



BuchalterNemer
A Professional Law Corporation

Patent Reform: Summary of Pending Legislation and Strategies for Dealing with Patent Troll Demands

By

Mark T. Cramer

Buchalter Nemer

1000 Wilshire Boulevard, Suite 1500

Los Angeles, California 90017-2357

(213) 891-5067

mrcramer@buchalter.com

**The Hospitality Law Conference
February 12, 2014**

Mark T. Cramer

Los Angeles, California
Shareholder

P (213) 891-5067

F (213) 630-5606

mrcramer@buchalter.com



Mark Cramer is a Shareholder in the Litigation Practice Group in Los Angeles. Mark has extensive experience litigating in trial and appellate courts at the state and federal level, with an emphasis on complex commercial, intellectual property, bankruptcy, and class action litigation. He counsels and represents clients on a wide range of disputes, including breach of contract, breach of fiduciary duty, unfair competition, false advertising, fraud, defamation, misappropriation of trade secrets, and other business torts. He has successfully resolved hundreds of disputes through litigation, arbitration, mediation, and direct negotiations.

Mark is actively involved in pro bono work. He obtained a unanimous reversal in the Ninth Circuit in a case of first impression under the Hague Convention on the Civil Aspects of International Child Abduction. *In re B. Del C.S.B.*, 559 F.3d 999 (9th Cir. 2009). The ruling was widely reported by the *Los Angeles Times*, the *Orange County Register*, and the *Associated Press*. In addition, Mark served as amicus counsel to a number of crime victims and relatives of crime victims in a post-conviction DNA testing case in the United States Supreme Court. *District Attorney's Office v. Osborne*, 557 U.S. 52 (2009). The *amicus* brief was featured by Nina Totenberg, the award winning legal correspondent on National Public Radio. Mark also served as amicus counsel to The Claremont Institute Center for Constitutional Jurisprudence in a redevelopment abuse case, *Fontana Redevelopment Agency v. Torres*, 153 Cal. App. 4th 902 (2007), in which he successfully advocated for the reversal of a trial court decision validating a redevelopment agency's misuse of property tax revenues.

For the past six years, Mark has been named a "Rising Star" after a nomination and polling process conducted by Law and Politics and published by *Los Angeles Magazine* and *Southern California Super Lawyers*.

Speaking Engagements

- Adjunct Professor of Law, Pepperdine University School of Law
- "Civil Litigation and Discovery: A Cost-Benefit Analysis," presented at a joint symposium organized by the International Law Section of the State Bar of California and the Tokyo Dai-Ichi Bar Association to discuss the propriety of potential changes to Japan's Code of Civil Procedure to permit additional discovery procedures such as depositions and efforts to promote arbitration as an alternative dispute resolution tool (Tokyo, Japan; May 2010)
- Guest Lecturer, Commercial Speech and False Advertising Law, University of Southern California Annenberg School for Communication & Journalism (2010-present)

Memberships & Affiliations

- Western Center On Law & Poverty — Board of Directors (2007-present); Advisory Board President (2004-2007)
- Los Angeles County Bar Foundation Board of Directors, Vice President/Treasurer
- Los Angeles County Bar Association
- Pepperdine University School of Law Board of Visitors
- California State Bar, Committee on Federal Courts (2005-2007)

Education

Mark earned his J.D. at Pepperdine University School of Law, *magna cum laude*, where he was Note and Comment Editor of the *Pepperdine Law Review*. He received his B.A., *summa cum laude*, from Dickinson College where he was a member of Phi Beta Kappa.

