented, but licenses the technology to a company in order to keep focused on research. Both of the aforementioned scenarios seem to have positive outcomes, right? But what if it took a lawsuit, by either the small-time inventor or the university, rather than a bargain, to compel the license? “WHO CARES,” says the mob, they are both patent trolls! Unfortunately, widespread concern with enforcing patent rights without practicing those rights has resulted into a bewildering range of “anti-troll” activism.

But first, what is a “patent troll?” Wikipedia defines a “patent troll” as “a person or company who enforces patent rights against *accused infringers* in an attempt to collect licensing fees, but does *not manufacture products or supply services based upon the patents in question*, thus engaging in economic *rent-seeking*.”<sup>1</sup> Though patent trolls have certainly been labeled much worse things,<sup>2</sup> this “definition” is still bloated with tacit disapproval. For example, “accused infringers” only slightly obfuscates the implication that the *accused* infringers are not *actual* infringers. And the not-so-subtle condemnation for “not manufactur[ing] products or supply[ing] services based upon the patents in question” seems to imply that patents are meant only for those patentees that intend to manufacture and supply—despite the fact that patents provide no explicit or implicit right to actually do either.<sup>3</sup> Finally, “rent-seeking”—though somewhat out of context<sup>4</sup>—essentially implies that patent trolls create

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1. *Patent troll*, WIKIPEDIA, [http://en.wikipedia.org/wiki/Patent\\_troll](http://en.wikipedia.org/wiki/Patent_troll) (last visited Apr. 2, 2014) (emphasis added).

2. See, e.g., Kevin O'Connor, *How to Slaughter a Patent Troll in 5 Steps*, PANDODAILY (July 26, 2013), <http://pando.com/2013/07/26/how-to-slaughter-a-patent-troll-in-5-steps/> (labeling patent trolls as the “scum of the earth”).

3. See *General Information Concerning Patents*, UNITED STATES PATENT AND TRADEMARK OFFICE, [http://www.uspto.gov/patents/resources/general\\_info\\_concerning\\_patents.jsp#heading-1](http://www.uspto.gov/patents/resources/general_info_concerning_patents.jsp#heading-1) (last updated Apr. 4, 2012).

4. See, e.g., David R. Henderson, *Rent Seeking*, LIBRARY OF ECONOMICS AND LIBERTY, <http://www.econlib.org/library/Enc/RentSeeking.html> (last visited Apr. 2, 2014) (using the term “rent seeking” in a political context).

wealth for themselves without creating wealth for anyone else, but ignores the fact that in all likelihood the troll had to buy the patent from someone else (or the right to assert it), thereby creating wealth for someone else.

At times, “patent trolls” are referred to by more civilized acronyms. For example, the term “non-practicing entity” or “NPE” has been said to apply generally to entities that do not actually practice the patents they own.<sup>5</sup> As another example, the Federal Trade Commission (“FTC”) coined the term “patent assertion entity” or “PAE” to identify a narrower class of NPEs with a business model that “focuses on purchasing and asserting patents against manufacturers already using the technology, rather than developing and transferring technology.”<sup>6</sup> According to the FTC, “the term NPE encompasses patent owners that primarily seek to develop and transfer technology, such as universities and semiconductor designs. *Patent assertion entities do not include this latter group.*”<sup>7</sup> Some believe the term “patent monetization entities” (“PMEs”) better articulates the distinction between “all such efforts to monetize patent rights” and the “behavior involved in creating products and services based on the innovation covered by the patent.”<sup>8</sup> This camp, however, excludes universities from the definition of PMEs under the premise that universities’ core activities are education and academic research, not monetization.<sup>9</sup> In the following discussion, “patent troll” will be defined as an entity that owns a patent (or at least the rights to assert it) and who does not practice the patent or intend to practice the patent, but, instead intends merely to monetize the patent through litigations or threats of the same.

One would be hard-pressed to find a branch of the government (state or federal), journalist, reporter, pundit, critic, or other advocate that is not voicing an opinion. For example, President Obama said that patent trolls “hijack somebody else’s idea and see if they can extort some money out of them.”<sup>10</sup> Outspoken business owners have been similarly critical. For example, Mark Cuban proclaimed that “[d]umbass patents are crushing small businesses.”<sup>11</sup> Even the judges adjudicating the “trolling” are weighing in conspicuously, and not just through their normal mediums of written orders and judgments. For example, a New York Times article co-written by Chief Judge

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5. Sara Jeruss, Robin Feldman & Joshua Walker, *The America Invents Act 500: Effects of Patent Monetization Entities on US Litigation*, 11 DUKE L. & TECH. REV. 357, 366 (2012).

6. FED. TRADE COMM’N, *THE EVOLVING IP MARKETPLACE: ALIGNING PATENT NOTICE AND REMEDIES WITH COMPETITION* 8 (2011).

7. *Id.* at n.5 (emphasis added).

8. Jeruss, *supra* note 5, at 368.

9. *Id.* at 370.

10. *President Barack Obama’s State of the Union Address*, THE WHITE HOUSE (Jan. 28, 2014), <http://www.whitehouse.gov/the-press-office/2014/01/28/president-barack-obamas-state-union-address>.

11. *Id.*

of the Federal Circuit, Randall Rader, stated that “[t]he onslaught of litigation brought by ‘patent trolls’—who typically buy up a slew of patents, then sue anyone and everyone who might be using or selling the claimed inventions—has slowed the development of new products, increased costs for businesses and consumers, and clogged our judicial system.”<sup>12</sup> When otherwise circumspect members of the judiciary start penning op-eds for major news outlets rather than classical reporters, you know that the issue has hit a boiling point.

The level of attention garnered by patent trolls is not without objective basis. For example, it has been reported that the median cost of defending claims of patent infringement brought by an NPE ranges between \$600,000, where less than \$1 million is at risk, to \$4 million, where more than \$25 million is at risk.<sup>13</sup> As one commentator has noted: “even the weakest of claims” presents a “Hobson’s Choice,” where the defendant can choose between “settling and giving the plaintiff remedies to which it is not entitled, or spending a larger sum to prevail without any realistic prospect of fee recoupment.”<sup>14</sup>

“Trolling” is increasing. According to a study that analyzed all 13,000 patent infringement cases for the years 2007, 2008, 2011, and 2012, the percentage of suits brought by PME’s (excluding universities) increased from 24.6 percent in 2007 to 58.7 percent in 2012.<sup>15</sup> Meanwhile, the number of overall defendants in patent infringement lawsuits increased by about 129 percent from 2007 to 2011, with 89 percent of the increase attributable to software-related patents<sup>16</sup>—rumored favorites of the troll tribe.

The scope of patent troll “problem” is matched only by the scope of the “solutions” being proposed. This note will seek to consider the scope of the laws and all manner of other “solutions” being proposed, threatened and implemented in an effort to cure the patent troll problem. Admittedly, the consideration of each individual solution may, in some cases, be high-level. Many of the proposed solutions warrant an entire note unto themselves, and it is beyond the scope of this note to present every possible point with regard to every single proposal.

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12. See Randal R. Rader, Colleen V. Chien & David Hricik, *Make Patent Trolls Pay in Court*, N.Y. TIMES (Jun. 4, 2013), [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).

13. AMERICAN INTELLECTUAL PROPERTY LAW ASSOCIATION, REPORT OF THE ECONOMIC SURVEY 2013 35 (2013).

14. Brief for Petitioner at 3, *Octane Fitness v. Icon Health and Fitness*, 134 S.Ct. 1749 (2014) (No. 12-1184).

15. Robin Feldman, Tom Ewing & Sara Jeruss, *The AIA 500 Expanded: The Effects of Patent Monetization Entities*, available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2247195](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2247195).

16. U.S. GOV’T ACCOUNTABILITY OFFICE, GAO-13-465, *Intellectual Property: Assessing Factors That Affect Patent Infringement Litigation Could Help Improve Patent Quality* 14 (2013).

Nevertheless, in surveying the range of proposed solutions this note will try to swing the conversation back into the neighborhood of objectivity, and will consider each proposed “solution” against the backdrop of the statutory framework in which “trolling” is conducted. Additionally, this note will seek to identify the potential issues with various “solutions,” including the impact of the solutions not only on patent trolls, but also, arguably more importantly, on the patent system as a whole. Ultimately, this note will endorse certain approaches and condemn others.

If this has piqued your interest, then read on. What follows is a *very* brief background of the patent system and its purposes in Section II; a discussion of Executive Branch activism relating to trolling in Section III.A.; a discussion of Judicial Branch activism relating to trolling in Section III.B.; a discussion of Legislative Branch (federal and state) activism relating to trolling in Section III.C.; recommendations in Section IV; and concluding thoughts in Section V.

Spoiler alert: based on our review of all of the activism related to trolling, we recommend the following approaches, which balance the purposes of the patent system, including maintaining the value of said system, with the property rights of a patent owner: increasing the quality of patents through (1) increased training of patent examiners and (2) increased participation of the public through crowdsourcing of prior art discovery; revising discovery rules to better balance the cost burden of requesting and complying with discovery requests; implementing a two-way fee-shifting scheme; increasing the pleading standards for patent cases (including direct infringement); closing the procedural loophole in Section 299 regarding joinder; and adopting local rules that provide early case dispositive check-valves.

## II. Background

The Constitution provides the foundation for the patent system in Article I, Section 8, Clause 8, which states, “[t]he Congress shall have Power . . . [t]o promote the Progress of Science and useful Arts, by securing for limited Times to . . . Inventors the exclusive Right to their respective . . . Discoveries.”<sup>17</sup> As an indication of the relative importance of a patent system to our founders, the First Congress of the United States enacted the first Patent Act in 1790. The current patent laws are based on the Patent Act of 1952, as codified in Title 35 of the United States Code (“Code”), and were most recently updated by the Leahy-Smith America Invents Act<sup>18</sup>, which was signed into law on September 16, 2011.

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17. U.S. CONST. art. I, § 8, cl. 8.

18. Leahy-Smith America Invents Act (2011) (125 Stat. 284-341).

A patent issued by the United States confers a twenty-year “exclusive right” in the form of a “grant to the patentee, his heirs or assigns, of the right to exclude others from making, using, offering for sale, or selling the invention throughout the United States, or importing into the United States . . . .”<sup>19</sup> Notably, a patent *does not* provide a positive right to make, use, or sell the invention.<sup>20</sup> Rather, as the Supreme Court has explained, a patentee’s right to exclude others is the “very essence of the right conferred by the patent, *as it is the privilege of any owner of property to use or not use it, without question of motive.*”<sup>21</sup>

Like most types of property, patents and patent applications are transferrable (i.e. they can be bought, sold, licensed, etc.). Specifically, Section 261 states that “patents shall have the attributes of personal property” and “shall be assignable.”<sup>22</sup> More importantly, not only is the entire patent transferable, but the individual rights granted to a patent owner are also transferrable.<sup>23</sup> And beneficiaries of these rights (e.g. assignees and licensees) are entitled to exploit their patent rights (or not) in the same ways as the original inventors, and “without question of motive.”<sup>24</sup>

Infringement of a patent occurs when “*whoever* without authority makes, uses, offers to sell, or sells any patented invention, within the United States or imports into the United States any patented invention during the term of the patent . . . .”<sup>25</sup> And *all* patent owners—whether original or successors-in-interest—are promised a “remedy by civil action” when their patents are infringed.<sup>26</sup>

The Supreme Court has articulated several purposes of the patent system:

First, patent law seeks to foster and reward invention; second, it promotes disclosure of inventions, to stimulate further innovation and to permit the public to practice the invention once the patent expires; third, the stringent requirements for patent protection seek to assure that ideas in the public domain remain there for the free use of the public.<sup>27</sup>

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19. 35 U.S.C.A. § 154 (West 2014).

20. See *General Information Concerning Patents*, UNITED STATES PATENT AND TRADEMARK OFFICE, [http://www.uspto.gov/patents/resources/general\\_info\\_concerning\\_patents.jsp#heading-1](http://www.uspto.gov/patents/resources/general_info_concerning_patents.jsp#heading-1) (last updated Apr. 4, 2012).

21. *Continental Paper Bag Co. v. Eastern Paper Bag Co.*, 210 U.S. 405, 429 (1908) (emphasis added) (There, the Supreme Court opined that “Congress ha[d] not overlooked the subject of nonuser of patented inventions.”); see also *Patlex Corp. v. Mossinghoff*, 758 F.2d 594, 599 (Fed. Cir. 1985) (“The encouragement of investment-based risk is the fundamental purpose of the patent grant, and is based directly on the *right to exclude*.”).

