

Hearing before the
Senate Judiciary Committee
on
“Patent Reform: The Future of American Innovation”

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Chairman Leahy, members of the committee, my name is Bruce Bernstein. I am Chief Intellectual Property and Licensing Officer for InterDigital Communications Corporation and a long-time proponent of preserving and promoting American innovation. Thank you for the opportunity and honor to appear before you this morning to discuss the importance of strong patent rights to innovative and vital American companies like InterDigital. America’s patent system has been critical to InterDigital’s success and, more broadly, has helped shape the evolution of technologies and products used by billions of people around the world.

InterDigital is headquartered in King of Prussia, Pennsylvania, with major development facilities in Melville, New York. For over thirty years, InterDigital has been at the forefront of inventing and developing advanced wireless technologies and products that drive voice and data communications. Although we remain a relatively small company, our inventions are used in virtually every digital cellular phone, and we continue to invest heavily in ongoing research and development. As the inventor, owner and licensor of hundreds of US patents, InterDigital shares this committee’s commitment to improve the quality of issued patents and reduce the cost of patent litigation. However, we and others in the technology licensing community are deeply concerned that certain provisions of the Senate patent bill (S. 1145) would significantly undermine the enforceability, predictability and value of *all* patent rights and, in the process, encourage litigation and abuse. Of particular concern are proposals to mandate apportionment of damages and create a new and duplicative post-grant opposition system. We urge the committee to remove these and other problematic provisions from the bill and to limit legislative reforms to fair, balanced and judicious measures that will preserve the strong foundation of patent rights and remedies so essential to the future of American innovation.

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In my role with InterDigital, I head a small team that manages the company's intellectual property assets and our patent licensing business. I have over 15 years of experience in the intellectual property business and have developed and managed patent portfolios for a number of organizations, including universities, investment institutions, and both private

and public technology companies. Prior to joining InterDigital in 2005, I served as Vice President and Head of Patents at BTG International Inc., (BTG) where I developed and managed the company's physical sciences IP portfolio. Prior to joining BTG, I served as an associate at a number of law firms here in Washington, D.C. including Morgan Lewis & Bockius, LLP, Dickstein, Shapiro & Morin LLP and Finnegan, Henderson, Farabow, Garrett & Dunner LLP. Like many others involved in the patent and licensing businesses, I also have a background in technology; I earned my Bachelor of Science degree in Electrical Engineering from the University of Pennsylvania before earning my JD from American University.

Compared to other companies you may hear from today, InterDigital is a small company with less than 400 employees. But our size in human capital is not proportionate to our inventive capacity and global influence. The bulk of our staff is dedicated to research, development and engineering initiatives, and the majority of engineers have advanced degrees and decades of experience. Over the past three decades, our engineers have created many of the breakthrough inventions that have allowed InterDigital to make significant and ongoing investments in leading edge research and development for an increasingly competitive global market. Today, InterDigital holds over 3,000 U.S. and foreign issued patents combined. In addition, we have nearly 9,000 patent applications in process. Not surprisingly, we are passionate about a thoughtful approach to patent reform, and ever mindful that our ability to innovate and grow is directly dependent on the strength and health of America's patent system.

The wireless market offers tremendous challenges and opportunities. Today, it would be hard to imagine a world without mobile phones. Wireless technologies have changed the way we work, live, and play. By typical measures, the wireless market would be considered mature, but the reality is that the wireless industry is changing faster than ever before, with new technologies, products, applications, and services being introduced daily. As technologies, content, and devices blossom, the only limit on the opportunity for InterDigital is our engineers' imaginations.

At InterDigital, innovation is the DNA that runs through each of our employees. In the late 1960s, the company's founder recognized the enormous potential of cellular communications — quite prescient at a time when neither the Internet nor cellular phones were available. He assembled a group of engineers and incorporated in 1972. As his vision has evolved, InterDigital has remained a pioneer in advancing the wireless industry. When the rest of the world was working on existing analog technologies, we were already developing next generation digital technologies. When the rest of the world was working on existing voice technologies, we were working on advanced data technologies. While others were working on existing narrowband technologies, we were working on advanced broadband technologies. And, today, as most are grappling with the ever-growing library of current technologies -- 3G, WiMAX, or WiFi -- we are already working on solutions for seamless mobility between all standards, domestically and internationally. Our constant aim is to focus on the future of worldwide personal and business communications and to innovate for the public good.

Based on this innovation, we have built a worldwide patent licensing program with great success. Since 1992, manufacturers of some of the world's most popular brands, such as Nokia, Samsung, Sony, Ericsson, LG, NEC, Panasonic, Sharp and Research In Motion, have become our customers, and we have earned over \$1 billion in patent royalty and technology licensing revenues. In recognition of our successful licensing program, InterDigital received the prestigious Licensing Achievement Award from the Licensing Executives Society in 2006. Previous recipients of this award include Genentech (2004), the U.S. Department of Energy (2003), IBM Corporation (2002), Pfizer (2000), and Stanford University (1999).

Further, in addition to licensing our in-house patent portfolio, we commercialize our inventions by offering advanced products and technologies to manufacturers of mobile devices. This cycle of innovation—from technology inventions, to patent licensing and delivering products—is repeated with multiple technologies time and again. Indeed, our engineers are working today on solutions for the next generations of wireless technologies. Our experience and inventions reach across virtually all mobile and wireless standards. Our success in increasing the pace and breadth of our innovation reflects our fundamental commitment to remain a worldwide leader in the creation of pioneering technologies. To protect our ongoing new inventions, we have employed a comprehensive program of developing and protecting our intellectual property through the worldwide filing and issuance of our patents.

