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Joinder under the AIA: Shifting Non-Practicing Entity Patent Assertions away from Small Businesses

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NOTE

JOINDER UNDER THE AIA: SHIFTING NON-PRACTICING ENTITY PATENT ASSERTIONS AWAY FROM SMALL BUSINESSES

Xun (Michael) Liu*


When the America Invents Act ("AIA") was signed in September 2011, many feared the law might benefit larger corporations at the expense of small businesses. This Note examines how one portion of the AIA, governing joinder in patent cases, might actually benefit small businesses by reducing patent assertions from non-practicing entities ("NPEs"). NPE assertions disproportionately affect small businesses, both because NPEs target small businesses more frequently and because patent assertions have a greater impact on individual companies. Prior to the AIA, joining multiple defendants in a single lawsuit offered important advantages for patent holders and allowed NPEs to achieve a profitable economy of scale by targeting small businesses. The AIA, on the other hand, imposes a higher standard for joinder, changing both the litigation and economic dynamics of asserting patents against multiple defendants. Over the long run, the new joinder provision will likely reduce patent assertions against small businesses by increasing costs for NPEs and removing the litigation advantages of joining multiple defendants. This Note will also discuss how NPEs might adapt their assertion strategy in light of the joinder provision, as well as why some NPEs may continue to litigate against small companies, even at a short-term financial loss.

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Much has been written about the negative effects of non-practicing entities ("NPEs") on the technology industry. The corporate titans of Silicon Valley often point to the high costs of patent litigation as a tax on innovation and criticize NPEs for hindering productive businesses and increasing prices for consumers. Most often, the cases that draw media attention involve multi-national corporations hit with hundreds of millions of dollars in damages. But for every multi-million dollar damage award levied against companies like Microsoft or Apple, there are many more lawsuits filed against small- and medium-sized businesses, many of which are not even involved in the technology sector.

With the passage of the America Invents Act ("AIA"), Congress has implicitly addressed NPE litigation by limiting a patent holder's ability to join multiple defendants through 35 U.S.C. § 299. In the AIA legislative


2. See, e.g., Kent Walker, Google: Don't Let Trolls Exploit Patent System Flaws, WIRE (Nov. 19, 2012, 3:30 PM), http://www.wired.com/opinion/2012/11/googles/ ("We must improve our patent system to reduce the taxing effects of trolls, so companies can stop wasting money in court and get back to doing what they do best—building the great products and services we all enjoy.").


history, Congress specifically states that the purpose of the provision was to address the scenario in which defendants with tenuous connections to the underlying disputes are joined by the dozens, a common strategy for NPEs. While § 299 effectively limits joinder in patent cases, it is unclear if the new provision has actually reduced the total number of NPE lawsuits. Thus far, studies of the AIA have looked at NPE litigation in the aggregate, without accounting for how the provisions of the AIA might affect the distributional impact of NPE litigation. To address this gap, this Note analyzes how the AIA joinder provision will affect small businesses. In the long run, § 299 will likely reduce NPE assertions against small businesses by increasing the cost of enforcing patents against multiple alleged infringers and by removing strategic advantages of joining multiple defendants.

Section I of this Note looks at the NPE business model and investigates how the economics of patent litigation drive NPEs to consolidate their trials. Section II explains why allowing NPEs to consolidate trials disproportionally impacts small businesses. Section III examines the mechanics of consolidating trials before and after the AIA. Section IV highlights the NPE response to § 299 and analyzes how that response will affect small businesses. Finally, Section V explores why some NPEs may continue targeting small businesses to strengthen their future litigation position and drive up royalty rates for their patents. The Conclusion looks at the broader policies of patent litigation reform and promoting small business growth.

I. THE NPE BUSINESS MODEL

In general, the term NPE refers to any patent-holding individual or organization that does not practice the invention, but instead licenses or asserts its patents to generate revenue. The term may describe universities, research organizations, or other licensing entities. There is a subset of NPEs, sometimes called patent assertion entities, which use patent licenses and

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9. Bryant, supra note 7; Patent Reform, supra note 8.
damage awards as their only revenue source.\textsuperscript{12} These entities are also referred to as "patent trolls" because they characteristically hold patents until a related product becomes profitable, then emerge to demand payments from unsuspecting companies,\textsuperscript{13} much like the trolls of folklore that ambush unsuspecting passersby.\textsuperscript{14} For the purposes of the following discussion, the term NPE will be limited to these patent assertion entities.

The total private and social impact of NPEs remains unclear.\textsuperscript{15} While there are numerous examples of NPEs that have received astronomical damage awards,\textsuperscript{16} most NPE lawsuits end with settlements that are not made public.\textsuperscript{17} By analyzing changes in market capitalization following patent lawsuits, Bessen et al. estimated that the aggregate loss of wealth from NPE lawsuits is approximately $83 million per year.\textsuperscript{18} In terms of prevalence, NPE-initiated patent lawsuits are still less common than patent lawsuits among practicing entities.\textsuperscript{19} In one study, Sannu K. Shrestha estimated the percentage of NPE-initiated lawsuits to be anywhere between 2% to 17% of all patent lawsuits.\textsuperscript{20}

As with any other business, NPEs must generate more revenue than costs incurred to stay in business. Damage awards and settlement-induced licenses are NPEs' only source of revenue.\textsuperscript{21} This business model depends on three main factors: (1) revenue generated from defendants, (2) the cost of litigation, and (3) the likelihood of a favorable outcome.

Regarding the first factor, it is difficult to estimate how much revenue a patent holder can expect to earn from asserting their patent, since this

\begin{thebibliography}{9}
\bibitem{12} Id. at 2112.
\bibitem{13} McDonough, supra note 10.
\bibitem{14} \textit{Paul Galdone, The Three Billy Goats Gruff} 9 (1973).
\bibitem{15} Sannu K. Shrestha, Note, \textit{Trolls or Market-Makers? An Empirical Analysis of Non-practicing Entities}, 110 COLUM. L. REV. 114, 120–21 (2010) ("[I]t is unclear whether NPE-initiated suits are indeed significant enough to have an impact on the costs of most products.").
\bibitem{16} In one of the most noted patent infringement cases, the patent holding company NTP sued Blackberry maker Research in Motion ("RIM") and was awarded an injunction in addition to $53 million in damages. After losing on appeal, RIM ultimately licensed the patent for $612.5 million from NTP. NTP, Inc. v. Research in Motion, Ltd., 418 F.3d 1282, 1287 (Fed. Cir. 2005); accord Shrestha, supra note 15, at 114.
\bibitem{17} \textit{From Exposing NPE Myths to Explaining NPE Math}, RPX, http://www.rpxcorp.com/index.cfm?pageid=14&itemid=25 (last visited Feb. 9, 2013) (noting that 95\% of cases brought by NPEs are settled).
\bibitem{19} Shrestha, supra note 15, at 120–21.
\bibitem{20} Id.
\bibitem{21} Taurus IP v. DaimlerChrysler Corp., 519 F. Supp. 2d 905, 911 (W.D. Wis. 2007) ("[NPEs] do not manufacture products, but instead hold licenses to numerous patents, which they license and enforce against alleged infringers.").
\end{thebibliography}
amount varies greatly based on the industry and size of defendant.\textsuperscript{22} For example, median damage awards in the consumer products industry are well below $5 million, while median damage awards in the electronics industry run above $30 million.\textsuperscript{23} Across all industries, the median damage award of NPE-initiated lawsuits from 1995 to 2011 was approximately $6.9 million.\textsuperscript{24} While the median damage award illustrates the magnitude of NPE damages, the reported median only reflects NPE lawsuits that resulted in a verdict. The vast majority of NPE assertions end with settlement agreements that are not public.\textsuperscript{25} In fact, several studies have found that fewer than 5\% of patent infringement cases are resolved through trial.\textsuperscript{26}

