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THE PATENT TROLL MYTH

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Trolls are mythological figures in Scandinavian folklore. So what's the truth about so-called "patent trolls"? Let's start at the beginning. In July 2001, Brenda Sandburg wrote an article for an *American Lawyer* publication, *The Recorder*, titled "*Trolling for Dollars*." On page one was a picture of Intel's then Assistant General Counsel, Peter Detkin, holding a troll; below him was a picture of Jerry Hosier next to one of his five airplanes. On the second page, there was a picture of me (Ray Niro) with the caption: "*Patent Power*." The accompanying article began with the "once upon a time" claim that:

> In the sleepy village of Santa Clara, there lived a very wealthy but very frightened giant named Intel. Intel was plagued by a fearsome band of evil trolls - patent trolls to be exact - who wanted a glittering pot of gold in exchange for doing absolutely nothing. And they were very powerful because they said they owned the patent on some of the magic Intel used to become rich.

Poor Intel; victimized by evil trolls. Intel cried "foul" because it had been sued for defamation, as well as patent infringement, after publicly calling our client an "extortionist." So Detkin coined the term "troll" to avoid more lawsuits:

> "We were sued for libel for the use of the term 'patent extortionist' so I came up with 'patent trolls,'" Detkin said. "A patent troll is somebody who tries to make a lot of money off a patent that they are not practicing and have no intention of practicing and in most cases never practiced."

Detkin now is managing director of Intellectual Ventures, a company that buys patents by the hundreds, never practices any one of them and eventually hopes to accumulate enough patents to make a lot of money by obtaining licenses from most of the corporate world. As Intellectual Ventures' founder, Nathan Myhrvold, is quoted as saying: "If giant corporations are making billions of dollars off my ideas, I want something for it." The *Newsweek* article goes on to define Intellectual Ventures' business model as follows:

> With this large bankroll, the company is out buying existing patents in droves. (Myhrvold won't comment on these activities, but sources say he has already purchased about 1,000 patents.) The strategy is to set up a sort of patent marketplace. Patent owners get money upfront for the dusty ideas sitting on their shelves, the investors get the rights to use the ideas without being sued and Myhrvold gets to rent those same ideas to other companies that need them to continue creating products.
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> *Newsweek, "Factory of the Future*?", Stone B., November 22, 2004

This certainly seems to satisfy Detkin's definition of a "patent troll."

THE TRUTH ABOUT THE INTEL SUIT

A famous criminal defense lawyer, Percy Forman, once claimed that he sometimes had to "try" his case against the victims of the crime to divert the jury's attention from his client's bad acts. Maybe at some point the jury thought the victims really deserved to die -- victimology at its extreme. Other examples include: "I had to do it because I was the victim of abusive parents"; or "The system is out to get me: rush to judgment." Intel had to characterize itself as the victim to obscure what was really happening.

Our client, TechSearch, had purchased a patent from a company called International Meta Systems, Inc. ("IMS") in January 1998. IMS did not have the resources needed either to license or enforce its patent, but retained an interest in the patent in the hope of paying off its debts and having a little something left over for its owners and employees.

The IMS patent was an outgrowth of efforts to develop a microprocessor chip that would match Intel's fastest chips -- indeed, emulate them. Unfortunately, IMS could not get funding to continue its operations and filed for Chapter 11 bankruptcy. The principal reason IMS failed was that prospective partners in the industry were leery about their continued access to chip allocations from Intel.

Shortly after it acquired the patent, TechSearch notified Intel that certain of its products infringed. Intel refused a license and TechSearch filed suit alleging that Intel's Pentium Pro and Pentium II lines of products infringed. Based upon Intel's public filings, Intel was making approximately $8 billion a year in revenues from these products.

Intel's first defensive act was to hire the inventor of the patent and his attorney to elicit testimony that the patent was invalid. Then (several days after testifying in a deposition under oath that he did not know whether an alleged prior art publication was, indeed, prior art), at Intel's urging, the inventor tried to recant his testimony by changing an answer in his deposition from "That's right. I don't know [that it is prior art]" to "That's not right. Under that definition, I would consider it prior art."