In addition to our internal research and development, InterDigital has a track record of successful co-development programs with leading companies around the world. Just in the last few years alone, we have worked side-by-side with our peers at Infineon (Germany), NXP (Holland), General Dynamics (US) and SK Telekom (Korea) to solve unique problems. We also work closely with several universities on advanced research and innovation projects.

The US Patent System

Our country's founders understood the importance of innovation to America's economic prosperity and growth. Significantly, they also recognized that true innovation requires the same incentives, and merits the same rights and remedies, as other forms of property. These principles - and the foundation of our patent system - are reflected in Article 1, Section 8 of the US Constitution, which gives Congress the power "To promote the progress of science and useful arts, by securing for limited times to authors and inventors the exclusive right to their respective writings and discoveries."

The US patent laws, first codified in 1790, were developed in order to encourage inventors to disclose their inventions to the public in return for a period of exclusive rights to their patented inventions. The resulting public disclosure of inventions encourages inventors to share their inventions rather than hoard them in private. This sharing of ideas in turn fosters further innovation by allowing other inventors to develop improvements and next generation technologies. Our country's continued technological leadership is evidence of our patent system's success.

The exclusive rights granted to an inventor have been recognized since the inception of the US patent system as being necessary to reward innovation and encourage disclosure of inventions to the public. But such rights are not awarded without condition. Instead, an inventor is only entitled to an exclusive patent right for a limited time for those inventions which meet the statutory requirements of patentability – namely, those inventions that are useful, novel and non-obvious.

These are the fundamental principles of this nation’s patent laws. As such, efforts to improve our patent laws through legislative reform should be consistent with these important precepts. InterDigital believes that despite dramatic developments in technology in recent years, the underlying and originating purpose of the US patent laws continues to this day. As such, it remains essential that our patent laws continue to reward innovation with a strong and predictable framework of rights and remedies. Furthermore, provided that an invention satisfies the stringent requirements of patentability, an inventor should be entitled to a scope of protection coextensive with the metes and bounds of his or her invention.

In practice, it is the examination process conducted by the USPTO which initially determines whether, and to what degree, patent protection should be afforded to an inventor. This process is shared between applicant and examiner and often involves a significant exchange of argument and explanation before the examiner renders his final decision on patentability. Through this dialogue, an inventor may provide arguments of patentability over “prior art” references that have been asserted by the examiner as evidence against patentability. Frequently, an applicant will recognize some similarity between the prior art reference and the inventor’s claimed invention and respond with a request to amend the claims in order to appropriately define the limits of the applicant’s invention.

Through this examination process, an applicant is either denied a patent or granted an exclusive right to the invention defined in the claims of the application. Usually, these patent rights are appropriately granted. Sometimes, however, they are not. Some suggest that this “error rate” has spiraled out of control. I do not agree. In fact, in 2006, the USPTO achieved its lowest error rate in 20 years - 3.5 percent, as well as a record low patent allowance rate of 54 percent. Even in cases of error, moreover, the patent is typically overbroad and not invalid in its entirety. In such situations, the solution is to reexamine or reissue the patent and adjust it to its proper scope.

Nevertheless, critics of our patent system are now advocating legislative measures that would create additional and more expansive opportunities to invalidate an issued patent (without giving the patent holder a fair means of appropriately adjusting the patent’s scope), and fundamentally change our system of remedies to significantly reduce the cost of patent infringement. The premise of these so-called reforms is that the patent system is broken; the market is flooded with poor quality patents that were erroneously granted; and that patent plaintiffs are predominantly speculators who abuse the system to extract inflated settlements and judgments from large, established manufacturers.

In InterDigital's view, claims of this type are grossly exaggerated and dangerous in their potential impact on our patent system. To recklessly impugn the overall quality of America's patent portfolio is to denigrate the contribution of our most innovative companies, a growing percentage of which are licensing-based, patent-rich firms like InterDigital. And to diminish the value and enforceability of all patent rights is to destabilize the very foundation of our knowledge-based economy. With so much at stake, InterDigital urges the committee to proceed with great care and deliberation before approving measures that could fundamentally devalue American patents and weaken our global competitiveness.

With that said, much of the Senate bill is commendable, particularly those measures that are carefully tailored to improve patent quality and mitigate the subjective and costly aspects of patent litigation. InterDigital supports these goals and appreciates this committee's attention and commitment in addressing these important issues. As noted above, however, we are gravely concerned that other aspects of the bill would undermine the strength, value and enforceability of patent rights and hence increase litigation rates significantly, along with costs to patent holders and patent users alike. ***Namely, InterDigital opposes proposals to (i) mandate apportionment of damages, (ii) introduce an open-ended and duplicative post-grant opposition proceeding that would permit a challenger to invalidate an issued patent based on a reduced burden of proof and without affording the patent holder an adequate opportunity to adjust its scope, (iii) grant the USPTO expansive and unprecedented substantive rulemaking authority, and (iv) allow, as a matter of right, interlocutory appeal of claim construction decisions.*** Beyond the detrimental impact of these measures on patent rights and litigation costs, we are concerned that such proposals would further burden already strained USPTO and judicial resources.

It is important to note that InterDigital's concerns are shared by a large and growing number of innovative firms, universities and researchers within a broad range of industry sectors, including the technology field that we inhabit. Indeed, in a recent letter to House and Senate leaders, InterDigital joined with more than 100 other patent stakeholders, including universities, venture capital firms, small and large technology businesses and research parks across the country, to voice a shared concern about the potentially damaging patent reform measures. The letter was signed by representatives of the electronics, telecommunications, life sciences, computer hardware, financial services, chemical and biotechnology industries.