22. 35 U.S.C.A. § 261 (West 2014).

23. *Id.*

24. *Continental Paper Bag*, 210 U.S. at 429.

25. 35 U.S.C.A. § 271(a) (West 2014) (emphasis added).

26. 35 U.S.C.A. § 281 (West 2014).

27. *Aronson v. Quick Point Pencil Co.*, 440 U.S. 257, 262 (1979); see also Craig A. Nard, *THE LAW OF PATENTS* 3 (2d ed. 2011) (stating the patent system exists to “offer a potential financial reward

Thus, the patent system exists as “a carefully crafted bargain that encourages both the creation and the public disclosure of new and useful advances in technology, in return for an exclusive monopoly for a limited period of time.”<sup>28</sup> And more specifically, the limited monopoly provided by a patent is “intended to motivate the creative activity of . . . inventors by the provision of a special reward . . .”<sup>29</sup> where the “special reward” is “property in [the inventor’s] inventions . . . of which the law intended to give him the absolute enjoyment and possession.”<sup>30</sup>

As the Supreme Court has recognized, there are inherent costs associated with the patent system:

On the one hand, the promise of exclusive rights provides monetary incentives that lead to creation, invention, and discovery. On the other hand, that very exclusivity can impede the flow of information that might permit, indeed spur, invention, by, for example, raising the price of using the patented ideas once created, requiring potential users to conduct costly and time-consuming searches of existing patents and pending patent applications, and requiring the negotiation of complex licensing arrangements.<sup>31</sup>

Thus, the patent system must seek to balance the competing interest of motivating innovation through patent rights with avoiding monopolies that unnecessarily stifle competition.<sup>32</sup>

Critically, neither the Constitution nor the patent laws derived therefrom make any distinction in patent rights based on the identity of the patent owner. Put differently, the patent laws are generally agnostic to ownership. Consequently, the patent laws are applied in the same way whether the patent owner is an individual or a legal entity, whether or not the patent owner is original or a successor-in-interest, and whether or not the patent owner is exploiting the patented invention or licensing others too—even if that license is compelled.

So, what we are left with is a patent system that, unfortunately, has few mechanisms to filter harmful behavior (e.g., “trolling”) from beneficial behavior (e.g., investment and innovation). And as alluded to above, the patent laws provide little in the way of defensible positions that “trolling” is truly bad behavior—at least as far as the law is concerned. Notwithstanding, next we will consider many of the proposed solutions to the . . . problem?

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as an inducement to invent, to disclose technical information, to invest capital in the innovation process, and to facilitate efficient use and manufacturing of invention through licensing.”)

28. *Pfaff v. Wells Electronics, Inc.*, 525 U.S. 55, 63 (1998); see also *Bonito Boats, Inc. v. Thunder Craft Boats, Inc.*, 489 U.S. 141, 150-51 (1989).

29. *Sony Corp. of America v. Universal City Studios, Inc.*, 464 U.S. 417, 429 (1984) (emphasis added).

30. *Ex parte Wood*, 22 U.S. 603, 608 (1824).

31. *Mayo Collaborative Servs. v. Prometheus Labs., Inc.*, 132 S. Ct. 1289, 1305 (2012).

32. *Pfaff*, 525 U.S. at 63.

### III. Analysis

#### A. Executive Branch Activism

##### 1. *The President*

###### *i. Executive Actions to Combat Patent Trolls*

President Obama does not like patent trolls. In his most recent (2014) State of the Union Address, President Obama called on Congress to “pass a patent reform bill that allows our businesses to stay focused on innovation, not costly, needless litigation”<sup>33</sup>—a thinly-veiled reference to the so-called patent troll problem. And referring to the recently implemented America Invents Act (AIA), which includes some provisions<sup>34</sup> meant to curb trolling behavior, the President admonished that “our efforts at patent reform only went about halfway to where we need to go.”<sup>35</sup>

Given this backdrop, it is not surprising that the White House has issued a variety of executive actions “designed to protect innovators from frivolous litigation and ensure the highest-quality patents in our system.”<sup>36</sup> Specifically, in June of 2013, the White House issued five executive actions, including two that mentioned “patent trolls” by name<sup>37</sup>:

###### 1. Making “Real Party-in-Interest” the New Default.

*Patent trolls* often set up shell companies to hide their activities and enable their abusive litigation and extraction of settlements. This tactic prevents those facing litigation from knowing the full extent of the patents that their adversaries hold when negotiating settlements, or even knowing connections between multiple *trolls*. The PTO will begin a rulemaking process to require patent applicants and owners to regularly update ownership information when they are involved in proceedings before the PTO, specifically designating the “ultimate parent entity” in control of the patent or application. . .

3. **Empowering Downstream Users.** *Patent trolls* are increasingly targeting Main Street retailers, consumers and other end-users of products containing patented technology—for instance, for using point-of-sale software or a particular

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33. *President Barack Obama’s State of the Union Address*, THE WHITE HOUSE (Jan. 28, 2014), <http://www.whitehouse.gov/the-press-office/2014/01/28/president-barack-obamas-state-union-address>.

34. *See infra* Part III.B.1.

35. President Barack Obama, Remarks at Google+ Hangout (Feb. 14, 2014) (video available at <https://www.youtube.com/watch?v=VQ4Zo0XyNsw>) (last visited Apr. 1, 2014).

36. *Fact Sheet: White House Task Force on High-Tech Patent Issues*, THE WHITE HOUSE (Jun. 4, 2013), <http://www.whitehouse.gov/the-press-office/2013/06/04/fact-sheet-white-house-task-force-high-tech-patent-issues> [hereinafter *Executive Actions*].

37. *Id.* (emphasis added).

business method. End-users should not be subject to lawsuits for simply using a product as intended, and need an easier way to know their rights before entering into costly litigation or settlement. The PTO will publish new education and outreach materials, including an accessible, plain-English web site offering answers to common questions by those facing demands from a possible *troll*.

Notably, “making real party-in-interest the new default” is unlikely to do much to squelch trolling for at least a few reasons.<sup>38</sup> First, the person with the rights necessary to assert a patent against a defendant already has to be a party to any lawsuit.<sup>39</sup> Knowing whom that party is related to is, at best, cold comfort to a defendant. Second, for years the United States Patent and Trademark Office (“USPTO”) has provided a publically accessible system for identifying patent owners of record.<sup>40</sup> And the system is searchable both by patent number and by assignee name so that, for example, a single search could return many patents owned by a particular patent troll. To be fair, assignments are not always recorded and knowing the relationship between different entities could assist in an effort to ascertain the scope of the collective’s patent holdings. But the reality is that this is a very large hoop placed very close to the ground that any patent troll can easily jump through.

“Empowering downstream users” by providing “education and outreach materials” is a nice thought, but all the free advice in the world is unlikely to scare off patent trolls that stand to make millions off their portfolios. As frustrating as it is, settling with a patent troll for “nuisance value”—despite the merits—is often as financially sensible from the defendant’s side as it is lucrative from the plaintiff’s (i.e., troll’s) side. One wonders what kind of free advice can possibly unravel the patent troll’s otherwise very efficient business model.

And as a side note, contrary to the executive action, end-users of “products containing [valid] patented technology” *should be willing to pay for that right*, or otherwise be subject to a lawsuit and liable for damages. Otherwise, what is the point of the patent system?

In February 2014, after a renewed call for “meaningful legislation to combat patent trolls,” the White House issued a status report on the previous executive actions and issued three additional executive actions,

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38. However, real party-in-interest and privity considerations are proving to be dispositive issues for post grant proceedings, such as *inter partes* reviews. See, e.g., Ryan Davis, *PTAB Says VMWare Too Late with Patent Review Petition* (Mar. 9, 2015) available at <http://www.law360.com/articles/629225/ptab-says-vmware-too-late-with-patent-review-petition>.

39. See, e.g., FED. R. CIV. P. 17(a)(1) (“An action must be prosecuted in the name of the real party in interest.”).

40. See UNITED STATES PATENT AND TRADEMARK OFFICE, <http://assignments.uspto.gov/assignments/q?db=pat> (last visited Apr. 11, 2014).

which related to (1) crowd-sourcing prior art; (2) increasing training at the USPTO; and (3) expanding pro-bono and pro-se assistance programs for inventors who lack legal representation.<sup>41</sup> Crowd-sourcing prior art is described in more detail below.<sup>42</sup>

Increasing training at the USPTO can possibly improve the patent troll situation, albeit indirectly. One of the chief complaints of anti-troll advocates is that trolls only sue on worthless patents that should have never been issued. While that rhetoric is demonstrably false in the aggregate, it is certainly true in certain cases. In any event, improving the quality of examination at the USPTO should, over the long term, reduce the number of low-quality patents that make their way into patent troll's hands—or anyone's hands for that matter. Everyone wins (even patent trolls) when patent applications undergo a higher quality examination.

ii. *Executive Recommendations for Legislation to Combat Patent Trolls*

In conjunction with the executive actions, the White House has issued seven legislative recommendations, of which the following are most relevant to patent trolls:

1. **Require patentees and applicants to disclose the “Real Party-in-Interest,”** by requiring that any party sending demand letters, filing an infringement suit or seeking PTO review of a patent to file updated ownership information, and enabling the PTO or district courts to impose sanctions for non-compliance.

2. **Permit more discretion in awarding fees to prevailing parties in patent cases,** providing district courts with more discretion to award attorney's fees under 35 USC 285 as a sanction for abusive court filings (similar to the legal standard that applies in copyright infringement cases).

3. **Expand the PTO's transitional program** for covered business method patents to include a broader category of computer-enabled patents and permit a wider range of challengers to petition for review of issued patents before the Patent Trial and Appeals Board (PTAB).

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41. See *Fact Sheet: Executive Actions: Answering the President's Call to Strengthen Our Patent System and Foster Innovation*, THE WHITE HOUSE (Feb. 20, 2014), <http://www.whitehouse.gov/the-press-office/2014/02/20/fact-sheet-executive-actions-answering-president-s-call-strengthen-our-p> [hereinafter *Executive Actions II*].

42. See *infra* Part III.A.2.

4. **Protect off-the-shelf use by consumers and businesses** by providing them with better legal protection against liability for a product being used off-the-shelf and solely for its intended use. Also, stay judicial proceedings against such consumers when an infringement suit has also been brought against a vendor, retailer, or manufacturer . . .

6. **Use demand letter transparency** to help curb abusive suits, incentivizing public filing of demand letters in a way that makes them accessible and searchable to the public.<sup>43</sup>

Starting at the top, requiring patentees and applicants to disclose the “real party-in-interest,” is mostly a house-keeping measure. As mentioned above, it is already necessary to name the real party-in-interest on any formal complaint.<sup>44</sup> Thus, it is unlikely that having to disclose this information at other times will deter a patent troll from pursuing an alleged infringer.

Permitting more discretion in awarding fees to prevailing parties in patent cases, on the other hand, has bite. As discussed, *infra* Section III(C)(3), less than a year after the White House issued its legislative recommendations, the Supreme Court preempted Congress and unanimously overruled the Federal Circuit’s *Brooks Furniture* “exceptional” case standard, noting that existing standard was “unduly rigid.”<sup>45</sup>

Ultimately, granting more discretion to district courts should deter all plaintiffs (including patent trolls) from filing frivolous suits thereby deterring abusive litigation behavior.

Expanding the PTO’s transitional Covered Business Method Review (“CBM”) program “to include a broader category of computer-enabled patents and permit a wider range of challengers” could prove problematic in view of the performance of the current program. As it is currently implemented, CMB review allows a party that has been sued for infringement (or who otherwise has standing to bring a declaratory judgment action) to challenge the validity of a financial business method patent in a trial before the Patent Trial and Appeal Board (PTAB)<sup>46</sup>—*on any ground of patentability*.<sup>47</sup> This is in stark contrast to other post-grant review procedures that limit the grounds to novelty and obviousness and

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43. See *Executive Actions*, *supra* note 36.

44. See, e.g., FED. R. CIV. P. 17(a)(1) (“An action must be prosecuted in the name of the real party in interest.”).

45. *Octane Fitness, LLC v. ICON Health & Fitness, Inc.*, 134 S. Ct. 1749, 1755-56 (2014).

