

## A PROPOSAL FOR MANDATORY PATENT REEXAMINATIONS

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### ABSTRACT

This article provides a new approach to solving the ongoing problems caused by the issuance of bad patents and their enforcement by patent trolls or non-practicing entities. This issue was recently highlighted in the Supreme Court's decision in *Microsoft Corp. v. i4i Ltd. Partnership*, 131 S. Ct. 2238 (2011). However, the Supreme Court, decided to defer the issue to the legislature and thus the problems aforementioned continue today. Many scholars have proposed various solutions to the bad patent and patent troll problems, but those solutions wrongly focus on either (i) the initial examination of patents or (ii) changing the parties' incentives or strategies in litigation. As discussed in this article, both approaches have significant drawbacks. Focusing on the initial examination of a patent misplaces valuable resources and is unlikely to limit the number of bad patents that issue. Further, changing the parties' litigation behavior is unlikely to affect patent trolls because they are only interested in extorting a license for an amount less than the price of litigation. Thus, even with such changes, it is still economically rational for a defendant to settle rather than litigate.

The alternative solution proposed in this article is to require mandatory reexamination for all patents prior to their assertion in litigation. This proposal properly allocates resources to those patents that will actually be asserted. It also provides an opportunity for the accused infringers to actively participate in consideration of a patent application which will provide more prior art to the examiners and filter bad patents. Finally, this system discourages patent trolls or non-practicing entities from asserting patents solely to extract a nominal li-

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cense because of the risk that the patent would be found invalid in reexamination. By comparison, a patent holder with a "good patent" would be undeterred by reexamination and could be bolstered by the reaffirmance of his or her patent. Thus, the proposal provides a solution that properly balances all incentives in order to reduce the bad patent and patent troll problems.

## I. INTRODUCTION

On June 9, 2011, the Supreme Court issued its opinion in *Microsoft Corp. v. i4i Ltd. Partnership* (8i4iö)<sup>1</sup> which addressed whether an invalidity defense must be proved by clear and convincing evidence.<sup>2</sup> Despite the urging of Microsoft and numerous amici, the Supreme Court did not use the *i4i* decision as an instrument to curb the effectiveness of non-practicing entities,<sup>3</sup> or "patent trolls,"<sup>4</sup> asserting "bad patents."<sup>5</sup> Instead, the Supreme Court decided to defer to Congress, as it has done for "nearly 30 years," and not address the issues of bad patent or patent trolls. This article demonstrates why the current system encourages patent trolls and why the current proposed solutions, including those proposed by Microsoft and its supporting amici are flawed. Additionally, this article provides an alternative solution; namely, requiring mandatory reexaminations for all patents before they are asserted in litigation.

As explained in more detail below, a non-practicing entity ("NPE") primarily relies on the licensing and enforcement of its patents to generate income.<sup>6</sup> The patents licensed and enforced by NPEs or patent trolls are often considered "bad patents" because of the likelihood that they are invalid and were only issued because the U.S. Patent and Trademark Office ("USPTO") is

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<sup>1</sup> 131 S. Ct. 2238 (2011).

<sup>2</sup> *Id.*

<sup>3</sup> A non-practicing entity is a business entity focused solely on acquiring under-valued patents and realizing the value of those patents through licensing and enforcement of the patent right to exclude others from (1) making, (2) using, (3) selling, (4) offering for sale, or (5) importing an invention. *See, e.g.,* Miranda Jones, *Permanent Injunction, A Remedy by Any Other Name is Patently Not the Same: How Ebay v. Mercexchange Affects the Patent Right of Non-Practicing Entities*, 14 GEO. MASON L. REV. 1035, 1035636 & n.5 (2007).

<sup>4</sup> The term "patent troll" is the common derisive name given to NPEs who aggressively assert their patents, often with the sole intent to extort a license. *See id.* at 1036. The terms "NPEs" and "patent trolls" are used interchangeably in this paper to refer to these types of entities.

<sup>5</sup> *i4i*, 131 S. Ct. at 2251652.

<sup>6</sup> *See* Ranganath Sudarshan, *Nuisance-Value Patent Suits: An Economic Model and Proposal*, 25 SANTA CLARA COMPUTER & HIGH TECH. L.J. 159, 160 (2008).

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too overwhelmed to dedicate sufficient resources to each patent application.<sup>7</sup> As explained by one scholar, patent trolls “frequently approach companies with vague allegations of patent infringement, offering a license in exchange for a nuisance payment which amounts to less than the cost of litigating a defense.”<sup>8</sup> NPEs and patent trolls clog court dockets and cause corporations to waste valuable resources litigating and licensing patents that have minimal, if any, public contribution.<sup>9</sup>

Numerous amici in the *i4i* appeal and scholars advocate solving these problems by lowering the standard of proof for establishing patent invalidity.<sup>10</sup> They argue that lowering the standard of proof will shift the dynamic against NPEs and will enable potential targets to better defend themselves or obtain cheaper licenses.<sup>11</sup> As this Article explains, however, that argument is misplaced.<sup>12</sup>

Lowering the standard of proof for patent invalidity will not solve the bad patent or patent troll problems because that solution only alters party incentives *after* litigation has commenced. A proper solution must alter party incentives *before* litigation has commenced. Once litigation has commenced, patent trolls gain leverage over companies by imposing the specter of millions of dollars in legal fees to defend what are potentially meritless claims.<sup>13</sup> This Article advocates requiring a mandatory reexamination for patents prior to their assertion in litigation and before patent trolls gain leverage over their targets.

First, this Article discusses the current problems with the patent system that enable patent trolls to successfully extort settlements based on potentially meritless claims. Next, this Article briefly summarizes and discusses the *i4i* decision and its failure to address the “bad patent” problem. Next, it discusses some of the current proposed solutions to the patent troll problem, including Microsoft’s proposal of lowering the standard of proof for invalidity. Next, it proposes the mandatory reexamination solution to the bad patent and patent troll

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<sup>7</sup> *Id.* at 162, 169.

<sup>8</sup> *Id.* at 159.

<sup>9</sup> *See id.* at 172-77.

<sup>10</sup> *i4i*, 131 S. Ct. 2251652.

<sup>11</sup> *See e.g.* Brief of Business Software Alliance as Amicus Curiae in Support of Petitioner at \*9-12, *Microsoft Corp. v. i4i Ltd. P’ship*, 131 S. Ct. 2238 (2011) (No. 10-290).

<sup>12</sup> *See infra* Part III.

<sup>13</sup> John R. Allison et al., *Patent Litigation and the Internet*, 2012 STAN. TECH. L. REV. 3, 1 n.2 (noting that the American Intellectual Property Law Association reported in 2009 that the median cost to litigate a high stakes patent case through the end of discovery only was \$3 million); Sudarshan, *supra* note 6.

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problems. Finally, this Article contends with potential objections to this proposal.

### II. THE CURRENT PROBLEM

#### A. *Bad Patents*

As numerous scholars have identified, the USPTO routinely issues “bad patents.”<sup>14</sup> Although patent examiners may have the knowledge and experience necessary to determine whether a patent is valid, especially compared to judges and juries, their expertise does not overcome the poor conditions under which they regularly examine patent applications.<sup>15</sup> In fact, USPTO examiners face a multitude of problems and obstacles that hinder their ability to discern so-called bad patents from valid patents or “good patents.”

First, the USPTO does not have sufficient resources to dedicate to each patent application.<sup>16</sup> Due to the ever-increasing number of patent applications filed each year, examiners are forced to perform a quick and potentially incomplete examination of each patent.<sup>17</sup> In 2010, a total of 509,367 patent applications were filed.<sup>18</sup> The current backlog of patent applications is over one million,<sup>19</sup> and the average wait time for a patent is approximately thirty-four months.<sup>20</sup>

As a result of this pressure, examiners spend an average of sixteen to seventeen hours, often spread over a period of three to four years, on each application.<sup>21</sup> During this time, an examiner is expected to: (1) review the application; (2) understand the application’s disclosures; (3) identify any problems with

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<sup>14</sup> Sudarshan, *supra* note 6, at 169. A bad patent is one “that would have been rejected had the examiner possessed perfect knowledge.” See Mark A. Lemley, *Rational Ignorance at the Patent Office*, 95 NW. U. L. REV. 1495, 1500 (2001).

<sup>15</sup> Doug Lichtman & Mark A. Lemley, *Rethinking Patent Law’s Presumption of Validity*, 60 STAN. L. REV. 45, 46647 (2007).

<sup>16</sup> *Id.* at 53.

<sup>17</sup> See *id.*

<sup>18</sup> U.S. PATENT AND TRADEMARK OFFICE, PERFORMANCE AND ACCOUNTABILITY REPORT FISCAL YEAR 2010 126 tbl.2 (2010), available at <http://www.uspto.gov/about/stratplan/ar/2010/USPTOFY2010PAR.pdf>.

<sup>19</sup> *Id.* at 127 tbl.3.

<sup>20</sup> Betsi Fores, *New Patent Reform Law Promises Job Creation, Red-tape Trimming, B-to-B tensions*, THE DAILY CALLER (Sep. 16, 2011, 4:05 PM), <http://dailycaller.com/2011/09/16/new-patent-reform-law-promises-job-creation-red-tape-trimming-b-to-b-tensions/>.

<sup>21</sup> Lichtman & Lemley, *supra* note 15, at 53.