Despite media claims to the contrary, the IT industry is absolutely not united in its support for mandatory apportionment, post-grant opposition or other measures that would fundamentally weaken patent rights. To the contrary, tech industry support for such measures appears primarily limited to large, incumbent manufacturers that are opportunistically using the phrase patent "reform" to justify legislation that would reduce their litigation costs and liability when they infringe third party patent rights. These big tech manufacturers are well aware that the threat of meaningful damages is often the only leverage that a small patentee possesses to secure a licensing agreement with a corporate

giant; and they are equally aware that a mandatory apportionment standard would all but eliminate that leverage. Similarly, these large manufacturers view the proposed post-grant opposition system as a means of tying up, and more easily “busting” inconvenient patents, through endless administrative challenges, with little or no downside risk. In essence, these large tech manufacturing firms are seeking to unwind the very exchange implicit between the inventor and society when he or she discloses his or her invention in the first place.

In the wake of *eBay* and other recent Supreme Court decisions, the negotiating strength of patent owners has radically diminished, particularly to the detriment of smaller, less resourced firms that license their patented innovations. Mandatory apportionment, post-grant opposition and similar legislative measures would, for many such innovators, drive the final nail in the coffin.

Apportionment of Damages

InterDigital urges the committee to preserve the existing flexible, market-based principles that govern the calculation of reasonable royalties, and to remove from the bill the proposed mandatory apportionment test, which would devalue patents and increase the prevalence, uncertainty and cost of litigation.

Under the Senate bill, a court must ensure that a reasonable royalty “is applied only to that economic value properly attributable to the patent’s specific contribution over the prior art,” except where a patent has been shown to be “the predominant basis for market demand for an infringing product or process.” Thus, in virtually every patent case involving complex systems, this mandatory apportionment of damages would be applied above all other factors that might otherwise influence the determination of a reasonable royalty, including a patentee’s history of negotiated royalty rates and other licensing terms. Although intended to guard against allegedly inflated damage awards, this mandatory apportionment test would represent a dramatic departure from the market-based principles that currently govern damages calculations. Even worse, it would result in unpredictable and artificially low damages awards for the majority of patents, no matter how inherently valuable they might be.

For innovative companies like InterDigital, mandatory apportionment would encourage free-riders and even existing licensees to risk litigation rather than pay, or continue paying, a market-negotiated licensing fee. As a result, it would undermine the market-based licensing negotiations between the inventor and patent user that have driven our nation’s innovation dynamic for more than 200 years. No longer will the market be the arbiter of our technology’s value; instead, a paid expert and court will be. There will be very little downside to “rolling the dice” and litigating before taking a license.

When coupled with the heightened *eBay*¹ standard for injunctive relief, a mandatory apportionment test would further weaken and destabilize our system of patent rights and

¹ *eBay Inc. v. MercExchange*, 547 U.S. ____; 126 S. Ct. 1837 (2006).

jeopardize the very existence of smaller firms with an innovation and licensing based business model. Since *eBay*, courts are increasingly reluctant to award permanent injunctions to patent holders (historically, the first line of defense against infringement), unless the infringement undermines competition for the patentee's product. In cases where a patent holder licenses the right to practice its patented technology to others, but does not practice the technology itself (as is often the case with smaller inventors and universities that lack the resources and infrastructure to manufacture their innovations), courts have, since *eBay*, shown an even greater reluctance to award permanent injunctive relief. As a result, many innovative firms will be forced to permit ongoing use of their patented technologies pursuant to a court-imposed compulsory license (without the benefit of important standard non-royalty license terms such as confidentiality) and a court-dictated royalty. In the post-*eBay* world, it is thus all the more important that Congress preserve the ability of patent holders to obtain adequate damages for patent infringement, as this will be the only viable remedy in many cases.

Significantly, Congress expressly and resoundingly rejected mandatory "apportionment" in 1946 when it adopted the existing statutory standard for calculating damages, codified in Section 284 of the Patent Act. During hearings on the issue, Congress and other experts noted that apportionment was an overly complex and wholly unworkable test, resulting in excessive litigation costs, extreme delays and unfair damages awards for all parties. One patent expert described mandatory apportionment accountings as "the great evil that has grown up around the patent system." And another expert observed that many cases requiring apportionment had "run from 10 to 20 years, [...] and others I have known have gone on for 20 years. Some now are running that have been running 20 years and all the people that started in the [apportionment] accounting are dead."² To revert back to an apportionment standard that was universally condemned more than 60 years ago would represent a major step backwards for our patent system -- the very antithesis of patent "reform."

In lieu of a mandatory apportionment test, Congress in 1946 sought to create a damages standard that would afford courts the necessary flexibility and discretion to determine a fair and appropriate level of damages in cases where a patent has been deemed valid and infringed. Congress's aim, as reflected in the 1946 hearings, was also to ensure that damages awards were sufficient to compensate the patentee for past injury and to deter others from committing similar acts of infringement. With these time-honored and market-based principles in mind, Section 284 of the Patent Act provides that "Upon finding for the claimant the court shall award the claimant damages adequate to compensate for the infringement, but in no event less than a reasonable royalty for the use made of the invention by the infringer, together with interest and costs as fixed by the court." Under this provision, a "reasonable royalty" -- i.e., the amount that the patentee would have obtained from licensing its patent -- is the *minimum* amount of damages payable to the patentee. Any lesser amount of damages would reward and encourage

² Vincent P. Tassinari, *Compiled Legislative History of 35 U.S.C. §284: The Patent Compensation Statute*, 31 West. L.A. L. Rev. 45 (2000).

widespread continued infringement, increase costly litigation and ultimately diminish the value of the patent.