Turning to the second factor—cost of litigation—there are various estimates for how much money an NPE needs to launch a lawsuit. In general, legal fees often exceed $4 million to take a patent case through trial.\textsuperscript{27} Other studies estimate that NPEs will require approximately $2 million to launch a patent infringement lawsuit.\textsuperscript{28} While these legal fees may seem prohibitively high, the up-front costs for NPEs tend to be very low because many rely on law firms that accept contingency fee arrangements.\textsuperscript{29} By comparing the median damage award to the cost of litigation, it is evident that relatively few cases will result in huge windfalls for NPEs.

The third and final factor in the NPE business model is the likelihood of a favorable outcome. PricewaterhouseCoopers found that NPEs had an overall success rate of 24.3\% between 2006 and 2011.\textsuperscript{30} This study is consistent with data acquired from the Stanford IP Litigation Clearinghouse,\textsuperscript{31} which

\textsuperscript{23} Id. at 7; Matthew Fawcett & Jeremiah Chan, March of the Trolls: Footsteps Getting Louder, 13 INTL. PROP. L. REV. 1, 8 (2008).
\textsuperscript{24} Michael Risch, Patent Troll Myths, 42 SETON HALL L. REV. 457, 481 (2012); From Exposing NPE Myths to Explaining NPE Math, RPX, http://www.rpxcorp.com/index.cfm?pageid=14&itemid=25 (noting that, based on data in Risch’s empirical study, 95\% of cases brought by NPEs are settled).
\textsuperscript{26} Risch, supra note 25, at 467.
\textsuperscript{27} Shrestha, supra note 15, at 120.
\textsuperscript{28} In a contingency fee arrangement, the legal counsel is paid after the lawsuit has been resolved by receiving a portion of any damage award or settlement payment. David L. Schwartz, The Rise of Contingent Fee Representation in Patent Litigation, 64 ALA. L. REV. 335, 335 (2012).
estimated the success rate of NPE-initiated patent litigation cases to be around 24.1% from 2000 to 2008.32 Thus, given the high cost of litigation and relatively low rate of success, NPEs and their law firms take on substantial risk in litigating a case to trial.33 To compensate for this risk dynamic, NPEs will file lawsuits against deep-pocketed companies for tens of millions in damages or, alternatively, target a large number of companies to extract smaller settlement payments or damage awards.34

II. DISTRIBUTIONAL IMPACT OF NPE LITIGATION ON SMALL BUSINESSES

While NPEs assert patents against defendants of all sizes, NPE assertions against small companies warrant particular attention for two reasons. First, small businesses suffer greater direct impact from patent lawsuits because they pay more litigation costs relative to their size.35 Moreover, the time and effort devoted to patent litigation detracts significantly from routine business operations and may hamper long-term growth.36

Second, small businesses constitute the majority of defendants in NPE litigation. Based on the RPX database,37 Bessen and Meurer estimate that the median-sized defendant in an NPE lawsuit has $10.8 million in annual revenue.38 Similarly, Colleen Chien reports that 66% of defendants have less than $100 million in annual revenue, and 55% have less than $10 million.39 The sheer number of alleged infringers also distinguishes assertions against small companies.40 It is common for NPEs to target dozens, if not hundreds, of small businesses based on a few patents.41 In a sense, the two factors are intertwined since NPEs are more likely to target small businesses precisely because small companies are more vulnerable to lawsuits.42 Given their rela-

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32. Shrestha, supra note 15, at 158.
33. The risk of losing cases runs to the law firms that represent NPEs as well, since many NPEs rely on law firms that operate on contingency fees. Schwartz, supra note 29, at 335; see also Shrestha, supra note 15, at 120 (“Given the enormous cost of litigating infringement suits, it is doubtful whether a rational NPE, or a contingency fee attorney, would sue a defendant if there was a low probability of a positive outcome.”).
35. Id.
36. Startups, supra note 4, at 4–5.
38. Bessen & Meurer, supra note 34, at 2.
40. For example, Innovatio IP Ventures has sent over 8,000 demand letters to small businesses that provide wireless internet service. See also Startups, supra note 4, at 15.
41. Id.
42. Startups, supra note 4, at 4 (finding that small companies often cannot pay monetary damages); cf. Bessen & Meurer, supra note 34, at 15 (finding that NPEs are willing to file many lawsuits to extract small payments).
tive lack of financial resources to litigate a patent, small companies are more likely to settle with an NPE regardless of the merits of the claim.43

A. Direct Impact of NPE Assertions Against Small Companies

Not only do small companies bear the brunt of NPE assertions, but patent litigation also has a greater detrimental impact on small companies for two main reasons.44 First, small companies have comparably fewer resources to defend against allegations of patent infringement.45 Bessen and Meurer estimate that the median cost of litigation for a small- or medium-sized company is around half a million dollars.46 For defendants who earn less than $10 million in total revenue,47 spending hundreds of thousands of dollars on a lawsuit can be crippling. In some cases, even successful defendants have found that the time and money devoted to patent litigation has destroyed their competitive edge, leaving them with a Pyrrhic victory.48 In light of these costs, small businesses are likely to settle with NPEs or resort to tactics such as “life-support,” in which defendants file the minimum amount of work necessary to prevent a default judgment.49

Second, NPE lawsuits have a greater operational impact on small companies. In one survey of companies that received NPE demands, over half of companies with less than $1 million in revenue reported that the NPE assertions have forced them to change their business strategy, delay hiring, and make other significant operational changes.50 Conversely, no business with revenues over $100 million reported any significant operational impact.51 NPEs tend to hit start-up companies especially hard,52 as early stage businesses often need several rounds of financing before they become profita-