Contents

SCOPE OF ARTICLE..... iii

I. Summary of Pending Legislation..... iii

 A. House Bills iii

 1. The Innovation Act (H.R. 3309)..... iv

 2. The Stopping the Offensive Use of Patents Act, aka The STOP Act (H.R. 2766)..... iv

 3. The Demand Letter Transparency Act (H.R. 3540) v

 B. Senate Bills vi

 1. The Patent Transparency and Improvements Act (S. 1720) vi

 2. The Patent Litigation Integrity Act (S. 1612).....vii

 3. The Patent Abuse Reduction Act (S. 1013)vii

 4. The Patent Quality Improvement Act (S. 866).....viii

II. Strategies For Dealing With Patent Trolls And Patent Infringement Lettersviii

SCOPE OF ARTICLE

The number of patent infringement lawsuits has increased significantly in recent years. From 2010 to 2012, the number of patent lawsuits filed each year increased from approximately 2,500 to 4,700. Over that same period, the percentage of suits brought by so-called “patent trolls” increased from less than one-third to nearly two-thirds of total patent infringement suits. Sometimes referred to less pejoratively as “Patent Assertion Entities” or “Non-Practicing Entities,” patent trolls are businesses that do not make or sell products of their own, but instead specialize in enforcing patent rights against accused infringers in an attempt to collect license fees or monetary damages. Of course, the increasing number of patent troll lawsuits is only part of the problem. Patent trolls also send a staggering number of demand letters threatening litigation if an alleged infringer does not agree to a license agreement or settlement.

The dramatic rise in patent litigation and demand letters has not gone unnoticed in Congress. At least ten new patent-related bills were introduced in 2013—and patent trolls are the primary targets. Companies in the hospitality industry have not been spared from patent trolls’ threats and actions. Indeed, hotels, restaurants, bars, coffee shops, and other hospitality companies have been targeted, particularly with alleged infringement based on products (like WiFi routers and computer software) purchased from manufacturers or third-party vendors. But some relief may be on the way. With bipartisan support in Congress, and public encouragement from the White House, patent reform in 2014 seems inevitable.

The balance of this article provides a brief summary of some of the key provisions of the patent reform legislation making its way through Congress, followed by some considerations and strategies for dealing with patent trolls. No matter what the future holds for patent reform, patent trolls will continue to look for ways to pursue license fees and otherwise monetize their patent portfolios. Given that reality, companies of all sizes need to be prepared to defend and protect themselves from patent trolls’ demands.

I. Summary of Pending Legislation

A. House Bills

Six patent reform bills were introduced in the House of Representatives in 2013. One of the bills—The Innovation Act—passed by a wide margin in December 2013. As of this writing, two other bills are still under consideration. Three of the bills are no longer under consideration because similar provisions were incorporated into the Innovation Act. Key features of the Innovation Act and the two bills still under consideration are summarized below.

1. The Innovation Act (H.R. 3309)

Introduced by Rep. Goodlatte (R-Va) on October 22, 2013.

Passed by the House on December 6, 2013 by a 325-91 bipartisan vote.

- **Heightened Pleading:** Requires patent holders to provide basic details (such as which patents or parts of patents are at issue, as well as what products allegedly infringe and how) when it files a lawsuit.
- **Fee-shifting:** Gives the court discretion to require the losing party in a patent case to pay the prevailing party's attorneys' fees and costs, which should make it more difficult for patent trolls to use the high cost of defending patent lawsuits as a means of forcing early settlements.
- **Transparency:** Requires patent holder to reveal the parties that would actually benefit from the litigation (i.e. the real party in interest). If the patent plaintiff is a shell-company, the defendant could require the real party in interest to join the litigation and force them to pay if the patent plaintiff cannot or will not pay.
- **Staying customer suits:** Requires courts to stay patent litigation against customers and other end-users (such as hotels or restaurants using an off-the-shelf router to provide Wi-Fi) when there is parallel litigation against the manufacturer.
- **Discovery reform:** With limited exceptions (most of which are unlikely to apply to patent trolls), the act stays discovery until the court has interpreted the patent, making it easier for defendants to dispose of frivolous cases early before incurring high legal fees and expenses.

2. The Stopping the Offensive Use of Patents Act, aka The STOP Act (H.R. 2766)

Introduced by Rep. Issa (R-Cal.) on July 21, 2013.