In some cases, a patent owner may have licensed the infringed patent to others, thereby effectively setting an “established royalty” as the minimum baseline for damages awarded to the patent holder. However, in cases where there is no established royalty, courts have historically applied a wide variety of factors to determine the royalty the parties would have agreed to in a hypothetical negotiation. In the seminal *Georgia-Pacific* case³, the court identified 15 factors that courts had historically deemed relevant in determining a reasonable royalty, the first and most important being a history of “licensing proving or tending to prove an established royalty.”

Under *Georgia-Pacific*, once a patent has been deemed valid and infringed, the courts are provided the flexibility to consider the relevant market factors that would be at issue during a negotiation to arrive at a reasonable royalty for use of the *invention*. Under this established market-based approach to calculating an equitable award of damages, the court is provided the discretion to determine which factors should be considered for a particular patent and what relative weight should be given each factor. Indeed, in enumerating the list of potentially relevant factors, the *Georgia-Pacific* court explicitly rejected any kind of mandatory formula or test in deciding the relevance or relative weight of any one factor, other than an established royalty:

The drawing of proper conclusions from conflicting evidence concerning the amount of a reasonable royalty has been said to call "for the exercise of judicial discretion by the District Court." *General Motors Corp. v. Dailey*, 93 F.2d 938, 942 (6th Cir. 1937). Both sides agree that this Court has a broad range of judgment in evaluating the relevant factors. In the present case there is a multiplicity of inter-penetrating factors bearing upon the amount of a reasonable royalty. ***But there is no formula by which these factors can be rated precisely in the order of their relative importance or by which their economic significance can be automatically transduced into their pecuniary equivalent.*** In discharging its responsibility as fact finder, the Court has attempted to exercise a

³ *Georgia-Pacific Corp. v. United States Plywood Corp.*, 318 F. Supp. 1116 (S.D.N.Y. 1970). The *Georgia Pacific* factors include, for example: (i) the rates paid by the licensee for the use of other patents comparable to the patent in suit; (ii) the nature and scope of the license, as exclusive or non-exclusive; or as restricted or non-restricted in terms of territory or with respect to whom the manufactured product may be sold; (iii) the licensor's established policy and marketing program to maintain his patent monopoly by not licensing others to use the invention or by granting licenses under special conditions designed to preserve that monopoly; and (iv) the commercial relationship between the licensor and licensee, such as, whether they are competitors in the same territory in the same line of business; or whether they are inventor and promoter.

discriminating judgment reflecting its ultimate appraisal of all pertinent factors in the context of the credible evidence. (emphasis added)

This flexible, market-based process for calculating a reasonable royalty has been applied in thousands of patent cases. Congress should not depart from this well-established methodology, particularly when the proposed apportionment amendments appear to ignore hard-won lessons about the dangers of rigid damages rules and formulas. Indeed, by resurrecting a mandatory apportionment test, Congress risks repeating mistakes of the past and subjecting patentees and infringers to the same uncertainty, excessive litigation costs and unfair damage awards that ultimately led to the flexible, market-based damages standard codified in Section 284.

The Department of Commerce in a recent letter to Chairman Berman reiterated the importance of preserving the flexible methodology of *Georgia-Pacific*, despite questions about recent, seemingly high damage awards. Damages awards in patent cases can and should reflect a variety of factors; and neither courts nor juries should be precluded from considering potentially relevant factors, or required to elevate any one factor over another:

While the appropriateness of damage awards in a number of patent cases may be subject to debate, DOC does not believe that a sufficient case has been made for a legislative provision to codify or emphasize any one or more factors that a court may apply when determining reasonable royalty rates. . . . It appears that the courts have adequate guidance through *Georgia-Pacific* and, as a general matter, do in fact consider numerous factors in determining royalty rates. . . The amount of a reasonable royalty should turn on the facts of each particular case, as best as those facts can be determined.⁴

Of course, apportionment of damages may be appropriate in certain situations. Indeed, among the 15 factors enumerated by the *Georgia-Pacific* court is “The portion of realizable profit that should be credited to the invention as distinguished from non-patented elements, the manufacturing process, business risks, or significant features or improvements added by the infringer” (factor 13). Consistent with *Georgia-Pacific*, the Federal Circuit’s model jury instructions permit consideration of the “portion of the profit that is due to the patented invention, as compared to the portion of the profit due to other factors.” Apportionment, however, is not appropriate in all cases. In particular, courts have long held that the parsing of a patent’s value is sensible only if the patent represents a relatively insignificant and separable part of the overall product. In contrast, where a patent is responsible for all or substantially all of the product’s market value, apportionment is unnecessary and inappropriate. Similarly, apportionment is never

⁴ Letter from John J. Sullivan, General Counsel of the US Department of Commerce, to the Honorable Howard L. Berman, Chairman, Subcommittee on Courts, the Internet, and Intellectual Property, Committee on the Judiciary, US House of Representatives (May 16, 2007).

appropriate in cases where the patentee demonstrates an established, market-tested royalty.

