

Patent Assertion Entity Workshop
Opening Remarks of FTC Chairman Jon Leibowitz
As Prepared for Delivery
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Good morning. On behalf of my colleagues at the FTC and the Department of Justice, I am thrilled with the overwhelming response to this workshop, both among those of you in the audience today and those of you all over the world who are watching the webcast of this event.

A little over two years ago, the FTC, DOJ, and the United States Patent and Trademark Office gathered the public in Alexandria, Virginia to explore issues at the heart of competition policy and patent policy: the patent application backlog; permanent injunctions in the district courts and at the ITC; standard setting; and patent rights. By working together with our sister agencies, we increased our understanding of these important issues and used this knowledge when deciding, for example, to weigh in at the ITC on the issue of injunctive relief for standards essential patents. Judge Posner later cited the FTC's analysis in his decision to dismiss a trial between Motorola Mobility and Apple.

Patent issues raise a minefield of problems. Poor patent quality tips the balance between exclusivity and competition. Unclear scope and poor notice hurts innovation. But there have been improvements. We were happy to see Congress incorporate our recommendation for a more streamlined post-grant review process in the America Invents Act;¹ this presents a less-expensive means, short of litigation, to challenge patent validity. Echoing our policy recommendations, the Supreme Court expanded the standard for

¹ FED. TRADE COMM'N, TO PROMOTE INNOVATION: THE PROPER BALANCE OF COMPETITION AND PATENT LAW AND POLICY (2003) at 7 (herein, "2003 Report"); Leahy-Smith America Invents Act, Pub. L. No. 112-29, 125 Stat. 284-341 (2011).

invalidating patents on obviousness grounds – opening a channel to improve patent quality.² Joining Congress, the antitrust agencies, and most economists, the Court rejected the presumption that patents convey market power.³ Similarly, when the Supreme Court issued its *eBay* decision, it ended an almost automatic injunction rule for patent infringement.⁴ *eBay*'s equitable test now provides a much-improved framework to address a myriad of injunction issues, including those involving FRAND-encumbered SEPs.

Today, we look at the related issue of Patent Assertion Entity (“PAE”) activity and its impact on innovation and competition. What can the Agencies do to promote competition here? Before we dive into what I know will be a lively debate, however, let me briefly talk about acronyms. Here in DC, who doesn't love a good acronym?

We are looking today at PAE activity, not the more general non-practicing entity, or NPE, activity. The term NPE includes any entity that does not manufacture or sell products that use its patented technology. For example, universities are NPEs. They conduct research, patent their inventions, share this research with companies who seek to include this technology in new or improved products. By contrast, PAEs focus on purchasing patents from existing owners. PAEs make money by licensing the intellectual property to (or litigating against) manufacturers who are already using the patented technology. Acronyms aside, we all know a few colorful street names for PAEs, but we are not going to use any of them today. In this workshop, as my former colleague Chairman Bill Kovacic would say, we are merely seekers of the truth.

² *KSR v. Teleflex*, 550 U.S. 398, 415 (2007), *see also* 2003 Report at 22-24.

³ *Illinois Tool Works v. Independent Ink*, 547 U.S. 28, 45-46 (2006), *see also* U.S. DEP'T OF JUSTICE AND FED. TRADE COMM'N, ANTITRUST GUIDELINES FOR THE LICENSING OF INTELLECTUAL PROPERTY § 2.2 (1995).

⁴ *eBay v. MercExchange*, 547 U.S. 388 (2006).

A truthful fact: it is clear that PAE activity is a growing issue for the United States. There were more than 4,000 patent lawsuits filed last year. James Bessen and Michael Meurer report that PAE-generated revenue cost defendants and licensees \$29 billion in 2011, a 400% increase from 2005.⁵ They calculate that no more than 25% of this flowed back to innovation. Almost like lobbying in Washington, D.C., 75% was deadweight loss! Later today, we will hear a discussion of this point.

Another one: Congress is beginning to pay attention. The America Invents Act directed the Government Accountability Office to study the costs, benefits, and consequences of PAE litigation, and to recommend how to “minimize any negative impact” of PAE litigation. The GAO report will issue shortly, and like many of you, we are eagerly awaiting the results.

