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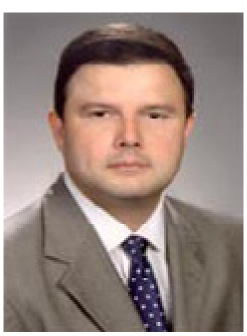
Jay Levine
Editor and frequent host of Porter Wright's *Antitrust Law Source*, Jay Levine is a partner based in Washington, D.C. Jay has extensive litigation experience in a variety of industries, particularly health care, pharmaceuticals and consumer products. Over the past few years, he has represented pharmaceutical companies in several antitrust and competition-related actions, many of which involved issues not previously litigated. Jay regularly represents clients before the government enforcement agencies, in both criminal and civil matters, and is currently defending clients in several different class actions.

Don Barnes
Don Barnes is also based in the Firm's Washington, D.C. office, where he chairs Porter Wright's Antitrust Law Practice Group. His practice is concentrated in antitrust/trade regulation law, agricultural cooperative law, trade association representation, and complex antitrust and commercial litigation. In addition to the agricultural sector, where he is recognized as one of the country's leading experts, Don has represented clients on antitrust matters in the defense, entertainment, high technology, health care, and construction industries.



John Monica
John Monica is an experienced litigation partner in the firm's Washington, DC office. His practice includes representing clients in complex antitrust class actions, as well as cases involving life sciences and products liability claims. He is also a nationally recognized authority on nanotechnology law, and wrote the full length legal treatise *Nanotechnology Law*, which was published by West/Thomson/Reuters in July 2009.

Molly Crabtree

Molly Crabtree is a partner based in Ohio's state capital of Columbus. She has significant experience representing both domestic and foreign companies with their complex litigation needs, including criminal antitrust investigations and litigation. One of Molly's litigation specialties is management and efficient analysis of electronically stored information to assist clients in effectively and defensibly protecting themselves from excessive discovery and production costs.

Ready. Set. Go. FTC patent troll study cleared for takeoff

August 15, 2014 | Jay Levine

Last week, the White House's Office of Management and Budget approved the FTC's request to study how patent assertion entities (PAEs or, less charitably, patent trolls) operate and to what extent they affect competition and innovation. The study was originally proposed in September 2013 and modified this past May in response to public comment.

As we described previously in a two-part series of articles (read part 1 and part 2), the study will be conducted in two segments and is designed to answer the following questions:

- How do PAEs organize their corporate legal structure, including parents, subsidiaries, and affiliates?
- What types of patents do PAEs hold and how do they organize their holdings?
- How do PAEs acquire patents; who are the prior patent owners; and how do they compensate prior patent owners?
- How do PAEs engage in assertion activity (i.e., how do they behave with respect to demands, litigation, and licensing)?
- What does assertion activity cost PAEs?
- What do PAEs earn through assertion activity?
- How does PAE patent assertion behavior compare to that of other entities that assert patents?
- As for when we can expect the study to be completed, an FTC spokesman was quoted as saying "sometime next year."

The FTC expects requests for information to be issued shortly. Recipients for the first part of the study will be 25 PAEs "that use different organizational models and assertion strategies." The requests will focus on the nature of the patent portfolios held, whether any are essential to industry standards, the costs of acquiring the patents and whether others share an economic interest in the portfolio. The FTC also is particularly interested in how the patents are asserted; thus, the requests will cover licensing and litigation activity as well as costs associated with the assertion.

For the second part of the study, the FTC will seek information from approximately 15 manufacturing firms and PAEs that have asserted patents in the wireless communications sector comparing how the various players assert their patent rights. Though some had requested that the FTC not limit this to the wireless communication industry, the FTC wants to limit its study because wireless communication "is relatively well-defined with a significant amount of assertion activity by PAEs, manufacturing firms, and NPEs."

The study will certainly be interesting, but we doubt it will stem the tide of states that will want to weigh in and propose some legislation to curtail PAE activity, especially considering the fact that Congress has not yet acted. As always, stay tuned!

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A new Ohio weapon against patent trolls?

July 28, 2014 | Dan Miller

Ohio may become the next state — after Virginia, Georgia, and thirteen other states — to take on the fight against patent trolls. A bill pending in Ohio's General Assembly, H.B. 573, would provide additional tools to thwart abusive tactics by patent trolls. But how useful those tools may prove in the battle against the problems they are intended to remedy is yet to be seen.