Intel then tried to buy the patent through a shell company it formed in the Cayman Islands. The company, named Maelen Limited, filed a motion asking the bankruptcy court to approve bringing an avoidance action against TechSearch to recover the patent for the estate. In an avoidance action, the bankrupt estate may recover an asset that was transferred within the prior year if it can show that the purchaser of the asset paid less than a reasonably equivalent value for the asset. The IMS estate had no funds. Maelen offered to pay administrative costs of the trustee and to fund costs of litigating the avoidance action with TechSearch. Maelen also proposed that if the estate recovered the patent, it would be auctioned and Maelen would make a minimum bid of $325,000 for the patent. A copy of Maelen's motion was sent to all IMS creditors.

After some investigation, everyone learned that Maelen was a Cayman Island shell corporation owned of record by a nominee of Bank of America for the account of Intel. Intel had acquired Maelen in August 1998, shortly after TechSearch sued Intel for patent infringement. Maelen, thus, came on the scene strictly for the purpose of acquiring the patent from the IMS estate. The officers and directors of Maelen were all Bank of America employees; Maelen had no income or other operations and its only asset was the $100 used to capitalize it. Maelen's "offices" were a file cabinet. Its designated witness, Mr. Carney, did not know of any reason for Maelen's existence, other than to disguise Intel's identity as the real party in interest. Maelen received instructions from Intel's in-house attorney who was defending TechSearch's patent infringement case and was told that the patent was worth a great deal more than what TechSearch paid for it.

In short, Maelen was formed by Intel to keep its identity secret from TechSearch, the bankruptcy court and the creditors and to manipulate the bankruptcy court into taking action that would undermine TechSearch's ability to prosecute the patent infringement case against Intel.

Maelen's motion to bring an avoidance action finally came up for a hearing before Judge Monroe in the bankruptcy court in Austin, Texas. TechSearch's attorney argued that Maelen's failure to disclose to the court and the creditors that it was a "front" for Intel was fundamentally improper, since Intel had an adverse interest to the estate (the estate held a financial interest in any recovery by TechSearch against Intel in the patent infringement action). In the bankruptcy court, Maelen claimed that the patent was worth far more than TechSearch paid for it; while in the patent case, Intel said the patent was clearly invalid and threatened TechSearch with sanctions if it did not abandon its lawsuit. In an extraordinary action, the U.S. Trustee (who had not been told of Intel's involvement with Maelen) made an appearance before the Court in support of TechSearch's position, stating:

> That lack of disclosure I think is fatal to the trustee and Maelen going forward with the motion. I think the creditors are entitled to know about the relationship. It's a significant fact and it was not clearly disclosed at all.

After hearing all the testimony and arguments, Judge Monroe issued his ruling denying Maelen's motion and finding that Intel was being deceptive:

> I would submit that neither Maelen nor Intel give a damn what this estate gets out of that [avoidance] litigation if, as and when it's brought, and that their sole interest is in defending the [patent infringement] lawsuit in California, and that they are using this estate in an attempt to bring leverage upon TechSearch in the litigation in California. That is so clear from this evidence that I can't reach any other result or conclusion.

Judge Monroe concluded that Intel (and its "shell," Maelen) had an actual conflict of interest in representing the estate, which was so "clear and pervasive" as to require disclosure and, when disclosed, to require that its proposed agreement with the estate not be approved.

