



June 18, 2014

**Comments of the Coalition for Patent Fairness on
“PAE Reports: Paperwork Comment; Project No. P131203”**

The Coalition for Patent Fairness (“CPF”) welcomes the initiative taken by the Federal Trade Commission to collect information and commence a study under Section 6(b) of the Federal Trade Commission (“FTC”) Act on Patent Assertion Entity (“PAE”) organization, structure, economic relationships, and licensing practices.

We believe the study proposed is designed to contribute to the understanding of policymakers and the public concerning the detrimental effects of PAE’s and should be approved by the Office of Management and Budget (“OMB”) and allowed to proceed. The study as proposed in the May 19, 2014 notice released by the Commission is targeted to produce useful information and not unduly burdensome. CPF respectfully submits the following comments on the proposed study.

I. Interest of Commenter

CPF is a diverse group of companies^[1] dedicated to enhancing U.S. innovation, job creation, and competitiveness by strengthening our nation’s patent system. CPF has spent the past eight years working to modernize and improve the U.S. patent system through legislative, administrative and judicial reforms.

CPF’s member companies are among the most innovative companies in the United States. Collectively, they hold tens of thousands of patents and support a strong patent system to reward and encourage innovation. But notwithstanding several improvements achieved by the America Invents Act, the U.S. patent system presents grave obstacles to innovation and competitiveness. In many cases, patents are too easy to obtain and too vague or ambiguous in scope. Patent litigation procedures are skewed in ways that tend to force defendants to settle rather than contest patent claims that may be meritless or inflated and purported damages, both in demand letters and in suit, are often disconnected to innovative contribution (if any) of the patent in question. This harms U.S. competitiveness by imposing unnecessary costs and stifling legitimate innovation.

II. The PAE Business Model[2]

PAEs are the dominant and fastest growing source of abuse in the patent system. They impose enormous costs on U.S. innovators, manufacturers, service providers, and, increasingly, consumers and end-users not just through litigation, but through the threats and demands that they make prior to initiating suit. No single PAE is the same and to truly understand the economic impact of their actions, it is important to understand the various organizational structures of different PAEs, their role in the current patent market, and how they interface with different actors up and down the business vertical.

PAEs are not traditional commercial innovators, like CPF's members. PAEs do not make up-front investments in research and development. They do not supply products and services to consumers or other businesses. They do not engage in pro-competitive, cross-licensing of technology to create new products using complementary technologies. Rather, PAEs are for-profit firms whose sole business consist of purchasing patents and asserting them through litigation. Because they produce nothing, cannot be cross-sued for infringing the defendant's patents. Rather, PAEs manipulate the current imbalances prevalent throughout the patent system to pursue litigation strategies free of the reputational concerns that constrain productive, consumer-facing companies.[3] They do so without regard to the economic impact these strategies may have on either the short-term financial future of a legitimate company or long-term ability for our country to foster the environment of innovation that has produced some of the greatest technological inventions in the world.

III. Need for an FTC 6(b) Study

A multi-faceted legal and policy response is needed by the Federal Government to combat the harm being done by PAEs' manipulation of the U.S. patent system. CPF believes that the proposed information to be collected and used by the FTC is an important part of that response. In particular, CPF believes that it important for the FTC to understand:

- How PAEs organize their corporate legal structure, including parents, subsidiaries, and affiliates. Although some of these entities are publicly traded organizations, the vast majority continue to be privately-held entities without a transparent corporate structure. They employ complex ownership structures to disguise the real party in interest. To make matters worse, they occasionally refuse to even disclose the patent portfolio they are offering, with threat of litigation, to license.
- How PAEs engage in the assertion activity. The goal of PAEs is not to defend or protect an innovative product. Rather, it is to maximize potential settlement or damages values. As such, PAEs typically sue late – both long after the patent

has been granted and long after the alleged infringement has occurred. Further, the scope of the alleged infringement generally has very little relation to the actual patent in question. They threaten or file suit after the defendant has generated a significant revenue stream and after the defendant is locked in to the allegedly infringing products and technologies. PAE litigation is characterized by an extraordinarily high ratio of legal costs (borne mainly by defendants)[2] to settlement values (with the former exceeding the latter in 90% of cases); and PAEs lose an extraordinarily high proportion of litigated cases (over 90% of software patent cases). In other words, PAE litigation is enormously costly for defendants and largely non-merits-based.