"Patent troll" is a pejorative term without a well-defined meaning. It is widely used to describe an entity that does not make or sell any products or services, but acquires patents from others and then seeks to exact licensing fees through abusive tactics, including meritless assertions of patent infringement. Because defending against patent infringement claims can be an expensive endeavor, those targeted by meritless lawsuits often opt to pay patent trolls' relatively low demands rather than aggressively defend against the claims in court. It is a decision that can leave business leaders steaming because, in their view, their companies are essentially being subjected to a shake-down by the threat of a meritless lawsuit.

In addition to frustrating business leaders, abusive practices in enforcing patents can stymie the economy. When companies are forced to settle meritless claims of infringement, they have less to spend on payroll, research and development, and other expenses that add value to the company and make it more likely to contribute to a thriving economy. Thus, patent trolls (as defined above) harm their targets, but they also negatively impact society more generally.

In light of the harm that patent trolls cause, federal and state governments have sought to act to protect businesses and the public. Unfortunately, correcting the problem is not as easy as it sounds. It is difficult to restrict the ability of patent trolls without also restricting the rights of patent holders legitimately seeking to protect their patent rights. This is particularly true of small independent inventors and universities who often do not produce products. Given the difficulty of creating reforms that specifically target patent trolls without also restricting the rights of other patent holders, it is not surprising that the federal response to patent trolls has been slow.

Though the U.S. House of Representatives passed a bill to address patent trolls in December with overwhelming bipartisan support, the Senate's anti-patent-troll bill was recently dropped unceremoniously. Senator Patrick Leahy, the chair of the Senate Judiciary Committee, said that he was essentially forced to drop the bill as Senate Majority Leader Harry Reid would not allow the bill to come to the Senate floor because groups opposed to the bill — including the bio-pharmaceutical industry, universities, and trial lawyers — could persuade other senators to filibuster the bill. Although Senator Leahy says that the Senate will revisit the anti-patent-troll bill later this year, others are less optimistic about the future of the federal legislation.

With Congress's effort apparently stalled, states are doing what they can to protect businesses from patent trolls. Several states have passed anti-patent-troll laws, and a greater number are considering such bills now. Many states penalize bad faith patent infringement claims asserted in demand letters sent into the state. Ohio may be the next state to do so.

If H.B. 573 is enacted, Ohio would prohibit a person from making "a bad faith assertion of patent infringement." To determine whether a patent infringement claim was asserted in bad faith, the bill directs courts to considers several factors, including whether the demand letter is vague or detailed, whether information regarding the patent is provided to the recipient of the demand letter upon request, whether the demand letter imposes an unreasonably short period of time for the recipient to pay the amount demanded, and whether the demand exceeds a reasonable estimate of the value of a license on the patent.

If a court determines that there is a reasonable likelihood that a patent infringement claim has been asserted in bad faith, the court can require an alleged patent troll to post a bond to cover the targeted alleged infringer's expected cost to litigate the case. If the target ultimately prevails and proves bad faith assertion of patent infringement, it can ask the court for a host of remedies, including injunctive relief, compensatory damages, costs, attorneys' fees, and punitive damages.

H.B. 573 would also authorize the Ohio Attorney General to commence a civil action against patent trolls who violate the statute.

H.B. 573 provides several new remedies, but it is far from certain to what extent H.B. 573 and similar laws in other states would actually provide protection from patent trolls. First, it is not clear to what extent states have the power to condition the ability of patent holders to enforce their rights in a federal court. Additionally, though states may have good intentions, legislation such as H.B. 573 might negatively impact the legitimate rights of non-troll patent holders to protect themselves against infringement of their patented inventions.

Apparently recognizing the limitations of state anti-patent-troll legislation, the attorneys general of 42 states wrote to Senator Leahy and three other senators in February, urging the Senate to pass patent reform. In their letter, the attorneys general recognized the importance of pending Congressional patent troll legislation, and they supported "structural federal patent litigation reform, which would create an environment in which abusers of the patent enforcement system cannot thrive." However, with Senator Leahy being forced to drop the Senate's anti-patent-troll bill only few months after receiving the AGs' letter, Ohio may wait for some time for federal legislation to complement H.B. 573.

