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The Impact of Abusive Patent Litigation Practices on the American Economy

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BEFORE THE

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CONTENTS

MARCH 18, 2015, 10:02 A.M.

STATEMENTS OF COMMITTEE MEMBERS

	Page
Grassley, Hon. Charles E., a U.S. Senator from the State of Iowa	1
prepared statement	48
Leahy, Hon. Patrick J., a U.S. Senator from the State of Vermont	3
prepared statement	51

WITNESSES

Witness List	47
Anderson, Steven E., Vice President and General Counsel, Culver Franchising System, Inc., Prairie du Sac, Wisconsin	10
prepared statement	53
Crum, Michael R., D.B.A., Vice President for Economic Development and Business Engagement, Iowa State University, Ames, Iowa	12
prepared statement	59
Gupta, Krish, Senior Vice President and Deputy General Counsel, EMC Corporation, Hopkinton, Massachusetts	13
prepared statement	67
Powers, Brad, General Counsel, KINZE Manufacturing, Inc., Williamsburg, Iowa	6
prepared statement	85
Sauer, Hans, Ph.D., Deputy General Counsel for Intellectual Property, Biotechnology Industry Organization, Washington, DC	8
prepared statement	89

QUESTIONS

Questions submitted to Michael R. Crum, D.B.A., by Senator Perdue	113
Questions submitted to Krish Gupta by Senator Grassley	111
Questions submitted to Hans Sauer, Ph.D., by Senator Perdue	114

ANSWERS

Responses of Michael R. Crum, D.B.A., to questions submitted by Senator Perdue	116
Responses of Krish Gupta to questions submitted by Senator Grassley	124
Responses of Hans Sauer, Ph.D., to questions submitted by Senator Perdue	134

MISCELLANEOUS SUBMISSIONS FOR THE RECORD

Submitted by Senator Coons:	
Association of American Universities (AAU), Washington, DC, statement	144
Association of Public and Land-grant Universities (APLU), Washington, DC, statement	145
Biotechnology Industry Association (BIO), Washington, DC, statement	146
Innovation Alliance, Washington, DC, statement	149

	Page
Submitted by Senator Coons—Continued	
Medical Device Manufacturers Association (MDMA), Washington, DC, statement	147
National Venture Capital Association (NVCA), Washington, DC, statement	148
New York Intellectual Property Law Association (NYIPLA), Fort Lee, New Jersey, a paper addressing the pleading requirements in patent infringement cases following enactment of the Federal Judicial Conference recommendation to abrogate Form 18 of Fed. R. Civ. P. 84, white paper	140
Pharmaceutical Research and Manufacturers of America (PhRMA), Washington, DC, statement	148
Submitted by Senator Durbin:	
Taylor, Robert, Founder and Owner, RPT Legal Strategies PC, San Francisco, California, statement	220
Submitted by Senator Grassley:	
Ackerman, Andrew, Managing Director, Dreamit NY, et al., March 17, 2015, letter	214
American Bankers Association, Washington, DC, et al., statement	201
Asay, Clark D., Brigham Young University J. Reuben Clark Law School, Provo, Utah, et al., economics and legal scholars who study innovation, intellectual property law, and policy, March 2, 2015, letter	171
Business Software Alliance (BSA—The Software Alliance), Washington, DC, March 17, 2015, letter	153
Capital Financial Partners, West Des Moines, Iowa, March 1, 2015, letter	154
Casey's General Stores, Inc., Ankeny, Iowa, March 23, 2015, letter	155
Delta Dental of Iowa, Johnston, Iowa, March 10, 2015, letter	156
Draper, Mike, Founder and Owner, RAYGUN, Des Moines, Iowa, letter	200
Duan, Charles, "The STRONG Patents Act Is a Death Squad for Innovation: Commentary," *Roll Call*, Beltway Insiders, March 17, 2015, op-ed article	207
Iowa Gaming Association, West Des Moines, Iowa, et al., Iowa associations, organizations, and businesses, March 13, 2015, letter	169
Iowa Gaming Association, West Des Moines, Iowa, March 16, 2015, letter	170
Iowa Wireless Services, LLC, Urbandale, Iowa, March 12, 2015, letter	180
Kinzenbaw, Jon, President and Chief Executive Officer, KINZE Manufacturing, Inc., Williamsburg, Iowa, "Stop patent trolls from preying on innovation," March 15, 2015, statement	205
Kreg Tool Company, Huxley, Iowa, March 16, 2015, letter	181
Kum & Go, L.C., West Des Moines, Iowa, March 13, 2015, letter	183
Mitchell, Matthew, Independent Insurance Agent, West Des Moines, Iowa, March 3, 2015, letter	184
National Association of Federal Credit Unions (NAFCU), Arlington, Virginia, March 17, 2015, letter	150
National Association of Realtors (NAR), Washington, DC, March 17, 2015, letter	185
National Retail Federation (NRF), Washington, DC, statement	187
Nelson, Curtis R., President and Chief Executive Officer, Entrepreneurial Development Center (EDC), Cedar Rapids, Iowa, March 10, 2015, letter	157
article	158
2014 stakeholder report	160
R Street Institute, Washington, DC, et al., letter to Hon. Bob Goodlatte, a Representative in Congress from the State of Virginia, and Hon. John Conyers, Jr., a Representative in Congress from the State of Michigan, March 12, 2015	151
Snively, David F., General Counsel, Monsanto Company, Creve Coeur, Missouri, statement	196
Stretch, Colin, Vice President and General Counsel, Facebook, Inc., Menlo Park, California, March 17, 2015, letter	166
United for Patent Reform (UPR), March 16, 2015, letter	209