46. *Transitional Program for Covered Business Method Patents*, UNITED STATES PATENT AND TRADEMARK OFFICE, [http://www.uspto.gov/aia\\_implementation/faqs\\_covered\\_business\\_method.jsp](http://www.uspto.gov/aia_implementation/faqs_covered_business_method.jsp) (last visited Apr. 2, 2014).

47. See *Id.* (response to Question CBMR4040).

severely restrict the evidence to prove the same.<sup>48</sup> Congress established the “transitional” (read: experimental) CBM program to provide alleged infringers with an alternative method to challenge patent validity that is quicker and cheaper than litigation.<sup>49</sup> And by limiting the program to “covered business methods”—a favorite of patent trolls—Congress has conspicuously targeted trolling behavior.

However, the current CBM program has many glaring issues. First, it defines a covered business method patent incredibly broadly as one “that claims a method or corresponding apparatus for performing data processing or other operations used in the practice, administration, or management of financial product or service, *except that the term does not include patents for technology inventions.*”<sup>50</sup> Thus, “technology inventions” are the only safe harbor. Unfortunately, the definition of a “technology invention” is far from clear. Rather, the rules state that figuring whether an invention is a “technology invention” requires “a case-by-case” determination of “whether the claimed subject matter as a whole recites a technological feature that is novel and unobvious over the prior art; and solves a technical problem using a technical solution.”<sup>51</sup> So . . . a *technology* invention is just a claim with a *technological* feature that solved a *technical* problem using a *technical* solution . . . technically, at least. In any event, the carve-out for “technology inventions” provides no clear guideposts to a safe harbor for those prosecuting patents now.

The results of the CBM program have been, perhaps not surprisingly, controversial. A review of the PTAB’s final written decisions issued as of early April 2014 reveals that the PTAB canceled 100% of all claims (249 of 249 claims in 10 CBMs) for which trial was instituted.<sup>52</sup> Statistics like these have led Chief Judge Rader to characterize the PTAB as “death squads . . . killing property rights.”<sup>53</sup> And one has to wonder whether the USPTO sees the irony in invalidating patents *it issued* at such an alarming

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48. See, e.g., *Comparison of Post-Grant Procedures Before and After The America Invents Act*, RATNERPRESTIA, <http://www.rppostgrant.com/ComparisonCharts/post-grant-review-comparison.html> (last visited Apr. 11, 2014) (comparison chart).

49. Kenneth N. Nigon, *Post Grant Review, Inter Partes Review and Transitional Program for Covered Business Method Patents*, IPWATCHDOG (Aug. 29, 2012), <http://www.ipwatchdog.com/2012/08/29/post-grant-review-inter-partes-review-and-transitional-program-for-covered-business-method-patents/id=27668/>.

50. 37 C.F.R. § 42.301(a); see also Leahy-Smith America Invents Act § 18(d)(1), (2011).

51. 37 C.F.R. § 42.301(b); see also Leahy-Smith America Invents Act § 18(d)(2), (2011).

52. Michelle Carniaux & Julia Tanase, *IPR and CBM Statistics*, KENYON & KENYON (April 7, 2014), <http://interpartesreviewblog.com> (detailed statistics available at <http://interpartesreviewblog.com/wp-content/uploads/2014/04/FORMATTED-IPR-CBM-Stats-Handout-4.pdf>).

53. Brian Mahoney, *Software Patent Ruling a Major Judicial Failure, Rader Says*, LAW360 (Oct. 25, 2013 6:36 PM), <http://www.law360.com/articles/482264/software-patent-ruling-a-major-judicial-failure-rader-says>.

rate. Either way, it is a frightening proposition to expand a program to include a broader category of computer-enabled patents when the existing death squad, err, program, is already killing patents at a “draconian”<sup>54</sup> rate. And as discussed further, below, it is even more frightening that Congress is considering expanding the CBM program to all subject areas—and *making it permanent*.

Protecting “off-the-shelf use by consumers and businesses” by providing them with better legal protection against liability for a product being used off-the-shelf and solely for its intended use is flat out contrary to law. In the context of a patented apparatus, the patent laws *only* ask whether an alleged infringer is making, using, selling, offering for sale or importing an infringing product; there is no consideration whatsoever of whether the product is being used as it is supposed to be, i.e., for its intended use.<sup>55</sup>

Finally, requiring demand letter transparency by, for example, incentivizing public filing of demand letters in a way that makes them accessible and searchable to the public, has been rationalized because sending demand letters is “[the] kind of activity that belongs in the same family as other types of unfair and deceptive trade practices.”<sup>56</sup> However, it is possible that such requirements would have the unintended consequences of (1) chilling legitimate efforts to put legitimate infringers on notice, which may raise First Amendment concerns, as well as (2) impacting a patent owner’s ability to market and license inventions, which undermines the patent owner’s fundamental right to exclude. Moreover, such a regulation would burden all patent owners alike, not just patent trolls. So at least insofar as limiting trolling behavior goes, requiring demand letter transparency does not appear to be an effective solution.

## 2. *The USPTO*

The USPTO<sup>57</sup> has responded to the executive actions with various rule changes and initiatives. The most significant proposed rule change would establish increased transparency of patent ownership during patent prosecution and at designated times throughout the life of the patent.<sup>58</sup>

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54. Robert G. Sterne & Gene Quinn, *PTAB Death Squads: Are All Commercially Viable Patents Invalid?*, IPWatchdog (Mar. 24, 2014), <http://www.ipwatchdog.com/2014/03/24/ptab-death-squads-are-all-commercially-viable-patents-invalid/id=48642/>.

55. See 35 U.S.C.A. § 271(a) (West 2014) (“[W]hoever without authority makes, uses, offers to sell, or sells any patented invention, within the United States or imports into the United States any patented invention during the term of the patent therefor, infringes the patent.”).

56. Jeff Sistrunk, *Congress Urged to Act on Abusive Patent Troll Leaders*, LAW360 (Apr. 9, 2014), <http://www.law360.com/articles/526310/congress-urged-to-act-on-abusive-patent-troll-letters>.

57. The United States Patent and Trademark Office (USPTO) is an office of the executive branch within the Department of Commerce.

58. Changes to Require Identification of Attributable Owner, 79 Fed. Reg. 4105 (proposed Jan. 24, 2014) (to be codified at 37 C.F.R. § 1).

Specifically, the rule would require the “attributable owner” including the “ultimate parent entity” to be identified when an application is filed, when there is a change in ownership during prosecution of the application, at the time the issue fee and maintenance fees are due, and any time the patent is challenged in a USPTO proceeding (such as a reexamination proceeding).<sup>59</sup> Professor Robin Feldman of the University of California Hastings College of the Law, criticized the proposed rule by saying, “[t]he patent office is asking for information at key moments, but those moments are too few and far between,” leaving out “a lot of critical time in the life of a patent.”<sup>60</sup> But even if the information were required more often, would it really affect trolling behavior? Probably not.

Most critics of trolling behavior would acknowledge that patent trolls are rarely if ever the original inventor, owner, or assignee of a patent application or issued patent. Rather, as Chief Judge Rader noted,<sup>61</sup> patent trolls usually acquire interest and ownership in that patent well after prosecution is complete. So rules designed to make ownership more transparent during prosecution are not likely to illuminate much with respect to trolls.

Moreover, increasing the transparency of patent ownership during any stage of the patent’s life does not change much substantively with respect to asserting that patent against a defendant, except maybe whose name shows up in a pleading’s caption. And, identifying the “attributable owner” would not affect the procedures that the USPTO follows when an issued patent is challenged by a defendant through, for example, an *ex parte* reexamination,<sup>62</sup> an *inter partes* reexamination,<sup>63</sup> or a CBM review.<sup>64</sup> Thus, as with the similar executive action discussed above, this is more of a house-keeping measure than an effective measure against patent trolls.

Another initiative being undertaken by the USPTO is the development of a better mechanism to enable crowdsourcing of prior art.<sup>65</sup> The initiative is meant to increase the ability of companies, subject matter experts, and the public to “crowdsource” prior art and to submit it to the USPTO in an effort to drive better patentability determinations.<sup>66</sup> It is widely acknowledged that patent examiners have too little time in most cases (and perhaps too little incentive in others) to complete a comprehensive review of the art.

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59. *Id.*

60. Ryan Davis, *USPTO Patent Transparency Plan Won't Stop Trolls*, LAW360 (Jan. 27, 2014 7:57 PM), <http://www.law360.com/articles/504233/uspto-patent-transparency-plan-won-t-stop-trolls>.

61. See Rader, *supra*, note 12.

62. See generally 37 C.F.R. §§ 1.501-1.625.

63. See generally 37 C.F.R. §§ 1.902-1.997, 42.108-42.207.

64. See generally 37 C.F.R. § 42.300-42.304.

65. *Executive Actions II*, *supra* note 40.

66. *Id.*

Crowdsourcing the search for relevant art—particularly by interested parties like potential defendants—could lessen the burden on the USPTO and increase the quality of examination. The White House believes that increasing third-party submissions of prior art will “help ensure that U.S. patents are of the highest quality.”<sup>67</sup>

It is worth noting, however, that the AIA has already instituted a form of crowdsourcing through third-party pre-issuance submissions, and those procedures have not been widely utilized.<sup>68</sup> Additionally, the public has been able to formally submit prior art to the USPTO through the provisions of 35 U.S.C. § 301 since at least 1981.<sup>69</sup> Notwithstanding, just like providing additional training to USPTO examiners, this measure may help the trolling problem indirectly by reducing the proliferation of low quality (but otherwise perfectly exploitable) patents.

## B. Legislative Activism

### 1. *The America Invents Act (Enacted)*

The America Invents Act (AIA), signed into law on September 26, 2011, significantly updated the Patent Act of 1952. While the AIA made many significant changes to the patent laws generally, the following is a discussion of certain provisions that may affect patent trolls.

#### *Joinder and Consolidation*

Before passage of the AIA, courts performed joinder and consolidation of parties for patent litigation in accordance with Rule 20 and Rule 42 of the Federal Rules of Civil Procedure (FRCP).<sup>70</sup> Under these rules, patent trolls “commonly employ[ed] a litigation strategy of initiating infringement suits against large numbers of unrelated, geographically diverse defendants in venues friendly to patent plaintiffs . . . .”<sup>71</sup> Joining multiple defendants in a single complaint offered several advantages to patent trolls, including reduced litigation

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67. *Executive Actions II*, *supra* note 40.

68. Gene Quinn, *PTO Seeks Comments on Crowdsourcing Prior Art*, IPWATCHDOG (Mar. 26, 2014), <http://www.ipwatchdog.com/2014/03/26/pto-seeks-comments-on-crowdsourcing-prior-art/id=48724/>.

69. See 35 U.S.C.A. § 301 (West 2014).

70. See FED. R. CIV. P. 20(a)(2) (“Persons . . . may be joined in one action as defendants if: (A) any right to relief is asserted against them jointly, severally, or in the alternative with respect to or arising out of the same transaction, occurrence, or series of transactions or occurrences; and (B) any question of law or fact common to all defendants will arise in the action.”); FED. R. CIV. P. 42(a) (“If actions before the court involve a common question of law or fact, the court may: (1) join for hearing or trial any or all matters at issue in the actions; (2) consolidate the actions . . . .”).

71. Tracie L. Bryant, Note, *The America Invents Act: Slaying Trolls, Limiting Joinder*, 25 HARV. J.L. & TECH. 673, 674 (2012).

costs, improved forum selection, reduced likelihood that defendants would be able to transfer the case to an undesirable forum, and reduced risk of inconsistent validity or claim construction determinations.<sup>72</sup>

On the other side of the ‘v,’ multiple defendant lawsuits tend to be inherently more complex for the individual defendants because, for example, there is an “exponential” increase in logistics and competing interests among defendants.<sup>73</sup> The complexity, in-turn, increases the perceived cost of litigation, compels defendants to settle, and places additional pressure on remaining defendants to do the same.<sup>74</sup> Additionally, often the co-defendants to these multi-defendant lawsuits are competitors, which increases tension between the defendants and prevents any marginal benefits of sharing the defense burden. Thus, suing numerous defendants in a single action has been an effective strategy for patent trolls in districts that allowed plaintiffs to join defendants based solely on the allegation they had infringed that same patent.<sup>75</sup>

Section 19(d) of the AIA amended 35 U.S.C. § 299 to prevent courts from joining unrelated defendants under certain circumstances.<sup>76</sup> Under the AIA, a court may join parties accused of infringement or consolidate their actions *for trial* only if the parties are alleged to be jointly or severally liable, or if the defendants’ alleged infringements arose out of the same transaction or occurrence, and there are questions of fact common to all defendants.<sup>77</sup> Unlike before, a court cannot join accused infringers nor consolidate their actions for trial “based solely on allegations that they each have infringed the . . . patents in suit.”<sup>78</sup> Commentators have speculated that the purpose of the change is to increase litigation costs for patent trolls and to prevent unfettered forum shopping.<sup>79</sup>

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72. *Id.* at 674-75; Scott W. Burt, Barry F. Irwin & Jonathan B. Tropp, *Intellectual Property Owners Association Litigation Committee White Paper: Impact of the Misjoinder Provision of the America Invents Act 8* (2012) available at [http://www.ipo.org/wp-content/uploads/2013/03/whitepaper\\_misjoinder1.pdf](http://www.ipo.org/wp-content/uploads/2013/03/whitepaper_misjoinder1.pdf).