45. *Startups*, supra note 4, at 1.
47. *Startups, supra* note 4, at 4–5.
48. C. Doughig & S. Lohr, *Patent Wars Among Tech Giants Can Stifle Competition*, N.Y. TIMES, Oct. 8, 2012, at A1 (discussing the case of Vlingo, a voice-recognition software firm that successfully defended a lawsuit for patent infringement, but devoted so much time and money that it was ultimately forced to sell the firm to a competitor).
49. *Startups, supra* note 4, at 11 (“‘[L]ife support,’ . . . [i]s to do the least that is required to avoid defaulting on the case and hope that larger companies with deeper pockets will take the lead.”).
50. *Id.* at 14.
51. *Id.*
52. Sarah McBride, *US Patent Lawsuits Now Dominated by ‘Trolls’*-Study, REUTERS* (Dec. 10, 2012), http://www.reuters.com/article/2012/12/10/patents-usa-lawsuits-idUSL1E8N A55M20121210 (“35 percent of startups that have raised $50 million to $100 million have been sued on a patent . . . as have 20 percent of the companies that have raised $20 million to $50 million.”).
ble. For example, Union Square Ventures, a New York–based venture capital fund, reports that almost one-third of the companies in its investment portfolio is facing patent assertions from NPEs. Investors, including venture capital firms, tend to favor companies with lower risk and will often avoid companies caught in patent litigation. The clean energy sector, which includes many growth-stage companies, has been particularly affected by NPE activity. CleanTech PatentEdge, an IP analytics firm for the clean energy sector, reports that NPEs own over 1,200 patents related to clean energy technology. Many of these patents have been asserted against clean energy companies such as LED manufacturers and smart electric grid producers.

B. NPEs Target Large Numbers of Small Businesses

NPE assertions against small companies do not depend on extracting large damage awards or settlements; instead, their strategy depends on volume. In general, small businesses settle NPE assertions for substantially


56. Startups, supra note 4, at 13 (“Pre-A round companies are really [ ] [s** out of luck]. It’s really a big problem. They can’t raise financing to defend the case. No one wants to fund an untested company. A piece of the funds, management time are [sic] bled out to lawyers. They can go out of business over [these kinds of suits].”).

57. See also Eric L. Lane, Keeping the LEDs on and the Electric Motors Running: Clean Tech in Court After eBay, 13 DUKE L. & TECH. REV. 1, 1–3 (2010).


60. Id.

61. Bessen & Meurer, supra note 34, at 15 (“Plaintiffs using this tactic are willing to settle for small payments, often no more than the amount a defendant would spend on legal fees to defend the case. As one such plaintiff lawyer put it, ‘An NPE intuitively understands that we could go for triples or home runs, but we can also go for singles and get a good return and work on other things.’”).

62. Ray Niro, who represents many NPEs at the law firm of Niro & Niro, discussed a subset of NPEs that target multiple defendants during an interview with IPwatchdog.com. Specifically, Mr. Niro stated that “they’re not as selective in what and how they enforce—they’re playing a numbers game. They don’t really care whether they win, lose, or draw, they get some lawyers to represent them and if I bring ten lawsuits and one turns out to be okay, that’s good for me.” Gene Quinn, An Exclusive Interview with Ray Niro, Mr. Patent Litigator, IP WATCH-
lower amounts than large companies.63 Bessen and Meurer found that the mean settlement amount—including damage awards—was $1.33 million for small- and medium-sized companies, in contrast to $7.27 million for large companies.64 Given the lower damage awards, NPEs hope to turn a profit by obtaining small settlements or damage amounts from many small business defendants. As such, NPEs that assert patents against small companies will often send demand letters to large numbers of alleged infringers with the aim of extracting a modest amount from each target.65

The most notable example of this tactic is Innovatio’s lawsuits against businesses that provide wireless Internet service.66 Innovatio IP Ventures was formed by Noel Whitley, a former Broadcom executive,67 and holds a number of patents on wireless network technology acquired from Broadcom.68 Since 2011, Innovatio has sent over eight thousand demand letters to retail outlets, retirement homes, hotels, coffee shops, and other businesses that provide wireless Internet to their customers, alleging that their wireless routers infringe Innovatio’s patents.69 These demand letters generally included an offer to license the patents for several thousand dollars,70 a relatively small amount in patent litigation. In the Northern District of Illinois alone, Innovatio filed lawsuits against hundreds of alleged infringers, often joining dozens of defendants in one lawsuit.71

Another example concerns Project Paperless, an NPE that owns two patents for scan-to-email technology.72 Rather than targeting manufacturers such as Xerox, Canon, or Hewlett Packard, Project Paperless launched a campaign against small companies that use commercial digital scanners in

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63. Bessen et al., supra note 18, at 12–13.
64. Id.
65. Id. at 15.
69. Id. at 9.
70. Id. at 10–11.
day-to-day operations. In one lawsuit against an Atlanta-based IT management firm, Project Paperless alleged damages of around one to two hundred thousand dollars.

As a final illustration, Acacia Media Technologies, a well-known NPE, filed a lawsuit naming over fifty alleged infringers, most of which operated adult entertainment websites. While Acacia may have selected an unlikely target for patent litigation, their strategy is paradigmatic. Acacia allegedly launched a plan that targeted small firms first and tried to convince them to settle. Accordingly, “[b]y selecting fragmented markets rather than going after big players like MSN or AOL, Acacia hoped to avoid getting embroiled in a debilitating legal battle.”

C. Implications of NPE Assertions Against Small Businesses

These cases illustrate an important point about NPE assertions, which is that NPEs will often have the ability to select defendants from a variety of potential infringers. Under 35 U.S.C. § 271, “whoever without authority makes, uses, offers to sell, or sells any patented invention . . . infringes the patent” and is liable for patent infringement. In the modern stream of commerce, products travel from manufacturers to distributors and retailers before they ultimately reach end-users. Any company in this chain of commerce could be held liable for patent infringement. For example, Innovatio had the option of suing large wireless router manufacturers such as Cisco or

77. Id.
79. Patent Claims Against Retailers 2, MORGAN LEWIS & BOCKIUS LLP (Sept. 2010), http://www.morganlewis.com/pubs/IP_PatentClaimsAgainstRetailers_WP_Sep2010.pdf (“The reason for this—and the single most important issue to keep in mind—is that U.S. laws impose liability for infringing a patent by making, using, or selling (or even offering to sell) the patented invention. Furthermore, patent infringement is a strict liability cause of action. In other words, it does not matter to the courts whether the retailer should have—or even could have—known of the asserted patent.”).
Netgear. Instead, Innovatio targeted thousands of small companies that purchased the routers and used them in their daily business operations. Likewise, Project Paperless asserted its patents against end-users of digital scanners rather than companies that actually designed and sold the accused products. Legally, a claim of patent infringement is no less valid because it is asserted against a small company that unknowingly uses an infringing technology product. The plain language of § 271 clearly states that any company that uses or sells a patented invention is liable for patent infringement, and patent law does not recognize an innocent use defense.