Similar to the Senate's Patent Quality Improvement Act (S. 866)

- **Maintains and Expands the Covered Business Method Program.** Amends the America Invents Act to make the covered business method (CBM) post-grant review program permanent. (It would otherwise sunset after eight years.) Expands the program to cover all industries. (Current law limits the program to financial products or services).
- **Provides Support For Under-Resourced Targets of Patent Infringement Claims.** Requires the Director of the Patent Office to work with and support intellectual property law associations throughout the United States, within established pro bono programs, to assist financially under-resourced resellers, users, implementers, distributors, or customers of an allegedly infringing product or process.

3. The Demand Letter Transparency Act (H.R. 3540)

Introduced by Rep. Polis (D-Co.) on November 19, 2013

- **National Database and Required Disclosures.** Directs the Patent Office to establish a publicly accessible and searchable national database of demand letters. Any entity that sends more than 20 demand letters in any 365-day period would be required to disclose the following, among other things:
 - the patent or patents at issue;
 - that the entity that sent the demand letter owns the patent and has the right to license it;
 - each entity asserting a claim with regard to the patent at issue;
 - all licenses for the patent (including the financial terms of each license);
 - the entity's ultimate parent company;
 - the number of recipients of the letter;
 - any cases the entity has filed related to the patent;
 - any ex parte or inter partes review of the patent.

Note: These disclosure requirements would not apply to: (1) original or joint inventors; (2) institutions of higher education; and (3) technology transfer organizations facilitating the commercialization of technology developed by institutions of higher education.

- **Minimum Content Requirements.** Demand letters must include the following information:
 - each claim of each patent allegedly infringed, including each accused instrumentality;
 - each party alleging infringement;
 - the direct infringement for each claim alleged to have been infringed indirectly;
 - the principal business of the party alleging infringement;
 - each complaint filed that asserts or asserted any of the same patents, each case filed by such entity, and any ex parte or inter partes review for each patent;
 - whether the patent is subject to any licensing term or pricing commitments;
 - each owner, co-owner, assignee, or exclusive licensee of the patent;
 - any person who has a legal right to enforce the patent;
 - any person with a direct financial interest in the outcome of the action; and
 - how the recipient can access the demand letter database.

In addition to the bills summarized above, the following three patent litigation reform bills were introduced in the House of Representatives in 2013 but are no longer under consideration in light of the passage of the Innovation Act:

- (1) Saving High-Tech Innovators From Egregious Legal Disputes (SHIELD) Act (H.R. 845);
- (2) End Anonymous Patents Act (H.R. 2024); and
- (3) Patent Litigation and Innovation Act (H.R. 2639).

Each of these bills contained proposals that are similar to one or more of the provisions incorporated in the Innovation Act.

B. Senate Bills

Four patent reform bills were introduced in the Senate in 2013. As of this writing, all of these bills are still under consideration. Key features of these bills are summarized below.

1. The Patent Transparency and Improvements Act (S. 1720)

Introduced by Sen. Leahy (D-Vt.) on November 18, 2013

- **Transparency:** Requires patent holder to disclose any and all persons that have a financial interest in the controversy or a party to the proceedings, or that have an interest that could be affected by the outcome of the proceedings. Also, when "all substantial rights in an issued patent" have been assigned, the name of the assignee and the ultimate parent entity of the assignee need to be recorded with the U.S. Patent Office within three months.
- **Staying customer suits:** Requires courts to stay patent litigation against customers and other end-users when there is parallel litigation against the manufacturer.
- **Bad-faith demand letters:** Makes it an unfair or deceptive act or practice under the FTC Act to send demand letters asserting patent infringement that (1) falsely threaten legal action if compensation is not paid or the infringement issue is not resolved; (2) lack reasonable basis in law or fact; or (3) are likely to materially mislead a reasonable recipient by not identifying the patent, the person asserting the patent right, and the basis of the alleged infringement.
- **Small business education and outreach:** Calls for the development of educational resources for small businesses to provide awareness of abusive patent litigation practices and address concerns arising from patent infringement.