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the patent on its face; (4) search for, identify and review prior art; (5) draft and issue office actions; and (6) review and respond to incoming correspondence and responses.<sup>22</sup> Sixteen to seventeen hours is simply not enough time for an examiner to effectively handle all of these tasks.<sup>23</sup>

Second, an effective review by the USPTO would be cost prohibitive.<sup>24</sup> The current abbreviated review process is already costly.<sup>25</sup> Procedures that would accurately evaluate every patent application would cost significantly more.<sup>26</sup> For example, the USPTO could hire industry experts to participate in the patent review or spend more time evaluating each patent application at great cost.<sup>27</sup> Although more extensive review may deter some patent applicants from filing, the reduction in applications would not offset the additional costs required to effectively review the remaining hundreds of thousands of patent applications.<sup>28</sup>

Third, the current review process is inherently limited because USPTO examiners do not have access to all the information necessary to determine whether a patent is valid. Examiners review patent applications ðearly in the life of a claimed technology,ö at a time when there is often limited publicly available information for an examiner to use in determining whether an invention is novel or nonobvious.<sup>29</sup> At this early stage, it is not yet apparent if the invention will be a market success or if the customers will view it as an advancement over existing alternatives.<sup>30</sup> With respect to obviousness, an examiner is unlikely to know at the time of evaluation whether other inventors have or will independently accomplish the same thing at the same time, or if competitors will copy the technology.<sup>31</sup> All of this information is objective evidence that indicates whether a patent is novel and nonobvious; it is not available at the time

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<sup>22</sup> *Id.*

<sup>23</sup> *Id.*

<sup>24</sup> Lemley, *supra* note 14, at 1509.

<sup>25</sup> *Id.* at 1499 (estimating annual patent prosecution costs over \$4 billion).

<sup>26</sup> *Id.* at 1509 (estimating that proper procedures would increase the cost of patent prosecution to \$5.85 billion annually); *see also* Lichtman & Lemley, *supra* note 15, at 53654 (calculating the cost of evaluating a year's worth of patent applications to be well over \$3 billion, not including overhead and examiner salaries).

<sup>27</sup> Lichtman & Lemley, *supra* note 15, at 53654.

<sup>28</sup> *Id.* at 54. Lichtman and Lemley also note that raising application fees to pay for the more in-depth review would not adequately defray the expense. *Id.*

<sup>29</sup> *Id.*

<sup>30</sup> *Id.* at 46, 55656.

<sup>31</sup> *Id.* at 55656.

of PTO review.<sup>32</sup> Moreover, additional prior art may become available to an examiner through the publication of already pending patent applications or through prior art submitted during the prosecution of other patent applications on related technologies.<sup>33</sup> Thus, the examination process is limited by factors other than the dedicated resources.

Fourth, the USPTO review process is also limited because it is not adversarial.<sup>34</sup> To the extent that any evidence bearing on obviousness or novelty exists, an adversary such as a competitor would be far more motivated than either the applicant or the examiner to bring such information to light.<sup>35</sup> In addition, competitors are more likely to understand if an application contains advancement over existing technologies or whether it is an obvious extension.<sup>36</sup> Nevertheless, practical considerations arguing against allowing third parties to participate in the USPTO review process include: (1) initial patent examinations are secret proceedings which encourages applicants whose applications will ultimately be rejected to apply, knowing that their unpatented work will not then be leaked to competitors; and (2) competitors have an interest in not identifying themselves as targets for potential litigation if the patent is issued.<sup>37</sup> Furthermore, opening up the current examination process would not necessarily guarantee better information, since it is likely that interested competitors may not even exist yet and, if they do, they may not be aware of patent applications in their field.<sup>38</sup>

The immense number of patent applications and the high cost of evaluating patents<sup>39</sup> combined with the fact that review does not elicit all the information relevant to patent validity<sup>40</sup> causes the USPTO to approve bad patents (i.e., patents that should have been rejected).<sup>39</sup> In some cases, these patents are outright invalid patents.<sup>40</sup> As discussed later, NPEs take advantage of these bad patents and use them to extort settlements and hold innovation hostage.<sup>41</sup>

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<sup>32</sup> *Id.*

<sup>33</sup> *Id.*

<sup>34</sup> *Id.* at 46, 54655 (explaining that the only parties involved in the initial patent application process are the applicant, the applicant's attorneys, and the examiner).

<sup>35</sup> *Id.* at 54655.

<sup>36</sup> *Id.*

<sup>37</sup> *Id.* at 55.

<sup>38</sup> *Id.*

<sup>39</sup> See *supra* text accompanying notes 14640.

<sup>40</sup> See, e.g., FED. TRADE COMM'N, TO PROMOTE INNOVATION: THE PROPER BALANCE OF COMPETITION AND PATENT LAW AND POLICY 217 (2003), <http://www.ftc.gov/os/2003/10/innovationrpt.pdf>.

<sup>41</sup> Sudarshan, *supra* note 6, at 160.

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### *B. Most Patents Lie Dormant after Issuance*

Even if increasing the USPTO's funding would reduce the number of bad patents, this would be a waste of resources because only a small percentage of all issued patents are ever litigated, licensed, or even read by people other than the applicant and his attorneys.<sup>42</sup> Indeed, only about 1.5% of all patents are ever litigated.<sup>43</sup> The number of patents licensed for royalties without litigation is higher, but still very small.<sup>44</sup> Instead, the vast majority of patents lie dormant after issuance; they are either forgotten about, turn out not to be useful, or are obtained for reasons unrelated to litigation or licensing.<sup>45</sup> Accordingly, it would be wasteful to invest substantial resources in examining patents whose validity will never be at issue.<sup>46</sup> A more efficient measure would be to take steps to ensure accurate validity determinations in the few cases where patent validity is actually challenged.<sup>47</sup>

### *C. Issued Patents Carry a Presumption of Validity*

Currently, when a patent is asserted in litigation, the patent enjoys a presumption of validity.<sup>48</sup> The U.S. Patent Act articulates the presumption of validity, providing that "[t]he burden of establishing invalidity of a patent or any claim thereof shall rest on the party asserting such invalidity."<sup>49</sup> Since its inception, the Federal Circuit has interpreted this statute, as well as extra-statutory common law rules, to require a party challenging a patent to prove invalidity by clear and convincing evidence.<sup>50</sup> That presumption was the focus of Microsoft's appeal in the *i4i* case.<sup>51</sup>

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<sup>42</sup> Lichtman & Lemley, *supra* note 15, at 54.

<sup>43</sup> Lemley, *supra* note 14, at 1507.

<sup>44</sup> *Id.* at 1507 & n.53 (estimating that 5% of patents issued are licensed or litigated).

<sup>45</sup> *Id.* at 1506 (giving examples of various types of entities that "obtain patents for reasons totally unrelated to litigation or licensing").

<sup>46</sup> *See id.*

<sup>47</sup> *See id.* at 1514 (arguing that the validity of unasserted patents does not matter because those who rely on information about these patents are sophisticated entities capable of easily assessing the probability that a patent is valid).

<sup>48</sup> 35 U.S.C. § 282 (2006).

<sup>49</sup> *Id.*

<sup>50</sup> *See, e.g.,* Dennison Mfg. Co. v. Panduit Corp., 475 U.S. 809, 810 (1986); Schumer v. Lab. Computer Sys., Inc., 308 F.3d 1304, 1315 (Fed. Cir. 2002); Ryco, Inc. v. Ag-Bag Corp., 857 F.2d 1418, 1423 (Fed. Cir. 1988); Am. Hoist & Derrick Co. v. Sowa & Sons, Inc., 725 F.2d 1350, 1360 (Fed. Cir. 1984) ("The burden is constant and never changes and is to convince

One rationale behind the presumption of validity is that the USPTO, even with its limited resources, is likely to be more effective than the courts at evaluating a patent's validity.<sup>52</sup> USPTO examiners have more experience evaluating patents than traditional fact finders and often are selected because they have backgrounds related to a patent's claimed technology.<sup>53</sup> Furthermore, even if expertise does not give examiners a significant advantage over the courts, the fact that an examiner already reviewed a patent renders a second look by a court redundant.<sup>54</sup> Another rationale behind the presumption is that it contributes to patent certainty, which encourages patentees to invest the necessary resources to bring their inventions to market by reassuring them that their patents will afford protection if they are successful.<sup>55</sup> Regardless of the rationale, the current patent system allows NPEs and patent trolls to abuse the presumption of validity.<sup>56</sup>

#### **D. Non-Practicing Entities and Patent Trolls**

NPEs and patent trolls capitalize on the profusion of bad patents and the associated presumption of validity.<sup>57</sup> Oftentimes, an NPE or a patent troll will acquire a patent and then wait for somebody to infringe that patent.<sup>58</sup> The NPE then offers the infringing party a license to continue practicing the claimed

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the court of invalidity by clear evidence.); *Connell v. Sears, Roebuck & Co.*, 722 F.2d 1542, 1549 (Fed. Cir. 1983) (‘[T]he requirement [is] that evidence establish presumption-defeating facts clearly and convincingly.’); *see also* *Buildex Inc. v. Kanson Indus., Inc.*, 849 F.2d 1461, 1463 (Fed. Cir. 1988) (explaining that clear and convincing evidence ‘produces in the mind of the trier of fact an abiding conviction that the truth of [the] factual contentions are highly probable’) (internal quotations and citations omitted); *Astra-Sjuco, A.B. v. U. S. Int’l Trade Comm’n*, 629 F.2d 682, 688 (C.C.P.A. 1980); Etan S. Chatlyne, *The Burden of Establishing Patent Invalidity: Maintaining a Heightened Evidentiary Standard Despite Increasing “Verbal Variances”*, 31 *CARDOZO L. REV.* 297 (2009).

