Patent Trolls Prey on Business Innovation

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Any business discussion of patents and innovation inevitably turns to the subject of "patent trolls." Patent trolls plague companies of every type, often forcing companies to pay hundreds of thousands, or even millions, of dollars or risk much bigger exposure in a lawsuit for patent infringement. "Patent trolls" are people or groups acquiring patents, sometimes from bankrupt firms, not to create new inventions or products, but to generate revenue by suing to enforce the patent. Since the cost of defending a patent infringement suit typically runs well over $1 million, many defendants instead pay for licenses to dubious intellectual property.

As home to many technology companies, Colorado is prolific in generating intellectual property ("IP") that may be at risk. Colorado ranks 13th overall in the number of patents issued to resident inventors since 2000. More than 20,000 patents have been issued to Colorado inventors and 7,800 patents have been assigned to Colorado companies in the same period. Since most entities patent only a fraction of IP they invent, the measure of technology vulnerable to attacks by patent trolls is much greater. Indeed, many companies choose to keep their most valuable technology as trade secrets rather than publicly disclose it, as is required to obtain a patent.

In one example of patent troll activity in Colorado, EchoStar Communications Corp. was sued by Forgent Networks Inc. for more than $200 million for allegedly violating a patent on digital video recording. Even though EchoStar won, it had to mount a costly legal defense and deal with months of uncertainty from the lawsuit. Further, Forgent generated more than $28 million in licensing revenues from other companies before EchoStar prevailed.

Congress is currently debating legislation to minimize the impact patent trolls can have on legitimate businesses. The House of Representatives passed H.R. 1908 on September 7, 2007. Among the provisions that might help companies facing a patent lawsuit are measures to minimize damages and reduce the locations in which a patent suit may be brought.

Currently, a patent owner can seek a reasonable royalty as a matter of course in a patent infringement suit. The new House bill provides guidance on the royalties due an infringer. Royalties are calculated based on the entire market value of a product only if the plaintiff can show the patented technology is the primary driver of market demand for a product incorporating that technology. Otherwise, royalties may be based only on the "economic value" that flows from the improvement of the patented technology over older technology. Thus, the actual damages due to a plaintiff from sales of a complex device incorporating a minor piece of patented technology could be quite small compared to current awards.

The bill also limits the ability of plaintiffs to choose a venue for patent lawsuits. In particular, a plaintiff cannot create venue by "assignment, incorporation, joinder, or otherwise" taking actions designed to have a suit heard in a particular court. Plaintiffs will no longer be able to transfer a patent to a holding company solely to get an infringement suit heard in a specific court. Plaintiffs can only bring suit in a district where: 1) the defendant has its principal place of business or is incorporated; or 2) the defendant committed "a substantial portion of the acts of infringement" and "has a regular and established facility" under its control.

For example, the Eastern District of Texas is popular for patent suits due to its pro-plaintiff slant. Under current law, so long as a defendant has substantial contact with the Eastern District of Texas, a plaintiff can bring a patent infringement action against the defendant there. This will not be possible under the proposed laws unless the defendant is incorporated in that district or both commits some portion of the infringement there and has a facility within the venue.

Although these changes limit the effectiveness of patent trolls, there's no guarantee they will become law, nor is there a date for enactment. In the meantime, here are some suggestions to reduce exposure to trolls.

First, have your patent counsel or a technologist familiarize themselves with the major trolls and commonly litigated patents in your company's industry. A surprising number of suits and settlements involve a very few entities holding frequently-asserted patents. If you know who these are and what they hold, you can either design around their patents or prepare defenses early.

Second, consider having a patent attorney provide a clearance opinion before entering into a new business line or launching a new product. You can reduce the costs of an opinion by having the attorney clear only patents owned by known patent trolls. Further, in the event you or your company are sued, an opinion of counsel can provide a defense against enhanced damages due to willful infringement.

Third, stay in contact with your peers at similar companies. Most patent trolls send waves of cease and desist letters. If a troll sends out enough letters seeking licenses, it could be more cost-effective for a group of companies to collectively bring a declaratory judgment action against the troll and split the legal costs.