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## Proposed U.S. Senate bill would limit patent lawsuit damages

East Bay Business Times - by [Marie-Anne Hogarth](#)

Technology giants like **Cisco Systems Inc.** say that large numbers of lawsuits and runaway damages in the patent arena are holding them - and American innovation - hostage.

They say they're being held captive by patent holding companies - sometimes called patent trolls - who acquire patents on small parts of technologies for the purposes of filing lawsuits and extracting settlements.

The emergence of these small players on the IT market over the last decade has changed the dynamic for big companies, who traditionally held large portfolios of patents and traded them with others making products, lawyers say. Unlike traditional competitors, these patent-holding companies don't make products and aren't interested in striking deals, just litigating.

The tech giants and their allies in Congress have been working for eight years to reform patent laws to address what they see as a costly impediment to innovation, and they are closer than ever to passing legislation known as the Patent Reform Act of 2007 that among other things could limit damages in patent lawsuits.

They face determined opposition, however, from biotechnology and pharmaceutical companies that fear any limitation on damages would undermine their patents. These companies are worried that limiting damages would actually encourage infringers, since there would be less of a consequence for stealing inventions.

"On the tech side, there's an argument that the lawsuits are causing a huge headache, and there should be something done about the damages that are paid out," said Kenneth Chahine, a patent attorney and the CEO of **Avigen Inc.**, the Alameda-based biopharmaceutical company. "On the other hand, I don't know that the legislation, the way it is crafted, completely makes sense."

Among other things, the legislation would base royalties in patent-infringement cases on the market value of a product only if the patented invention is the predominant basis for market demand of the infringing product.

"Patent holders think they have a shot at a royalty that is based on the value of a complex product even though their patent only affects a small part of it," said Mark Chandler, general counsel for Cisco Systems. The San Jose networking company has 5,000 patents worldwide and 7,000 applications for new ones.

The bill's opponents disagree with the idea that a jury could really discriminate between the value of a patent and a product. "The analogy I would use is would anybody consider selling their house for the cost of construction rather than the value that a third party would pay?" Chahine said.

The proposed legislation would also require a judge - not a jury - to determine if infringement was deemed "willful," which allows for damages to be tripled. Currently, courts provide little guidance in determining what "willful" means, although some courts require proof that plaintiffs did put defendants on notice that they were infringing prior to a lawsuit.

This is resulting in some companies routinely sending out vague letters alleging others might be infringing, while other companies say they've stopped doing patent searches altogether for fear they might uncover material that would be used against them in a lawsuit.

There were 900 patent suits involving 1,500 defendants nationally in 1990, according to **Justia Inc.**, a legal media company in Mountain View. Last year, there were more than 2,800 suits with more than 8,000 defendants.

The impetus to reform patent laws came after some high-profile patent disputes that resulted in big damage awards captured Congress' attention.

Among the largest, Research in Motion Ltd., the Canadian maker of the BlackBerry, agreed in 2006 to pay the Virginia patent-holding company **NTP Inc.** a \$612 million settlement after a ruling almost shut down sales of the ubiquitous hand-held devices.

In the East Bay, **AT&T Inc.**, which employs about 7,000 in the area, was ordered last September to pay \$156 million to the Dallas holding company **TGIP Inc.** in a dispute over patents for pre-paid telephone cards. A judge later set aside the verdict.

Fremont's Asyst Technologies Inc., which manufactures equipment for semiconductor foundries, also won a \$74 million award last year

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after a decade-long battle over the patent for a tracking technology with Germany's **Jenoptik AG**, which makes optics and lasers. That verdict also was set aside.

"The effect of several high verdicts, whether they get overturned or not, is to encourage more litigation and more threatened litigation," Cisco's Chandler said. "It is clear from speaking to my peers that a huge amount of money is getting paid out in the aggregate, and that is (not) just to defend unmeritorious lawsuits ... but in payments of settlements."

Cisco says it spends \$40 million annually on the U.S. patent system - a large part on paying outside lawyers and settlements or awards in defensive litigation.

"I spend more on the patent system today than I do on the salaries of the 150 people who work for me, whose job it is to go out and sell our products and go out and negotiate contracts with our customers," Chandler said.

"Cisco, in the last three years of the last century, we were already a very large company at the time; we had five patent suits in the entire three-year period. All of them were with other companies in the industry," he added. "In the last three years, we had close to 30 suits that we had to defend - and only one of them involved a company that brought products to market."

The number of companies laying claim to similar patents is discouraging companies from making investments in certain areas for fear of being sued by companies that may hold patents sometimes merely for the purpose of litigation.

"That is the biggest issue that companies like Cisco and **3Com** (Corp.) are facing," said Jeffrey Lindgren, a shareholder with **Morgan Miller Blair** in Walnut Creek, who defends IT companies in patent litigation. "It has changed the nature of how they look at patents."

The standard for wireless Internet technology, 80211, is an often cited example.

"There are 73 different U.S. patent holders that claim you can't build equipment with that standard," Chandler said.

The tech companies are joined in their reform effort by other corporate giants, including **Wachovia Corp.**, **Citigroup** and San Ramon's **Chevron Corp.**

The biotech lobby has garnered support from labor unions, including the group representing patent examiners, and the Bush administration, who so far seem to have put the breaks on the legislation sponsored by Sen. Patrick Leahy, D-Vermont, and Sen. Orrin Hatch, R-Utah.