73. Brian M. Buroker & Maya M. Eckstein, *Multiple Defendant Patent Infringement Cases: Complexities, Complications and Advantages 1* (2007) available at [http://www.hunton.com/files/Publication/e7e49e13-2327-4d36-a04c1dcc301527c4/Presentation/PublicationAttachment/b2cc8f60-eb07-41f7-8949787a644f1cff/Multiple\\_Defendant\\_Paper\\_AIPLA.pdf](http://www.hunton.com/files/Publication/e7e49e13-2327-4d36-a04c1dcc301527c4/Presentation/PublicationAttachment/b2cc8f60-eb07-41f7-8949787a644f1cff/Multiple_Defendant_Paper_AIPLA.pdf).

74. *Id.*

75. Bryant, *supra* note 71, at 675.

76. Leahy-Smith America Invents Act § 19(d), 35 U.S.C. § 299 (2011); *see also* Burt, *supra* note 74, at 7 (“[The] legislative history reveals, Section 299 was intended to resolve a split of authority among the district courts relating to joinder under [Rule 20].”).

77. 35 U.S.C.A. § 299(a) (West 2014).

78. 35 U.S.C.A. § 299(b) (West 2014).

79. Alison Frankel, *Patent Trolls and Multidistrict Litigation: It's Complicated*, REUTERS (May 10, 2013), <http://blogs.reuters.com/alison-frankel/2013/05/10/patent-trolls-and-multidistrict-litigation-its-complicated/>.

In practice, the new joinder rules have resulted in fewer multiple-defendant patent infringement suits,<sup>80</sup> but patent trolls have countered by increasing the number of filings against individual defendants who would have previously been named in a single complaint.<sup>81</sup> And while AIA Section 299 prevents joinder and consolidation of multiple unrelated parties *for trial*, it does not explicitly “prevent the consolidation or coordination of multiple cases for purposes of *pre-trial* activities,”<sup>82</sup> such as discovery and claim construction, which can be astronomically expensive activities for the defendants especially. Discovery is particularly troubling in this context because patent trolls usually have little in the way of discovery burdens because many patent trolls do not do anything other than sue. On the other hand, defendants (often high-tech companies) are faced with the unnerving task of spilling their company secrets over and over again to patent trolls and within earshot of their fiercest competitors within the same lawsuits.

Patent trolls are employing at least two strategies to circumvent the spirit of Section 299. First, some patent trolls are employing multidistrict litigation (MDL) procedures to bind cases for pre-trial activities.<sup>83</sup>

Specifically, patent trolls are relying on Section 1407 of Title 28 of the U.S. Code, which states: “[w]hen civil actions involving one or more common questions of fact are pending in different districts, such actions may be transferred to any district for coordinated or consolidated pretrial proceedings.”<sup>84</sup> The Judicial Panel on Multidistrict Litigation (JPMDL) administers MDL, and may transfer an action on its own initiative or in response to a motion filed by a party to the action.<sup>85</sup> Thus MDL procedures have been used as an end-run around the new joinder rules. On a positive note, more patent trolls might be exploiting the MDL procedures but for the fact that employing MDL means losing control over the venue or judge for MDL proceedings<sup>86</sup>—the JPMDL chooses both.<sup>87</sup>

Second, and perhaps more devious, patent trolls have purposefully incorporated in Delaware to collocate with a large pool of defendants.<sup>88</sup> This strategy effectively prevents defendants incorporated in Delaware

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80. Burt, *supra* note 74, at 3.

81. *Id.*

82. *Id.* at 11 (emphasis added).

83. See, e.g., *In re Bear Creek Technologies Inc.*, 2013 WL 3789471 (D. Del. 2013) (transferring actions from Eastern District of Virginia to the District of Delaware as a MDL).

84. 28 U.S.C.A. § 1407(a) (West 2014).

85. 28 U.S.C.A. § 1407(c) (West 2014).

86. *Id.*

87. 28 U.S.C.A. § 1407 (West 2014).

88. Frankel, *supra* note 81.

from seeking a transfer to a more convenient forum. And because Delaware is a relatively small forum, patent cases are routinely assigned to the same judge,<sup>89</sup> which tends to result in consolidation. Thus, a patent troll can exploit the likelihood that multiple defendants reside in a single forum in order to circumvent the amended joinder rules and to combine separate actions related merely by the same patents-in-suit for pre-trial activities.

In sum, while the new AIA joinder rules have the best intentions, they fall short of really impacting a primary strategy of patent trolls: forcing many defendants into disadvantageous defense groups in an effort promote quick, often “nuisance value” settlements.

### *Post Grant Challenges*

The AIA implemented three new post grant procedures: *inter partes* review (IPR), post-grant review (PGR), and covered business method patent review (CBMR). CBMR was previously discussed, above. IPR is similar to the pre-existing *inter partes* reexamination procedure available before the AIA. But PGR is all new and merits some discussion.

PGR became available on March 16, 2013. In order to instigate a PGR, a petition must be filed within nine months after issuance of the patent.<sup>90</sup> What makes PGR significant relative to IPR is that a broader range of challenges may be made in a PGR petition. Specifically, the PGR petition can be based on Sections 101 (subject matter), 102 (novelty), 103 (obviousness) and 112 (written description, except for best mode),<sup>91</sup> whereas IPR can only be based on Sections 102 and 103. Further, prior art is not limited to patents or printed publications in PGR like it is in IPR. Instead, evidence of public use, on-sale activity, or other public disclosures is admissible.<sup>92</sup>

However, the additional avenues of attacking a patent’s validity in PGR are not provided without risk. Perhaps most daunting, the estoppel created by PGR applies to all USPTO proceedings, ITC proceedings, and district court litigations.<sup>93</sup> Additionally, the estoppel attaches immediately upon a determination of the Patent Trial and Appeal Board, rather than

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89. *Id.*

90. *See Post Grant Review*, UNITED STATES PATENT AND TRADEMARK OFFICE, [http://www.uspto.gov/aia\\_implementation/faqs\\_post\\_grant\\_review.jsp#heading-3](http://www.uspto.gov/aia_implementation/faqs_post_grant_review.jsp#heading-3) (last visited Apr. 17, 2014).

91. *See Changes to Implement Inter Partes Review Proceedings, Post-Grant Review Proceedings, and Transitional Program for Covered Business Method Patents*, 77 Fed. Reg. 48,680, 48,684 (Aug. 14, 2012) (to be codified at 37 C.F.R. pt. 42).

92. *Id.*

93. *Id.*

after all possible appeals like an IPR.<sup>94</sup> So, in essence, if a petitioner's argument does not carry the day during PGR, then it will never carry the day, and it will immediately eviscerate that party's ability to challenge the validity of the PGR'ed patent in a later district court or ITC case.

As discussed above, patent trolls typically are not the original owners or assignees of a patent. Therefore, it is hard to characterize post-grant review as an "anti-troll" provision. However, as discussed in the context of other provisions, post-grant review may indirectly improve the issue of patent trolling by eliminating bad patents well before they can be found, acquired, and monetized by a patent troll.

### *Prior-User Defense*

The AIA substantially expanded the scope and applicability of the prior-user defense beyond the previous version codified in Section 273.<sup>95</sup> Notably, the revised Section 273 expands the scope of the defense to cover almost all patents. "One specific reason for this broadening amendment was to specifically insulate businesses from having to disclose their internal processes or manufacturing materials"<sup>96</sup> by defensively patenting them and thereby making them public record. Another notable change is that new Section 273 expanded the scope of the entities that can assert the defense. Specifically, Section 273(e)(1)(A) now expands the defense to "the person who performed or directed the performance of the commercial use described in subsection (a), or by an entity that controls, is controlled by, or is under common control with such person."<sup>97</sup> According to the Congressional record, the new provision is intended to expand the defense to include contractors, vendors, or other third parties over whom the person asserting the defense had control.<sup>98</sup>

As a result of the AIA, an accused infringer may now assert the prior-user defense under Section 273 against *any claimed invention* in any patent that issues on or after September 16, 2011, provided that the accused infringer commercially used the subject matter in the United States at least one year prior to the effective filing date of the claimed invention.<sup>99</sup>

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94. *Id.*

95. See Jeff Mikrut, *How the America Invents Act Revived the Prior-User Defense*, AMERICAN BAR ASSOCIATION (Feb. 20, 2012), <http://apps.americanbar.org/litigation/committees/intellectual/articles/winter2012-prior-user-defense-america-invents-act.html>; see also generally 35 U.S.C. § 273 (2010).

96. *Id.*

97. 35 U.S.C.A. § 273(e)(1)(A) (West 2014).

98. See 157 CONG. REC. S5430–31 (daily ed. Sept. 8, 2011) (statement of Sen. Kyl).

99. See 35 U.S.C.A. § 273(a) (West 2014).

Here again, this change to the law is not patent-troll-specific, but it nevertheless addresses a tendency of patent trolls to shop for patents that are already widely practiced by companies. The expanded prior-user defense under Section 273 may significantly shorten a patent troll's timeframe to locate, acquire, and assert a patent against an already practicing entity. At the same time, this change strikes a balance with the broader purposes of the patent system by allowing a patent to issue despite prior uses that do not qualify as prior art (e.g. trade secret use) such that the patent can be asserted against those that do not qualify as prior users.

## 2. *Innovation Act*

The Innovation Act (H.R. 3309) is a bill currently being considered by Congress with the conspicuous purpose of curbing patent trolling. The Innovation Act passed in the House of Representatives by an overwhelming majority (325-91) on December 5, 2013. The Innovation Act includes many provisions from other, concurrent bills that are being considered with varying levels of support. As such, consideration of the following key anti-troll provisions associated with this particular bill will act as a proxy for other bills with similar provisions.

### *Revised Exceptional Case Standard*

The Innovation Act proposed a hybrid loser-pays system. Under the proposed Innovation Act, a revised Section 285 provided that "[t]he court shall award, to a prevailing party, reasonable fees . . . *unless* the court finds that the position and conduct of the nonprevailing party or parties were *reasonably justified* in law and fact or that special circumstances (such as severe economic hardship to a named inventor) makes an award unjust."<sup>100</sup>

Proponents of the proposed fee shifting system believe it will "make it harder for trolls to use the extraordinary expense of patent litigation to force a settlement."<sup>101</sup> Ultimately, one of patent trolls' biggest advantages to date has been the disparity of financial risk in undertaking a troll suit. Exacerbating this issue is the fact that many troll suits are run on contingency, which means that the patent trolls do not even have to pay

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100. Innovation Act, H.R. 3309, 113th Cong. (as passed by the House, Dec. 9, 2013) (emphasis added).