The Senate apportionment proposal departs from these principles in numerous, significant respects that would greatly diminish the patent rights and remedies of InterDigital and other innovative firms that rely upon their patents to generate licensing revenue and fund ongoing research and development. Beyond the rigid mandate that courts apportion damages in virtually all cases, the proposed amendment would create an entirely new standard of apportionment that limits a patent's value to its "specific contribution over the prior art." In addition, the court must exclude from the royalty amount the "economic value properly attributable to the prior art, and other features or improvements, whether or not themselves patented, that contribute economic value to the infringing product or process." This unprecedented and subjective analysis could lead to absurd and wholly inequitable results in which a patented technology is deemed to have little or no demonstrable value, even in cases where a well-established history of licensing exists.

In contrast, the existing apportionment test, as articulated in *Georgia-Pacific*, looks to the value of the entire patented "invention," as defined by the examination process. Once granted, the patent as a whole has been deemed useful, novel and non-obvious and thus entitled in full to exclusive rights and remedies. The Senate's mandatory apportionment proposal would, in effect, call into question the significance of this examination process, and signal that only certain parts of the patent, as arbitrarily defined by the court, are valuable and thus eligible for damages.

The only proposed exception to mandatory apportionment is a new and much-heightened formulation of the "entire market value rule", which requires the patentee to show that the patent's "specific contribution over the prior art is the predominant basis for market demand for the infringing product or process." Here again, the terminology "specific contribution over the prior art" has no defined or well-understood meaning under existing patent law and, as a result, will inject considerable uncertainty into damages proceedings. Similarly, the requirement that a patent's "specific contribution" be the "predominant" basis for market demand will for most complex technologies erect an insurmountable burden of proof that will gut the "entire market value rule" of any relevance.

Perhaps most troubling is the fact that the bill relegates evidence of negotiated licensing terms to a secondary consideration that can and must be ignored by the court to the extent that such terms conflict with the dictates of apportionment. Under the Senate bill, a court must apply the new apportionment analysis even in cases where the patentee demonstrates a history of negotiated royalties and licensing terms; moreover, the court has discretion to ignore these terms altogether. There is simply no economic or legal justification for mandating that a court and jury second-guess the market, and doing so will only encourage infringement.

Under the new mandatory apportionment provision, many infringers will feel emboldened to continue their infringing activity because their exposure to damages under

the amended Section 284 is dramatically decreased or at least made less certain. Infringers, to the extent they are willing to engage at all in licensing discussions with a patent holder, will adopt negotiating positions with intractably low financial elements, thereby significantly reducing the likelihood of arriving at a negotiated license agreement. At the same time, patent holders that rely upon licensing as the mechanism for securing a return on their investment in innovation will be forced to litigate in order to achieve at least a modest financial reward for their inventive contribution to society.

Negotiated licenses, absent litigation, will decrease because infringers will demand royalty terms significantly below what their exposure may be at trial. With diminished risk to an infringer for continued unlicensed activity, negotiated resolutions of patent disputes will significantly decrease and litigation will increase commensurately. Along with an increase in litigation, costs for legal proceedings will also grow as the new process for calculating damages will in virtually every case require the court to determine “the patent’s specific contribution over the prior art.”

The extreme difficulty and cost of administering such a novel and complex standard was emphasized in a recent letter to Chairman Leahy and Senator Hatch from Chief Judge Paul Michel of the US Court of Appeals for the Federal Circuit, the judicial circuit that hears all appeals from federal district courts arising under US patent laws. In his letter, Chief Judge Michel noted that courts and juries are ill-equipped to interpret or apply this new apportionment test, and the requirement that they do so will inevitably lead to costly battles between expert witnesses and increased litigation costs and delays:

This is a massive undertaking for which courts are ill-equipped. For one thing, generalist judges lack experience and expertise in making such extensive, complex economic valuations, as do lay jurors. For another, courts would be inundated with massive amounts of data, requiring extra weeks of trial in nearly every case. Resolving the meaning of this novel language could take years, as could the mandating of proper methods. The provision also invites an unseemly battle of “hired-gun” experts opining on the basis of indigestible quantities of economic data. Such an exercise might be successfully executed by an economic institution with massive resources and unlimited time, but hardly seems within the capability of already overburdened district courts.⁵

Chief Judge Michel concludes by stating that he is “unaware of any convincing demonstration of the need” for this new mandatory apportionment standard.

What makes the practical application of this new requirement even more dubious is that patent examiners themselves do not engage in determining a patent application’s “specific contribution over the prior art.” Instead, during examination, a patent is

⁵ Letter from Chief Judge Paul R. Michel of the US Court of Appeals for the Federal Circuit, to the Honorable Patrick Leahy and the Honorable Orrin G. Hatch, US Senate (May 3, 2007).

awarded if the applicant can demonstrate that claimed invention is useful, novel and non-obvious. A patent applicant is not required, nor should he or she be, to articulate the *specific* contribution of the patent application over the prior art. Rather, the applicant need only demonstrate that the claimed invention *is* novel and non-obvious over the prior art. Put differently, it is the *entire claimed invention*, not merely a parsing of claim elements, that reflects the patent's contribution over the prior art. Thus, the process of determining a patent's *specific* contribution over the prior art is one which has never been undertaken by the courts, juries or even by the USPTO. Clearly, then, the apportionment measure will decrease incentives to innovate and increase the frequency and cost of litigation.

Post-Grant Opposition

Although InterDigital recognizes that existing reexamination procedures are capable of improvement, we oppose the introduction of a new, duplicative and potentially burdensome post-grant opposition process as both premature and harmful to the thousands of innovative firms that rely upon enforceable patent rights to fund ongoing research and development.

Reexaminations procedures are an important part of our patent system and a critical check on the small percentage of patents that are erroneously granted each year. At the same time, however, such procedures must also strive to preserve the value and enforceability of the vast majority of meritorious patents.

