



# BEWARE OF THE PATENT TROLL TAX

Henry Sneath and Robert L. Wagner Picadio Sneath Miller & Norton, P.C.

Does your company use GPS to guide its vehicles? Does your company's webpage have photographs or drop-down menus? Do your employees scan documents and then e-mail them? Congratulations. As other companies have found out, your company could be a target for a patent "troll" and face the prospect of paying millions to defend a patent infringement lawsuit. Manufacturers and high-tech companies are not the only ones facing patent infringement lawsuits. Patent owners are now going after customers and users, and just about anyone can be a target.

## PATENTS ARE SUPPOSED TO ENCOURAGE INNOVATION

Patents are supposed to reward inventors for their creativity and encourage innovation. This principle is built into the Constitution, and the Patent Act was one of the earliest pieces of legislation passed by the first Congress. In its current incarnation, a patent owner has the exclusive right to limit others from using a new and novel invention for a period of twenty years.

Those violating this exclusive right can be found liable for patent infringement,

which is a strict liability offense. It does not matter if you were unaware of the patent or thought that you did not infringe. Anyone who makes, uses, sells, offers to sell, or imports a product using a patented invention is potentially liable to pay at least a reasonable royalty for doing so.

## PAE LITIGATION THREATENS INNOVATION

While in the past, most patent infringement lawsuits involved competitors suing each other, a new form of litigation has emerged in which entities that do not make or sell products target users of products that allegedly use their inventions. They acquire their patents in a variety of ways – such as by paying individual inventors, acquiring unused patents from companies, or through litigation settlements – but generally not by inventing anything themselves. These plaintiffs are often called non-practicing entities (NPEs) or patent assertion entities (PAEs), and sometimes more colorfully, patent "trolls." Businesses targeted by PAEs have expressed frustration over these lawsuits because PAEs make little to no contribution to innovation and, instead, act as a form of

parasitic private taxation in the marketplace. One study estimated that these PAE lawsuits cost companies \$29 billion a year.

For example, one patent holder began sending licensing letters to companies, demanding that they pay between \$900-\$1,200 per employee for the privilege of being able to use their own networked document scanners with their e-mail. The patent holder wasn't selling software or hardware to do this. Instead, it contended that the companies' systems infringed its patents.

Another patent holder claimed that any website with JPG pictures on it (the kind from any digital camera) violated its patent rights and filed numerous lawsuits alleging infringement.

In another lawsuit, a patent holder sued more than 200 trucking companies for their use of a GPS-based vehicle tracking system. These companies faced the very real issues of being a defendant in a large patent infringement lawsuit over products that they purchased from other vendors.

PAEs commonly adopt a volume approach by suing many companies and seeking a relatively modest licensing fee (\$25,000-\$100,000) for a fully paid-up, per-

petual license. When a typical defense to a patent infringement lawsuit can easily cost more than \$1,000,000 and take years, it is easy to see how attractive the certainty and convenience of a license at this price can be, especially to smaller companies that do not have the resources or desire to fight such a battle. PAEs count on this low-ball offer being irresistible, even if their patent is weak or proving infringement is unlikely.

### ADDITIONAL PROBLEMS WITH PAE LAWSUITS

PAE lawsuits pose additional challenges for defendants. Unlike a typical lawsuit between competitors, which is often more symmetrical in its risks and burdens, a PAE lawsuit is often very asymmetric, with almost all of the risks and burdens falling on the defendants.

PAEs are often shell companies with few assets. As a result, they are generally immune from counterclaims, and there is little risk that their initiation of a lawsuit will put their business at risk. Their entire business is filing lawsuits and licensing patents.

In addition, PAEs face minimal discovery burdens because they often have little to no documents to review or witnesses to be deposed. In contrast, defendants often will have a significant number of documents to review and witnesses to be deposed, which impose substantial costs in terms of both time and money. Indeed, there is often very little a defendant can do to stop a PAE from imposing onerous discovery burdens, especially if a court is not attentive to the true dynamics of the situation.

The patent laws do provide that in exceptional cases a defendant can be awarded its attorneys' fees in having to defend a meritless case. Unfortunately, the burden to prove this is sufficiently high that most defendants cannot rely on this relief. And, even if the court does shift fees, many PAEs are essentially judgment proof.