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Patent troll moves forward with antitrust claim against defensive anti-troll

December 19, 2013 | Karri Allen and Jay Levine

Can a group of defendants refuse to settle with a non-practicing entity (NPE)? Can they collectively refuse to license patents from a "troll"? Or does that refusal subject them to antitrust scrutiny? These are the issues at the heart of a Northern District of California case: *Cascades Computer Innovation LLC v. RPX Corp.*

Cascades manages a portfolio of patents and filed suit against a number of large technology companies for infringement. Those companies are members of RPX Corporation (RPX), a defensive patent aggregator formed to protect its members from NPEs who file infringement claims. When RPX, on behalf of its members, failed to reach a licensing agreement with Cascade, Cascade sued RPX and its members — including Dell, HTC, LG, Motorola and Samsung — claiming that defendants' alleged collective refusal to deal with it constituted an antitrust violation.

Not only is this case unique in that an NPE, or "patent troll" in some circles, is striking out at alleged infringers with an antitrust attack, but the case was dismissed with what many thought was no hope of revival. Alas, Cascades' amended complaint included enough additional facts to allow the case to move forward.

Original complaint dismissed
Cascades' original complaint alleged that RPX and its members formed a boycott not to license Cascades' patents in violation of the Sherman Act and related California state law prohibiting monopsonization (a buyers' monopoly) and conspiracies and attempts to monopsonize. *Cascades Computer Innovation LLC v. RPX Corp.*, 2013 U.S. Dist. LEXIS 10526 (N.D. Cal. Jan. 24, 2013). Cascades claimed that it was unable to license its technology patents, including one to optimize the popular Android operating system, to the manufacturer defendants because they allegedly agreed to:

- negotiate for any such licenses only through RPX;
- jointly refuse to license Cascades' patents;
- not negotiate a license with Cascades independently; and
- infringe on Cascades' patents.

According to Cascades, the defendants' goal was to force Cascades to abandon its licensing efforts, accept a below-market value price or go out of business from costly litigation. Cascades had previously sued the manufacturing defendants for patent infringement in the Northern District of Illinois.

The court dismissed the complaint, finding that the antitrust allegations were "threadbare recitals of conspiracy" that lacked answers to the basic questions of who, what, where and when. In light of the lack of detail, the court refused to presume that the alleged conspiracy made any economic sense. According to the court, the complaint was further defective because Cascades only alleged "parallel behavior" which, without more, does not support a claim for conspiracy to violate antitrust laws. The court also found that the complaint failed to allege sufficient facts to show that any injury suffered by Cascades was the result of unlawful conduct by defendants. The court granted the defendants' motions to dismiss but allowed the plaintiff another chance to amend its complaint.

Amended complaint survives

Surprising many in the industry, Cascades' amended complaint survived a renewed motion to dismiss. Alleging the same basic claims, the court found that the beefed up complaint alleged facts that raised a reasonable inference of a hub-and-spoke conspiracy to force below market pricing for Cascades' patent licenses through monopsonization of the market for these patent licenses.

For instance, the complaint alleged that RPX and Cascades had reached agreement on pricing, yet RPX later withdrew from the deal because at least one RPX member refused to pay the amount. Similarly, the court found sufficient allegations of a vertical agreement between RPX and the manufacturing defendants, including that no defendant responded to Cascades' individual offers. The amended complaint also cured another defect of the original complaint by alleging a relevant market. The defendants did win one concession in that the court issued an order to show cause why the antitrust action should not be stayed pending the resolution of the merits in the patent litigation in the Northern District of Illinois.

Time will tell whether other "patent trolls" will wield the antitrust sword any time a group of defendants choose to litigate and not attempt to negotiate a license. But the fact that this case is moving forward means that entire world of patent litigation and the issues swirling around NPEs, just got more interesting and complicated.

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FTC study on “patent troll” behavior: innovation enhancers or competition killers?