<sup>51</sup> Brief for Petitioner at 13 *Microsoft Corp. v. i4i Ltd. P’ship*, 131 S. Ct. 2238 (2011) (No. 10-290).

<sup>52</sup> Lichtman & Lemley, *supra* note 15, at 47 (‘The theoretical justification is that patent examiners have expertise when it comes to questions of patent validity, and if patent examiners have decided that a given invention qualifies for protection, judges and juries should not second-guess the experts.’).

<sup>53</sup> *See id.*

<sup>54</sup> *See id.*

<sup>55</sup> Chatlyne, *supra* note 53, at 321 (‘The clear and convincing standard . . . provides inventors with some certainty that . . . their patents . . . will be able to withstand validity challenges.’).

<sup>56</sup> Sudarshan, *supra* note 6.

<sup>57</sup> *See id.*

<sup>58</sup> *Id.* at 159.

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technology in exchange for a fee.<sup>59</sup> Even though the allegedly infringing party may have a viable defense, it often chooses to pay the fee because the NPE strategically priced it at slightly less than the cost of litigating a defense<sup>60</sup>; when this scenario involves a bad patent, the license fee amounts to a tax on legitimate business activity.<sup>61</sup>

Bad patents can benefit NPEs because they often cover technology that is obvious or not novel, making it more likely that others will infringe the patent.<sup>62</sup> The presumption of validity also benefits NPEs because it makes it more difficult, and therefore more expensive, for an accused infringer to prove that the patent is invalid in court.<sup>63</sup> Because NPEs seek to avoid the high costs of litigation, they may even assert invalid patents when they anticipate settlement before a validity ruling.<sup>64</sup> Along with other factors, the increasing number of bad patents and cost of litigation has led to the proliferation of NPEs that use this strategy to extract royalties from parties who do not use or benefit from their patents.<sup>65</sup> Capitalizing on the cost inequities of patent litigation, NPEs account for an ever increasing portion of patent lawsuits.<sup>66</sup>

Even without abuse by NPEs, patent litigation is extraordinarily expensive. In 2003, the median cost to litigate a large patent case<sup>67</sup> was almost \$4 million.<sup>68</sup> By 2009, this amount had increased to \$5.5 million per party.<sup>69</sup> This is in part due to an extensive pretrial discovery process, in which both parties

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<sup>59</sup> *Id.*

<sup>60</sup> *Id.*

<sup>61</sup> Lichtman & Lemley, *supra* note 15, at 48.

<sup>62</sup> *Id.*

<sup>63</sup> Sudarshan, *supra* note 6, at 174675.

<sup>64</sup> *Id.* at 172673.

<sup>65</sup> *See id.* at 169670.

<sup>66</sup> *See, e.g.,* Joe Mullin, *Patent Litigation Weekly: Data Shows That Troll Problem Persists*, CORPORATE COUNSEL (Aug. 2, 2010), <http://www.law.com/jsp/cc/PubArticleFriendlyCC.jsp?id=1202464087434> (noting that, "since 2007, more than 1,500 companies per year are hit with lawsuits brought by [ ] more than 300 NPEs" and that "NPE litigation has grown from where it accounted for between 2 to 3 percent of all patent suits a decade ago to the point that it now accounts for 17 percent").

<sup>67</sup> A large patent case is defined in this context as one in which more than \$25 million is at risk. *Id.*

<sup>68</sup> *Id.*

<sup>69</sup> *See generally* AM. INTELLECTUAL PROP. LAW ASS'N, 2009 REPORT OF THE ECONOMIC SURVEY (2009).

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must search for and produce a high volume of documents, as well as highly specialized expert witnesses to testify about the claimed technology.<sup>70</sup>

When the patent holder is an NPE, however, the costs are disproportionately placed on the accused infringers.<sup>71</sup> NPEs, by definition, do not have business operations (other than litigation) that generate documents.<sup>72</sup> Additionally, NPEs regularly exacerbate the disproportionate cost differential by employing contingency fee arrangements with their attorneys, which defer legal fees, until they obtain a recovery.<sup>73</sup> NPEs also regularly sue multiple defendants in the same action, which lowers their average cost per suit.<sup>74</sup> Although the presence of multiple defendants helps minimize the NPEs' legal costs, it does not reduce the defendants' litigation costs to the same extent because most aspects of defensive litigation cannot be divided between defendants.<sup>75</sup> Finally, countersuit is generally unavailable due to the NPEs' lack of business operations.<sup>76</sup>

Moreover, NPEs are incentivized more than traditional patent holders to push for a higher cost of litigation, among other reasons, to increase the viable settlement amounts for the defendants.<sup>77</sup> NPEs use several techniques to maximize the cost of defense.<sup>78</sup> First, they can demand broad discovery that they have no intention of using.<sup>79</sup> Second, they can broaden their infringement accusations to include a defendant's entire system or multiple products sold by the defendant.<sup>80</sup> Third, the plaintiff can assert infringement of more than one patent, requiring the defendant to spend more resources mounting a defense.<sup>81</sup> Fourth, the plaintiff can file suit in an inconvenient jurisdiction, requiring the defendant to spend more money traveling and hiring local counsel or, alternatively, challenging jurisdiction and venue.<sup>82</sup>

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<sup>70</sup> Sudarshan, *supra* note 6, at 173.

<sup>71</sup> *Id.* at 166667.

<sup>72</sup> *Id.* at 167.

<sup>73</sup> *Id.* at 166.

<sup>74</sup> *Id.* at 166667.

<sup>75</sup> *Id.* at 166667.

<sup>76</sup> *Id.* at 167.

<sup>77</sup> *See id.* at 164.

<sup>78</sup> *Id.* at 164665.

<sup>79</sup> *Id.* at 164.

<sup>80</sup> *Id.* at 164665.

<sup>81</sup> *Id.*

<sup>82</sup> *Id.* at 165.

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Thus, NPEs, or patent trolls, compound the problems with bad patents by using them to extort settlements and stifle innovation.<sup>83</sup> However, as explained below, changing the presumption of validity granted to issued patents likely would not have a deterrent impact on patent trolls. Consequently, imposing a system of mandatory patent reexaminations would be a more effective way to control patent trolls.

**E. Problems with Current Reexamination Procedures**

Patent law already provides one alternative to costly litigation in the form of reexamination proceedings.<sup>84</sup> The purpose of reexamination is to provide parties with an avenue for resolving validity disputes.<sup>85</sup> There are currently two types of reexamination proceedings: *ex parte* and *inter partes*.<sup>86</sup> In an *ex parte* reexamination, any person may request that the USPTO reexamine an issued patent with respect to newly submitted patents or printed publications.<sup>87</sup> If these documents raise a substantial new question of patentability, then the USPTO examines the patent anew, this time giving the patent priority and not treating it as presumptively valid.<sup>88</sup>

The *inter partes* reexamination procedures are currently the same, except that third-party requesters may participate in the reexamination by submitting written comments to the USPTO along with the patentee's responses.<sup>89</sup> Additionally, if the USPTO finds the patent valid again, the third party may appeal this determination to the Board of Patent Appeals and then to the courts.<sup>90</sup> As will be discussed below, the procedure for *inter partes* reexamination was

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<sup>83</sup> We have been unable to locate any studies containing data describing the frequency with which NPEs settle their cases. At least one author has tried, *see, e.g.,* Sannu K. Shrestha, *Trolls or Market-Makers? An Empirical Analysis of Nonpracticing Entities*, 110 COLUM. L. REV. 114, 146647 (2010), however, this study is flawed because it fails to account for the full universe of NPEs and does not count each defendant's settlement separately in multiple defendant lawsuits. *Id.* In particular, the study only focuses on 51 NPEs that could be easily identified through LEXIS research, *id.*, when there are hundreds if not thousands of NPEs in the market, *All About NPEs: Most Pursued Companies*, PATENTFREEDOM, <https://www.patentfreedom.com/about-npes/pursued/> (last visited Apr. 14, 2012).

<sup>84</sup> *See* 35 U.S.C. §§ 302, 311 (2006).

<sup>85</sup> *See id.* §§ 305, 314.

<sup>86</sup> *Id.* §§ 302, 311.

<sup>87</sup> *Id.* § 302.

<sup>88</sup> *Id.* §§ 304-305.

<sup>89</sup> *Id.* § 314.

<sup>90</sup> 35 U.S.C. § 315(b).

recently modified by the America Invents Act with changes to take effect next year.<sup>91</sup>

At first glance, it would appear that the current reexamination procedure could help solve the bad patent problem and the proliferation of patent troll activity for at least two reasons. First, reexamination procedures reduce the number of bad patents. Reexaminations do not suffer from the same resource problem that initial examinations do because the examiners prioritize reexamination (perhaps at the expense of initial exams).<sup>92</sup> Further, the passage of time between the initial examination and the reexamination allows for a better review of the patent because the examiner now has perspective of the natural development of the art and has access to additional prior art.<sup>93</sup> Second, there is no presumption of validity, so the patent is scrutinized more carefully than during litigation.<sup>94</sup> In fact, for all of these reasons, most patents have some of their claims cancelled or narrowed during reexamination.<sup>95</sup>

The current reexamination system, however, does not do enough to solve the bad patent or patent troll problems. A party with a bad patent—regardless of whether they are a practicing or a non-practicing entity—has little incentive to request a reexamination of its own patents.<sup>96</sup> In addition, the current regime does not necessarily rescue alleged infringers who request reexamination from the threat of costly litigation, or the slightly less costly licensing fees that NPEs offer as an alternative, because requesting reexamination of a patent does not automatically halt the progress of litigation related to that patent.<sup>97</sup> An alleged infringer may request that a court stay ongoing litigation until the end of

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<sup>91</sup> Leahy-Smith America Invents Act, Pub. L. No. 112-29, sec. 6, §§ 311619, 125 Stat. 284, 2996304 (2011).