101. Zachary Graves, *New Proposal to Slay Patent Trolls Would be a Boon to the Digital Economy*, HUFF POST TECH (Oct. 7, 2013 12:26 PM), [http://www.huffingtonpost.com/zachary-graves/new-proposal-to-slay-pate\\_b\\_4024831.html](http://www.huffingtonpost.com/zachary-graves/new-proposal-to-slay-pate_b_4024831.html); see also Colleen V. Chien, *Reforming Software Patents*, 50 HOUS. L. REV 325, 369 (2012) ("Fee-shifting changes the economics by requiring an unsuccessful plaintiff to foot the defendant's legal fees, punishing and deterring low-probability claims.").

most of the attorney's fees to litigate the case. Contingency fee cases shift much of the financial burden to eager plaintiff's attorneys looking for a big score. Notably, though, a successful patent troll will also benefit from this change by having its fees paid by a losing defendant.<sup>102</sup>

Opponents, on the other hand, believe that while fee shifting may deter frivolous claims, it will almost certainly deter meritorious claims as well.<sup>103</sup> This is, of course, due to the increased financial risk to bring a case in such a system—even if the intentions and merits are solid. It is certainly not a goal of the patent laws to prevent rightful owners from exercising their property rights. Otherwise, the value of patents could be negatively impacted. Critics also point out that patent trolls may be able to circumvent loser-pays rules by suing under shell companies meant to insulate their investors from liability—a well-established practice among sophisticated patent trolls.<sup>104</sup> Though, Congress could mitigate this strategy by requiring plaintiffs to post a bond.<sup>105</sup>

The Innovation Act was unable to gain traction in the Senate, and was withdrawn from consideration by the Senate Judiciary Committee in May 2014.<sup>106</sup> But as discussed, *infra* Section III(C)(3), in April 2014, the Supreme Court's *Octane Fitness* and *Highmark* decisions granted district courts increased discretion to determine whether a case is "exceptional" under Section 285 and warrants an award of attorneys' fees to the prevailing party.<sup>107</sup> While a step in the same direction as proposed by the Innovation Act, the Court's decisions did not implement a loser-pays system, where fee shifting is the default rather than the exception.

### *Heightened Pleading Standards*

The Innovation Act also proposed heightened pleading requirements compared to those required by FRCP Form 18. Currently, the plaintiff only needs to identify the patent number; provide a brief description of the invention covered by the patent; allege that the defendant has infringed and is still infringing the patent by making, selling, or using a product that embodies the patented invention; and affirm that the plaintiff has given

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102. Chien, *supra* note 103, at 370.

103. *Id.* at 373 ("[T]he real losers are those with credible but uncertain cases who cannot bear the risk of paying the opposing party's costs if, despite the strength of the case, they nonetheless lose in Court.")

104. *Id.* at 382-83.

105. *Id.* at 383.

106. Patrick Leahy, *Comment of Senator Patrick Leahy (D-Vt.), Chairman, Senate Judiciary Committee, On Patent Legislation* (May 21, 2014), available at [http://www.leahy.senate.gov/press/comment-of-senator-patrick-leahy-d-vt\\_chairman-senate-judiciary-committee-on-patent-legislation](http://www.leahy.senate.gov/press/comment-of-senator-patrick-leahy-d-vt_chairman-senate-judiciary-committee-on-patent-legislation).

107. *Octane Fitness*, 134 S. Ct. at 1755-56.

proper notice of infringement—either actual or constructive notice.<sup>108</sup> The Innovation Act would have increased the requirements for the plaintiff such that the complaint would have to identify each alleged infringed patent and claim; and identify each accused instrumentality (process, machine, manufacture, or composition of matter), including a specific product name or model number (if known). Additionally, it would have required the plaintiff to state where each element of each claim is found within the accused instrumentality and how each limitation of each claim is met by the accused instrumentality<sup>109</sup>—a step that is presently performed much later in discovery.

The proposed heightened patent pleading standards closely matched the local rules for the Eastern District of Texas, which require a party claiming patent infringement to serve on all parties a “Disclosure of Asserted Claims and Infringement Contentions” no later than 10 days before the Initial Case Management Conference pursuant to FRCP 26(f).<sup>110</sup>

Heightened pleading standards may reduce the burden on a defendant to defend a suit with little or no information about the substance of the actual lawsuit. Patent trolls have been known to cast wide nets and to rely on the pleading standards and broad discovery rules to essentially harass defendants into settling. Thus, increasing the pleading standards could beneficially shift the burden back to the plaintiff to do more diligence before filing a suit, which, incidentally, could also increase the chances of an exceptional case finding where a patent troll really is acting frivolously. Notably, pleading standards have already effectively been increased for claims of indirect infringement.<sup>111</sup>

However, the desire to increase pleading standards has to be balanced by the reality that sometimes even the most well-intentioned and deserving plaintiff can only derive so much detail from publicly accessible information. For example, a patent holder may surmise that a piece of software is infringing a patent based on functional capabilities of that software, but may nonetheless be unable to prove anything without review of the source code, which could only happen through discovery in a lawsuit.

Overall, heightening the direct infringement pleading standards seems like an obvious and effective choice for reducing frivolous litigation, whether or not it is brought by a patent troll. Importantly, heightened pleading standards affect the possibility of a case ever being filed, and

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108. FED. R. CIV. P. 84 (Form 18).

109. Innovation Act, H.R. 3309, 113th Cong. (as passed by the House, Dec. 9, 2013).

110. See E.D. Tex. Civ. R. App. B (Local Civil Patent Rules), R. 3-1; see also N.D. Cal. Patent R. 3-1 (requiring a “Disclosure of Asserted Claims and Infringement Contentions” within 14 days of the Initial Case Management Conference).

111. See, e.g., *In re Bill of Lading Transmission & Processing Sys. Patent Litig.*, 681 F.3d 1323, 1337 (Fed. Cir. 2012) (discussing heightened pleading standards for contributory and induced infringement).

provide immediate grounds for attack of a frivolous-looking suit. Also, heightened pleading standards for direct infringement would bring the standards more in-line with the already heightened standards for indirect infringement. Finally, as discussed more below, the Supreme Court's recent precedent supports heightened pleading standards for patent cases.

#### *Discovery Modifications*

The Innovation Act also addresses one of the most abused procedures during litigation—discovery. Patent trolls are particularly apt to abuse the broad discovery rules because they typically have nothing that is discoverable and are therefore not bound by any desire to balance discovery. Put differently, patent trolls always want it all, and they want it right now.

To address these abuses, the Innovation Act includes a variety of provisions, including:

- (1) direct[ing] the Judicial Conference of the United States to develop discovery rules and procedures that address whether and to what extent each party to the action is: (a) entitled to receive specified categories of core documentary evidence and is to be responsible for the costs of producing such evidence within its possession or control; and (b) permitted to seek any additional document discovery if the requesting party bears the reasonable costs, including reasonable attorney's fees, of the additional discovery;
- (2) provid[ing] for discovery of electronic communications (including emails, text messages, or instant messages) only if the parties determine that it is appropriate under procedures that address whether such discovery is to occur after the parties have exchanged initial disclosures and core documentary evidence;
- (3) direct[ing] the Judicial Conference to consider a prohibition that would bar additional document discovery unless: (a) the parties mutually agree otherwise; or (b) the requesting party posts a bond, or provides security, in an amount sufficient to cover the expected costs or shows that it has the financial capacity to pay such costs;
- (4) requires the Judicial Conference to consider whether courts, in response to a motion, may: (a) determine that a request for additional document discovery is excessive, irrelevant, or abusive; (b) modify discovery rules; or (c) include computer code in the discovery of core documentary evidence.<sup>112</sup>

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112. See Innovation Act, H.R. 3309, 113th Cong. § 6 (as passed by the House, Dec. 9, 2013).

Taken together, these provisions primarily seek to formalize certain types of “core” discovery to avoid disputes, and more importantly, to shift the cost burden of discovery onto the requesting party in many circumstances. Shifting the cost burden to the requester could be a real game changer given that complex discovery in patent cases—much of which is completely useless gamesmanship—can cost millions of dollars. And while these provisions are certainly not patent-troll specific, they may seriously undermine a common tactic of patent trolls, which is to push higher “nuisance values” of settlement based on the perceived cost of discovery.

### 3. *Other Federal Bills*

The Innovation Act, discussed above, is one of the primary pieces of proposed anti-troll legislation being debated currently, and it draws many of its provisions from other bills that are being considered. It is beyond the scope of this note to examine each and every proposed “anti-troll” bill if for no other reason than a new one seems to pop up every day. But for the sake of completeness, in addition to the laws and bills already discussed herein, one might also consider the following proposed bills to get an idea of the range of direct and indirect anti-troll provisions:

**Patent Quality Improvement Act** (S. 866), which would make the Covered Business Method review program available to all industries, and make the program permanent.<sup>113</sup>

**Patent Abuse Reduction Act** (S. 1013), which contains a number of provisions to deal with patent troll litigation, including: (1) raising the pleading requirements; (2) fee shifting discovery costs for any requests beyond core documentary evidence; and (3) a two-way cost and fee-shifting provision (but no bond).<sup>114</sup>

**Patent Litigation Integrity Act** (S. 1612), which would require the patent owner to post a bond against fees, with exceptions for companies that actually practice the patent or license to a company that practices the patent (this requirement is similar to the Patent Abuse Reduction Act).<sup>115</sup>

**Patent Transparency and Improvements Act** (S. 1720), which focuses on end-user protection (similar to the Innovations Act), demand letters, and transparency of patent ownership (similar to the Innovations Act).<sup>116</sup>

**Transparency in Assertion of Patents Act** (S. 2049), which sets minimum requirements for a notice of patent infringement and authorizes the Federal Trade Commission to enforce those requirements.<sup>117</sup>

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113. See Patent Quality Improvement Act of 2013, S. 866, 113th Cong. (2013).

114. See Patent Abuse Reduction Act of 2013, S. 1013, 113th Cong. (2013).

115. See Patent Litigation Integrity Act of 2013, S. 1612, 113th Cong. (2013).

116. See Patent Transparency and Improvements Act of 2013, S. 1720, 113th Cong. (2013).

**Saving High-Tech Innovators from Egregious Legal Disputes** (SHIELD) Act (H.R. 845), which would force patent trolls to post a bond to cover a defendant's legal fees and costs.<sup>118</sup>

**End Anonymous Patents Act** (H.R. 2024), which would force patent owners, as well as other real parties in interest, to be transparent.<sup>119</sup>

**Patent Litigation and Innovation Act** (H.R. 2639), which includes pleading, joinder, discovery provisions, sanctions, and end-user protection provisions.<sup>120</sup>

**Stopping the Offensive Use of Patents Act** (STOP) (H.R. 2766), which would make the Covered Business Method review program applicable to all industries and make the program permanent.<sup>121</sup>

**Demand Letter Transparency Act** (H.R. 3540), which would create a national database of demand letters that patent trolls must submit their letters to as well as minimum content for those demand letters.<sup>122</sup>

Notably, though there are many bills pending in Congress, most of them share a core set of ideas, including: (1) transparency; (2) pleading requirements; (3) discovery modifications; and (4) expanded patent review provisions.

#### 4. State Legislative Activism

Despite patent law being federal law, states have recently jumped on the anti-troll bandwagon. Specifically, states have recently proposed legislation designed to combat the use of deceptive "demand letters," which patent trolls use to target small businesses and non-profit organizations (among others). Typically these demand letters make vague claims regarding fairly common end-user technology, and the demand letters threaten patent infringement litigation unless the recipient agrees to take a license.