In a *Wall Street Journal* article that followed, Intel was taken to task for its arguably unethical tactics:

> Initially, Intel didn't disclose its involvement in international Meta's bankruptcy case. But after it admitted its ownership of the Cayman company in court, Judge Frank R. Monroe, who is overseeing the proceedings, concluded that Intel and the Cayman company had portrayed themselves as trying to help the bankrupt debtor when they were in fact really out to undermine the patent case. "They are using this estate in an attempt to bring leverage upon TechSearch and the litigation in California," the judge said, describing the maneuver as "totally inappropriate."
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> **Chuck Mulloy, an Intel spokesman, acknowledged the company's use of the Cayman company. But he says Intel was using "tactics appropriate to the plaintiff in this matter." He called TechSearch a "patent extortionist."**
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> * * * *
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> Charles Wolfram, a Cornell University law professor and an ethics expert, said Intel appeared to disclose its role only when a "gun was to their heads," under the pressure of discovery rules. "I am distressed by this," Prof. Wolfram said. "What is a big company like Intel doing sneaking around like this?"

Wall Street Journal, "Intel's Bold Steps to Thwart Foe In Patent Case", Takahashi, D., April 16, 1999 (emphasis added).

So the evil trolls were not so evil after all. They were called "patent extortionists" (later, "trolls") as a justification for tactics that were borderline at best. TechSearch, in turn, was at least

trying to help a company that had effectively been driven out of business by Intel. And TechSearch later granted rights to an Intel rival that needed the patent to defend itself against a series of infringement suits brought by Intel.

From this background emerged the patent "troll" -- Intel's justification for trying to secretly buy the very patent it argued was invalid based upon testimony from an inventor Intel put on its payroll.

SINCE WHEN ARE NON-MANUFACTURING PATENTEES BAD?

Ironically, the marketplace now abounds with non-manufacturing entities large and small -- often represented by the largest IP law firms in the country -- looking to buy patent rights. These folks now call themselves "IP prospectors" (See L. Lerer, *Going Once, IP Law & Business*, October 2005). Presumably, they will be less strident about non - manufacturing entities in the future. But the bottom line is that the expansion of marketplace opportunities to exploit patents -- both by the original inventor and by the ultimate purchaser -- can only provide additional incentive to innovate and patent.

And consider these names of individual inventors who ultimately formed companies to exploit their ideas but initially manufactured nothing: Westinghouse (air brake), Ford (car), Gillette (razor), Hewlett-Packard (oscillation generator), Otis (elevator), Harley (motorcycle shock absorber), Colt (revolving gun), Goodrich (tires), Goodyear (synthetic rubber), Carrier (air treatment), Noyce (Intel), Carlson (Xerox), Eastman (laser printer camera), Land (Polaroid), Shockley (semiconductor), Kellogg (grain harvester), DuPont (gun powder), Nobel (explosives), the Wright brothers (aircraft), Owens (glass), Steinway (pianos), Bessemer (steel), Jacuzzi (hot tub), Smith & Wesson (firearm), Burroughs (calculator), Carothers (nylon), Curtiss (aircraft), Houdry (catalytic cracker), Marconi (wireless communication), Goddard (rocket), Diesel (internal combustion engine), Fermi (neutronic reactor), Disney (animation), Sperry (Gyroscope), Williams (helicopter), even Abraham Lincoln who was granted U.S. Patent No. 6,469. These are individuals who, in most cases, worked alone, without government or corporate support, yet, created not just new inventions, but, in some cases, whole new industries. The patent system is designed to encourage such innovation by both those who simply create ideas and those that can commercialize them as well.

It can be argued, of course, that ultimately these inventors became manufacturing companies and that companies that merely buy patents from individual inventors contribute nothing. But doesn't the compensation of inventors for their inventions foster, not hinder, innovation? And what about small companies that are struggling to compete against corporate giants and need a strong patent system to level the playing field? As the inventor of the MRI scanning machine, Dr. Raymond Damadian, observed, it's the small companies that often provide the economic spark for new jobs:

> Few Americans realize that the great majority of new jobs created for the public are provided by small companies with fewer than 500 employees. From 1981 to 1988, companies with fewer than 500 employees contributed 11.7 million new jobs to the economy. In this period, America's small companies generated two thirds of all new employment.