October 8, 2013 | Jay Levine

Executive Summary

Almost half of all infringement actions brought these days are brought by patentholders that do not practice the invention, but rather by holders who seek to capitalize on the value of the patent through either licensing fees or via damage awards in infringement actions. While simply asserting patent rights cannot be an antitrust violation, the manner in which these patent holders — referred to Patent Assertion Entities (PAEs) or sometimes, pejoratively, as “patent trolls” — amass their portfolios and assert their patents can raise antitrust concerns. Given the enormous toll that patent litigation takes on our innovation economy, the Federal Trade Commission has proposed a study “to understand how PAE behavior compares with patent assertion activity by other patent owners.” This post provides background on the issue and why PAEs are singled out separately from other types of patent holders. A subsequent post will discuss potential antitrust concerns with PAE activity, what information the FTC is seeking from PAEs and others, and what the study means for you.

Background

For years, patent law and antitrust law have butted heads because patent law, which grants the patentee the right to exclude, is the antithesis of antitrust law, which seeks to increase output and maximize consumer welfare. Although the Sherman Act, the federal government’s basic antitrust law, has been hailed as the “magna carta of free enterprise,” patent law is rooted in the Constitution and accordingly has emerged victorious when the two have come into conflict. Over the past decade, abuses of the patent system and the soaring cost of litigation has had many re-examine the traditional balancing of patent and antitrust policy. Much of the debate over the last several years has focused on two distinct areas — Standard Essential Patents (SEPs) and the activities of PAEs. The federal government has held workshops on both of these issues and is now, pursuant to Section 6(b) of the Federal Trade Commission Act, the FTC is proposing to collect non-public information from a number of industry participants in order to commence a research study that would investigate the impact of PAE activity.

In December 2012, the Federal Trade Commission and the Antitrust Division of the Department of Justice — the federal government’s two antitrust enforcers — jointly sponsored a workshop to understand better the impact of PAEs on innovation and competition. The workshop included representatives of PAEs, as well as some of their most vocal critics. Members of industry and academia identified several areas of potential harm, along with a number of areas of efficiencies. Universally, though, the belief was that the lack of empirical data on the true effects of PAE activity hampered effective policy-making and law enforcement efforts. To fill that knowledge gap, the FTC has voted to engage in a research study to better understand PAE activity and its costs and benefits. Unlike prior studies that focused only on publicly available litigation data, the FTC will used its Congressionally mandated authority to collect non-public information on licensing agreement, patent acquisitions, and costs and revenue data. The goal is that through collection of such non-public information a more accurate assessment of PAE activity can be made.

Why are they picking on PAEs?
Patent infringement is extremely expensive and is a huge drain on the time and resources of the defending company. So why pick on PAEs when the same could be said for any patent holder asserting its rights? According to one panelist at the workshop, 40% of infringement actions are now brought by "patent monetizers." A study cited at the workshop estimated that PAE activity imposed $29 billion in costs in 2011, only 25% of which "flowed back to innovation." Certainly, PAEs provide a unique benefit. They provide an ability for individual inventors and small start-ups to monetize their patents, which further spurs innovation. Yet, the litigation they commence can cripple a defendant's own ability to innovate, and may well chill future innovation for fear of running afoul of a patent in a nameless PAE portfolio.

PAEs have also become the focus of enforcement priorities because of the type of infringement actions they bring. For example, many PAEs assert longstanding patents against operating companies' existing products, a practice that some say result in "higher prices, reduced output, and stifled innovation for consumers." Similarly, it is believed that PAEs often assert vague patents, which are very difficult to defend against because the alleged infringers cannot identify the scope of those patents, and they often bring cases at a time when there is maximum lock-in and holdup. The Hobson's choice facing many defendants — defend the suit at huge costs and distraction or agree to unreasonable settlement terms — often results in settlements simply because they are the lesser of the two evils.

Additionally, one of the biggest differences between PAEs and other patent holders is the differing incentives to litigate. For example, patent holders that practice and market the invention (operating companies) are often reluctant to bring an infringement suit because such litigation is expensive, tends to provide a low return on investment, and invites counterclaims. Think "mutually assured destruction." PAEs, on the other hand, have almost every incentive to litigate because they can reduce their "per patent" enforcement expenses by including more patents in a suit. More importantly, however, there is no MAD deterrent because they do not practice any invention and thus do not run the risk of a countersuit.