<sup>92</sup> 35 U.S.C. §§ 305, 314 (statutory requirement that reexaminations be handled by “special dispatch”); Robert Greene Sterne et. al., *Reexamination Practice with Concurrent District Court Patent Litigation*, 9 SEDONA CONF. J. 53, 53 (2008) (the Central Reexamination Unit of the PTO prioritizes reexaminations).

<sup>93</sup> See Lichtman & Lemley, *supra* note 15, at 46.

<sup>94</sup> See 35 U.S.C. §§ 305, 314.

<sup>95</sup> In *ex parte* reexaminations from 1981 to 2011, 66% of patents had some of their claims changed and 11% of patents were canceled in whole. See U.S. PATENT AND TRADEMARK OFFICE, *EX PARTE REEXAMINATION FILING DATA 162* (2011), [http://www.uspto.gov/patents/EP\\_quarterly\\_report\\_Sept\\_2011.pdf](http://www.uspto.gov/patents/EP_quarterly_report_Sept_2011.pdf).

<sup>96</sup> See Lichtman & Lemley, *supra* note 15, at 47 (defining a “bad patent” as one that “on the merits, should never have been issued”); Sudarshan, *supra* note 6, 160.

<sup>97</sup> Katherine D. Prescott, *Interplay Between Reexamination and Litigation: Temporary Restraining Orders, Preliminary Injunctions, and Litigation Stays*, in PARALLEL PATENT LITIGATION AND REEXAMINATION PROCEEDINGS 2007, at 130-33 (PLI Intellectual Prop., Course Handbook Series No. 13599, 2007), available at WL 908 PLI/PAT 125.

reexamination, but this decision is within the sole discretion of the judge and often results in a denial of the stay.<sup>98</sup> Thus, in many cases the USPTO and the court will simultaneously consider the validity of the same patent.<sup>99</sup> If the court does not stay the litigation, the NPE whose patents are probably invalid and who wants to settle with the defendant is incentivized to delay the reexamination procedure for as long as possible.<sup>100</sup> Accordingly, the accused infringer still faces the dilemma of undergoing expensive litigation or settling with the NPE.<sup>101</sup>

### F. *America Invents Act*

On September 16, 2011, Congress enacted the America Invents Act (AIA).<sup>102</sup> The AIA sets forth three provisions that allow a third party to challenge patent validity: (1) pre-issuance third-party submissions;<sup>103</sup> (2) post-grant review;<sup>104</sup> and (3) *inter partes* review.<sup>105</sup> While all three provisions may decrease the number of bad patents, they will likely not have a substantial impact nor affect the behavior of patent trolls.

The pre-issuance third-party submissions, while beneficial, will likely not have a substantial impact on either bad patents or patent trolls. Most third parties are ignorant of ongoing patent applications because they are difficult to locate and track.<sup>106</sup> Further, as discussed above, in many cases a party may start practicing the alleged invention long after a patent has issued and, therefore, have no interest in an application while it is pending. Moreover, even when a party is interested in an application, it may not submit prior art to avoid becoming a target of the applicant. Further, once the patents do issue, NPE incentives remain unaltered.

The post-grant review provides a single nine month period after the grant of a patent during which a challenger may institute post-grant review of the patent's validity by the USPTO.<sup>107</sup> The petition may request cancellation on

<sup>98</sup> Nationally, approximately 50% of motions for litigation stays pending reexamination are granted. *Id.*

<sup>99</sup> *Id.*

<sup>100</sup> *See id.*

<sup>101</sup> *See id.*

<sup>102</sup> Leahy-Smith America Invents Act, Pub. L. No. 112629, sec. 1, 125 Stat. 284 (2011).

<sup>103</sup> *Id.* sec. 6, §§ 311619.

<sup>104</sup> *Id.* sec. 6, §§ 321629.

<sup>105</sup> *Id.* sec. 8.

<sup>106</sup> *See supra* note 34 and accompanying text.

<sup>107</sup> Leahy-Smith America Invents Act, Pub. L. No. 112629, sec. 6, § 321(c), 125 Stat. 284, 307 (2011).

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prior art grounds or on defects in the specification.<sup>108</sup> This proposal suffers many of the problems previously identified: it dedicates resources to patents that may not be litigated; it fails to allow for the passage of time for the discovery and/or development of additional prior art; and third parties may not know about or may not want to participate in a post-grant review.

Once the nine month period for the post-grant review expires, the AIA provides for *inter partes* review.<sup>109</sup> *Inter partes* review differs from the current *inter partes* reexamination process in two substantive ways, neither of which will drastically affect the bad patent problem.<sup>110</sup> First, the AIA transferred *inter partes* review responsibilities from USPTO examiners to administrative law judges on the Patent Trial and Appeals Board.<sup>111</sup> Second, the AIA raised the standard for an *inter partes* review from a “substantial new question of patentability” to a “reasonable likelihood” that the requester will prevail on reexamination.<sup>112</sup> Consequently, the changes will decrease the number of *inter partes* reexaminations granted. Any other effects are uncertain at this point, but there is no reason to believe that these changes will have a significant impact on the number of bad patents issued or on the behavior of patent trolls for the same reasons that current reexamination procedures do not curb these problems.

**III. THE *i4i* DECISION**

In its 2011 *i4i* decision, the Supreme Court addressed whether section 282 of the U.S. Patent Act “requires an invalidity defense to be proved by clear and convincing evidence.”<sup>113</sup> Despite the pleas of Microsoft and numerous amici, the Supreme Court rejected lowering the standard to a preponderance of the evidence and upheld the existing clear and convincing standard.<sup>114</sup> In reaching its conclusion, the Supreme Court found that Congress did not change the existing standard of proof when it enacted section 282 of the U.S. Patent Act in 1952.<sup>115</sup>

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<sup>108</sup> *Id.* § 321(b).

<sup>109</sup> Leahy-Smith America Invents Act, sec. 6, §§ 311619.

<sup>110</sup> *See id.*

<sup>111</sup> *Id.* § 318.

<sup>112</sup> *Id.* § 314(a).

<sup>113</sup> *Microsoft Corp. v. i4i Ltd. Pøship*, 131 S. Ct. 2238, 2242 (2011).

<sup>114</sup> *Id.*

<sup>115</sup> *Id.* at 2247.

In its briefs, Microsoft argued that the standard of proof for establishing invalidity should be lowered to a preponderance of the evidence standard.<sup>116</sup> In the alternative, Microsoft argued that the standard of proof should be lowered only for prior art references or arguments that were not previously considered by the USPTO.<sup>117</sup> In support of these positions, Microsoft made several arguments based on statutory interpretation and legislative intent, all of which were rejected by the Court.<sup>118</sup>

In addition, as explained in the next Part, Microsoft and its supporting amici also argued that the standard of proof should be lowered as a potential solution to the bad patent and patent troll problems identified above.<sup>119</sup> The Supreme Court, however, declined to consider the public policy arguments proffered.<sup>120</sup> Instead, it deferred to Congress, finding that Congress has previously amended the patent laws to account for concerns about bad patents, including by expanding the reexamination process to provide for *inter partes* proceedings.<sup>121</sup> The Supreme Court also noted that despite the ongoing criticism from numerous scholars, including those discussed below, Congress has not acted to modify the existing standard of proof for invalidity.<sup>122</sup>

Thus, this Article now considers the public policy arguments left unconsidered by the Supreme Court in the *i4i* decision and proposes an alternative solution to the bad patent and patent troll problems.<sup>123</sup>

#### IV. THE MICROSOFT SOLUTION

##### A. *The Proposed Microsoft Solution*

As a potential solution to the bad patent problem, in its petition for a writ of certiorari and subsequent briefing, Microsoft advocated lowering the standard of proof necessary for establishing invalidity from the current clear and convincing standard to a preponderance of the evidence standard (the Mi-

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<sup>116</sup> Brief for Petitioner, *supra* note 51, at 14.

<sup>117</sup> *Id.* at 33.

<sup>118</sup> *i4i*, 131 S. Ct. at 2247.

<sup>119</sup> *Id.* at 2251-652.

<sup>120</sup> *Id.* at 2252.

<sup>121</sup> *Id.*

<sup>122</sup> *Id.*

<sup>123</sup> *See infra* Part III.