THE IMPACT OF ABUSIVE PATENT LITIGATION PRACTICES ON THE AMERICAN ECONOMY

WEDNESDAY, MARCH 16, 2016,

UNITED STATES SENATE,
COMMITTEE ON THE JUDICIARY,
Washington, DC.

The Committee met, pursuant to notice, at 10:02 a.m., in Room 226, Dirksen Senate Office Building, Hon. Charles E. Grassley, Chairman of the Committee, presiding.

Present: Senators Grassley, Hatch, Cornyn, Lee, Flake, Perdue, Tillis, Leahy, Feinstein, Schumer, Durbin, Whitehouse, Klobuchar, Franken, Coons, and Blumenthal.

OPENING STATEMENT OF HON. CHARLES E. GRASSLEY, A U.S. SENATOR FROM THE STATE OF IOWA

Chairman GRASSLEY. We're here today to discuss the topic of patent litigation abuse, and in particular, the destructive tactics of so-called "patent trolls." This practice of patent trolling has hit businesses both big and small across all industries and is having a harmful effect on the economy.

Patent litigation abuse imposes high costs on American businesses. It wastes resources that could instead be utilized for research, development, job creation and economic growth. It undermines the innovation and creativity that patents are supposed to protect.

Patent assertion entities focus on buying and asserting patents rather than on developing or commercializing patented inventions.

Now, I want to make clear that licensing one's patents is not itself a bad thing. Inventors and patent owners, including universities, often are not in a position to commercialize their patented inventions, but they certainly have the right to protect their intellectual property against infringers.

Patent trolls, however, are entities that engage in abusive and deceptive tactics to assert poor-quality patents against businesses already utilizing technologies as common as wireless email, digital video, and internet. They use overly broad patents to allege infringement against companies that are simply engaging in normal business activities or have bought a technology, product or service from a vendor, many times buying that right off the shelf.

They send out intentionally evasive and misleading blanket demand letters and employ overly aggressive litigation practices to extort settlements. They frequently hide behind patent-holding

subsidiaries, affiliates, and shells of operating companies in order to escape scrutiny.

Frivolous patent lawsuit filings have increased over the years and they rarely have merit. But the extent of the problem is actually much worse because most cases do not reach merit judgment stage. Patent trolls strategically set their royalty demands below litigation costs to entice companies to settle rather than run the risk of expensive and risky patent litigation.

Many companies do not have that expertise or even the resources to litigate these cases. So, most of the time they have no choice but to submit to this patent extortion.

This, in turn, drives up the costs many times; then those costs are passed on to the consumer.

We will be hearing from three witnesses today about their experiences with, and the impact of, abusive patent litigation tactics. These witnesses represent businesses from different industries. Two of these companies have patent portfolios, while one company doesn't own patents.

Yet, their conclusion is the same—patent troll abuse is counterproductive to our Nation's economic growth.

The United States should remain at the forefront of technology, innovation, creativity. Patents and the U.S. patent system are a significant component of the American tradition of opportunity, invention and innovation. But we should not allow bad actors to bring the entire system down.