THE MISINFORMATION THAT SUPPORTS THE PENDING LEGISLATION

An Intel executive who apparently didn't take the time to actually study the *TechSearch v. Intel* case had this to say in recent testimony before Congress:

> "If someone buys a patent for 50,000 bucks and their business model is suing people, should they be able to get an injunction?" he asked.
>
> That's the situation Intel faced several years ago when TechSearch, a patent-holding company in Northbrook, Ill., acquired a patent for $50,000 and then sued Intel, demanding $5 billion to settle the case. Simon cited this case in

> testimony before an April 21 Senate hearing on patent reform. While Intel had won summary judgment in that case, Simon testified that there are many district courts where judges are less likely to grant summary judgment. He cited one forum, which he didn't identify, where all the verdicts issued over an eight-year period were in favor of the plaintiffs.

We suppose if Intel had bought the IMS patent (as it tried to do) and then sued its competitors for an injunction, that would be okay. With such misinformation, it is small wonder that we have Representative Lamar Smith, a Texas Congressman who introduced the anti-patent bill in the House saying, "I think patent trolls are abusing the system." "*Congress Targets Rise In Patent Suits*," Werner, E., June 9, 2005.

Who decides who is abusing the patent system? Did Xerox abuse the patent system when it obtained hundreds of patents on copier designs it never intended to make? What about IBM that reported $1.7 billion in licensing revenues in its 2002 Annual Report or Qualcomm with $850,000 in annual licensing revenues or Texas Instruments which expects $1 billion in licensing fees from a single patent license with Hyundai Electronics? What about Intel's own aggressive litigation tactics against its competitors?

An individual inventor or small company that lacks the financial resources to take on the big guy in high-stakes litigation should not be forced to grant compulsory licenses. And, tellingly, the voices urging that the current system is unfair have yet to identify a single example where the issuance of an injunction for a non-manufacturer was inappropriate under the circumstances.

COMPULSORY LICENSES WILL UNDERMINE THE PATENT SYSTEM

As Alex Poltorak, Chairman and CEO of General Patent Corporation, said: "God created big companies and small inventors. And He created an injunction to make them equal." The right to exclude is the essence of property. Without it, the playing field can never be leveled. Who fears a compulsory license? Certainly not a corporate giant who can protract a lawsuit by as much as four to six years and afford to pay $2 to $10 million in fees. The big guy wants a compulsory license since, by eliminating the threat of an injunction, it can achieve a "heads, I win; tails, you lose" situation. Patent infringers, of course, should not be permitted to take a "heads, I win; tails, you lose" approach to damages. If they lose at trial, infringers are not treated like willing licensees: "[an] infringer would have nothing to lose, and everything to gain if he could count on paying only the normal, routine royalty non-infringers might have paid." *Panduit Corp. v. Stahlin Bros. Fibre Works*, 575 F.2d 1152, 1158 (6th Cir. 1978) (opinion written by former Chief Judge Markey of the Federal Circuit).

Raising the bar to obtain injunctive relief as the Supreme Court has done in *eBay Inc., et al. v. MercExchange*, No. 05-130, May 15, 2006, has brought the threat of compulsory licensing one step closer to reality. And the little guy, no matter how it gets sugar-coated, will suffer. Ironically, this "reform" will increase - not decrease - the burden on the judiciary, as infringers (willful or unwitting) will have little or no incentive to negotiate a settlement.

Also forgotten in these debates about patent trolls, the unfairness of injunctions, the need to eliminate findings of willfulness and the like is the important role played by trial judges. Injunctions are discretionary, not mandatory. So, too, are increased damage awards after a jury finding of willfulness. If there is something amiss, the trial judge can fix it by granting JMOL, denying an injunction or refusing to increase damages.

So where is all this patent trolling stuff coming from? No doubt, the enforcement of patents can become abusive if a good-faith basis to assert a patent does not exist. But that threshold applies to every party -- large or small. And those who accept cases on a contingent-fee basis would be foolish to take questionable cases that are destined for failure.