For some NPEs, targeting small businesses instead of large corporations offers direct financial rewards as well as strategic benefits. As previously discussed, small companies are more vulnerable to the costs of litigation and thus will often settle a patent claim regardless of the merits. By launching a campaign against a large number of small companies, NPEs can quickly collect settlement payments from multiple alleged infringers. Furthermore, license terms for a patent can be used in subsequent litigation to establish a reasonable royalty rate for damage calculations. As a result, NPEs may also target small companies to strengthen their position in future infringement claims by establishing a favorable royalty rate for their patents.

While patent law allows NPEs to selectively target small companies, public policy should divert litigation away from small companies given their important role in the U.S. economy. According to the Small Business Administration, small businesses generated 65% of new jobs in the last seven-

81. Id.
83. Roger D. Blair & Thomas F. Cotter, Strict Liability and Its Alternatives in Patent Law, 17 BERKELEY TECH. L.J. 799, 800-01 (2002) ("Patent infringement is a strict liability tort in the sense that a defendant may be liable without having had any notice, prior to the filing of an infringement action, that her conduct was infringing. In other words, innocent (i.e., unintentional or inadvertent) infringement is not a defense to a patent infringement claim, and a court usually will enjoin the defendant from infringing even though she was put on notice only by the filing of the lawsuit.").
85. Blair & Cotter, supra note 83, at 800-01.
86. Startups, supra note 4, at 15.
87. Id. at 4.
88. Id. at 15.
89. Parker Kuhl, Rescue Me!: The Attack on Settlement Negotiations After Resqnet v. Lansa, 26 BERKELEY TECH. L.J. 269, 271 (2011); see infra Section IV.B.
teen years and employ half of all private sector employees. Furthermore, a system that creates incentives for patentees to litigate against small companies appears to contradict Congress’s stated policy of fostering small business growth and development.

To some extent, the addition of 35 U.S.C. § 299 may address this important policy goal by making it more difficult to simultaneously litigate against multiple defendants. While there is no legislative history to suggest that Congress drafted § 299 for the benefit of small businesses, the law inadvertently helps small businesses by making it more difficult for patent holders to join dozens of small businesses in one lawsuit.


Sections I and II examined how the economics of NPE assertions lead to patent assertions against large numbers of small businesses. When patent assertions turn into patent lawsuits, NPEs will often consolidate alleged infringers into as few trials as possible. Joining multiple defendants offers several important advantages for NPEs, especially those that assert patents against small businesses. First, NPEs avoid the cost of litigating against each defendant separately. Given the high cost of patent litigation, the economies of scale achieved by consolidation are crucial for NPEs that target small businesses. From the NPE’s perspective, joining additional defendants in a single action increases potential revenue without a corresponding cost increase.

91. 15 U.S.C. § 631a (2011) (“For the purpose of preserving and promoting a competitive free enterprise economic system, Congress hereby declares that it is the continuing policy and responsibility of the Federal Government to use all practical means and to take such actions as are necessary...in order to: foster the economic interests of small businesses; insure a competitive economic climate conducive to the development, growth and expansion of small businesses; establish incentives to assure that adequate capital and other resources at competitive prices are available to small businesses; reduce the concentration of economic resources and expand competition; and provide an opportunity for entrepreneurship, inventiveness, and the creation and growth of small businesses.”).
94. Cf. Donald R. Banowit et al., AIA Effects on Parallel Section 337 Practice—Joinder Under the AIA, in 2 PATENT OFFICE LITIGATION § 17:14 (2012) (discussing how patent holders will be deterred from separately enforcing their patent against individual defendants if the anticipated recovery is not significant).
Second, by joining a large numbers of defendants, NPEs can hale more small businesses into court and make the threat of litigation more realistic.95 NPEs launch assertion campaigns by sending demand letters to numerous companies.96 These letters usually allege infringement of one or more patents and include an offer to license the asserted patents for a fee.97 The bargaining position of NPEs ultimately depends on their ability to launch a costly lawsuit if the alleged infringer refuses to pay the license fee.98 While receiving a demand letter may be intimidating, one in five start-up companies reported that they simply ignored the letter,99 suggesting that some companies realize that many NPEs are simply seeking a quick settlement payment rather than protracted legal battles.100 In colloquial terms, some small companies are “calling the bluff” because they know that NPEs are unlikely to follow through on all of their demand letters.101

Consolidating trials also offers important litigation advantages. By joining geographically diverse defendants in a favorable jurisdiction, NPEs reduce the likelihood that a defendant can transfer the case to another

95. There is an underlying question of whether NPEs that send demand letters to small companies actually have valid claims for infringement, or if they are making meritless demands to intimidate small businesses into settlements. NPEs could be conceivably asserting weaker claims against small businesses because they believe small businesses are more likely to settle frivolous lawsuits. Regardless, it is important to examine the economic and strategic reasons for targeting small businesses instead of large companies, irrespective of the merits of the claims.

96. Quinn Emmanuel Urquhart & Sullivan LLP, Best Practices for Defending Against Patent Trolls, JDSUPRA (July 26, 2011), http://www.jdsupra.com/legalnews/best-practices-for-defending-against-pat-72782/; Christopher T. Vrountas & Richard S. Loftus, Escaping the Snare of the Patent Troll’s Net, NiELSON KinDER & MOsSEAU P.C., http://www.nkms.com/resources/index.php?n=186 (last visited Feb. 12, 2013) (“Upon assembling its patent portfolio, the troll will send out demand letters to a host of businesses, alleging that they may be infringing on the troll’s patents. Often, these demand letters are short on specifics, make very broad claims, and are accompanied by an offer to reach a “reasonable” agreement with the business, which typically includes a “reasonable” licensing fee in the form of either monthly payments or a lump sum amount.”).

97. Quinn Emmanuel Urquhart & Sullivan, supra note 96.

98. Jason Rantanen, Slaying the Troll: Litigation as an Effective Strategy Against Patent Threats, 23 Santa Clara Computer & High Tech. L.J. 159, 166 (2006) (“Finally, a patent troll makes heavy use of the threat of litigation—and the threat of an injunction—to force a license of its patent. In order to make that threat a viable one, patent trolls often do, in fact, engage in litigation to enforce their patent. Without the ability to enforce their patent, a patent troll simply has an expensive piece of paper.”).

99. See Startups, supra note 4, at 10.

100. See, e.g., In re Acacia Media Techs. Corp., 2005 WL 1683660, at *2 (N.D. Cal. July 19, 2005) (describing Acacia’s strategy of seeking settlements from small companies, while avoiding legal battles with more established companies).