Fundamentally, PAEs are seen as companies who acquire patents in order to assert them against others in the hopes of achieving a lucrative licensing arrangement or a significant damage award (or settlement) in resolution of litigation. Indeed, because of their aggressive nature and their readiness and willingness to litigate, PAEs are often pejoratively referred to as "patent trolls." The irony, of course, is that many large operating companies have themselves established PAEs, some for defensive purposes, while others use their affiliates offensively. Thus, which PAE is truly a "troll" depends on one's perspective. Whatever their moniker, the exponentially growing cost of their activity has caused the agencies to focus on their activity.

In the second of this two part series, we dig a bit deeper on the FTC's recently proposed study on patent assertion entity (PAE) activity. In Part 1, we covered some background on PAEs and why they are singled out separately from other types of patent holders. Here in part 2, we discuss potential antitrust concerns with PAE activity, what information the FTC is seeking from PAEs and others, and — importantly — what the study means for you.

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FTC study on "patent troll" behavior: innovation enhancers or competition killers? Part 2

October 14, 2013 | Jay Levine

In the second of this two part series, we dig a bit deeper on the FTC's recently proposed study on patent assertion entity (PAE) activity. In Part 1, we covered some background on PAEs and why they are singled out separately from other types of patent holders. Here in part 2, we discuss potential antitrust concerns with PAE activity, what information the FTC is seeking from PAEs and others, and — importantly — what the study means for you.

Potential antitrust issues

To place into context the entire concern with PAEs, as well as to better understand why the Federal Trade Commission is seeking the type of information it is requesting, we delineate briefly the potential antitrust concerns with PAE activity. It must be understood that a valid patent holder unquestionably has the right to exercise his/her patent, or to sit back and sue for infringement should another entity utilize the patent without permission. The mere assertion or enforcement of a PAE patent cannot, without more, constitute an antitrust violation. Nevertheless, a number of different antitrust concerns are implicated with PAE activity, the most prominent of which are presented below.

<u>1. Acquisition and licensing of patents</u>

A patent is an asset and, like any other asset, the more one acquires within a given market, the greater the concern that the acquirer will eventually garner market power and the ability to price its products/services above competitive levels. Or, in the patent context, license the patents above competitive levels. Though not a concern indigenous to PAEs, many such companies have amassed a large portfolio of patents and use it to threaten potential infringers, demanding portfolio-wide licenses. The problem with this can be several-fold. First, many PAEs refuse to disclose the patents they own or even which patents they believe are being infringed. Thus, potential defendants must either choose between expensive litigation or taking a portfolio-wide license, all the while never fully knowing whether their product infringed anything at all. Second, many PAE portfolios combine several weak patents with a few strong patents, thus boosting the exclusionary effect of the weak patents.

Third, acquisitions of patents by PAEs from operating companies may raise particular antitrust concerns when the operating company plays an ongoing role in the licensing of the patents. The operating company that transferred the patents can use the PAE to raise its rival's costs and allow it to engage in exclusionary conduct behind the scenes.

Fourth, the sheer size and breadth of some PAE portfolios may substantially raise barriers to entry. As the FTC stated back in 1997, the aggregation of numerous patents may "heighten barriers to entry by combining portfolios of patents and patent applications of uncertain breadth and validity, requiring potential entrants to invent around or declare invalid a greater array of patents."

Finally, as noted above, many PAEs demand portfolio-wide or package license agreements, conditioning the licensing of the allegedly infringed patent on the licensing of the entire portfolio. Such a practice may arguably violate the antitrust laws' prohibition on tying the sale or license of one product on the sale or license of another.

2. Ability to manipulate SSO and cause SEP issues

Though beyond the scope of this post, one of the thorniest issues in the patent-antitrust debate is standard essential patents (SEPs). As its name implies, SEPs are patents that have been incorporated in an industry-approved standard. Many of these standard have been developed through standard setting organizations that require patent holders prophylactically to agree to license its patents on fair, reasonable and non-discriminatory (F/RAND) terms. What constitutes F/RAND is currently a hot topic and being litigated in federal court. In any event, because the standard incorporating the SEP is widely employed, the lock-in costs are enormous. In other words, it may be prohibitively difficult and expensive to switch to a different technology within the established standard or to a different standard entirely.

