900 17th Street, N.W.
Suite 1100
Washington, DC 20006
Phone: 202.783.0070
Fax: 202.783.0534
Web: www.ccianet.org
Computer & Communications Industry Association

ABSTRACT

PATENT REFORM

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- The America Invents Act of 2011 offers little relief for the patent problems of the IT and Internet sectors, which continue to suffer from large numbers of low-quality patents and unproductive strategic practices.
- Apple's aggressive attacks on Android manufacturers have upset an implicit truce over patents based cross-licensing and reciprocity.
- Major companies are shedding all or portions of their portfolios, creating more opportunities for trolls to hold up operating companies.

***Background*:** While patents are very important in pharmaceuticals because a single patent can protect hundreds of millions of dollars in investment, they are less important than other means for rewarding innovation (secrecy, lead-time, complements, complexity, etc.) in most industries. In IT, individual patents are less valuable because a product or service can contain tens of thousands of patentable functions. At the same time, because IT products and services are complex, interconnected, and standards-dependent, they are especially vulnerable to assertions of patent infringement. In short, our one-size-fits-all system is optimized for billion-dollar drugs. In the long run, this works to channel investment away from IT and into other industries where the patent system works better.

With the inauguration of the specialized Court of Appeals for the Federal Circuit in 1982, patent institutions effectively dominated policy and legal debate – and benefited from the expanding scope and scale of the patent system. Beginning with the FTC/Justice hearings of 2002, the consequences of an overextended patent system have become increasingly apparent, especially in information technology where the troll phenomenon has gained considerable attention. The Supreme Court has since reversed Federal Circuit case law in a number of high-profile cases. 2010 and 2011 witnessed a substantial jump in patents granted, reaching record numbers. In recent years, the growth in ICT patents including software, has made up for lack of growth (or decline) in other sectors.

Major patent reform legislation was introduced in Congress in 2005 and in subsequent Congresses. IT and financial services pushed hard for modest reforms, but other interests, including pharma, biotech, patent departments in mature industries, independent inventors, universities, as well as the patent bar, successfully resisted. From the IT perspective, key issues included post-grant review with a second window as an alternative to litigation, calculation of damages based on the economic contribution of the patented technology, and additional rule-making authority for the PTO.

The America Invents Act (AIA) of 2011 was enacted and signed by the President in Septermber

2011. It featured a change to a first-to-file system more in line with the rest of the world (although the 12-month grace period gives priority to inventors that publish before filing – and it remains to be seen how this will play out). The AIA also introduced a post-grant review process limited to nine months after grant. This may be useful in some industries but will be of little value in IT and Internet sectors, because of the extreme volume of patents granted, the velocity of technical change, and the very small number that ultimately prove relevant. One reform may prove tactically helpful: The AIA included a provision limiting the joinder of defendants on the basis that they infringed the same patent, which should dramatically reduce the number of cases against multiple defendants in the notorious Eastern District of Texas. Otherwise, AIA only addresses the troll problem by tasking the Government Accountability Office to conduct a study. The structural problems of overpatenting, notice failure, low quality, and the failure of the notice and disclosure functions were left unaddressed by the legislation.

Until recently, major operating companies have observed an implicit truce with respect to patents. Cross-licensing among competitors has been the rule, Apple's declaration of war on Android and its attempts to exclude Android phones from entry into the U.S. market have led to highly publicized wars. Last summer, a consortium led by Microsoft and Apple successfully bid $4.5 billion for the 6000 patents owned by bankrupt Nortel. Google then announced that it was buying Motorola Mobility (25,000 patents and patent applications) for $12.5 billion. Meanwhile, litigation continues unabated, and major companies are increasingly selling patents to trolls, whether for financial return or to raise rivals' costs.

Smart phones have erased lines between market segments and brought companies across the board into competition. By squeezing diverse technologies into a product of unprecedented complexity – and adding new location-based technology, smart phones have become uniquely vulnerable to patent hold-up, whether by rivals or trolls. While the Supreme Court's *eBay* decision abolished automatic injunctive relief in civil litigation, the Federal Circuit has ruled that it does not apply to exclusionary orders issued by the International Trade Commission. Because all smartphones are imported, the ITC has become a chokepoint for patent holders seeking maximum leverage over defendants. The growth of global value chains and the surge of patenting in China suggests that China will soon become another global chokepoint since it is where most products are assembled.

***CCIA's Position*:** Today's patent system hinders high-tech more than it helps. Real reform on damages and is necessary in order to spare U.S. technology producers from crippling litigation and wasteful over-patenting. Although CCIA successfully sought the inclusion of prior user rights, we did not view the America Invents Act as a step forward in addressing the problems of IT. CCIA has filed numerous *amicus* briefs before the Supreme Court, where more progress has been made than in Congress. CCIA has also argued against the use of the International Trade Commission to block products based on infringement of a minor patent as blatantly discriminatory against imports.

***Current Status*:** Congress is suffering from patent fatigue and is unlikely to attempt major reforms in the near future. In the near term, reform efforts are directed at the International Trade Commission (which is within the jurisdiction of trade committees rather than the judiciary committees), where legislation could require adherence to *eBay* and clearly exclude patent assertion entities from the domestic industry requirement.