Microsoft Solution).<sup>124</sup> Relying on many of the scholarly articles cited herein,<sup>125</sup> Microsoft argued that a clear and convincing standard is inappropriate because the issuance of bad patents demonstrates that the current USPTO review is not sufficient to warrant a presumption of validity for all issued patents.<sup>126</sup> In addition, Microsoft argued that the “standard of proof that courts apply to invalidity defenses . . . directly affects whether patent litigants can cull invalid patents from the modern patent thicket and, less directly, whether our patent system is calibrated to promote progress in the useful arts, or stifle it.”<sup>127</sup>

Some of the scholars Microsoft relied upon take the argument a step further, stating that the “culprit [behind the bad patent problem] is a legal doctrine known as the presumption of validity.”<sup>128</sup> For example, Lichtman and Lemley argue that lowering the standard of proof for invalidity among other reforms would “reduce applicants’ incentive to file undeserved applications in the first place . . . reduce the disruption caused by any undeserved applications that might accidentally slip through, and at the same time provide a greater degree of certainty to patentees who deserve it.”<sup>129</sup> Their proposal of lowering the standard of proof for invalidity would accomplish these goals by better harnessing the information currently residing in private hands (e.g., competitors) and causing them to disclose it during an adversarial hearing (e.g., via patent litigation).<sup>130</sup> Further, Lichtman and Lemley argue that the Microsoft Solution would also stymie the efforts of patent trolls by eliminating their ability to exploit the

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<sup>124</sup> Petition for a Writ of Certiorari *Microsoft Corp. v. i4i Pøship*, 131 S. Ct. 2238 (2011) (No. 10-290), 2010 WL 3413088 at \*13614, \*24625.

<sup>125</sup> The articles cited in Microsoft’s petition include: Mark A. Lemley & Bhaven N. Sampat, *Examiner Characteristics and the Patent Grant Rate* (John M. Olin Program in Law & Econ., Stanford Law Sch. Working Paper No. 369, 2009), available at <http://ssrn.com/abstract=1329091>; Mark A. Lemley & Carl Shapiro, *Probabilistic Patents*, 19 J. ECON. PERSP., Spring 2005, at 75, 79; Matthew D. Henry & John L. Turner, *The Court of Appeals for the Federal Circuit’s Impact on Patent Litigation*, 35 J. LEGAL STUD. 85 (2006); Glynn S. Lunney, *Patent Law, the Federal Circuit, and the Supreme Court: A Quiet Revolution*, 11 SUP. CT. ECON. REV. 1 (2004); John R. Allison & Mark A. Lemley, *Empirical Evidence on the Validity of Litigated Patents*, 26 AIPLA Q.J. 185 (1998); Alan Devlin, *Revisiting the Presumption of Patent Validity*, 37 SW. U. L. REV. 323, 338 (2008) B.D. Daniel, *Heightened Standards of Proof in Patent Infringement Litigation: A Critique*, 36 AIPLA Q.J. 369, 412 (2008).

<sup>126</sup> Petition for Writ of Certiorari at 18619, *Microsoft Corp. v. i4i Pøship*, 598 F.3d 831 (No. 10-290) 2010 WL 3413088 at \*19622.

<sup>127</sup> *Id.* at \*21.

<sup>128</sup> Lichtman & Lemley, *supra* note 15, at 47.

<sup>129</sup> *Id.* at 51.

<sup>130</sup> *Id.* at 65.

current system.<sup>131</sup> As discussed below, however, these assertions of the benefits of the Microsoft Proposal are unfounded and optimistic.

### ***B. The Problem with the Microsoft Solution***

The inherent problem with the Microsoft Solution is that it assumes that the standard of proof by which a patent must be shown to be invalid (whether it is by clear and convincing or by a preponderance of the evidence) bears on (1) the number of patent applications filed; (2) the number of patents issued by the USPTO; or (3) the number of infringement cases brought by NPEs. Not only are these assumptions incorrect, but the Microsoft Solution would actually harm the patent system by deterring the assertion of “good patents.”

#### **1. The Microsoft Solution Would Not Decrease the Number of Patent Applications Filed**

Neither Microsoft, nor any of the scholars that it relies upon, can demonstrate that the legal standard for invalidity directly impacts the number of patent applications that are filed. Presumably, when an applicant files an application, it does so with a reasonable expectation that the USPTO will grant the patent. Further, it would also be unusual for an applicant to file an initial application with an eye towards asserting the patent against a specific third party because if a third party is already practicing the claimed invention at the time of filing, then the patent is likely invalid.<sup>132</sup> Even if the applicant has an eye towards litigation at the time of filing, the cost of the patent application (approximately \$10,000 to \$20,000) is miniscule compared to the cost of patent litigation (approximately \$5,500,000), thus it would be reasonable for an applicant to risk the cost of the application to reserve its right to later pursue litigation.<sup>133</sup> Finally, changing the presumption of validity at trial does not alter the examination process, meaning that applicants would still have the same chances of receiving a patent. For all these reasons, it is unlikely that a change in the presumption of validity granted to patents at trial will affect the number of patent applications filed.

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<sup>131</sup> *Id.* at 71.

<sup>132</sup> An applicant filing a continuation application may have greater reason to expect litigation. But continuation applications only make up 39% of all patent applications. Cecil D. Quillen, Jr. & Ogden H. Webster, *Continuing Patent Applications and Performance of the U.S. Patent and Trademark Office—One More Time*, 18 FED. CIR. B.J. 379, 392 (2009).

<sup>133</sup> The estimated cost to file and prosecute a patent application is based on the authors' personal experience and can vary from application to application.

## 2. The Microsoft Solution Would Not Decrease the Number of Patents Issued

Not only would the Microsoft Solution not affect the number of patent applications filed, but it would also not affect the number of patents issued. As explained above, a change in the presumption of validity at trial will not alter the examination process. Regardless of the standard of proof, the USPTO considers applications without any presumption of validity and gives patent claims their broadest reasonable construction.<sup>134</sup> Moreover, the Microsoft Solution would not provide additional opportunities for third parties to disclose additional prior art to the USPTO nor would it increase the resources available to examiners. Therefore, there is no reason to expect that the percentage of patent applications that yield issued patents would decrease as a result of the Microsoft Solution.

## 3. The Microsoft Solution Would Not Significantly Decrease the Number of Patent Infringement Cases Instituted by NPEs.

At most, the Microsoft Solution likely will have a negligible impact on the number of patent infringement cases filed by patent trolls or NPEs. As explained above, the likelihood of success on the merits is a secondary consideration for most NPEs.<sup>135</sup> Instead, their focus is on extorting the cost of litigation from the defendants.<sup>136</sup> Historically, NPE settlement amounts indicate that their litigation decisions are, at most, loosely related to their likelihood of success on the merits.<sup>137</sup> For example, many patent cases are settled only for a fraction of the amount demanded in damages.<sup>138</sup> Thus, either the NPEs' settlement decisions are not based on their likelihood of success on the merits, or they already view their chances of success on the merits as minimal. In either case, lowering NPEs' likelihood of success on the merits by lowering the standard of proof of invalidity at trial is unlikely to alter their initial decision-making process.

Of course, some defendants may be emboldened by a change in the standard of validity and decide against settlement even if it is not a fiscally pru-

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<sup>134</sup> See, e.g., *In re Swanson*, 540 F.3d 1368, 1377679 (Fed. Cir. 2008).

<sup>135</sup> See *supra* Part I.D. (explaining that NPEs generally pursue settlement or licensing fees before a case is tried on the merits to completion).

<sup>136</sup> *Id.*

<sup>137</sup> Sudarshan, *supra* note 6, at 162.

<sup>138</sup> *Id.* at 160, 162.

dent decision. A defendant's decision to defend itself through trial, however, is made after a patent infringement suit is filed. Thus, a change in the presumption of validity would, at most, decrease the amount that an NPE will seek in settlement, but not whether it institutes a case initially.

Finally, it is difficult to estimate the effect of a lower standard of validity on pre-litigation negotiations (*e.g.*, when an NPE sends a licensing letter indicating that a company may be infringing its patents). For the same reasons discussed above, under a lower standard of validity, an NPE may decrease the amount it will seek for a license even in pre-litigation negotiations. In addition, an emboldened accused infringer may be more apt to file for a declaratory judgment action challenging the validity of a patent. Ultimately, however, a lowered standard of validity would not alter the negotiating dynamic— an accused infringer still has two options regardless of the standard of proof: (1) pay to litigate or (2) settle for less than the cost of litigation.

In short, the Microsoft Solution does not reduce the incentives of NPEs to institute lawsuits, and it does not affect the economic incentives of defendants to settle cases for less than the cost of litigation. Thus, it is unlikely that the Microsoft Solution will have an impact on the number of cases instituted by NPEs.

#### **4. The Microsoft Solution Would Harm Legitimate Patent Holders.**

The Microsoft Solution will likely have the unwanted effect of hindering the ability of practicing entities to enforce "good patents." Unlike NPEs, practicing entities usually enforce their patents in order to prevent competition and thus are concerned with their likelihood of their success on the merits. In addition, a practicing entity will incur far greater litigation costs than an NPE and thus will be more focused on the outcome at trial. When the expected costs of litigation outreach the expected recovery,<sup>139</sup> a practicing entity is unlikely to pursue litigation. Altering the presumption of validity will decrease the expected recovery at trial and, therefore, likely decrease the number of practicing entities who enforce their patents and the amount they recover. This, in turn, may decrease the incentive to invest in developing good patents and consequently, limit the advancement of science.

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<sup>139</sup> Expected recovery is the expected damages award multiplied by the likelihood of success. A lower standard of validity theoretically should not alter the amount of a damages award, but it will decrease the likelihood of success by a patent holder.

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For the reasons set forth above, and because it focuses on trial incentives instead of pre-trial incentives, the Microsoft Solution will likely have a minimal impact on bad patents and NPEs, and could adversely affect practicing entities and the assertion of good patents.

**V. OTHER PROPOSALS**

The Microsoft Solution is not the only proposed solution to the bad patent/NPE problem. Scholars and policy makers have suggested a variety of methods to reduce the prevalence of bad patents and NPE suits.<sup>140</sup> This paper does not seek to describe the multitude of other proposals in detail, but only to highlight the most commonly discussed and their corresponding problems.