Under Chapters 30 and 31 of the Patent Act, a patent can be challenged at the USPTO through both *ex parte* and *inter partes* reexamination procedures, respectively. Unlike *ex parte* reexamination, *inter partes* reexamination allows the third party to participate during the process of reexamination by submitting written comments addressing issues raised by the patent examiner or the patent owner's response to the PTO. The opportunity for reexamination under these two sections of the Patent Act extends for the life of the patent. However, a party is estopped from raising at a later time any ground for invalidity that the third party raised or could have raised during the reexamination proceedings, unless the assertion of invalidity is based on newly discovered prior art unavailable to the challenger and PTO at the time of the original reexamination proceedings.

During the process of reexamination, the patent owner may make amendments to the claims of the patent in order to arrive at the proper scope of protection for the claimed invention. In some cases, every claim of a patent is canceled, but usually the claims are confirmed or substituted with new or amended claims. This process recognizes that although certain issued patent claims may be invalid in view of newly identified prior art, the patent holder should be able to modify the scope of patent protection in view of this prior art and retain rights in the adjusted claims. In that respect, the goal of reexamination is not to "bust" patents, but to ensure that their scope is appropriate in view of the prior art.

This Senate bill proposes yet another mechanism for reviewing issued patents in addition to *ex parte* and *inter partes* reexamination, and also expands the existing *inter partes* process by narrowing its estoppel effect and permitting challenges of all issued patents. The proposed post-grant opposition process would allow parties to petition the PTO to cancel claims of a granted patent, but in the context of a quasi-judicial proceeding with administrative judges, discovery, cross-examination and other costly aspects of litigation. This post-grant review would be available to petitioners during a “first window” lasting 12 months after the grant of the patent and during a “second window” which may be opened if the petitioner receives notice of infringement of the patent or if the petitioner establishes a substantial reason to believe the patent claim is likely to cause the petitioner significant economic harm. A patent may also be reviewed at any time upon written consent of the patent owner.

InterDigital believes that adding an expansive and duplicative new post-grant opposition process, while maintaining and expanding the existing *inter partes* reexamination process, would subject patents to an unfair and unreasonable number of duplicative attacks on validity. Under the proposed opposition system, only those grounds that are actually raised by a petitioner are estopped from being asserted again in a subsequent administrative proceeding or civil action. This narrow estoppel effect will encourage duplicative administrative and judicial challenges -- a threat further exacerbated by the bill’s narrowing of the *inter partes* estoppel effect.

In addition to the threat of harassment, patentees will find it far more expensive to defend administrative challenges under the proposed opposition system. A post-grant opposition system would combine aspects of a judicial and administrative reexamination process, but eliminate or substantially dilute existing safeguards that have effectively discouraged misuse of the system. In the process, it would create a quasi-judicial system of administrative litigation that heavily tips the balance in favor of the challenger’s interests. Unlike a civil proceeding, a post-grant opposition system would facilitate invalidation by eliminating the patent’s presumption of validity and reducing significantly the challenger’s evidentiary burden to mere preponderance of the evidence (compared with the rigorous clear and convincing standard that governs judicial invalidity challenges). Moreover, because the proposed opposition system would unnecessarily restrict the patentee’s ability to amend its claims (in contrast with the flexible *inter partes* reexamination process), it would encourage outright invalidation of a patent that may simply require an adjustment in scope. This threat will be used aggressively by accused infringers against patent owners.

Patent owners will bear the brunt of these increased litigation costs, particularly if opposition is permitted for any issue of patentability throughout the life of the patent. In contrast, a competitor or free rider - relieved of robust evidentiary requirements and the risk of estoppel - would have every incentive to seek opposition, regardless of the patent’s strength. Such a system would inevitably invite abuse, allowing corporate giants to misuse opposition litigation as a means of blocking patents that frustrate their business interests. Indeed, by stripping a patent holder of the protections that guard against

baseless challenges, an open-ended opposition threat would cast a permanent cloud over a patent's legitimacy and enforceability.

This potential for costly, duplicative and harassing attacks on granted patents would be extremely detrimental to patent holders that rely upon negotiated license agreements to secure revenue and financing. The proposed regulations and sanctions for abuse would do little to prevent gamesmanship of the system, since demonstrating misuse would be an extremely difficult exercise. The proposed post-grant opposition system would thus allow infringers to utilize different channels of post-grant review to avoid legitimate licensing efforts. Such a result would be particularly devastating for start-ups and other smaller firms whose very survival is often dependent on early stage venture capital and licensing revenue.

Significantly, the current proposal for post-grant review would do little to improve patent quality. If afforded an indefinite "second window" that can be triggered by virtually any challenger at any time, third parties in possession of relevant prior art would have little incentive to bring such references to the PTO's attention, particularly if the estoppel effect of a second window is no broader than that of the first window. Instead, a potential infringer would almost always be inclined to hold onto the prior art until the last possible moment (e.g., after repeated attempts by the patent holder to negotiate a patent license resulting in a dispute that appears headed for litigation) before filing a "second window" petition for cancellation of the patent.

Finally, a surge in complex post-grant proceedings will further strain an already overburdened and under-funded USPTO staff, thus jeopardizing the agency's ability to improve pre-grant patent quality. The Department of Commerce echoed this concern in its letter to Chairman Berman, noting that the proposed "second window coupled with the substantial number of patents subject to the proposed review procedures create very legitimate concerns about the USPTO's ability to effectively handle the potential workload." With a portfolio of some 400,000 patent applications per year, the USPTO is struggling to perform its core examination functions, as evidenced by application pendency periods of 30-40 months. The proposed post-grant opposition system will inevitably divert funding from the examination corps, potentially resulting in even greater delays and, most importantly, diminished patent quality.

