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Facts Show Patent Trolls Not Behind Rise In Suits

Law360, New York (January 15, 2014, 12:39 AM ET) -- The American patent system is at a crossroads. Just two and a half years removed from passage of the America Invents Act — the most dramatic overhaul of the U.S. patent system in generations — we see almost monthly legislative efforts to reform the system yet again. Driving this sentiment in large measure are well-publicized abuses of the patent system, particularly by opportunists referred to politely as "patent assertion entities" (and not-so-politely as "patent trolls").

This kind of opportunistic behavior is inevitable in capitalist economic systems when there are gaps in the law that are available to be exploited. The abuses by today's "trolls" are not much different from the manipulation that took place in equity markets over a century ago — manipulation that led to regulatory reform eventually channeling behavior in more productive directions. Current efforts (legislative, judicial and administrative) to re-channel the opportunistic behavior of patent assertion entities can be considered a modern-day analogue.

Yet to hear it from some alarmists, the building *is* on fire — and patent trolls are the arsonists. Panicked calls for immediate action have risen up repeatedly. The alarmists warn that patent litigation abuse has "reached a crisis level"[1] and that without reform — and fast — innovation will cease in Silicon Valley[2], access to cutting edge technologies will be eviscerated[3], and that the patent laws have ushered in an era of unfettered "legalized extortion.[4]"

But these urgent cries are based on anecdotal stories or even less — unbound rhetoric. While their anecdotal nature alone is not cause for dismissal — if the building is on fire, the fact that individual observers report the fire is by no means problematic — it should prompt a few additional questions. The patent system is far too vital to the U.S. economy to be governed by extraordinary anecdotes and rhetorical flourishes. Innovation industries accounted for 27.7 percent of all jobs in the U.S. economy and 24.8 percent of U.S. GDP according to a 2010 study. Corrections to the system may be in order, but it is crucial that they are informed by actual data where data are available. And conditions driving these changes must be verifiable by sustained investigation of factual circumstances, not by mere hyperbole.

Fortunately, two groups have taken a data-driven approach to investigating the impact of patent assertion entities. A recent study by Christopher Cotropia, Jay Kesan and David Schwartz[5] bolsters an earlier study by the Government Accountability Office released in August[6], which together paint a clearer picture of the role patent assertion entities play in patent litigation. To the disappointment of IP alarmists, these fact-based studies conclude that patent assertion entities are not responsible for the recent uptick in patent litigation. The building is not on fire. And complaints over the sheer number of patent lawsuits cannot simply be chalked up to "too many trolls."

The Cotropia/Kesan/Schwartz study examines patent litigation and — in a key departure from the rhetoric — actually releases publicly its underlying data and reveals its classification of patent holders at the center of the studied cases. This classification scheme divides patentees into one of eight categories.[7] And the granular subdivision marks a major improvement over the binary "patent assertion entity" versus "non-patent-assertion entity" approach — a basic flaw in the data relied on by the alarmists. Problematically, previous studies failed to disclose underlying data showing what parties were considered patent assertion entities. These studies produced misleading statistics (e.g., that patent trolls accounted for 62 percent of patent lawsuits in 2012, up from only 29 percent in 2010, at a cost of tens of billions of dollars to the U.S. economy). But without a transparent and appropriately scoped definition of "patent troll," such statistics are unhelpful at best, and more likely hurtful by representing as "data-driven" a picture that is actually badly distorted. Broad definitions will inevitably result in higher numbers, making these studies useful for rhetorical flourish but dangerously unreliable as policymaking guideposts.

To be sure, the number of patent lawsuits is up — roughly doubling from 2010 to 2012. But the Cotropia/Kesan/Schwartz study (analyzing 2,521 utility patent infringement cases in 2010 and 5,195 in 2012) reveals that nearly all of this increase results from changes to the joinder rules effected by the AIA.[8] Looking at the number of patentees filing suit (as opposed to the number of lawsuits) supports this conclusion: In 2010, the study observed 1,610 unique patentees filing suit compared with 1,696 in 2012. And the total number of parties excluding the patentee marginally decreased from 11,671 in 2010 to 11,604 in 2012. The essentially stable number of patentees and defendants dispels any notion that we are facing a crisis. Mechanical changes brought on by the AIA's reworking of joinder rules have prompted more lawsuits, but this is less relevant to the patent assertion entity debate than the number of actual litigants. Critically, the distribution among the various categories of patentees is nearly identical in both years — so even were the increase in lawsuits cause for concern, it is simply incorrect to target patent assertion entities as responsible for the increase.

The Cotropia/Kesan/Schwartz study of patent infringement data since the AIA's implementation is consistent with key findings by the (GAO)in its assessment of patent infringement data prior to the AIA's implementation. The GAO study found that patent assertion entities brought about a fifth of all lawsuits from 2007-2011; companies that actually make products brought the majority of lawsuits. And the GAO report found no statistically relevant change in this percentage split during the period of the study.

Entities that exist solely to extract settlements by threatening spurious patent infringement claims place an unwarranted burden on our innovation ecosystem. But we must be careful that we lock our sights onto the appropriate target: bad faith assertions — as opposed to loosely defined categories of patent holders. Reform proposals professing to "take aim at patent trolls" miss the mark. The problem must be framed in terms of actions and behaviors, enabling us to identify behaviors that fall outside appropriate bounds and then prohibit or regulate those behaviors.

Critically, proposals for new regulations must be based on data and not rhetoric. Invocation of a crisis mentality risks overreaction, with its concomitant potential of creating a "fix" that is worse than the problem. When it comes to retooling the greatest innovation engine the world has ever known, prudence is in order. There will always be alarmists whose prerogative is to fan the flames of controversy and incite a stampede. But the prudent path — the best path — toward striking the optimal innovation balance exalts fact over fanfare.

—By David J. Kappos, Cravath Swaine & Moore LLP

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[1] http://1776dc.com/2013/12/03/op-ed-patent-trolls-have-turned-into-patent-monsters/

[2] http://www.forbes.com/sites/realspin/2013/11/18/absent-patent-troll-reform-silicon-valleys-innovation-leadership-could-end/

[3] http://articles.latimes.com/2013/aug/22/opinion/la-oe-duan-troll-patent-abuse-consumer-20130822

[4] http://stoppatenttrolls.info/cartoon-video-explains-patent-troll-problem/

[5] Christopher A. Cotropia, Jay P. Kesa and David L. Schwartz, Patent Assertion Entities (PAEs) Under the Microscope: An Empirical Investigation of Patent Holders as Litigants. Available at: http://ssrn.com/abstract=2346381

[6] U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-13-465, INTELLECTUAL PROPERTY: ASSESSING FACTORS THAT AFFECT PATENT INFRINGEMENT LITIGATION COULD HELP IMPROVE PATENT QUALITY (2013).

[7] (1) University/college, (2) individual/family trust, (3) large aggregator, (4) failed operating company/failed start-up, (5) patent holding company, (6) operating company, (7) IP holding company of operating company, and (8) technology development company.

[8] Further, this increase was not dramatic. For at least 75 percent of patentees analyzed, patent litigation remained nearly the same for 2010 and 2012.