101. Cf. Startups, supra note 4, at 7 (suggesting that ignoring a demand letter may sometimes be the best strategy in responding to an NPE assertion). But see Quinn Emmanuel Urquhart & Sullivan, supra note 96, at 1 (advising against ignoring demand letters because it makes the defendant appear callous about the alleged infringement if the patent assertion does result in litigation).
jurisdiction, since there will be no district that is convenient for all the joined defendants.\textsuperscript{102} Furthermore, joining multiple defendants lowers the risk of an invalidity finding.\textsuperscript{103} Alleged infringers will often defend against a lawsuit by invalidating the asserted patents.\textsuperscript{104} Once a patent is declared invalid, the patentee is estopped from asserting it against other alleged infringers.\textsuperscript{105} By consolidating its cases, the NPE reduces the number of times that a court will examine the patent's validity, thereby reducing the likelihood that its patent will be declared invalid.

Prior to the AIA, a minority of jurisdictions held that a patent holder could join defendants under Rule 20(a) of the Federal Rules of Civil Procedure by simply asserting that all the defendants infringed the same patents.\textsuperscript{106} The AIA joinder provision expressly prohibits this practice\textsuperscript{107} and effectively forces NPEs to litigate against most companies individually. Under the new provision, the prospect of litigating against each small business defendant separately will likely dissuade many NPEs from launching campaigns targeting small companies. The remainder of this Section will compare the available joinder procedures both before and after the AIA and will discuss the practical implications of the new Act.

A. Joining Alleged Infringers Before the AIA

Before the AIA, district courts interpreted the standard for joinder in patent cases inconsistently.\textsuperscript{108} Under Rule 20(a) of the Federal Rules of Civil Procedure, defendants may be joined if the claims arise "(i) out of the same transaction, occurrence, or series of transactions or occurrences; and (ii) any question of law or fact common to all defendants will arise in the action."\textsuperscript{109} Most courts have interpreted Rule 20 as a two-pronged test that requires claims to (1) arise out of the same transaction or occurrence and (2) present common questions of law or facts.\textsuperscript{110} In patent cases, alleged infringement of the same patents may present similar issues of law or fact, but may not

\begin{itemize}
  \item \textsuperscript{102} See Bryant, supra note 7, at 691–92.
  \item \textsuperscript{103} \textit{Id.} at 704 ("If a patent troll files separate suits against multiple defendants claiming infringement of the same patent, one of the defenses that many, if not all, of the defendants will raise is that the patent is invalid. As follows from the Due Process Clause, a later defendant is not precluded from arguing that a patent is invalid, notwithstanding a prior finding, involving an unrelated defendant, that a patent is valid."); see also A.J. Davis & K. Jesien, \textit{The Balance of Power in Patent Law: Moving Towards Effectiveness in Addressing Patent Troll Concerns}, 22 \textit{Fordham Intell., Prop., Media \& Ent. L.J.} 835, 850 (2012).
  \item \textsuperscript{104} Bryant, supra note 7, at 704.
  \item \textsuperscript{105} \textit{Id.}
  \item \textsuperscript{107} 35 U.S.C. § 299(b) (2011).
  \item \textsuperscript{108} Bryant, supra note 7, at 696–97.
  \item \textsuperscript{109} \textit{Fed. R. Civ. P.} 20(a).
  \item \textsuperscript{110} Bryant, supra note 7, at 696–97.
\end{itemize}
constitute claims arising out of the same transaction or occurrence. For example, in *Philips Electronics v. Contec*, Phillips joined four companies manufacturing remote control units that allegedly infringed its patents. One of the defendants, CMT, moved to sever the trial, arguing that it produced the remote controls in a different factory and did not have a business relationship with the other defendants. The court found that the only commonality between CMT and other alleged infringers was that they allegedly infringed the same patents, “which is an insufficient basis to join unrelated parties as defendants in the same lawsuit.” The district court did not articulate a specific standard for joinder, but implied that defendants could be joined if they produced the same product and shared some form of business relationship.

While most jurisdictions required the alleged infringement to arise from the same transaction or occurrence, a minority of jurisdictions—most notably, the Eastern District of Texas—combined the two prongs of analysis under Rule 20(a). In *MyMail v. America Online*, the Eastern District of Texas denied America Online’s Rule 21 motion to sever the defendants. MyMail sued seven Internet service providers based on a single method patent for accessing a computer network. One defendant moved to sever the claims, citing *Phillips Electronic*, among other cases, to support the proposition that “acts of infringement by separate defendants do not satisfy the same transaction requirement.” The court, however, rejected this proposition and reasoned that the “same transaction or occurrence” requirement is satisfied if “there is some connection or logical relationship between the various transactions or occurrences,” clarifying that “[a] logical relationship exists if there is some nucleus of operative facts or law.” From this reading of Rule 20(a), the court held that alleged infringement of the same patent raises common legal questions, such as claim scope, and constitutes a sufficient basis to join multiple defendants. A number of jurisdictions adopted

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113. *Id.*
114. *Id.*
115. *Fed. R. Civ. P. 21* (stating in part that “[o]n motion or on its own, the court may at any time, on just terms, add or drop a party. The court may also sever any claim against a party”); *MyMail, Ltd. v. Am. Online, Inc.*, 223 F.R.D. 455, 456 (E.D. Tex. 2004).
116. *Id.* at 455.
117. *Id.* at 455 n.1.
118. *Id.*
119. *Id.* at 455–56.
120. *Id.* In another example, the Eastern District of Texas found that when a plaintiff alleges that multiple defendants have infringed the same patents, “there will be significant
the *MyMail* interpretation of Rule 20(a), including the District of Kansas,\(^{121}\) the Northern District of Texas,\(^{122}\) and the Eastern District of Louisiana.\(^{123}\)

While only a minority of districts followed *MyMail*, the broad reach of personal jurisdiction in patent cases allows NPEs to forum shop extensively.\(^{124}\) For example, small companies that sell products through the Internet are often subject to jurisdiction in faraway and patentee friendly districts.\(^{125}\) Given the inconsistent interpretations of Rule 20(a) prior to the AIA, NPEs could often avoid the higher standard for joinder by suing defendants in districts that joined defendants based solely on commonly infringed patents.\(^{126}\)

### B. Joining Alleged Infringers After the AIA

To introduce a uniform standard,\(^{127}\) Congress drafted a new joinder provision for patent cases in § 19 of the AIA, which came into effect as 35 U.S.C. § 299 on September 16, 2011.\(^{128}\) Section 299 largely tracks the language of Rule 20(a) and states that accused patent infringers may be joined only if the claims arise out of the same transaction and occurrence relating to the making, using, importing, or selling of the same accused product and that questions of fact are common to all defendants.\(^{129}\) More importantly, 35 U.S.C. § 299(b) specifically provides that "accused infringers may not be joined in one action as defendants . . . based solely on allegations that they each have infringed the patent or patents in suit."\(^{130}\) The legislative history of the AIA reveals that Congress intended to abrogate the *MyMail* line of overlap among the issues of claim validity, claim construction, and claim scope. Severance and transfer would create duplicative proceedings on the same patents, unnecessarily wasting judicial resources." Innovative Global Sys. LLC v. Tpk. Global Techs. L.L.C., 6:09-CV-157, 2009 WL 3754886 (E.D. Tex. Oct. 20, 2009).