Accordingly, the owner of the SEP has every incentive to "hold up" the companies that are using the standard, enabling it to exclude a competitor from a market or obtain a higher price for its use than would have been possible before the standard was set, when alternative technologies could have been chosen. Though enforcing SEPs is an issue in its own right, the issue can become exacerbated when it is owned by an PAE. For instance, as described above, many PAEs seek a portfolio-wide license even if the alleged infringement related to only a small fraction of the portfolio. If the portfolio includes an SEP, therefore, a portfolio-wide license demand may make the entire portfolio a de facto standard-essential portfolio.

Additionally, ownership of the SEP is often unclear. Though admittedly this is because of a flaw in the patent recordation system, as there is no requirement to use the PTO system, a PAE — the ownership of which is itself often unclear — can use this to maintain obscurity and avoid licensing obligations. Without truly knowing who controls the PAE and therefore the SEP, it is extremely difficult to determine whether the owner is bound to any F/RAND commitment that may have been given at the time the standard was developed. Indeed, the commitment would be associated with the then-SEP holder, not the SEP itself. Or consider the following. A PAE investor that is participating in a standard setting organization might promote a patent that the PAE controls, without anyone knowing the investor's affiliation with the PAE or that the PAE controls the patent. Once the standard has been adopted, however, the investor stands to gain when the PAE sues to enforce its patent rights free of any licensing obligations.

Another way in which PAEs can exacerbate the exclusionary effects of an SEP is a function of the difference between PAEs and operating companies. In other words, because PAEs do not manufacture or sell any product, they are less worried about retribution from a standard setting organization than would be an operating company. Consequently, PAEs may be less worried than operating companies about circumventing prior owners' F/RAND commitments.

What information they seek and from whom?

The FTC proposes to send information requests to approximately 25 PAEs. To compare PAE behavior with the behavior of other patent holders that assert their patents, the FTC also proposes sending information requests to approximately 15 other entities asserting patents in the wireless communications sector, including manufacturing firms and other non-practicing entities and organizations engaged in licensing.

The information requests are designed to elicit information to answer six questions:

1. How do PAEs organize their corporate legal structure, including parent and subsidiary entities?
2. What types of patents do PAEs hold, and how do they organize their holdings?
3. How do PAEs acquire patents, and how do they compensate prior patent owners?
4. How do PAEs engage in assertion activity (i.e. demand, litigation, and licensing behavior)?
5. What does assertion activity cost PAEs?
6. What do PAEs earn through assertion activity? (Request H)

Specifically, the information requests will seek information concerning:

- The response's author
- The company itself
- The patents held
- The portfolio as a whole
- The acquisition and transfer of the various patents held
- Any assertion of patents held
- Costs of patent acquisition and assertions
- Aggregate revenue

The information request is quite broad and detailed. *See the FTC's Notice and request for public comment*. For starters, it seeks information going back to 2008. Additionally, the request teases out the identity of the PAE's investors and further seeks to determine whether the PAE holds any SEPs within its portfolio. The request also seeks very detailed information about every act of patent assertion, including demands, litigation and licensing. Besides information, the requests also asks for broad categories of documents including, among other things: each license agreement entered into, documents relating to the rationale for each assertion made, documents relating to each patent acquisition and transfer, and all documents relating to the PAE's "reasons or business strategy for organizing the Patent(s) into Portfolio(s)."

What does this mean for you?

Obviously, recipients of the information request will be affected. The FTC estimates that a response can take between 90 and 400 hours, and could take longer depending on the size and complexity of the organization. But beyond that, the fact that such a study is being undertaken represents a relatively significant advancement in the debate involving the propriety of PAE activity specifically, and application of the antitrust laws to patent assertion activity more generally.

There is no question that patent litigation has exploded and that its costs impose an enormous burden on our economy and innovation. Equally true, the debate over the propriety of PAE activity — which at its core is simply asserting rights guaranteed by the Constitution and federal law — has become vitriolic. Indeed, some have suggested using RICO laws to push back against PAEs. See "*Here's how a law designed to fight the Mafia could stop abusive patent lawsuits*," Washington Post, Sept. 17, 2013; and "*Controlling patent trolling with Civil RICO*," Yale Journal of Law & Technology, Volume 11, 2009.

The question, therefore, is not whether there is a problem, but how big a problem it is. The FTC study will hopefully start to answer that question.

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