One of the most widely discussed reforms is a damages cap, which would limit the amount of damages a plaintiff can recover in a patent suit.<sup>141</sup> This solution is modeled on damage caps in medical malpractice and other areas of tort reform.<sup>142</sup> Decreasing the overall value of a suit could potentially decrease the settlement amounts in cases that are filed.<sup>143</sup> A damages cap, however, would have at most a minimal impact on patent applications and no impact on the quality of patent review. More importantly, a damages cap would not decrease the cost of litigation and thus NPEs could still extort settlements. Finally, a damages cap would limit recovery on good patents, thus discouraging investment in research and development.

Lichtman and Lemley approvingly incorporate Alan Devlin's proposal to allow an applicant to obtain a "gold-plated" review which would be entitled to a higher standard of validity than patents subject to a regular review.<sup>144</sup> This proposal, however, would not affect NPEs—they could still obtain patents through a "regular" review and hold a defendant hostage for the cost of litigation. The gold-plated review proposal could help legitimate patent holders by cementing the validity of their patents, but whether even a legitimate patent holder would want to risk subjecting a patent to further scrutiny unnecessarily is an open question.

Another proposal, modeled on tort reform, is to apply the "English rule" of fee shifting—requiring the loser of a suit to pay the winner's legal fees—to

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<sup>140</sup> Sudarshan, *supra* note 6, at 182.

<sup>141</sup> *Id.* at 177.

<sup>142</sup> *Id.* at 177-78.

<sup>143</sup> *Id.* at 178.

<sup>144</sup> Devlin, *supra* note 125, at 323.

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patent suits.<sup>145</sup> This proposal relies on the assumption that patent trolls' cases are often weak.<sup>146</sup> Requiring a patent troll to pay a defendant's fees would discourage the defendant from settling for the cost of litigation. At the same time, it would encourage patent trolls to be more selective about asserting a patent.<sup>147</sup> The problem with this proposal, however, is that it would have no impact on the number of patent applications or the patent review process. Moreover, even with bad patents, one can never be certain that a patent is invalid or not infringed prior to extensive review or litigation.<sup>148</sup> In addition, even if an NPE may not obtain a large verdict at trial, it may nonetheless be able to show de minimis infringement, thus imposing costs and fees on the defendant. In such a case, the potential to also pay the NPE's fees may further encourage an extorted settlement.

Still other scholars propose an "option to bar settlement," a rule that would grant defendants the right to request a court to not enforce a settlement agreement between parties.<sup>149</sup> This would allow defendants to force patent trolls to either pursue a claim to trial or drop the suit.<sup>150</sup> Again, the problem with this proposal is that it is difficult for a defendant to recognize that a plaintiff is not willing to go to trial.<sup>151</sup> Further, defendants may not be willing to commit the resources to bring a case to trial.<sup>152</sup>

Another option is an open post-grant patent review procedure.<sup>153</sup> Under this proposal, every time a patent is renewed or sold, it is subject to review by the USPTO.<sup>154</sup> This proposal would cause patent trolls to be less likely to acquire bad patents and, therefore, unable to extract royalties unjustly.<sup>155</sup> The Federal Trade Commission has suggested that its administrative procedures could evaluate the validity of a patent in a broader, and thus less expensive and time-

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<sup>145</sup> Sudarshan, *supra* note 6, at 179680.

<sup>146</sup> *Id.* at 180.

<sup>147</sup> *Id.*

<sup>148</sup> *Id.* at 180681.

<sup>149</sup> *Id.* at 181.

<sup>150</sup> *Id.*

<sup>151</sup> *Id.* at 1816182.

<sup>152</sup> *Id.*

<sup>153</sup> Victoria E. Luxardo, *Towards a Solution to the Problem of Illegitimate Patent Enforcement Practices in the United States: An Equitable Affirmative Defense of "Fair Use" in Patent*, 20 EMORY INT'L L. REV. 791, 820 (2006).

<sup>154</sup> *Id.*

<sup>155</sup> *Id.* at 820621.

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consuming, manner than would occur during litigation.<sup>156</sup> This solution, however, is overbroad. As explained above, only 1.5% of patents are actually litigated.<sup>157</sup> This proposal would not encourage adversarial involvement in the review process. Further, this proposal would drastically increase costs to the applicants and the FTC by enforcing an examination procedure every time a patent is transferred.

There are a multitude of other proposals to improve patent quality and to deter bad patents. Some propose defendants bring antitrust and state unfair competition claims against patent trolls, while others suggest requiring both parties to proceed to the summary judgment phase of litigation before entering into a settlement.<sup>158</sup> Other possibilities include providing an equitable defense for defendants who can show that their use does not create market harm for the plaintiff because the plaintiff, as an NPE, does not use or practice the art,<sup>159</sup> or requiring parties to submit to alternative dispute resolution.<sup>160</sup> In the end, none of these proposals provide the proper balance of disincentives to NPEs while not overburdening the USPTO.

**VI. THE MANDATORY REEXAMINATION SOLUTION**

Our alternative to the proposals discussed above is to require a mandatory reexamination of any patent that the patent holder wishes to assert in litigation (the “Mandatory Reexamination Proposal”). Under this proposal, any patent holder that wants to assert its rights under a patent against an alleged infringer would be required to pay for and file an *ex parte* reexamination with the USPTO for each patent it seeks to assert.<sup>161</sup> Any third party (*e.g.*, an alleged infringer) who wishes to disclose additional prior art on an *ex parte* basis during the reexamination process may do so upon paying some modest fee to the USPTO. A third-party also could convert the *ex parte* reexamination to an *inter*

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<sup>156</sup> *Id.* at 821.

<sup>157</sup> Lemley, *supra* note 14, at 1507.

<sup>158</sup> Sudarshan, *supra* note 6, at 183.

<sup>159</sup> Luxardo, *supra* note 153, at 826627.

<sup>160</sup> David A. Fitzgerald II, *Saving Alternative Dispute Resolution in Patent Law: Countering the Effects of the Patent Troll Revolution*, 23 OHIO ST. J. ON DISP. RESOL. 345 (2008).

<sup>161</sup> Currently, the USPTO fee for an *ex parte* reexamination is \$2,520. *Fee Schedule*, U.S. PAT. AND TRADEMARK OFF., (Jan. 10, 2012), <http://www.uspto.gov/web/offices/ac/qs/ope/fee092611.htm>.

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*partes* reexamination by paying an additional fee.<sup>162</sup> Only upon issuance from the reexamination process could the patent be enforced through litigation.<sup>163</sup>

After a patent issues from the mandatory reexamination process, and its owner asserts it in litigation, the current presumption of validity accorded issued patents would apply. In addition, any party participating in an *inter partes* reexamination process, or the new *inter partes* review process under the America Invents Act, would be precluded from contesting validity at trial based upon arguments or evidence that was known or should have been known at the time of the *inter partes* reexamination or review.<sup>164</sup>

As discussed below, the Mandatory Reexamination Proposal solves each of the problems that were unsuccessfully addressed by scholars advocating the Microsoft Solution.

### A. Improves the Overall Review Process

One obvious benefit of the Mandatory Reexamination Proposal is to improve the overall review process. Under this proposal, the proposed reexamination process focuses only on patents to be asserted in litigation; thus, it can warrant the dedication of significant additional resources, including the dedication of the USPTO's most experienced examiners. Considering the cost to defend a patent lawsuit, it is reasonable to raise the cost of these proposed reexaminations from the current amount of \$2,520 to \$10,000 to provide the USPTO with the necessary funding for the mandatory reexaminations.<sup>165</sup> With this additional funding, the USPTO could pay to retain its most senior examiners, fund the use of multiple examiners per reexamination, or retain third-party prior art search firms to locate relevant prior art.<sup>166</sup>

In addition, mandatory reexamination would improve the review process by allowing third-party participation. An alleged infringer would be incentivized to invalidate the patent during reexamination to avoid the high cost of patent litigation.<sup>167</sup> Similarly, an alleged infringer will likely invest significant

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<sup>162</sup> Currently, the USPTO fee for an *inter partes* reexamination is \$8,800. *Id.*

<sup>163</sup> As discussed in the objections section below, special exceptions will be made to allow a patent to be asserted in litigation without reexamination upon an initial showing of cause.

<sup>164</sup> See 35 USC § 315(c).

<sup>165</sup> In the case of hardship or need, a patent holder could petition the USPTO for lower fees.

<sup>166</sup> It is unlikely that raising the fees for mandatory reexamination would stunt investment in patents because the initial cost to obtain a patent would remain the same and the raised reexamination cost would only be triggered through litigation.

<sup>167</sup> To further encourage third-party participation, the patent owner could be required to identify the alleged infringers of its patents as part of the reexamination process. If the patent owner

resources in locating prior art to bolster their invalidity arguments. Even if a company is not put on notice that it is the likely target of a patent in reexamination, frequent patent troll targets would likely monitor USPTO proceedings in order to determine if they should participate in a reexamination. Moreover, companies may form or join associations or coalitions to monitor patent trolls within a given field, *e.g.*, smart phones or LCD manufacturers. Those associations or coalitions could not only reduce the cost to their individual members, but they also could prevent a target from being placed on any individual defendant.