Other groups representing small inventors from a swathe of industries have also joined biotech companies in opposing the legislation, among them patent holders that don't fit the typical profile for so-called "patent trolls," like the University of California.

"The university has expressed concern about changes that would weaken a patent as an economic tool, because the university uses patents as an economic tool to induce investment in technology," said Palmer Martin Simpson Jr., with University of California Office of the General Counsel. He said the university licenses its patented technologies to get them into the market.

For smaller players, especially, there is also concern that limiting damages in patent trials would turn off investors who finance companies over the many years that it takes to develop a drug and take it to market, because lower damages might open the door to more patent infringements.

"Venture capitalists and inventors put a premium on patent portfolios," said Todd Gillenwater, vice president of public policy for the California Healthcare Institute Inc., a trade group for biomedical, academic and research institutions. "If a VC investor is approached to invest in a new technology and there is the sense that the patent portfolio that goes into producing the technology is less valuable, venture capitalists have indicated that they would be less inclined to make millions of dollars in investments."

Pharmaceutical companies say they might spend 15 years and half a billion dollars developing a single drug, and investors need assurance that they'll have a return on their investment down the line. The threat of hefty damages in a patent infringement suit provides that assurance today, industry groups say.

"Who would spend 15 years and half a billion dollars on something that in the end of the day they wouldn't have the exclusivity to recoup their investment?" Chahine said.

"I don't know what (IT) we'll be using in 15 years," he added. "But it probably isn't going to be iPhones and iPods. So in technology you don't have the same need of having (IP) protection 15 years down the line. Their business cycle and their invention cycle is much, much quicker and that is how fundamentally the two sides differ."

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#### Patent Reform Act of 2007 explained

The act, also known as Senate Bill 1145, would:

- Change the way damages are calculated in patent trials. For example, it would base royalties in patent-infringement cases on the market value of a product only if the patented invention is the predominant basis for market demand of the infringing product.
- It would require a judge - not a jury - to determine if infringement is "willful," which allows for damages to be tripled.
- It would establish a faster, more efficient procedure for challenging the validity of a patent after it has been issued by the U.S. Patent and Trademark



Office. This new "post-grant procedure" is important to computer giants and other companies who say that overloaded patent examiners are granting patents for inventions that are too similar to ones that are already patented. Biotech companies and other opponents of the legislation say these new procedures would provide competitors with an easy venue to repeatedly attack their patents.

- It includes language to ensure lawsuits are brought only in the district where a party resides or where a defendant has committed acts of infringement. This is important due to the number of cases that have been brought in venues such as the Eastern District of Texas, which has a reputation for big jury awards. The committee working on the legislation took steps to include language that states a company can't establish a venue in a state by simply incorporating there, but must show that it is the company's principle place of operation.
- It would put the U.S. patent system more in line with other countries by changing it from a "first to invent" to "first to file" system. This resolves disputes when it isn't clear who invented something.
- It would alter what materials might be cited by a patent examiner as the basis for rejecting a patent application.

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#### Advice from the lighter side of patent law

##### **Gregory Scott Smith**

**GSS Law Group**, Newark

Smith represented the inventors of the swingless golf club, for people who need a little help driving a ball down the fairway. The club uses a small explosive cartridge - similar to that found in a nail gun - to cause a piston to extend and drive the ball.

In a review of materials, the examiner from the U.S. Patent and Trademark Office produced a comic strip depicting a golf club with an explosive that would cause the ball to fly down the green. "I think he thought it was funny," Smith said.

PATENT ADVICE: "He didn't reject us based on it (the cartoon), but because it didn't show how to do it," Smith said.

In a less successful attempt, Smith represented the inventors of Kissing Candy in a patent application. This device used in the romantic sharing of food allowed two people to eat the same piece of chocolate and end their last bite in a kiss. "The examiner rejected the application saying it was too similar to the scene in "Lady and the Tramp," where both dogs eat the same piece of spaghetti and end up smooching.

##### **Stuart West**

**West & Associates**, Walnut Creek

West represented a retailer accused of infringing on the patent for a night light that changes colors. The retailer was never actually sued, however, because West just kept peppering the competitor with questions.

West said he kept his eyes on two things: the length of time that his client wanted to have the product on the shelves and the statute of limitations for filing the lawsuit. Altogether, he fended off litigation for his client for three years.

PATENT ADVICE: "Act quickly and don't let things drag on, and don't be fooled into waiting," West said.

##### **Morgan Tovey and William Overend**

**Reed Smith LLP**, San Francisco

The attorneys represented the nonprofit **Seed Corp.** after it was accused by another company, Pumpkin Masters, of infringing the company's patent for a pumpkin carving set.

The patent required a set of saws and drills, but the Seed Corp. kit has just one saw. Tovey recalls, "We took the position that we didn't require the patent because we had no set."

The plaintiffs retorted that a mathematical set might include just one tool or even none.

"Our position was that people who made pumpkin carving kits were not really immersed in that mathematical theory," Overend said. "And a set meant more than two." The Reed Smith attorneys prevailed.

PATENT ADVICE: "Make sure your legal argument passes the straight-face test," Overend said.

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