To guard against these negative effects, we urge Congress to consider improvements to the existing post-grant system of *inter partes* reexamination in lieu of a new, duplicative and potentially burdensome administrative review process. If post-grant opposition is ultimately deemed to be a necessary and preferable alternative to *inter partes* reexamination, implementation of a new opposition proceeding should not occur until the USPTO has demonstrated its ability to perform core examination functions in a timely manner and is given the resources to manage the significant demands of a new system of administrative litigation. Even at that time, opposition proceedings should be limited to a single window of review (i.e., within 12 months of issuance) and combined with adequate safeguards against abusive challenges, including a meaningful estoppel effect and a mechanism to allow the patent holder to freely amend his/her claims as in the current

reexamination process, to ensure that patent owners enjoy clear title over their inventions throughout the lives of their patents.

Substantive USPTO Rulemaking Authority

InterDigital believes that substantive and potentially significant changes to patent rules are ill-suited to administrative rulemaking processes and should remain the exclusive domain of Congress.

The Senate bill would empowers the Director of the USPTO with unprecedented and expansive substantive rulemaking authority, which would encompass any “rules, regulations, and orders that the Director determines appropriate to carry out the provisions of [the Patent Act] or any other law applicable to the [USPTO] or that the Director determines necessary to govern the operation and organization of the Office.” This rulemaking authority would pave the way for well-intentioned but inadvisable regulatory changes, including severe restrictions on continuation and claim practice that are opposed by the overwhelming majority of patent holders. Significantly, even the Department of Commerce voiced concerns about “unbounded discretion” in its letter to Chairman Berman and recommended against an overly broad grant of rulemaking authority.

Because of various limits on its jurisdiction, the USPTO lacks meaningful exposure to the commercial and economic complexities of patents post-issuance, and thus lacks the breadth of perspective and experience to legislate effectively in substantive and critical areas of patent prosecution. As evidence of this, the USPTO has recently proposed significant regulatory changes that would negatively impact innovators and economic growth, including unprecedented limitations on continuation and claims practice. The fact that the USPTO has hastily finalized these new rules -- without disclosing its underlying studies and despite overwhelming opposition among patent holders -- confirms that its rulemaking procedures are ill-equipped to conduct administrative patent reform with the necessary deliberation and transparency.

Interlocutory Appeals

Although InterDigital shares the committee’s desire to reduce litigation costs and delays, we fear that immediate appeals of claim construction rulings would have the opposite effect and benefit only those litigants with deep pockets.

The Senate bill would expressly authorize an immediate appeal to the Court of Appeals for the Federal Circuit (CAFC) after a pre-trial *Markman* hearing on claim construction. Although aimed at reducing the length and cost of patent litigation, InterDigital believes that an immediate appeal right could have the reverse effect of increasing the costs and delays of litigation, as noted in Chief Judge Michel’s letter to Chairman Leahy and Senate Hatch. We thus encourage the committee to remove this amendment from the bill.

Claim construction in a patent infringement litigation is conducted pre-trial during a proceeding known as a *Markman* hearing. Upon considering briefs and oral arguments, the court issues an order construing contested claim terms in a patent. The claim construction is the framework used by the jury (or the court in a bench trial) to determine whether an accused method or device infringes the patent at issue.

Under current law, issues concerning claim construction may be appealed to the CAFC upon a judgment from the lower court. The Senate bill would allow a party, as a matter of right, to appeal from an interlocutory order on claim construction. Since claim construction is a crucial component to virtually all patent infringement cases, a party dissatisfied with the lower court's order will most likely pursue an appeal to the CAFC. As a result, this right of appeal will significantly delay final judgments from the lower court and result in increased delays in reaching potential settlements, as well as increased litigation costs.

Similarly, a dramatic increase in the number of appeals brought to the CAFC will further stretch its limited resources, causing further delays and costs at the appellate level. In his letter to Chairman Leahy and Senator Hatch, the CAFC's Chief Judge Michel noted that based on empirical studies, immediate appeal of claim construction rulings could double the number of filings to the CAFC and also double the amount of time necessary to resolve an appeal from one to two years. In the meantime, proceedings at the trial court level would be frozen, thus doubling delays in district courts, which according to Judge Michel, are typically two to three years. InterDigital also shares Judge Michel's concern that claim construction appeals could lead to significant inefficiencies, as claim construction rulings are subject to change during summary judgment proceedings or trials.

InterDigital Supports Balanced Reforms that Promote Patent Quality, Fairness and Incentives to Innovate

InterDigital supports legislative reforms that would enhance pre-grant patent quality and reduce the uncertainty and inefficiency of patent litigation, including, for example, [a permanent end to fee diversion, enhanced third party prior art submissions, universal publication of patent applications and enhanced judicial training.]

The concept of patent "reform" signifies improvements to the efficiency, fairness and overall strength of our patent system. As a licensing-based business that lives or dies on the strength of its patents, InterDigital is a staunch advocate of true patent reform, particularly measures that enhance patent quality, preserve incentives to innovate, and promote a fair and balanced playing field among all stakeholders, large and small.