Finally, the review process is likely to be improved on reexamination because the additional time that elapses between the initial examination and the mandatory reexamination will likely allow for a more thorough examination. As an initial matter, examiners will become more familiar with the prior art, and additional prior art will be indexed in the USPTO based on the examinations of other patents covering the same or similar subject matter.<sup>168</sup> In addition, examiners will have a better understanding of the obvious improvements in a field as opposed to the novel improvements. Moreover, some co-pending patent applications could blossom into prior art for the reexamination even though they were not prior art at the time of initial examination.<sup>169</sup> For example, if a patent was pending and not published during the initial examination, it is not available for an examiner to consider during the initial examination. However, the passage of time between the original examination and the reexamination could essentially create additional prior art by allowing the pending application to be published or to issue as a patent prior to the reexamination.

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did not put an alleged infringer on sufficient notice of the mandatory reexamination, the patent owner would lose the ability to later sue that alleged infringer for infringement. In such a case the patent holder would have to institute another reexamination in order to sue that alleged infringer. The counter argument for such an identification requirement is that such a requirement may lead to multiple mandatory reexaminations and unnecessarily delay the assertion of patents already deemed valid through a prior reexamination. Multiple reexaminations, however, are unlikely to require the same time and resources as the initial reexamination because it is likely that the USPTO considered the most relevant prior art in the first reexamination. Thus, a later reexamination would only be time consuming if the USPTO is presented with a substantial new question of patentability, in which case, a potentially bad patent could be invalidated.

<sup>168</sup> When a patent is examined, the USPTO indexes all prior art that is submitted with the patent application so that it may be located by other examiners.

<sup>169</sup> Under 35 U.S.C. § 102, a patent application is not considered prior art until it is either published under 35 U.S.C. § 122 or it issues. 35 U.S.C. §§ 102, 122 (2012).

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For all these reasons, a mandatory reexamination of a patent before it is allowed to be asserted in litigation will provide for a more thorough and well-reasoned examination process.

### *B. Limits Bad Patents Asserted in Litigation*

One obvious consequence of improving the review process is a limitation on the number of so called "bad patents" that can be asserted in litigation.<sup>170</sup> During examination, including reexamination, patent claims are given their broadest reasonable interpretation.<sup>171</sup> A reexamination with the additional resources and the additional prior art identified above will likely lead to the invalidation of many of the bad patents that previously issued. Even where a patent survives reexamination with modified claims, it is less likely that the patent holder will assert such a patent because patent holders cannot obtain past damages for infringement of modified claims.<sup>172</sup> Furthermore, there will likely be some self-screening of bad patents; that is, patent holders will be less likely to assert a patent if they have to incur the cost of reexamination, and they believe that the reexamination will likely result in an invalidation of the patent. Thus, even if the Mandatory Reexamination Proposal does not limit the number of bad patents that initially issue, it will likely significantly decrease the number asserted in litigation.

### *C. Limits Patent Troll Cases*

Not only will the Mandatory Reexamination Proposal limit the number of bad patents asserted in litigation, but it will also limit the number of infringement lawsuits initiated by patent trolls. This proposal will force patent trolls to internalize the risks and costs of an invalidity determination. A rational patent troll should not initiate a lawsuit when the risks and costs of an invalidity finding outweigh the expected recovery if the patent survives reexamination. In such a case, patent troll may find more value in selling the patent to a practicing entity than risk the asset's entire value in a mandatory reexamination. Thus, NPEs may end up liquidating their existing stores of bad patents instead of attempting to assert them and subjecting themselves to the costs and uncertainty of the mandatory reexamination. In such a case, the industry associations or

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<sup>170</sup> The existence of bad patents without the threat of enforcement has little or no impact on the marketplace.

<sup>171</sup> MANUAL OF PATENT EXAMINING PROCEDURE § 2111 (8th ed., 8th rev. 2010).

<sup>172</sup> 35 U.S.C. § 252 (2006)

coalitions could potentially buy the trolls' patents at a fraction of the cost of settling the lawsuits in which the bad patents would be asserted.

Similarly, patent trolls will be deterred from acquiring new patents, especially "bad patents," given the increased costs and risks associated with asserting those patents. At the same time, the demand for "good patents," patents likely to survive mandatory reexamination, and the cost to acquire them will likely increase, making good patents harder for patent trolls to acquire.

#### *D. Increased Certainty for Good Patents*

The Mandatory Reexamination Proposal would also increase the certainty associated with good patents. By definition, a good patent would have little difficulty passing a mandatory reexamination proceeding. Upon issuance from the reexamination, the patentee would be confident about the validity of the patent and could enforce his or her rights under the patent. Thus, it would be easier to license a good patent because the increased certainty on the patent's validity would enable the parties to eliminate the validity issue from negotiations. In addition, patentees will be able to recover full value for good patents because they will be less concerned with the risks of invalidity when a patent is litigated on its merits.<sup>173</sup> Thus, the mandatory reexamination proposal will be beneficial for the holders of good patents.

For the reasons set forth above, the Mandatory Reexamination Proposal is likely to improve the patent review process, limit the number of bad patents asserted in litigation, and limit the number of lawsuits brought by patent trolls.

### **VII. POTENTIAL OBJECTIONS TO THE MANDATORY REEXAMINATION PROPOSAL**

We have identified five expected objections to the Mandatory Reexamination Proposal: (1) it will impose unnecessary or excessive costs on the patent holders; (2) it will overwhelm the USPTO; (3) it will unreasonably delay a patent holder's ability to enforce its patents; (4) it will deprive patent holders of the right to select their own venue; and (5) it will be hindered by the current limitations on the reexamination process. Each objection is addressed in turn below.

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<sup>173</sup> See, e.g., Alberto Galasso & Mark Schankerman, *Patent Thickets and the Market for Innovation: Evidence from Settlement of Patent Disputes* (Ctr. for Econ. Policy Research, Working Paper No. 6,946, Aug. 2008), available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=1401775](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1401775) (reporting faster settlement agreements where there is greater certainty in outcome).

## MANDATORY PATENT REEXAMINATIONS

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### *A. The Financial Cost of the Mandatory Reexamination Proposal*

One potential objection to the Mandatory Reexamination Proposal is that it will impose a significant financial cost on patent holders wishing to assert their patents. As set forth above, the current cost of an *ex parte* reexamination is \$2,250, and an *inter partes* reexamination costs \$8,800. Assuming that costs under the Mandatory Reexamination Proposal rise to accommodate the need to retain additional examiners, the cost for the mandatory reexamination could be as high as \$15,000 with an additional \$50,000 if it becomes an *inter partes* review.<sup>174</sup> That cost, however, is small when compared to the average cost of patent litigation.<sup>175</sup> Further, any patent infringement claim that does not merit a \$15,000 investment on behalf of the patentee is likely properly excluded from the courts. In the likelihood that a patent holder cannot afford the cost, an application for reduced fees could be allowed by the USPTO with a showing of need. Thus, we do not expect the additional cost to the patentee to be a significant obstacle to the Mandatory Reexamination Proposal.

### *B. The USPTO Resources Necessary to Handle the Mandatory Reexamination Proposal*

A second potential objection to the Mandatory Reexamination Proposal is that the USPTO will not have the resources necessary to handle the additional reexaminations. However, over the last ten years, on average about 2,500 patent infringement lawsuits are filed each year.<sup>176</sup> Thus, under the Mandatory Reexamination Proposal, the USPTO would be required to handle approximately 2,500 new reexaminations each year.<sup>177</sup> Currently, there are over 400,000 patent

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<sup>174</sup> At those costs, the USPTO could afford to retain prior art search firms or retain other private contractors in order to assist its examination.

<sup>175</sup> The average cost of patent litigation in 2009 was \$5.5 million per party. *See supra* note 69.

<sup>176</sup> Mark A. Lemley, *Where to File Your Patent Case*, 38 AIPLA Q. J. 401, 404 (2010) (noting that over 25,000 suits had been filed between 2000 and 2010).

<sup>177</sup> It is difficult to estimate the actual number of mandatory reexaminations that would be necessary. On one hand, patent holders would likely be deterred by the mandatory reexamination process, thus reducing the number of reexaminations necessary. In addition, many of the 2,500 yearly patent infringement cases involve the same patents which are asserted by patent trolls against numerous different defendants. On the other hand, patent infringement lawsuits rarely involve only a single patent, thus increasing the number of mandatory reexaminations required. In those cases, however, the patents may be related and/or claim highly related subject matter and, thus, the mandatory reexaminations would likely focus on the same issues decreasing the burden on the USPTO. The number of mandatory reexaminations would be

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applications filed each year, and over 1,000 reexaminations were filed in 2011.<sup>178</sup> Thus, an additional 2,500 reexaminations is only a modest increase in workload for the USPTO. Moreover, the proposed additional cost of the reexaminations will allow the USPTO to retain more experienced examiners by rewarding them with higher pay and to retain outside search firms to conduct supplemental prior art searches. Thus, it is unlikely that the USPTO will be overwhelmed by the additional reexamination requests triggered by the Mandatory Reexamination Proposal.

### *C. Delays Caused by the Mandatory Reexamination Proposal*

A third potential objection to the Mandatory Reexamination Proposal is that it would impose a substantial time delay on a patent holder wishing to assert his or her patents. Currently, an *ex parte* reexamination takes on average two-and-a-half years to complete while an *inter partes* reexamination requires on average over three years to complete.<sup>179</sup> For a patent holder seeking to exclude its competitor from the market by enforcing its patent rights, waiting even one month can be a significant delay.