Vermont was the first to respond legislatively by amending its consumer protection laws in 2013, making it a state crime to "make a *bad faith* assertion of patent infringement."<sup>123</sup> Vermont's new law<sup>124</sup> "established an open-ended subjective test to determine bad faith assertion, including eight factors tending to demonstrate bad faith and six factors indicating absence of bad faith."<sup>125</sup> The law also establishes a requirement for the patentee to post a bond of up to \$250,000 to continue litigation where the court has established a "reasonable

117. See Transparency in Assertion of Patents Act, S. 2049, 113th Cong. (2014).

118. See Saving High-Tech Innovators From Egregious Legal Disputes Act of 2013, H.R. 845, 113th Cong. (2013).

119. See End Anonymous Patents Act, H.R. 2024, 113th Cong. (2013).

120. See Patent Litigation and Innovation Act of 2013, H.R. 2639, 113th Cong. (2013).

121. See STOP Act, H.R. 2766, 113th Cong. (2013).

122. See Demand Letter Transparency Act of 2013, H.R. 3540, 113th Cong. (2013).

123. VT. STAT. ANN. tit. 9, § 4197(a) (West 2014) (emphasis added).

124. VT. STAT. ANN. tit. 9, §§ 4195-99 (West 2014).

125. Michael Sherby, *Vermont's Move to Target Patent Trolls*, BAKER BOTTS (Jul. 2013), [http://www.bakerbotts.com/file\\_upload/IPReport201307-VermontsMovetoTargetPatentTrolls.htm](http://www.bakerbotts.com/file_upload/IPReport201307-VermontsMovetoTargetPatentTrolls.htm); see also VT. STAT. ANN. tit. 9, § 4197 (West 2014).

likelihood” that the patentee “has made a bad faith assertion.”<sup>126</sup> Oregon enacted a similar law to Vermont in 2014, including a multifactor balancing test to determine bad faith assertion.<sup>127</sup> Additionally, Kentucky, Maine, Nebraska, New Jersey, Pennsylvania, and South Carolina have also introduced bad faith patent assertion bills.<sup>128</sup>

A key question regarding the states treading into patent (federal) law territory is whether the federal patent laws will preempt the state laws under the Supremacy Clause of the U.S. Constitution.<sup>129</sup> Federal precedent appears to bar liability for a patentee communicating its rights to an alleged infringer because “[p]atents would be of little value if infringers of them could not be notified of the consequences of infringement or proceeded against in the courts. Such action considered by itself cannot be said to be illegal.”<sup>130</sup> Additionally, the Federal Circuit has stated, “[s]tate tort claims against a patent holder . . . based on enforcing a patent in the market place, are preempted by federal patent laws, unless the claimant can show that the patent holder acted in *bad faith* in the publication or enforcement of its patent.”<sup>131</sup> Vermont and the states that have followed its lead recognize the possibility of federal preemption and have crafted their bills to take advantage of the “bad faith” exception articulated by the Federal Circuit.<sup>132</sup> Furthermore, attorneys general from forty-two states sent a letter to the Senate asking for an explicit provision supporting states’ rights to enforce state bad faith patent assertion laws.<sup>133</sup>

The Supreme Court addressed the issue of federal preemption of state patent-related laws in the seminal *Bonito Boats v. Thunder Craft Boats* case.<sup>134</sup> In *Bonito Boats*, the Court considered a Florida statute that prohibited the use of

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126. VT. STAT. ANN. tit. 9, § 4198 (West 2014).

127. See S. 1540, 77th Leg. Assemb., Reg. Sess. (Or. 2014) (enacted).

128. See S. 116, 2014 Gen. Assemb., Reg. Sess. (Ky. 2014); S. 654, 126th Leg., Reg. Sess. (Me. 2013); Leg. 677, 103d Leg. Reg. Sess. (Neb. 2014); Assemb. 2462, 216th Leg., Reg. Sess. (N.J. 2014); S. 1222, 2014 Gen. Assemb., Reg. Sess. (Pa. 2014); H. 4629, 120th Gen. Assemb., Reg. Sess. (S.C. 2014).

129. U.S. CONST. art. VI, cl. 2 (“The Constitution, and the laws of the United States . . . shall be the supreme law of the land . . .”).

130. *Mikohn Gaming Corp. v. Acres Gaming, Inc.*, 165 F.3d 891, 897 (Fed. Cir. 1998) (quoting *Virtue v. Creamery Package Mfg.*, 227 U.S. 8, 37-38 (1913)); see also Sherby, *supra* note 125.

131. *800 Adept, Inc. v. Murex Sec., Ltd.*, 539 F.3d 1354, 1369 (Fed. Cir. 2008) (emphasis added).

132. See VT. STAT. ANN. tit. 9, § 4195(a)(3) (West 2014) (“The General Assembly also recognizes that Vermont is preempted from passing any law that conflicts with federal patent law.”).

133. Daniel Wilson, *AGs Urge Federal Support for State Patent Troll Battles*, LAW360 (Feb. 25, 2014, 7:03 PM), <http://www.law360.com/articles/513117/ags-urge-federal-support-for-state-patent-troll-battles>.

134. See *Bonito Boats, Inc. v. Thunder Craft Boats, Inc.*, 489 U.S. 141, 143 (1989).

a direct molding process used to duplicate unpatented boat hulls.<sup>135</sup> The law would have prevented competitors from reverse engineering an unpatented commercially available product using a specific process, thereby granting the original manufacturer a partial monopoly outside the patent system.<sup>136</sup>

To decide the case, the Court performed a conflict preemption analysis.<sup>137</sup> Conflict preemption applies “where compliance with both state and federal regulations is either a physical impossibility, or . . . stands as an obstacle to the accomplishment and execution of the full purpose and objectives of Congress.”<sup>138</sup> The Court found that the Florida law, by offering “patent-like protection,” prevented the “ultimate goal of public disclosure and use which is the centerpiece of federal patent policy.”<sup>139</sup> Perhaps more importantly, the Court found the federal government had preempted the entire field of patent law.<sup>140</sup> The Court stated, “[t]he patent statute’s careful balance between public right and private monopoly to promote certain creative activity is a scheme of federal regulation . . . so pervasive as to make reasonable the inference that Congress left no room for the States to supplement it.”<sup>141</sup> The Court held that federal law preempted the statute because it offered “patent-like protection” for unpatented ideas.<sup>142</sup>

While the statute considered in *Bonito Boats* is certainly different from the statutes enacted by Vermont and Oregon, *Bonito Boats* is still instructive for how the Supreme Court is likely to analyze preemption in the context of state bad faith patent assertion laws. In view of *Bonito Boats*, it seems unlikely that the states will be given any “room” to supplement the Federal patent laws, even in the context of simple patent infringement demand letters. Moreover, state-by-state enforcement of different laws regarding demand letters could create extreme uncertainty for patent owners who wish to assert their patent rights against infringers. Even if every state adopted a similar subjective multifactor “bad faith” test, there would be significant variation in its application from state to state. Such “[d]isuniformity in patent law” and “disparate circuit court treatment of patents” are disfavored and routinely cited as reasons for creation of the Federal Circuit.<sup>143</sup>

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135. *Bonito Boats*, 489 U.S. at 167.

136. *Id.* at 160.

137. *Id.* at 156-57.

138. *Pharm. Research & Mfrs. of America v. Dist. of Columbia*, 406 F. Supp. 2d 56, 65 (D.D.C. 2005) (internal quotations omitted).

139. *Bonito Boats*, 489 U.S. at 156-57.

140. *Id.* at 167.

141. *Id.* (quoting *Rice v. Santa Fe Elevator Corp.*, 331 U.S. 218, 230 (1947)) (emphasis added and internal quotations omitted).

142. *Bonito Boats*, 489 U.S. at 168.

143. Nard, *supra* note 27, at 25.

Accordingly, the various state efforts to supplement the patent laws with state-specific provisions seem unlikely to survive a preemption analysis. And as such, they are unlikely to impact patent trolls in any meaningful way.

### C. Judicial Activism

#### 1. Patentable Subject Matter

Another possible avenue of limiting patent trolling is to limit their favorite patentable subject matter—business methods and other computer-implemented processes.

Under Section 101 “any new and useful process, machine, manufacture, or composition of matter, or any new and useful improvement thereof,” is patent eligible.<sup>144</sup> However, the Supreme Court has identified “three specific exceptions to § 101’s broad patent-eligibility principles: laws of nature, physical phenomena, and *abstract ideas*.”<sup>145</sup>

Seminal cases in this area include: (1) *Gottschalk v. Benson*,<sup>146</sup> where the Supreme Court held that “the discovery of a novel and useful mathematical formula may not be patented,”<sup>147</sup> (2) *Parker v. Flook*,<sup>148</sup> where the Supreme Court similarly stated that “if a claim is directed essentially to a method of calculating, using a mathematical formula, even if the solution is for a specific purpose, the claimed method” is not patentable,<sup>149</sup> and (3) *Diamond v. Diehr*,<sup>150</sup> where the Supreme Court reaffirmed that a mathematical formula in isolation is not patentable,<sup>151</sup> but offered that “when a claim containing a mathematical formula implements or applies that formula in a structure or process which, when considered as a whole, is performing a function which the patent laws were designed to protect (e.g., transforming or reducing an article to a different state or thing), then the claims satisfies the requirements of § 101.”<sup>152</sup>

Based on these decisions, the Federal Circuit developed the “machine-or-transformation test” for subject matter eligibility under Section 101.<sup>153</sup> Under this test, a claim is eligible subject matter if it is “tied to a particular machine” or if it “transforms an article.”<sup>154</sup> Additionally, the claimed machine or transformation “must impose meaningful limits on the claim’s scope” and “the involvement of the machine or transformation in the claimed process must not

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144. 35 U.S.C.A. § 101 (West 2014).

145. *Id.* (internal quotations omitted).

146. *Gottschalk v. Benson*, 409 U.S. 63, 65 (1972).

147. *Parker v. Flook*, 437 U.S. 584, 585 (1978) (citing *Gottschalk*, 409 U.S. 63).

148. *Flook*, 437 U.S. at 585.

149. *Id.* at 595.

150. *Diamond v. Diehr*, 450 U.S. 175, 192-93 (1981).

151. *Id.* at 188.

152. *Id.* at 192.

153. *See In re Bilski*, 545 F.3d 943, 959 (2008).

154. *In re Bilski*, 545 F.3d at 961.

merely be insignificant extra-solution activity.”<sup>155</sup> However, in *Bilski v Kappos*,<sup>156</sup> the Supreme Court held that the “machine-or-transformation test is not the sole test for deciding whether an invention is a patent-eligible ‘process,’” rather it is a “useful and important clue” or “investigative tool.”<sup>157</sup> Additionally, the Court held that business method patents are not categorically excluded subject matter.<sup>158</sup>

After *Bilski*, the Federal Circuit (sitting en banc) further confused the issue in *CLS Bank International v. Alice Corporation*.<sup>159</sup> The Supreme Court granted certiorari to answer the question of “[w]hether claims to computer-implemented inventions, including claims to systems and machines, processes, and items of manufacture are directed to patent-eligible subject matter within the meaning of 35 U.S.C. § 101 as interpreted by this Court?”<sup>160</sup>

In *Alice Corporation v. CLS Bank International*, the Supreme Court affirmed the two-step framework it set forth in *Mayo Collaborative Services v. Prometheus Laboratories, Inc.*, 132 S.Ct. 1289 (2012) “for distinguishing patents that claim laws of nature, natural phenomena, and abstract ideas from those that claim patent-eligible applications of those concepts.”<sup>161</sup> The first step is to “determine whether the claims at issue are directed to one of those patent-ineligible concepts.”<sup>162</sup> And the second step is to “consider the elements of each claim” to determine whether it contains an “inventive concept” sufficient to “transform the nature of the claim into a patent-eligible application.”<sup>163</sup>

In this case, the Court considered claims to a “computer-implemented scheme for mitigating settlement risk by using a third-party intermediary.”<sup>164</sup> Applying the *Mayo* framework, the Court found the “claims at issue [were] directed to the abstract idea of intermediated settlement,” and “fail[ed] to transform that abstract idea into a patent-eligible invention” by “merely require[ing] generic computer implementation.”<sup>165</sup> The Court explained, “the relevant question [was] whether the claims here [did] more than simply instruct the practitioner to implement the abstract idea of intermediated settlement on a generic computer.”<sup>166</sup>

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155. *Id.* at 961-62.

156. *Bilski v. Kappos*, 130 S. Ct. 3218, 3223 (2010).

157. *Id.* at 3227.

158. *Id.* at 3228; *Cf. Mayo Collaborative Servs. v. Prometheus Labs. Inc.*, 132 S. Ct. 1289 (2012); *Assoc. for Molecular Pathology v. Myriad Genetics, Inc.*, 133 S. Ct. 2107 (2013) (The Supreme Court addressed patent-eligible subject matter again in *Mayo* (laws of nature) and *Myriad* (natural phenomenon) but neither of these decisions provided clarification on patentability of software or business method patents).

159. *CLS Bank Int'l v. Alice Corp. PTY. LTD.*, 717 F.3d 1269, 1274 (Fed. Cir. 2013) (en banc).

160. *Question Presented: 13-298 Alice Corp. PTY. LTD. v. CLS Bank Int'l*, SUPREME COURT OF THE UNITED STATES, <http://www.supremecourt.gov/qp/13-00298qp.pdf> (last visited Apr. 9, 2014).

161. *Alice Corp. Pty. v. CLS Bank Int'l*, 134 S. Ct. 2347, 2355 (2014).

162. *Id.*

163. *Id.*

164. *Id.* at 2351-52.

165. *Id.* at 2357.

166. *Alice Corp. Pty.*, 134 S.Ct. at 2359.