Yet another: one of our panelists, Robin Feldman, and her colleagues, who worked on the GAO study, report that PAE suits are on the rise.⁶ Five years ago, 22% of cases were filed by patent monetizers. In the most recent year, this number increased to almost 40%. Most of these cases settled before summary judgement. Of the five parties in the sample who filed the greatest number of lawsuits in the period studied, four were patent monetizers. The study also found that universities accounted for 0.2% of the cases in the sample. This means that of all of the patent litigation occurring, PAEs bring almost 40% of these cases and settle before determination on the merits. Another recent study found that when PAE suits proceed to merits judgments, PAEs lose 92% of the time.⁷

⁵ James Bessen and Michael J. Meurer, *The Direct Costs from NPE Disputes* (Boston Univ. School of Law, Law and Economics Research Paper No. 12-34, 2012).

⁶ Sara Jeruss, Robin Cooper Feldman, and Joshua H. Walker, *The America Invents Act 500: Effects of Patent Monetization Entities on US Litigation* (UC Hastings Research Paper No. 3, 2012).

⁷ John R. Allison, Mark A. Lemley, and Joshua Walker, *Patent Quality and Settlement Among Repeat Patent Litigants*, 99 GEO. L.J. 677, 694 (2011).

That is astonishing.

Even if you are not bowled over, it is clear that the time has come to address PAE activity and its possible costs to civil society.

What is to be done? The FTC has a number of tools in its arsenal. We can bring enforcement actions based on violations of the antitrust laws. Our Section 5 authority prohibits “unfair methods of competition.” If a party engages in misrepresentation, we can use our authority to prohibit “unfair acts or practices,” which we considered, but did not use, in our recent Bosch consent. In addition to enforcement authority, we have a number of policy and advocacy tools readily available. For example, the FTC will continue to recommend improvements to notice and remedies to address issues with the patent system that may encourage PAE harms. We also have rulemaking authority on the antitrust side, although we have not exercised this authority in a number of years.

Today, we will begin with presentations by Colleen Chien and Carl Shapiro. Professor Chien will explore the increase in PAE litigation and the legal framework behind the PAE licensing model. Professor Shapiro, a longtime friend of the antitrust agencies, will outline the economic framework of PAE licensing, exploring ways in which PAE activity seeks to maximize revenue from IP transactions.

After they set the stage, we will gather industry representatives in our first session to hear their real-world experiences. Panelists will include PAEs, large and small operating companies, defensive aggregators, and members of the open source community. This panel will explore pressing questions such as: How do operating companies decide to transfer IP to PAEs? Do PAEs facilitate the transfer of patent rights? What is the reaction of operating companies when PAEs seek to license or

litigate their intellectual property? What role do defensive aggregators play in this model?

After lunch, we will hear from Stuart Graham, the Chief Economist of the United States Patent and Trademark Office. I am especially glad that Stu has joined us today. He will address the PTO's efforts to improve transparency concerning the ownership of patent applications and patents. Now I am just a government lawyer, but let me ask you this: why is there no disclosure of real-party-in-interest information for all patents and patent applications? I commend the PTO for their upcoming roundtable on this topic, but preliminary responses from our panellists today would be greatly appreciated.

In our second session, we will examine the potential efficiencies and harms of PAE activity. Supporters of the PAE business model believe that PAEs promote invention and investment in R&D by reducing transaction costs, managing the risks of monetizing inventions, maximizing revenue, and compensating small inventors. Not surprisingly, others believe that PAE activity imposes a "tax on innovation," undermining the incentives to engage in R&D. Detractors also raise concerns about operating companies transferring IP to PAEs as a means of raising rivals' costs. If that is actually happening – perhaps because of asymmetries of information and liability – it would seem, well, kind of unsavory.

Finally, our last session brings together academics and outside counsel to discuss whether competition law can play a role in enhancing the potential efficiencies and reducing the potential harms of PAE activity.

The FTC and DOJ value your input on these important issues. We are holding the public comment period open until March 10, and actively seek your observations. Right

now, I look forward to hearing the panelists offer a better sense of how the Agencies can be constructive. That is how we determine whether we need to do more, or whether we need to do less, or whether we should let the marketplace sort itself out, which is often our preference.

Thank you.