There are several ways to alleviate the potential delay problem. As a starting point, as detailed above, the additional resources that will be available to the USPTO through the Mandatory Reexamination Proposal should expedite the reexamination process. Nevertheless, even with these improvements, the Mandatory Reexamination Proposal would delay the assertion of patent rights. Thus, the Mandatory Reexamination Proposal also must include a way to expedite patent cases where time is essential.

Patent cases under the Mandatory Reexamination Proposal could be expedited in one of two ways. First, a patent holder who seeks and obtains a preliminary injunction could be exempt from the mandatory reexamination requirement. A preliminary injunction hearing allows a court to quickly determine if the merits of the case warrant delaying the case for a reexamination pro-

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less than the 2500 new patent infringement cases filed each year because patent holders would likely be deterred by the mandatory reexamination process.

<sup>178</sup> In 2011, 759 *ex parte* and 374 *inter partes* reexaminations were filed in 2011, and the number of reexaminations filed has generally increased every year since 2003. *Ex Parte Reexamination Filing Data*, U.S. PAT. AND TRADEMARK OFF., (Sept. 30, 2011), available at [http://www.uspto.gov/patents/EP\\_quarterly\\_report\\_Sept\\_2011.pdf](http://www.uspto.gov/patents/EP_quarterly_report_Sept_2011.pdf); *Inter Partes Reexamination Filing Data*, U.S. PAT. AND TRADEMARK OFF., (Sept. 30, 2011), [http://www.uspto.gov/patents/IP\\_quarterly\\_report\\_September\\_2011.pdf](http://www.uspto.gov/patents/IP_quarterly_report_September_2011.pdf).

<sup>179</sup> *Reexamination Operational Statistics*, U.S. PAT. AND TRADEMARK OFF., [http://www.uspto.gov/patents/Reexamination\\_operational\\_statistic\\_through\\_FY2011Q4.pdf](http://www.uspto.gov/patents/Reexamination_operational_statistic_through_FY2011Q4.pdf).

ceeding. Second, the Mandatory Reexamination Proposal would not apply if a patent holder makes an initial showing to a court that it is asserting its patent against a direct competitor or to prevent a competitor from entering the market. Under either scenario, it is highly unlikely that an NPE or patent troll would be able to make a sufficient showing to escape mandatory reexamination.

There are also methods to deter patent holders from exploiting the above-described mandatory reexamination exemptions. One option is to impose costs and fees on a patent holder that seeks to proceed without a mandatory reexamination and fails to show direct competition. Another option is to require a patent holder who proceeds without a mandatory reexamination to do so without the presumption of validity currently accorded. In other words, if a patent holder wished to proceed without a mandatory reexamination, it would do so according to the terms of the Microsoft Proposal.<sup>180</sup> Thus, in most cases it would be in the patent holder's best interest to proceed with the mandatory reexamination.

By its nature, the Mandatory Reexamination Proposal would necessarily impose some delays in the majority of patent cases. In many cases and most patent troll cases, however, a delay is not detrimental to the patent holder, especially given that a patentee can recover up to six years of past damages.<sup>181</sup> In the cases where timing is important, however, the Mandatory Reexamination Proposal could minimize delays by allowing a patent holder to proceed with a showing of cause, such as in the preliminary injunction and competitive injury situations outlined above. Therefore, any delays imposed by the Mandatory Reexamination Proposal would have only an insubstantial negative impact on the patent system as a whole.

#### ***D. Venue Selection under the Mandatory Reexamination Proposal***

A fourth potential objection to the Mandatory Reexamination Proposal is that it potentially deprives the patent holder its choice of venue.<sup>182</sup> Tradition-

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<sup>180</sup> *Gulf Oil Corp. v. Gilbert*, 330 U.S. 501, 508 (1946) (“[U]nless the balance is strongly in favor of the defendant, the plaintiff's choice of forum should rarely be disturbed.”)

<sup>181</sup> 35 U.S.C. § 286 (2012). That six-year clock begins from the filing of a lawsuit and, if the Mandatory Reexamination Proposal is implemented, the six year damages clock could begin with the initiation of a mandatory reexamination if the alleged infringer is identified as part of the reexamination process.

<sup>182</sup> Considering the number of cases filed in and subsequently transferred from the Eastern District of Texas, a perceived patent friendly venue, we may question the wisdom of allowing a patent holder to determine the proper venue.

ally, a plaintiff's choice of forum is entitled to deference.<sup>183</sup> Under the Mandatory Reexamination Proposal, however, both a patent holder and an accused infringer could engage in a race to the courthouse immediately after a patent issues from the mandatory reexamination. This race to the courthouse would waste both parties' resources engaging in the race and the courts' resources in resolving the question of venue selection. Thus, the Mandatory Reexamination Proposal should provide a grace period—for example, fifteen (15) days—during which only the patent holder could institute a lawsuit involving the reexamined patent.<sup>184</sup> Ideally, most cases could be settled during that fifteen day grace period because the validity of the patent has been affirmed, and the parties have a better sense of the merits of the case. Nevertheless, where a case proceeded to litigation, the patent holder would have first choice of forums within that fifteen day grace period. That choice, however, would not be absolute. Venue selection could still be challenged for lack of personal jurisdiction or convenience of the parties.<sup>185</sup>

#### *E. Limitations on the Scope of Reexaminations*

A fifth and final potential objection to the Mandatory Reexamination Proposal is that reexaminations currently do not consider all types of invalidity arguments that can be presented at trial. Under 37 CFR 1.552, prior art rejections can only be made on the basis of prior art patents or printed publications in reexaminations.<sup>186</sup> Thus, rejections cannot be made, for example, based on prior use, sale, or inventorship. Indeed, the prior art at issue in *i4i* was a prior sale that was not eligible to be considered in a reexamination proceeding.<sup>187</sup> In addition, a reexamination currently will not reevaluate compliance with the specification requirements of 35 U.S.C. § 112 unless new matter is added to the disclosure or the claims are amended.<sup>188</sup>

Both limitations may curb the effectiveness of the Mandatory Reexamination Proposal in a subset of cases, but it is unlikely that either limitation will

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<sup>183</sup> *HollyAnne Corp. v. TFT, Inc.*, 199 F.3d 1304, 1307 n.2 (Fed. Cir. 1999).

<sup>184</sup> There would also have to be an outer bound (e.g., two years from the issuance from reexamination) from which a reexamined patent can be asserted in litigation without being subject to additional reexamination. This requirement prevents patent holders from obtaining a reexamination early in the life of a patent and then sitting on those rights.

<sup>185</sup> 28 U.S.C. § 1404 (2012).

<sup>186</sup> 37 C.F.R. § 1.552 (2012).

<sup>187</sup> *Microsoft Corp. v. i4i Ltd. Pøship.*, 131 S. Ct. 2238, 2243644 (2011).

<sup>188</sup> 37 C.F.R. § 1.552.

have a substantial effect for the following reasons. Even limited to a consideration of printed publications and issued patents, a mandatory reexamination, for the reasons set forth above, will still eliminate many of the bad patents. In addition, where there is a prior use or a prior sale, it is also likely that there is supporting documentation that could be considered as a printed publication during reexamination (e.g., a training manual, a patent application, or a scholarly article). Moreover, the § 112 issues are more likely to have been properly decided during the initial examination because, unlike a validity analysis, consideration of § 112 compliance is not resource intensive and merely requires a review of the application.

Nevertheless, if after the Mandatory Reexamination Proposal is implemented for some period of time, it is determined that the effectiveness of the proposal is undermined by either of these limitations, then the mandatory reexamination process could be modified to eliminate either limitation. The elimination of the limitation on reconsideration of § 112 issues would not be a significant inconvenience or burden on the reexamination. Additionally, as set forth above, the mandatory reexamination process would be sufficiently funded to consider all types of prior art, if needed. Therefore, we do not expect that the limitations on the reexamination process to ultimately hinder the Mandatory Reexamination Proposal.

## VIII. CONCLUSION

Absent massive systemic reforms and increased funding, the USPTO will continue to be overwhelmed by the over 500,000 new patent applications filed each year and the resultant bad patents will continue to issue. As such, patent trolls and NPEs will continue to abuse these bad patents to extort settlements. The solution advocated by Microsoft and its cited scholars is insufficient to solve either problem because it addresses neither the incentives to file a patent application nor patent trolls' incentives to institute infringement lawsuits. As an unfortunate side-effect, the Microsoft Proposal will likely harm the enforcement of good patents. By comparison, as explained above, the Mandatory Reexamination proposal before a patent is litigated will improve the overall review process and directly reduce patent trolls' incentives.

The mandatory reexamination will improve the overall patent review process by increasing the resources available to the USPTO, focusing the review on the 1.5% of all patents that are actually litigated, providing the USPTO with additional prior art and perspective on the invention, and by making the reexamination process more adversarial. Additionally, mandatory reexamination will alter patent trolls' incentives by subjecting the patents at issue to a potentially adversarial validity determination on the merits. Although there are some minor

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obstacles facing a mandatory reexamination process, this article acknowledges these obstacles and shows that they can be easily overcome with a well-planned system. In *i4i*, the Supreme Court declined to implement the Microsoft Proposal of changing the standard of proof for invalidating a patent, opting instead to leave systemic reforms and the problem of patent trolls and bad patents to the legislature.<sup>189</sup> Congress is now in the position to stop the tide of invalid patents and nuisance suits by implementing a system of mandatory reexamination before litigation.

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<sup>189</sup> *i4i*, 131 S. Ct. at 2252.