127. *Id.*


130. *Id.*
cases. With § 299, Congress effectively prohibited the practice of joining defendants based solely on the alleged infringement of the same patents.

Thus far, § 299 has largely succeeded in bringing uniformity to the joinder standard in patent litigation. In Phoenix Licensing v. Aetna, the Eastern District of Texas determined that, in light of § 299, a patentee cannot join multiple defendants based solely on alleged infringement of common patents. In Phoenix, an NPE named over forty alleged infringers of business method and software patents. The court determined that joining the defendants was not appropriate because the "AIA clearly requires an additional party to have sufficient facts in common with all defendants beyond sole allegations of patent infringement. . . . Section 299(b) clearly states that the common question of fact must extend beyond the allegations of patent infringement." Small businesses that only sell or use accused products have a further advantage under the new joinder provision. Under § 299, courts have found that sales at different points in the stream of commerce represent separate transactions; for example, retailers cannot be joined with manufacturers just for selling the same accused products. In one case, Digitech Image Technologies, an NPE that held patents related to digital image technology attempted to join over forty camera retailers and manufacturers in the Central District of California. Digitech argued that its claims arose from a single series of transactions because the camera retailers all sold infringing products from the same manufacturers. The court rejected this argument, finding that separate sales of the same accused product constitute separate transactions.

Likewise, in Mednovus v. QinetiQ, the court found that joinder was not appropriate for alleged infringers who sold different products. In Mednovus, the patentee joined a product manufacturer with two of its distributors. While the retail defendants sold largely different products, the patentee alleged that there was some overlap. The court stated that "Plain-
tiffs' allegations that each Defendant infringed on a different set of products fails § 299(a)(1)'s requirement that Plaintiff's right to relief arise out of producing or selling the same accused product."  

Additionally, the court found that even if the defendants sold the same product, the sale between the manufacturer and the distributor and the sale between the distributor and the end-user would not constitute the same transaction or occurrence.

Conversely, courts have allowed joinder under § 299 if the alleged infringers have a close working relationship related to the same accused product. In Omega Patents v. Skypatrol, the court denied a motion to sever a distributor of vehicle tracking technology from its manufacturer. One of the alleged infringers, Enfora, produced vehicle-tracking technology that was sold to a distributor. Upon receiving such technology, the distributor "reconfigures, modifies, and rebrands the same product—using information and documentation provided by Enfora—for distribution under its own name." The court found that in this case, joinder was appropriate given the close working relationship between the manufacturer and the distributor, which constituted a single series of transactions and gave rise to common questions of fact.

In practice, § 299 forces NPEs to litigate against most small companies in separate trials. While Omega Patents indicates that courts will still join companies with a close working relationship, the AIA prohibits courts from joining large numbers of defendants based solely on commonly infringed patents or the sale of similar products. As a result, NPEs will ultimately face higher costs when asserting patents against small companies. Furthermore, it will be more difficult for NPEs to prevent small businesses from transferring cases out of patentee-friendly jurisdictions because individual defendants, especially small business defendants with offices in a single location, will be able to show a more convenient venue for trial.

IV. THE NPE RESPONSE TO § 299

Critics of § 299 argue that it will have a minimal impact on NPE activity because patent holders can circumvent the new limitation on joinder through the International Trade Commission ("ITC") and Multi-District Liti-
These studies, however, neglect to consider how the joinder provision may affect the distributional impact of NPE assertions. First, it is true that NPEs will likely file more complaints against alleged infringers in the ITC, which is not subject to the AIA’s joinder provisions.5 On the other hand, NPEs that assert patents against small companies are less likely to turn to the ITC because users and distributors of technology can usually switch to substitute products if an NPE obtains an exclusionary order.152 Second, NPEs may consolidate cases by centralizing pretrial proceedings through MDL.153 Yet this tactic will offer very limited benefits to NPEs that assert patents against large numbers of small businesses, since the NPE will still need to try each case separately, often in different jurisdictions.

A. Turning to the ITC

The ITC is an independent administrative agency that investigates allegations of unfair trade practices and exercises in rem jurisdiction over all products imported into the U.S.154 Additionally, 19 U.S.C. § 1337 gives the ITC authority to exclude importation of any articles that infringe a valid U.S. patent.155 Since the Supreme Court outlined the four-part test for injunctions in patent cases in eBay v. MercExchange,156 the ITC has become an increasingly popular venue for NPE patent litigation. Unlike district courts, the ITC is not subject to the eBay holding and may prohibit importation of infringing products without undertaking the test for a permanent injunction.157 Addi-

155. 19 U.S.C. § 1337(d) (2011) (“If the Commission determines . . . that there is a violation of this section, it shall direct that the articles concerned, imported by any person violating the provision of this section, be excluded from entry into the United States . . . .”); accord id. § 1337(a)(1) (defining the importation of a product that infringes a valid and enforceable U.S. patent as a violation of this section).
156. eBay Inc. v. MercExchange, L.L.C., 547 U.S. 388, 391 (2006) (“According to well-established principles of equity, a plaintiff seeking a permanent injunction must satisfy a four-factor test before a court may grant such relief. A plaintiff must demonstrate: (1) that it has suffered an irreparable injury; (2) that remedies available at law, such as monetary damages, are inadequate to compensate for that injury; (3) that, considering the balance of hardships between the plaintiff and defendant, a remedy in equity is warranted; and (4) that the public interest would not be disserved by a permanent injunction.”).
tionally, the AIA joinder provision does not apply to the ITC because ITC investigations are not civil actions under Title 35 of the United States Code.\textsuperscript{158} Multi-defendant litigation at the ITC remains common and will likely increase in the years following the implementation of the AIA. While there are no empirical studies on the size of respondents at the ITC, one study of ITC complaints from 1995 to 2007 found that 57\% of domestic respondents were publicly traded companies,\textsuperscript{159} suggesting that most respondents are larger companies.