- **Studies:** Calls for various studies to be carried out by the Patent Office or other organizations, including a study "to develop legislative recommendations to ensure greater transparency and accountability in patent transactions occurring on the secondary market," "to examine the economic impact that the patent secondary market has on the United States," "to examine licensing and other oversight requirements that may be placed on the patent secondary market," "to examine the requirements placed on other markets," and to examine the idea of a patent small claims court.

2. The Patent Litigation Integrity Act (S. 1612)

Introduced by Sen. Hatch (R-Utah) on October 30, 2013

- **Fee-Shifting.** Requires courts to award a prevailing party reasonable attorneys' fees and other expenses associated with defending a patent case, unless the court finds that the position or conduct of the non-prevailing party was substantially justified or that special circumstances make an award unjust.
- **Bond Requirement.** Authorizes courts, in response to a motion, to order the party alleging infringement to post a bond sufficient to ensure payment of such fees and expenses of the accused infringer. In determining whether to grant a motion for a bond, the court must consider whether:
 - the party alleging infringement has the ability to pay the other party's fees and expenses;
 - the party alleging infringement is a named inventor, original assignee, or makes or sells a product related to the patent at issue.
 - the bond will burden the party alleging infringement's ability to pursue activities unrelated to the assertion, acquisition, litigation, or licensing of any patent;
 - the party alleging infringement is an institution of higher education or a non-profit technology transfer organization;
 - a licensee, who has an exclusive right under a patent held by such an institution of higher education or non-profit organization, conducts further research or development to make the subject matter more licensable.

3. The Patent Abuse Reduction Act (S. 1013)

Introduced by Sen. Cornyn (R-Tex.) on May 22, 2013.

- **Transparency.** Requires a patent plaintiff to disclose the substance of their claim and reveal their identities when they file their lawsuit as well as the identity of any person with a direct financial interest in the outcome of the action.

- **Fee-Shifting.** Requires courts to award reasonable attorneys' fees and other expenses to the prevailing party in a patent case, unless the court finds that the non-prevailing party's position or conduct was objectively reasonable and substantially justified or that exceptional circumstances make an award unjust. If the non-prevailing party cannot pay the attorney fees, the bill would allow those fees to be paid by others with an interest in the litigation.
- **Heightened Pleading.** Requires a complaint to include "detailed specificity" as to "how the terms in each asserted claim[s] ... correspond to the functionality of the accused instrumentality."
- **Discovery Limits and Cost-Shifting.** Limits discovery until after claim construction is complete. Shifts costs and attorneys' fees associated with certain discovery (if permitted) to the party seeking the discovery.

4. The Patent Quality Improvement Act (S. 866)

Introduced by Sen. Schumer (D-NY) on May 6, 2013
Similar to The STOP Act (H.R. 2766)

- **Maintains the Covered Business Method Program.** Amends the America Invents Act to make the covered business method (CBM) post-grant review program permanent. (It would otherwise sunset after eight years.)
- **Expands the CBM Program to cover all industries.** Current law limits the program to financial products or services.

II. Strategies For Dealing With Patent Trolls And Patent Infringement Letters

With or without patent reform legislation, patent trolls will undoubtedly find ways to continue their activities. Many businesses and industries, including the hospitality industry, will continue to be targets of threatened litigation accompanied by demands for settlements and license fees. Here are some steps that companies should take when they receive a patent troll demand letter:

First, the company should consult legal counsel, preferably attorneys with experience handling patent issues (and, ideally, attorneys who have experience with patent litigation). While this advice may appear self-serving coming from an attorney, this is not a situation in which companies should attempt to engage in self-help.

Second, the company should send a document retention notice to any employees who may have documents or electronic data related to the issues raised in the demand letter. The company should work with IT personnel to suspend its ordinary document retention practices and otherwise preserve potentially relevant electronic data.