In our view, mandatory apportionment, post-grant opposition, expansive USPTO rulemaking authority, and interlocutory appeals fall outside the realm of patent "reform" and, in fact, would degrade patent rights and increase the prevalence, costs and uncertainty of litigation, particularly for smaller innovators. The aim of patent reform is

not to gut the patent rights critical to today's knowledge-based economy, but instead to bolster the system with measures that will improve *pre-grant* patent quality.

Patent quality is best achieved by pre-grant measures that provide examiners with the resources, training and information needed to properly assess whether an invention is, in fact, novel, non-obvious and useful. A recent study by the National Research Council also demonstrates that increases in patent examination resources yield important reductions in post-grant litigation, further underscoring the critical importance of such measures.⁶ To its credit, the USPTO has taken several steps in recent years to improve pre-grant quality, including by hiring of thousands of new examiners and strengthening its training programs.⁷ The results are promising. In December 2006, the USPTO reported a significant decrease in the patent allowance rate to a record low of 54 percent - - a dramatic drop from the 2000 rate of 70 percent. In addition, the USPTO in 2006 achieved its lowest error rate in 20 years -- 3.5 percent. Of course, to maintain this trend, it is imperative that the USPTO continue to receive the resources necessary to evaluate an escalating number of patent applications. And to that end, what is most needed is legislation to permanently end patent fee diversion. Patent reform legislation stands little chance of achieving positive and concrete improvements without addressing vital resource issues. InterDigital is well aware that the committee shares our concerns about fee diversion, and we are very appreciative of your long-standing efforts to ensure that the USPTO retains its fees.

In that same vein, increased USPTO resources will yield quality gains only if examiners have the information and incentives to recognize and reject claims for obvious or non-novel inventions. InterDigital thus supports measures that would foster an environment of cooperation between patent examiners and applicants and increase the prior art available to examiners. These include, for example, the Senate bill's proposal to increase third-party submissions and mandate universal publication of all patent applications.

InterDigital also supports reforms designed to reduce litigation costs, uncertainty and abuse. It is a mistake, however, to characterize efforts to weaken the enforceability of legitimate patents as litigation reforms. Not only would such measures undercut the rights of all patent owners to protect a few corporate giants from potential infringement litigation, they would ultimately increase the number of lawsuits by encouraging infringers to seek court-ordered rather than market-based solutions.

We believe that litigation reforms should reduce the subjective, unpredictable and inefficient aspects of patent litigation that negatively impact patent owners and users alike. For example, we would encourage the committee to reintroduce an amendment to

⁶ *Patents in the Knowledge-Based Economy*, Wesley M. Cohen and Stephen A. Merrill, Editors, Committee on Intellectual Property Rights in the Knowledge-Based Economy, National Research Council (2003).

⁷ In addition, the USPTO just announced a revolutionary beta program to identify the most relevant prior art through the use of peer review system. Innovative approaches of this type should be encouraged.

eliminate the best mode requirement. A narrow but meaningful reform of this type strikes the right balance by reducing subjective aspects of the patent system that escalate litigation costs, without diminishing the rights and remedies of legitimate patent owners. Similarly, InterDigital supports measures that would enhance judicial training in patent law and, in turn, steer patent cases towards district court judges with the desire and expertise to take on these complex and highly technical matters. Reforms of this type would heighten the fairness, predictability and efficiency of patent litigation for all stakeholders. We also believe that statutory clarification of the inequitable conduct defense could benefit all participants in the patent system, provided that such a measure appropriately balances the interests of patent owners and users.

Conclusion

Given the critical importance of our patent system to American innovation and economic leadership, it is imperative that patent reforms be carefully tailored to achieve necessary improvements and, in all cases, to promote and protect investments in innovation. The over-arching goal of patent quality is ill-served by measures that would destabilize our current system of patent rights and remedies and, in turn, jeopardize the global leadership of this country's most innovative industries.

If our shared objective is to improve patent quality while preserving incentives to innovate, we should instead pursue reforms that enhance patent examination resources and capabilities within the USPTO and make it harder for questionable patent applications to survive pre-grant scrutiny. The USPTO has already taken important steps to achieve these goals, hiring thousands of new examiners, instituting new training programs and committing annually to performance benchmarks. But it needs Congress's support in the form of a predictable flow of resources and hence a permanent end to fee diversion. In addition, InterDigital encourages this committee to pursue constructive but narrowly tailored reforms that would increase access to prior art and lessen the subjective aspects of litigation. Carefully structured measures of this type would ultimately fortify the health of our patent system without endangering the rights of American's most innovative firms.

The Senate patent bill has been described as the most significant piece of patent legislation in over 50 years. As such, it is no exaggeration that this bill and its proposed changes to our patent system will have a dramatic impact on the future course of American innovation. Although InterDigital believes that many of the bill's provisions will have a positive impact, encouraging companies like ours to invest in the cutting edge innovations that will secure our country's economic leadership, we fear that mandatory apportionment, open-ended post-grant opposition, broad administrative rulemaking authority and interlocutory appeals could have a very detrimental effect, particularly if they signal to other countries a weakening of America's commitment to strong patent rights.

America's system of patent rights and remedies can and should be improved, but it is universally recognized throughout the world as the gold standard. As such, it has given

us the moral authority and credibility to fight for stronger protection of U.S. innovations in other markets. Maintaining that authority is critical in today's increasingly competitive global economy. America's leadership in this knowledge-based economy is highly dependent upon the ideas and innovations that constitute our most valuable natural resources and our most desirable exports. If the United States weakens patent rights and remedies at home, our ability to press foreign countries to respect American intellectual property will be greatly diminished. Indeed, we will embolden other countries to adopt even more damaging policies that could jeopardize the continued preeminence of America's most productive industries.