PAEs are subject to the same antitrust laws as productive companies, and CPF encourages the antitrust agencies to enforce the law vigorously against abuses by PAEs, whether they involve acquisition of substitute technologies to accumulate market power, hybrid PAEs combining with product market competitors to raise rivals' costs, use of patent litigation and threats thereof to deter innovation by rivals, cheap exclusion by threats and sham litigation, or other abuses. PAEs may benefit from de facto antitrust loopholes, however, insofar as the technology/patent markets in which they exercise power are difficult to define and assess, both because there is no market share data in the traditional sense and because of PAEs' success in obscuring both the real party in interest and the competitive significance of their assets. Given these difficulties, and the general lack of pro-competitive benefit inherent in the PAE business model, antitrust enforcement should take a particularly aggressive approach towards PAEs.

The information obtained through this study will allow the DOJ and FTC to better determine the nature of potential antitrust violations by PAEs. For example, some patent acquisitions may violate section 7 of the Clayton Act by creating market power in a technology market, and some arrangements between PAEs and other firms, or attempts by PAEs to evade FRAND commitments made by a patent's prior owner, may raise Sherman Act issues. The antitrust agencies have a broad role to play in deploying their economic expertise and investigatory power in their traditional competition advocacy role to help legislators, the PTO and the courts reform the patent system.

We understand that some questions have been raised as to the potentially beneficial role of PAEs in the patent market. CPF would stress that review and potential recommendations for reform be guided by the principle that the patent system is intended to incentivize and reward innovation. PAEs, however, are exploiting problems in the patent system by attacking firms that bring innovative products and services to market, and rewarding rent-seeking by PAEs that have no involvement in the development of those innovative products and services except to demand an extortionate share of the revenue they generate. Further, the patent system is also meant to embody a social contract: Congress grants lucrative rights of exclusion to inventors in exchange for their both investing in research and development and publishing an invention that can be put into practice to benefit the public. This is a contract that the members of CPF take seriously, each company alone investing millions of dollars investing in not only their own research and

development but also in the development of promising technology. Instead of making clear and beneficial public disclosures, PAEs hide in a thicket of broad, vague and overlapping patents, owned by obscure networks of subsidiaries and related companies, and then ambush productive entrepreneurs who have already brought innovation to the marketplace.

CPF believes that the study proposed by the FTC as outlined in the Federal Register -- a targeted investigation of PAEs, their business model, and the costs it imposes -- will not be unduly burdensome and would bring significant transparency to this ongoing issue. In sum, the proposed study is narrowly and appropriately tailored to the important questions the FTC is asking.

We urge the Commission to move swiftly to implement this plan. In doing so, it will be important that the Commission resist calls for delay. Given that this process has been under way for over a year and the public interest need for bringing swift transparency to this matter, there is no reason for delay. Likewise, we urge the Commission to avoid protracted negotiations over subpoena responses. As entities largely created for the purpose of litigation and skilled at evading responsibility, PAEs will no doubt be ready to resist requests, claim ignorance, and avoid production of meaning answers. CPF believes that the FTC must proceed forward and resist such objections. Although the targets of the investigation will indeed need to spend some resources answering the questions, those burdens are very small compared to the harms the PAEs inflict on innovative companies which is estimated to be in the billions of dollars per year.

If the Commission deems it feasible, CPF would encourage the release of an interim report on this matter. The debate over the impact of PAEs and the policy and legal changes needed to address the negative impacts and safeguard the patent system is happening in real time. The input of the FTC has been a valuable, independent and substantive addition to that discussion. We believe that an interim report would be both appropriate and useful.

CPF welcomes the attention these issues have begun to receive from the President, Congress, the Department of Justice, the Federal Trade Commission, and the U.S. Patent and Trademark Office, and it encourages all parties to work together on a continuing basis to achieve a fuller understanding of the PAE problem and to implement strong and effective reforms.

Respectfully submitted,

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[1] CPF's members include Adobe, Blackberry, Cisco, Dell, Google, Intuit, Oracle, Rackspace, Salesforce, Samsung, SAP, and Verizon.

[2] While PAEs impose high legal costs on defendants, PAEs' legal costs are generally low. PAEs generally produce little in discovery, because they acquire patents without acquiring the history of development that led to the patent.