Despite the ability to join multiple defendants, NPEs are not likely to hale small businesses into the ITC. Unlike district courts, the ITC cannot grant damages.\textsuperscript{160} Instead, NPEs use the ITC to engage in patent hold-up,\textsuperscript{161} a strategy characterized by using the threat of an injunction to drive up royalty rates.\textsuperscript{162} Patent hold-up strategy is particularly effective against companies that have made significant investments into designing, manufacturing, and marketing a product.\textsuperscript{163} NPEs will allege that one component of the product has infringed a patent.\textsuperscript{164} The allegedly infringing component is often a small portion of the overall product, but it may be vital to the product’s operation.\textsuperscript{165} Faced with an ITC exclusionary order, a producer has several options: (1) stop importing the infringing product, which may mean losing investments in research and development (“R&D”) and overseas production capacity; (2) redesign the infringing product, which often involves more R&D money and may not even be feasible; or (3) negotiate for a license.\textsuperscript{166} Therefore, even if the patent is not valuable by itself, the alleged infringer will often pay a high license rate to avoid an exclusionary order,\textsuperscript{167} and NPEs rely on this dynamic to obtain high royalty rates from producers.

By comparison, few small companies have made extensive R&D investments in any particular product. Downstream sellers and users of technology

\begin{footnotesize}
\textsuperscript{158} Thomas Martin, \textit{The International Trade Commission—A More Desirable Venue For Patent Infringement Actions In The Wake Of The America Invents Act}, 10 \textsc{Baker Botts Intellectual Property Report} 2 (2013), \textit{available at} http://www.bakerbotts.com/file\,upload/IPReport201302-TheInternationalTradeCommission.htm (“Section 299 applies only to ‘civil actions’, which are heard by Article III, or judicial, tribunals. By contrast, the ITC is an Article I, or legislative, tribunal that hears only those actions enumerated by Congress in the Tariff Act.”).


\textsuperscript{160} Dolan, \textit{supra} note 154, at *11, *19.

\textsuperscript{161} \textit{Id.} at *18.


\textsuperscript{163} \textit{See} Lemley & Shapiro, \textit{supra} note 162, at 1992–93.

\textsuperscript{164} \textit{Id.}

\textsuperscript{165} \textit{Id.}

\textsuperscript{166} Dolan, \textit{supra} note 154, at *19-22.

\textsuperscript{167} Lemley & Shapiro, \textit{supra} note 162, at 1992–93.
\end{footnotesize}
can usually switch to substitute products if an NPE obtains an exclusionary order against an infringing component. As stated in Section III, Project Paperless is an NPE that sent demand letters to small businesses for using certain digital scanners.\textsuperscript{168} Suppose that Project Paperless threatened defendants with an exclusionary order from the ITC, instead of a lawsuit in district court. If the ITC then granted an exclusionary order over the accused scanners, it would have effectively prohibited Xerox, Canon, and other manufacturers from importing their scanners, dealing a significant blow to these companies. Conversely, small businesses that use scanners in their daily business would not be liable for damages and could continue to use the technology or purchase non-infringing scanners as necessary. In this scenario, few small businesses would likely be willing to negotiate with an NPE to remove an exclusionary order, thus limiting the ITC’s utility to NPEs.

B. Pretrial Centralization Through Multi-District Litigation

Some commentators have also suggested that the availability of MDL will minimize the impact of 35 U.S.C. § 299.\textsuperscript{169} MDL is governed by 28 U.S.C. § 1407, which states that “[w]hen civil actions involving one or more common questions of fact are pending in different districts, such actions may be transferred to any district for coordinated or consolidated pretrial proceedings.”\textsuperscript{170} For patent cases, common questions such as claim construction may be consolidated through MDL.\textsuperscript{171}

The Judicial Panel on Multi-District Litigation (“JPML”) determines transfers in MDL. The JPML consists of seven federal judges selected by the Chief Justice of the U.S. and has the responsibility of selecting cases with common questions of fact that are pending in different districts for pretrial consolidation.\textsuperscript{172} The pretrial proceedings are transferred to a single district court selected by the JPML.\textsuperscript{173} In theory, after pretrial proceedings are complete, the transferee court will remand the cases to the transferor district courts for trial.\textsuperscript{174} In practice, the majority of cases will be disposed of by settlement or a judgment on a dispositive motion before the cases are remanded.\textsuperscript{175}

\textsuperscript{168} Michael Rundle, \textit{Project Paperless: American ‘Patent Troll’ Demands $1,000 Per User of Scanners}, 
\textit{HUFFINGTON POST UK} (Jan. 3, 2013), http://www.huffingtonpost.co.uk/2013/01/03/project-paperless-scanner-1000-dollars_n_2401204.html.

\textsuperscript{169} Quinn Emmanuel Urquhart & Sullivan LLP, \textit{supra} note 150.


\textsuperscript{172} \textit{Id.}

\textsuperscript{173} Daniel A. Richards, \textit{An Analysis of the Judicial Panel on Multidistrict Litigation’s Selection of Transferee District and Judge}, 78 \textit{FORDHAM L. REV.} 311, 317 (2009) (finding that only 20% of cases are remanded to the original transferor districts).

\textsuperscript{174} \textit{Id.}

\textsuperscript{175} \textit{Id.}
Unlike the standard for joinder, the standard for centralization does not require a common transaction or occurrence. Rather, centralization is appropriate if the different cases share common questions of fact, for which commonly infringed patents will suffice. In a case involving several alleged infringers of a pharmaceutical patent, the JPML found that, because all of the pretrial matters involved a single patent, “[c]entralization under Section 1407 [was] thus necessary in order to eliminate duplicative discovery, prevent inconsistent pretrial rulings, and conserve the resources of the parties, their counsel and the judiciary.”

The JPML has explicitly stated that the AIA joinder provision does not apply to centralization under § 1407. In Bear Creek Technologies, which involved a patent for Voice over Internet Protocol technology, the patentee moved to consolidate multiple alleged infringers—including many of the major telecommunications companies—through MDL. One of the alleged infringers, Vonage, argued that the new provision of the AIA prevents the JPML from centralizing the cases. The JPML found that “the America Invents Act [did] not alter [its] authority to order pretrial centralization of this litigation.” The panel went on to note that transfer under § 1407 and joinder under § 299 have always operated under different standards, and there is no overlap between the two sections because § 299 is focused on consolidation for trial while § 1407 only encompasses pretrial proceedings. Finally, the JPML stated that “if Congress intended to amend Section 1407 it would have done so in a more direct fashion than Vonage now advocates.”

Likewise, in Body Science, the JPML centralized five separate infringement actions over the opposition of the defendants. Although the defendants manufactured different products, the JPML found that centralization would “allow a single judge—as opposed to the now five judges in five districts—to preside over discovery relating to the two patents at issue . . . and to consistently rule on challenges to the validity of those patents.”