Third, the company should notify its insurance providers of the demand letter. The company should work with counsel to analyze the insurance policies and determine whether there is coverage, including coverage for the company's legal fees and costs.

Fourth, if the company licensed or purchased the allegedly-infringing product from a vendor, it should notify the vendor and seek its cooperation. The vendor may be able to help formulate arguments in response to the demand letter, particularly if the product or service involves highly-technical applications or components that are unknown or unfamiliar to the company. The vendor may also be able to help develop a technical workaround to mitigate potential exposure. The company may be entitled to indemnification from the vendor, as well.

Fifth, the company should consider contacting industry groups, trade associations, and similarly-situated businesses. These groups and businesses can be valuable sources of information about other demand letters or actual or threatened litigation. In addition, businesses that received similar demand letters may be interested in forming a joint defense group to share information and the costs associated with researching and defending a potential patent infringement claim.

In addition to these steps, the company should develop a strategy for responding to the demand letter (or making the considered decision not to respond). This strategy should be developed thoughtfully and carefully, with advice and guidance from counsel. Potential strategies include the following:

Lay Low. In most situations, it is ill-advised to ignore a demand letter altogether. That said, depending on various factors (including the company itself, the particular patent troll, the strength of the asserted patent or patents, and the proposed terms of a settlement or license) it may be in the company's best interest to remain silent. Patent trolls that send out hundreds or thousands of letters to different companies are likely to focus on companies that respond and may lose track of companies that keep a low profile.

Attack. At the opposite extreme, rather than ignoring the letter, the company could bring legal action of its own as a preemptive strike. For example, the company could file a declaratory judgment action seeking a declaration that the patent troll's patent is invalid or that the company is not infringing it. This is an attractive option when the patent at issue is particularly weak or when the defenses to infringement are particularly strong. Depending on the applicable state law, the company may also bring an action against the patent troll for unfair or deceptive business practices. The state of Vermont already passed a law targeted at curbing patent trolls' activities and other states are following its lead. One of the upsides of initiating a lawsuit is that it gives the company control over the forum. It also allows the company to be the first to frame the issues for the court. On the other hand, initiating a lawsuit guarantees that the company will be involved in litigation, which is not a forgone conclusion. Not all demand letters result in lawsuits. Indeed, as noted above, there are numerous instances of patent trolls sending demand letters and failing to follow-up.

Push Back. A middle-ground approach is to send a thoughtful responsive letter in which the company (1) acknowledges and affirms its respect for patents and other intellectual property rights; and (2) requests additional information not included in the demand letter. For example, to the extent not specified in the demand letter, the company should ask the patent troll to identify:

- the infringing product or service
- the specific patent claims the product or service supposedly infringes
- the principal business of the party alleging infringement
- each owner, co-owner, assignee, or exclusive licensee of the patent
- anyone that has a legal right to enforce the patent
- anyone that has a direct financial interest in the outcome of the dispute
- all licenses for the patent or patents at issue (and provide copies, if any)
- each complaint filed that asserts or asserted any of the same patents, each case filed by such entity, and any ex parte or inter partes review for each patent

Note that many of these requests overlap with the minimum content requirements for demand letters set forth in the proposed legislation pending in Congress. Whether or not that legislation passes, there is little downside to requesting this information.

Sending a response to the patent troll has several advantages. It provides the company and its counsel with more time to research and investigate the patent troll's demand, including analyzing the patent and conducting prior art searches. It also gives the company time to refine its strategy and coordinate with other potential defendants. When applicable, it also provides time to explore and develop workarounds of the accused product or service to mitigate potential damages. In addition, if the patent troll provides any of the information requested in the response letter, then the company would obtain free discovery that may assist with its defense or potential settlement negotiations.

Of course, the appropriate strategy will depend on the specific circumstances of any given demand letter, as well as the nature of the patent troll involved, the patents and patent claims at issue, and the accused product or service. A company facing a patent troll demand would be well-advised to consult experienced counsel and carefully tailor an approach to resolve the dispute as effectively (and cost-effectively) as possible.