On the surface, the Court merely affirmed *Mayo*. But as one informed commentator stated: “Based on this decision it is hard to see how any software patent claims written in method form can survive challenge.”<sup>167</sup> In fact, *Alice* has left a huge wake of turmoil regarding patent-eligible subject matter, with the courts invalidating software patents at an “alarming rate.”<sup>168</sup> The Federal Circuit appears divided on its application of the *Mayo* Framework, with decisions highly dependent on the mix of panel members. For example, the Circuit’s decisions in *Ultramercial, Inc. v. Hulu, LLC*, 772 F.3d 709 (Fed. Cir. 2014) and *DDR Holdings, LLC v. Hotels.com, L.P.*, 773 F.3d 1245 (Fed. Cir. 2014) are difficult to reconcile.<sup>169</sup>

In *Ultramercial*, the court considered the patent-eligibility of claims directed to a method for “distributing copyrighted media products over the internet where the consumer receives a copyrighted media product at no cost in exchange for viewing an advertisement, and the advertiser pays for the copyrighted content.”<sup>170</sup> Applying step one, the court found the claims at issue were directed to the abstract idea that “one can use an advertisement as an exchange or currency.”<sup>171</sup> The court also found that the claims failed step two and were not patent-eligible, because they “simply instruct[ed] the practitioner to implement the abstract idea with routine, conventional activity.”<sup>172</sup> The court emphasized that the claims were “not tied to any particular novel machine or apparatus, only a general purpose computer.”<sup>173</sup>

On the heels of *Ultramercial*, the court in *DDR* considered the patent-eligibility of claims directed to “systems and methods of generating a composite web page that combines certain visual elements of a host website with content of a third-party merchant.”<sup>174</sup> The court punted on step one, stating that under any characterization of the abstract idea, the claims at issue satisfied step two and were thus patent-eligible. Specifically, “the claims recite an invention that is not merely the routine or conventional use of the Internet,”<sup>175</sup> instead, “the claimed solution is necessarily rooted in computer technology in order to overcome a problem specifically arising in the realm of computer networks.”<sup>176</sup> The *DDR* court distinguished the claims in

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167. Gene Quinn, *A Software Patent Setback: Alice v. CLS Bank*, IPWATCHDOG (Jan. 9, 2015), <http://www.ipwatchdog.com/2015/01/09/a-software-patent-setback-alice-v-cls-bank/id=53460/>.

168. Gene Quinn, *Federal Circuit Finds Software Patent Claim Patent Eligible*, IPWATCHDOG (Dec. 5, 2014), <http://www.ipwatchdog.com/2014/12/05/federal-circuit-finds-software-patent-claim-patent-eligible/id=52510/>.

169. *Ultramercial* was decided by Judges Lourie, Mayer, and O’Malley. *DDR* was decided by Judges Wallach, Mayer, and Chen.

170. *Ultramercial*, 772 F.3d at 712.

171. *Id.* at 714.

172. *Id.* at 715.

173. *Id.*

174. *DDR*, 773 F.3d at 1248.

175. *Id.* at 1259.

176. *Id.* at 1257.

*Ultramercial* as merely applying a known business process—use of an advertisement as an exchange or currency—to the particular technological environment of the Internet.<sup>177</sup>

Thus, the metes and bounds of Section 101, particularly as they relate to business methods and computer-implemented methods, has always been and remains intractably murky. And yet, these are exactly the types of patentable subject matter that have been applied for in huge numbers in the recent past, and are favorites of patent trolls to boot.

More importantly, even if altering the current understanding of patentable subject matter under Section 101 could completely alleviate patent trolling, it is still unadvisable. As demonstrated by *Alice*, even a small shift in the interpretation of eligible subject matter under Section 101 stands to dramatically affect a huge number of existing patents and patent owners—both those patent owners who are trolling, and those who are not by rendering thousands of patents invalid *after the fact*. That is, after the USPTO had examined those patents under a different understanding of what is patentable subject matter.

Practitioners and patent owners alike are united in the hope that either the Supreme Court will further refine *Alice* in order to protect subject matter that has always *seemed* patentable under Section 101, or Congress will step in and further refine the actual statute. Congress's decision not to amend Section 101 with the America Invents Act, however, suggests that the Supreme Court may be the only realistic option.

## 2. Judge Created Early Case Dispositive Procedures

It's not only the Supreme Court and Federal Circuit that have considered changes to patent law to address patent trolling. Some district courts have implemented rules designed to short-circuit a patent case where a case-dispositive issue may be identified early in the case. For example, the Northern District of California has implemented a rule that requires parties to identify the *most significant* terms for claim construction.<sup>178</sup> Specifically, the rule states “[t]he parties shall also jointly identify the *10 terms likely to be most significant to resolving the parties' dispute*, including those terms for which construction may be *case or claim dispositive*.”<sup>179</sup> Such rules are being developed in response to the ever increasing length, complexity, and cost of patent cases. And while these rules are certainly not patent-troll specific, they recognize the value of pre-empting cases that lack merit—the types of cases that patent trolls are consistently accused of bringing.

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177. *Id.* at 1259.

178. See Douglas A. Cawley, *District Court Patent Case Management Post-AIA*, 14 SEDONA CONF. J. 77, 84 (2012).

179. N.D. Cal. R. 4-1(b) (emphasis added).

Likewise, in response to “nuisance value” or “cost-of-defense” litigation tactics in cases involving a large number of defendants, the Eastern District of Texas has employed “an early and limited *Markman* and summary judgment hearing to eliminate claims against defendants who do not belong in the litigation.”<sup>180</sup> In such cases, the court has ordered defendants to “submit three potentially case-dispositive claim terms for an early *Markman* hearing, and set a summary judgment hearing regarding those terms.”<sup>181</sup> The court has also stayed most if not all discovery until after these claim construction rulings.<sup>182</sup> In doing so, “the Eastern District of Texas has provided defendants a new and potentially very effective mechanism to quickly and efficiently dispose of questionable patent infringement lawsuits before incurring large discovery cost.”<sup>183</sup>

More recently, Federal Circuit Judge Mayer argued (in a concurrence) that subject matter challenges under Section 101—which are suddenly relevant again post-*Alice*—should be considered at the outset of a case (even before claim construction) in order to conserve scarce judicial resources.<sup>184</sup> In particular, Judge Mayer opined that “failure to recite statutory subject matter is the sort of ‘basic deficiency,’ that can, and should, ‘be exposed at the point of minimum expenditure of time and money by the parties and the court,’” and that resolving subject matter eligibility at the outset provides a “bulwark against vexatious infringement suits.”<sup>185</sup> Judge Mayer further decried that “[t]he scourge of meritless infringement claims has continued unabated for decades due, in no small measure, to the ease of asserting such claims and the enormous sums required to defend against them.”<sup>186</sup>

### 3. *New Exceptional Case Standard*

Section 285 provides, “The court in exceptional cases may award reasonable attorney fees to the prevailing party.”<sup>187</sup> Beginning with *Brooks Furniture Mfg., Inc. v. Dutailier Int’l, Inc.*, 393 F.3d 1378 (Fed. Cir. 2005), the Federal Circuit established a two-step inquiry to determine whether to award attorneys’ fees under Section 285.<sup>188</sup> First, a district court had to “determine whether the prevailing party ha[d] proved by clear and convincing evidence

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180. Fred Berretta & Nick Transier, *New Eastern District of Texas Procedures Aim to Curb “Nuisance Value” Lawsuits*, SIDEBAR (Summer 2011) at 14, available at <http://knobbe.com/pdf/2011-August-New-Eastern-District-of-Texas-Procedures-Aim-to-Curb-Nuisance-Value-Lawsuits.pdf>.

181. *Id.* at 14-15.

182. *Id.* at 15.

183. *Id.*

184. *Ultramercial*, 772 F.3d at 718 (J. Mayer concurring).

185. *Id.* at 718-19 (quoting *Bell Atlantic Corp. v. Twombly*, 550 U.S. 544, 558 (2007)).

186. *Id.*

187. 35 U.S.C.A. § 285 (West 2015).

188. *Eon-Net LP v. Flagstar Bancorp*, 653 F.3d 1314, 1323 (Fed. Cir. 2011).

that the case [was] exceptional.”<sup>189</sup> Second, if the court found the case to be exceptional, it then had to decide whether attorneys’ fees were warranted.<sup>190</sup> The Federal Circuit held that “[a] case may be deemed exceptional” under Section 285 only “when there has been some material inappropriate conduct,” or when it is both “brought in subjective bad faith” and “objectively baseless.”<sup>191</sup> Further, the Federal Circuit reviewed the objective prong *de novo*—extending no deference to the trial courts—and the subjective prong for clear error.<sup>192</sup> Some argued that this framework “so severely limit[ed] district court discretion to award fees” that such awards were “essentially non-existent.”<sup>193</sup>

In two recent cases, the Supreme Court turned the exceptional case standard on its head: *Octane Fitness, LLC v. ICON Health & Fitness, Inc.*, 134 S. Ct. 1749 (2014) and *Highmark Inc. v. Allcare Health Mgmt. Sys., Inc.*, 134 S. Ct. 1744 (2014). Calling the Federal Circuit’s exceptional case framework “unduly rigid” and an “encumb[rance] [on] the statutory grant of discretion to district courts,” the Supreme Court overruled *Brooks Furniture*.<sup>194</sup> In its place, the Court in *Octane Fitness* held that, “an exceptional case is simply one that stands out from others with respect to the substantive strength of a party’s litigating position . . . or the unreasonable manner in which the case was litigated.”<sup>195</sup> And whether a case is exceptional is a matter of “discretion” for the district courts.<sup>196</sup> The Court also rejected the requirement that litigants must prove by clear and convincing evidence that a case is exceptional.<sup>197</sup> Finally, in *Highmark*, the Court held that “an appellate court should apply an abuse-of-discretion standard in reviewing all aspects of a district court’s § 285 determination.”<sup>198</sup>

*Octane Fitness* and *Highmark* appear to have had an immediate impact on the prevalence of fee shifting. As explained in a recent article, the new standard under *Octane Fitness* could provide a much more substantial shield to defendants:

While the strength of a plaintiff’s litigation position has been the dominant factor in recent decisions awarding fees, the district

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189. *Id.*

190. *Id.*; see *Brooks Furniture Mfg., Inc. v. Dutailier Int’l, Inc.*, 393 F.3d 1378, 1382 (Fed. Cir. 2005) (“Even for an exceptional case, the decision to award attorney fees and the amount thereof are within the district court’s sound discretion.”).

191. *Brooks Furniture*, 393 F.3d at 1381.

192. *Highmark Inc. v. Allcare Health Mgmt. Sys. Inc.*, 687 F.3d 1300, 1309-10 (Fed. Cir. 2012).

193. Brief for Petitioner at 2, *Octane Fitness v. Icon Health and Fitness*, 134 S. Ct. 1749 (2014) (No. 12-1184).

194. *Octane Fitness*, 134 S. Ct. at 1755.

195. *Id.* at 1756.

196. *Id.*

197. *Id.* at 1759.

198. *Highmark*, 134 S. Ct. at 1749.

court's ability to consider the totality of circumstances in a case provides defendants with more flexibility in establishing that a case is "exceptional."<sup>199</sup>

Practitioners have reported anecdotal evidence of an increase in the number of motions filed seeking exceptional case treatment and an increase in the overall recovery of attorneys' fees.<sup>200</sup> Consistent with this, statistical analysis of exceptional case rulings suggests that success rate of exceptional case motions has returned to and even exceeded the rate before *Brooks Furniture*.<sup>201</sup>

In addition, some have speculated that these two decisions, among other factors, have contributed to the recent and sharp decrease in new patent litigation.<sup>202</sup>

Further, district courts are now considering NPE-specific behavior within the "totality of the circumstances" under *Octane Fitness* in order to award fees under Section 285. For example, in *Lumen View Technology LLC v. Findthebest.com Inc.*, the district court specifically characterized the plaintiff as "a patent holding 'Non-Practicing Entity' that acquires patents and instigates patent infringement lawsuits," and admonished that the plaintiff's "motivation in this litigation was to extract a nuisance settlement," which "counsels . . . in favor of a finding of an exceptional case" under the *Octane Fitness* test.<sup>203</sup> NPEs beware.

#### 4. *Reconsidering the Patent Infringement Pleading Standard*

Pleading standards for patent cases have turned into something of a duel between the Supreme Court and the Federal Circuit. Specifically, in a recent case, the Federal Circuit held that, although the Supreme Court had tightened the pleading requirements in the *Iqbal*<sup>204</sup> and *Twombly*<sup>205</sup> cases, those decisions did not formally amend the Federal Rules of Civil Procedure, which contain model forms for pleading, including Form 18 for pleading patent infringement.<sup>206</sup> Therefore, for direct infringement at least,

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199. See "3 Takeaways From Post-Octane Fitness Cases", LAW 360, available at <http://www.law360.com/articles/598264/3-takeaways-from-post-octane-fitness-cases> (last accessed Mar. 26, 2015).