While it is conceivable for NPEs to centralize cases against small businesses through MDL, it will likely remain a tool for use against larger corporations. As the JPML stated in Bear Creek, the key feature of MDL—and

177. Id.
178. Id. at 1376.
179. Bear Creek, 858 F. Supp. 2d at 1378–79.
180. Id. at 1376. 181. Id. at 1377–79.
182. Id. at 1378.
183. Id.
184. Id.
186. Id. at *1.
the reason why it is not subject to the AIA joinder provisions—is that it only consolidates pretrial proceedings. After the transferee court has completed pretrial proceedings, any remaining proceedings are remanded to the original jurisdictions. MDL allows NPEs to establish patent validity and claim construction at a single venue. This will reduce the risk of estoppel as well as limit discovery and the cost of pretrial proceedings. However, NPEs will still need to try the case against each individual defendant once the transferee court remands the cases to their original jurisdictions. For NPEs that assert patents against hundreds of small businesses, litigating against every alleged infringer will require a litany of trials across the country, and the cost of enforcing their patents may deter NPEs from suing small businesses. Additionally, the patentee cannot dictate the forum for pretrial proceedings in MDL, which represents a further disadvantage for NPEs.

While NPEs have been quick to adapt to changes in the law in the past, there does not appear to be any easy procedural way for NPEs to join large numbers of small companies at the present time. As such, the joinder provision will likely shift NPE litigation away from small businesses, potentially reducing the negative social impact of patent litigation.

V. SMALL BUSINESSES AS PAWNS: THE PROBLEM OF ROYALTY PADDING

The previous sections highlight how § 299 of the AIA will likely reduce the number of NPE lawsuits against small businesses. While it is unclear whether § 299 will reduce the aggregate impact of NPEs as Congress intended, it certainly limits NPEs' ability to achieve a profitable economy of scale against small businesses. Some NPEs, however, may still target small businesses to validate their patents and drive up the royalty rate of licenses in order to pursue larger companies. This strategy, sometimes known as "royalty padding," involves suing small defendants first and settling the lawsuits through licenses that carry low dollar amounts but represent high royalty rates. Subsequently, the NPE will target a large company and introduce the previous royalty rate as evidence to drive up the damage award. To discourage this tactic, the courts and Congress should discourage the use of licenses reached under the threat of litigation to demonstrate the reasonable royalty rate.

187. Bear Creek, 858 F. Supp. 2d at 1378–79.
188. Id.
190. See, e.g., Body Sci., 833 F. Supp. 2d at 1346.
191. Startups, supra note 4, at 5; Kuhl, supra note 89, at 273 ("Prior licenses can also provide evidence of nonobviousness to support a claim of validity.").
192. Startups, supra note 4, at 5.
In patent infringement cases, the most common method of finding damages is by determining a reasonable royalty rate for the patent. In Georgia-Pacific v. U.S. Plywood, the court outlined twelve factors used to determine a reasonable royalty rate for a patent license. The most important factor is the royalty rate “received by the patentee for the licensing of the patent in suit,” or in other words, previous licenses of the same patent. In most jurisdictions, prior licenses are only admissible if they are reached through an arms-length transaction, without the threat of litigation. A 2010 case in the Federal Circuit Court of Appeals, however, raised doubts regarding this rule. In ResQNet v. Lansa, the Federal Circuit Court of Appeals found that litigation-induced licenses can be more probative of the reasonable royalty rate than non-litigation-induced licenses. Subsequent courts have read this to mean that litigation-induced licenses are no longer precluded from evidence, opening the door for NPEs to use these licenses to demonstrate a reasonable royalty rate. While litigation-induced licenses may be probative, courts need to account for the relative bargaining positions of the parties that negotiated the previous license. Licenses between NPEs and small companies, reached after a demand letter or other threat of litigation, are likely the result of unequal bargaining positions and should not be used to determine future royalty rates. This rule would help remove the incentive to target small businesses merely to validate the patent or drive up subsequent royalty rates.

193. Patent Litigation Study, supra note 22, at 11 (finding that reasonable royalty rate is used to determine damages in 81.9% of cases).
195. Id.
196. See, e.g., Wang Labs., Inc. v. Mitsubishi Electronics Am., Inc., 860 F. Supp. 1448, 1452 (C.D. Cal. 1993) (“It is a century-old rule that royalties paid to avoid litigation are not a reliable indicator of the value of a patent, and should therefore be disregarded when determining reasonable royalty rates. This is because royalties paid under threat of suit may reflect the licensee’s desire to avoid the risk and expense of litigation.”).
198. The court compared litigation-induced licenses that only involved the claimed invention with non-litigation-induced licenses that conveyed broader rights than the asserted patents and concluded that the litigation-induced licenses were a better measure of reasonable royalty. Id.
CONCLUSION

In the wake of the financial crisis and the 2008 recession, many in Congress have promoted a policy of small business growth. There is a perception that legal and compliance costs inhibit business development, and the federal government has responded with deregulation. While deregulation may play a role in small business growth, Congress and the courts should also address problems in the litigation system that create incentives to target small businesses because of their financial and operational vulnerabilities.

In the past decade, there have been many proposals for patent reforms aimed at reducing overall NPE activity. Examples include establishing an independent invention defense and fee shifting in patent litigation cases. This author cautions against reforms that would systematically impose higher burdens on patentees. NPEs represent a broad group of patent holders, including both independent inventors and universities. Likewise, the patent portfolios of both large and small companies represent their ingenuity and investment. In a speech at the Eastern District of Texas Judicial Conference, Chief Judge Rader of the Federal Circuit Court of Appeals cautioned against focusing on patent trolls at the expense of “patent grasshoppers,” which he described as “the entity that is quick to steal the ‘inventor-ant’s’ work and research investment because he did no work himself and the winter of competition approaches. We can recognize the grasshopper because he refuses to pay any license fee until his legs and claws are held to the proverbial litigation fire.” As discussed in Section I, enforcing a patent through litigation is already a multi-million dollar undertaking for patent holders. If courts impose a higher burden on patent holders, such as by shifting legal fees if their patents are invalidated, then it will become even more difficult for inventors to capitalize on their ingenuity.

Rather than reforming patent law at the expense of all patent holders, Congress and the courts should craft policies that distinguish between patentees attempting to realize the value of their innovation, and groups that use

202. See, e.g., Samson Vermont, Independent Invention as a Defense to Patent Infringement, 105 MICH. L. REV. 475 (2006); Jay P. Kesan, Carrots and Sticks to Create a Better Patent System, 17 BERKELEY TECH. L.J. 763, 787 (2002) (“The final strategy is to create a one-way, pro-defendant, fee-shifting system if patent claims are invalidated or revoked in a litigation or opposition proceeding based on certain categories of prior art that are reasonably likely to be discovered by a diligent patentee.”).
204. Risch, supra note 25, at 467.
205. Kesan, supra note 202, at 787.
patent litigation as a predatory tactic to extract value from vulnerable parties. Section 299 takes a step in the right direction by making it more difficult for NPEs to exploit economies of scale to assert patents against small businesses.