### CURRENT STRATEGIES FOR DEFENDING AGAINST THESE LAWSUITS

Companies faced with PAE patent infringement lawsuits recognize that there are currently no good solutions to the problem. As a result, they typically follow four less-than-ideal approaches.

First, a defendant can settle quickly for a modest amount to avoid the substantial litigation costs, regardless of the merits of the case. The advantage of this approach is that it minimizes the risks and avoids the substantial distraction and costs of a lawsuit. Unfortunately, it also encourages PAEs to file additional lawsuits and feeds their war

chests, thereby perpetuating the system. It can also result in the defendant being targeted in the future as one that is known to settle quickly.

Second, there are mechanisms that allow third parties to request that the USPTO reexamine the patent. This can be done either in an adversarial manner (with both the PAE and third party appearing before the USPTO) or on an *ex parte* basis (with only the PAE appearing before the USPTO). The new patent law enacted last year (the America Invents Act) provides more options and makes this approach easier. There are some significant advantages to this approach, including cost savings and requiring the PAE to litigate the validity of its patent first before a tribunal that likely has more technical expertise than a judge or jury. Of course, there are also disadvantages, including losing the ability to use prior inventions cited to the USPTO during the litigation and strengthening the patent in the eyes of the judge or jury if the PAE prevails in the USPTO.

Third, customers who purchased products or systems that allegedly infringe can try to get the manufacturer to step in. This is not a "get-out-of-jail-free card," though. Unless the PAE agrees to drop the customer, it will still be a party to the lawsuit and face all of the consequences and distractions that come with that.

Finally, a defendant can adopt a litigate-at-all-costs approach in order to defeat the claim and discourage other PAEs from targeting it in the future. Most PAEs are looking for easy targets that will settle quickly. Engaging in long-term litigation that threatens the existence of the patent is the last thing a PAE wants, especially if it becomes clear to a judge or jury that the PAE is really trying to extort the defendant with either a weak patent or one that really does not cover the accused products. However, this approach is expensive and runs the risk of the judge or jury concluding that the patent is valid and infringed, thereby costing the company both the damages award and its legal fees.

### LONG-TERM SOLUTIONS

Congress and the President are looking for ways to address the perceived inequities in many lawsuits brought by PAEs. Part of the problem is definitional – trying to determine exactly which lawsuits are problematic and which are tolerable.

Currently, Congress is considering at least six bills in this area. Among the many proposed solutions are fee-shifting provisions to make losing plaintiffs pay defendants' costs and fees, mechanisms that allow

customers to bow out and be replaced by manufacturers, limiting the amount and timing of discovery, and requiring cost-shifting for additional discovery. These proposals, while interesting, are unlikely to be the final solution, as there are a number of loopholes and ambiguities that would be easy for a PAE to avoid.

The Federal Circuit, which hears all appeals involving patents, is encouraging District Court judges to more freely consider awarding attorneys fees against PAEs when they lose. While encouraging, this approach still requires that a defendant aggressively litigate a case that it could lose and that the trial court judge appreciate the exact nature of the situation. Unfortunately, even in the best-case scenario, the defendant is only reimbursed for its legal costs. All of its indirect costs in the form of aggravation and diverted time and energy from its core business remain uncompensated.

None of these approaches really address the problems posed by PAEs, however. As long as cost imbalances remain that incentivize PAEs to file multiple lawsuits and defendants to settle quickly, this PAE problem will not go away soon. Further input and increased pressure from businesses will be necessary to make a dent in the PAE problem.



*Henry Sneath is a business trial attorney with Picadio Sneath Miller & Norton, P.C. in Pittsburgh, Pa., specializing in business, intellectual property, insurance, energy sector and tort litigation matters. He is listed in*

*Pennsylvania Super Lawyer and Best Lawyers in the litigation fields of Business, Intellectual Property, Patent, Personal Injury Defense and Legal Malpractice Defense. He is the Immediate Past President of DRI-The Voice of the Defense Bar.*



*Robert L. Wagner is an associate at Picadio Sneath Miller & Norton, P.C. in Pittsburgh, Pa. He focuses his practice on patent and intellectual property matters, and his peers recently named him a "Super*

*Lawyer" in IP litigation. He has tried cases to verdict in federal court and argued before the Federal Circuit.*