200. Andrew v. Devkar, *Examining the Present and Future Impact of Recent Patent Law Cases*, ASPATORE, Oct. 2014, at 1.

201. See Randy Lipsitz, Aaron Frankel and Hanna Seifert, *Recent Supreme Court Decision Takes Us Back to the Future: Attorney Fees Award Rate Increases in Patent Cases*, BLOOMBERG LAW, available at <http://www.bna.com/recent-supreme-court-n17179921906/> (last accessed Mar. 26, 2015) (noting that before *Brooks Furniture*, the success rate of exceptional case motions was around 42 percent, after *Brooks Furniture* it dropped to around 32 percent, and after *Octane Fitness*, it has risen to at least 45 percent).

202. Dennis Crouch, *A Major Drop in Patent Infringement Litigation?*, PATENTLYO (Oct. 9, 2014), <http://patentlyo.com/patent/2014/10/patent-infringement-litigation.html>.

203. No. 13-cv-3599, 2014 WL 2440867 (S.D.N.Y. May 30, 2014).

204. See generally *Ashcroft v. Iqbal*, 556 U.S. 662 (2009).

205. See generally *Bell Atlantic v. Twombly*, 550 U.S. 544 (2007).

206. *In re Bill of Lading Transmission & Processing Sys. Patent Litig.*, 681 F.3d 1323, 1333-34 (Fed. Cir. 2012).

the bare requirements of Form 18<sup>207</sup> suffice because “Federal Rule of Civil Procedure 84 states that ‘the forms in the Appendix suffice under these rules . . . .’”<sup>208</sup>

Defendants have criticized the form’s simplicity as inadequate, because in many cases they must incur the cost of discovery simply to determine exactly what the plaintiff is alleging.<sup>209</sup> Additionally, the limited nature of Form 18 appears to be in conflict with the heightened pleading standard announced by the Supreme Court in *Twombly* and *Iqbal*.<sup>210</sup> The Federal Circuit, however, held that patent cases are an exception to *Twombly* and *Iqbal* because Rule 84 “makes clear that a proper use of a form contained in the Appendix of Forms effectively immunizes a claimant from attack regarding the sufficiency of the pleading.”<sup>211</sup>

In response, the Judicial Conference of the United States—established to make policy with regard to the administration of federal courts<sup>212</sup>—has released a preliminary draft of their proposed amendments to the FRCP, which, among other things, advises abrogating all Rule 84 forms, including Form 18. In particular, the report states, “[s]ome of the forms have come to seem inadequate, particularly the Form 18 complaint for patent infringement.”<sup>213</sup> As discussed above, increasing and harmonizing the pleading standards for direct and indirect claims of patent infringement makes sense on many levels.

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207. *Id.* at 1334 (“Form 18 requires: (1) an allegation of jurisdiction; (2) a statement that the plaintiff owns the patent; (3) a statement that defendant has been infringing the patent ‘by making, selling, and using [the device] embodying the patent’; (4) a statement that the plaintiff has given the defendant notice of its infringement; and (5) a demand for an injunction and damages.”).

208. *Id.* at 1334.

209. Ryan Davis, *Judges’ Plan to Raise Pleading Bar May Curb Trolls*, LAW360 (Feb. 14, 2014, 7:52 PM), <http://www.law360.com/articles/509906/judges-plan-to-raise-patent-pleading-bar-may-curb-trolls>.

210. See *Twombly*, 550 U.S. at 555 (holding that to survive a 12(b)(6) motion to dismiss in an antitrust case, “[f]actual allegations must be enough to raise a right to relief above the speculative level, on the assumption that all the allegations in the complaint are true (even if doubtful in fact) . . . .”); *Iqbal*, 556 U.S. at 678 (extending *Twombly* to all areas of law; holding that to survive a 12(b)(6) motion to dismiss, “a complaint must contain sufficient factual matter, accepted as true, to state a claim to relief that is plausible on its face,” that “allows the court to draw the reasonable inference that the defendant is liable for the misconduct alleged.”).

211. *K-Tech Telecomm. v. Time Warner Cable, Inc.*, 714 F.3d 1277, 1283 (Fed. Cir. 2013).

212. *Judicial Conference of the United States*, UNITED STATES COURTS, <http://www.uscourts.gov/FederalCourts/JudicialConference.aspx> (last visited Mar. 26, 2014).

213. COMMITTEE ON RULES OF PRACTICE AND PROCEDURE OF THE JUDICIAL CONFERENCE OF THE UNITED STATES, Preliminary Draft of Proposed Amendments to the Federal Rules of Bankruptcy and Civil Procedure 276 (2013).

#### IV. Recommendations

In an address to the Eastern District of Texas Bar Association, Federal Circuit Chief Justice Randall Rader admonished that “litigation abuse” has contributed most to the “crisis of confidence in patent law” and that “judicial correction” is the proper remedy.<sup>214</sup> And Judge Rader cautioned against legislative actions that would attempt to solve the problem by “definition and characteristic”—that is, new laws that would specifically target trolls—because litigation abuse is largely a case-by-case factual issue.<sup>215</sup> Justice Rader opined that:

American law and ethics does not enforce or condition enforcement of basic laws and policy on the characteristics of a party. American law treats big company and small company, foreign entity and domestic entity, different genders, races, and ethnicities alike. Our law does not make distinctions based on the characteristics of parties but on their actions proven in a court of law. The definition of a “troll” will always be over-inclusive or under-inclusive to the detriment of justice. Instead of finger-pointing and name-calling, the law needs to focus on blameworthy conduct.<sup>216</sup>

Justice Rader’s suggested judicial remedies include: (1) increased use of summary judgment to “weed out the cases lacking true merit;” (2) more discretion to shift fees under Section 285; and (3) expansion of the use of model orders to create efficiency and reduce litigation costs—which in turn reduces the leverage that spawns litigation abuse.<sup>217</sup>

We agree with Justice Rader’s suggestions for the most part. In particular, we agree that attempting to devise laws that single out specific categories or definitions of entities (e.g., patent trolls, NPEs, PAEs, PME’s, etc.) are ultimately unworkable. This note led with two specific factual examples of parties (recall: a small-inventor and a university), that would be categorized as patent trolls under most prevailing definitions. And most reasonable minds would agree that those are just the type of entities that the patent system is trying to incentivize to buy into the patent system.

Furthermore, we believe that proposed solutions that target specific patent types, such as business method patents, are worrisome for a variety of reasons. First of all, changing the rules with regard to subject matter eligibility may

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214. Randall R. Rader, Chief Justice, United States Court of Appeals for the Federal Circuit, Keynote Address at the 2013 Eastern District of Texas Bar Association Conference: Patent Law and Litigation Abuse 6 (Nov. 1, 2013) *available at* [http://www.edtexbar.com/2013\\_conference/](http://www.edtexbar.com/2013_conference/).

215. *Id.* at 7.

216. *Id.* at 6-7.

217. *Id.* at 8.

seriously undermine the expectations of those who have invested in patents regarding particular subject matters under the existing subject matter laws. And there is no guarantee in any event that patent trolls will not just pick up and move on to another subject matter area if a particular area is fouled by anti-troll provisions. Ultimately, breeding uncertainty with respect to subject matter eligibility will inexorably lead to devaluation of patents generally, which may in-turn drive inventors away from the system altogether, thereby undermining a fundamental purpose of the patent system.

It is also worth considering that the current Patent Laws have been, more or less, around for over 60 years, and only recently needed updating. This time of relative consistency in the statutory framework of patent law suggests at least two things: (1) the laws are reasonably effective; and (2) the laws should be updated only when they absolutely have to be, and even then, the updates should be the result of a calm, analytical approach (*not* the scatter-shot approach that the various stakeholders seem to be utilizing at present).

Putting it all together, we endorse and recommend provisions that primarily improve the quality of patents and deter abusive litigation tactics. Such provisions are in keeping with the purposes of the patent system articulated above, i.e., (1) “seek[ing] to foster and reward invention”; (2) “promot[ing] disclosure of inventions, to stimulate further innovation and to permit the public to practice the invention once the patent expires”; and (3) “assur[ing] that ideas in the public domain remain there for the free use of the public.”<sup>218</sup> Under these guiding principles, we endorse the following ideas as discussed herein:

(Executive/Legislative) Increase the quality of patents through (1) increased training of patent examiners and (2) increased participation of the public through crowdsourcing of prior art discovery. These measures should increase the quality of patents going forward without affecting current patent owner property rights. Further, these measures are not specific to a type of patent applicant or owner, but rather seek to increase the quality of the system as a whole. Finally, these measures may be effective in an indirect way against patent trolls that seek to assert low quality patents against unsophisticated clients by preventing those patents from ever issuing.

(Legislative/Judicial) Revise discovery rules to better balance the cost burden of requesting and complying with discovery requests. Such a provision should reduce one of the primary drivers of expense during a patent case, and decrease the perceived “nuisance value” of a case, which in-turn may lower the expected value of trolling. Critically, such a provision is agnostic to patent ownership, and does not affect any fundamental rights of a patent owner. Rather, they are meant to deter litigation misconduct.

(Legislative) As described above, the judiciary has already taken steps to put the bite back into Section 285. But we still believe that amending Section 285 to provide a two-way fee-shifting scheme for patent cases is worth further consideration. An appropriate fee-shifting scheme rebalances

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218. *Aronson*, 440 U.S. at 262.

the cost/benefit analysis of all parties alike—including trolls—in deciding whether or not to pursue a questionable case. In particular, it may cause a law firm willing to take a case on contingency on a wing and a prayer to reconsider. But the two-way nature mitigates the troublesome aspects of most fee-shifting provisions and allows latitude for a patent owner to bring a case in good faith, even if they ultimately lose. In other words, the scheme recognizes that it is typically not possible to predict the outcome of a case without at least some discovery.

(Judicial/Legislative) Increase the pleading standards for patent cases (including direct infringement). This idea further enforces the idea of increasing the due diligence done before a case is filed, which should (in theory at least) decrease the number of completely frivolous cases filed. Increased pleading standards also plays well with changes to the exceptional case standard, since under an increased pleading standard scheme, a frivolous plaintiff would have even less justification for a frivolous case. This idea also affects all patent owners alike.

(Judicial) Adopt local rules that provide early case dispositive check-valves (e.g., early and limited *Markman* procedures) designed to flush out cases lacking merit. This idea could significantly reduce the average time and cost of dealing with a frivolous lawsuit, whether or not it is brought by a patent troll. It also would serve to save judicial resources for meritorious cases.

(Legislative) Enact legislation to close the loophole in Section 299 that allows courts to consolidate and coordinate multiples cases, based solely on allegations they have infringed the same patents in suit, for purposes of pre-trial activities. This idea is meant to finish what was started with the AIA. While it is acknowledged that judges need to have authority to manage their caseload, the current consolidation practices may heavily favor plaintiffs in patent lawsuits.

A common characteristic of our recommended approaches is that they have the long-term, and not the nightly news cycle, in mind. As such, we believe that these approaches are likely to engender the most benefits to the patent system with the least negative consequences.

#### IV. Conclusion

Among others, we started with a question of: what is a “patent troll?” Unfortunately, we cannot provide any clear answer because the term tends to take on the definition of whatever behavior a particular stakeholder wants to prevent. And no matter how the line is drawn, the definition of “patent troll” will appear hopelessly under or over-inclusive depending on perspective.

As a result, it became clear that rather than refining the definition of the term “patent troll,” we needed to instead consider whether the patent law framework can be improved regardless of the “existence” of patent trolls. We reached this conclusion because, generally speaking, patent trolls—however they should be defined—are just acting to their advantage within an existing

legal framework that explicitly allows such activity. Now, that is not to say that there are not patent trolls out there misusing and abusing the system. There are. But, changes to the patent system should be made with a scalpel and not a sledgehammer.

Looking at the issue objectively, the disdain for patent trolls really boils down to a lot of subjective criticism and very little reasoned analysis. But before such critics can truly add value to the discussion, they must come to terms with the fact that *any* patent owner asserting a valid patent is well within their rights to pursue potential infringers broadly and vigorously. That is the foundational *quid pro quo* upon which the patent system is built.