I have heard many Iowans express concerns about this problem and the need for Congress to take action. One example is a letter I just received coming from industry groups, representing a diverse mix of Iowa businesses, letters from the Iowa Gaming Association, the Iowa Bankers, Homebuilders of Iowa, Restaurant Association, Retail Federation, Communications Alliance, Grocery Industry Association, Lodging Association, Iowa Credit Union League and Iowa Realtors Association.

They urge Congress to address these abuses, stressing that—and I have a long quote—"meaningful reforms that make it difficult for patent trolls to continue their destructive business models by improving patent quality, streamlining litigation, enhancing discovery protections and pleading requirements, as well as increasing transparency will drastically reduce costs for Iowa businesses and entrepreneurs," end of quote.

I would put these letters and several others, without objection, in the record.

[The information appears as submissions for the record.]

Chairman GRASSLEY. In the last Congress, the House passed an overwhelming vote on the Innovation Act, which the White House supported. And although we started working on a product here in the Senate Judiciary Committee, we were not able to proceed last year.

Almost everyone agrees this is a problem and a drag on our economy, but there are those concerned that certain proposals could undermine the ability of legitimate patent holders to enforce patent rights.

They maintain that recent Supreme Court decisions on pleading standards, fee shifting, and patent quality, as well as actions by

the Federal Trade Commission and the U.S. Patent and Trademark Office have largely taken care of all these issues, and comprehensive legislation, then, is unnecessary.

We will be hearing from representatives of two different stakeholder communities that believe certain proposals under consideration by Congress will harm legitimate patent holders.

I do not dispute that we should preserve patent rights and valid patent enforcement rules. We do need to strike the right balance, but Congress should act decisively if we want to alleviate the problems that are harming businesses both big and small. This will strengthen our patent system, benefit inventors, businesses and consumers. So, here we are, back at it again in this Congress.

Chairman Goodlatte of the House has reintroduced the Innovation Act. It has 9 Republican and 11 Democratic cosponsors. I look forward to working with Ranking Member Leahy, Senators Cornyn and Schumer, as well as with any other Judiciary Committee colleagues that want my attention on this issue, on passing meaningful legislation that will provide a strong deterrent to those who prey on innocent businesses.

I thank my witnesses who are here today to provide us with their valuable insights on patent litigation abuse and how they think Congress should address the issue.

[The prepared statement of Chairman Grassley appears as a submission for the record.]

Chairman GRASSLEY. Now it is my privilege to turn our attention to the Ranking Member, former Chairman of the Committee, Pat Leahy.

OPENING STATEMENT OF HON. PATRICK J. LEAHY, A U.S. SENATOR FROM THE STATE OF VERMONT

Senator LEAHY. Thank you very much, Mr. Chairman.

I am glad we are having this hearing and you have got an impressive group here.

It goes without saying that our patent system fuels our Nation's greatest innovations. It is one of the reasons I have worked so hard over the years to finally be able to pass the Leahy-Smith bill, one of the great bipartisan efforts of both the Senate and the House.

But we have seen some bad actors who have used the patent system in ways that detract from its purpose.

I am home several times a month and I talk to small businesses in Vermont who tell me they have been threatened with patent suits simply for using office equipment that they purchased off the shelf and it is a case of, do we fight it or we just pay a nuisance settlement. But the nuisance settlements are sometimes 3 months' to 4 months' profits.

website owners have faced costly litigation for using basic software in e-commerce. So, what happens, instead of using patents to drive new creation, bad actors have held up Main Street businesses and innovative companies to extort financial settlements.

Last Congress, the Senate Judiciary Committee dedicated months of work to develop a bipartisan solution to such behavior. We wanted to promote transparency that hold the bad actors accountable. We wanted to curb misleading demand letters. We wanted to protect customers who are targeted simply for using a product when the manufacturer itself should defend the suit.

We also considered measures relating to patent litigation to address concerns. It is usually difficult to defend against frivolous patent suits, the extreme cost of discovery and the fact that today a patent holder can file a lawsuit with only minimal information. So, a defendant cannot even assess whether they are liable.

Many have raised concerns that, if taken too far, litigation reforms like those in the House-passed Innovation Act would harm legitimate patent holders when they enforce their rights in court.

I agree we must find a balance. Everybody knows the story of the man who developed a windshield wiper delay and had to fight for it until he was actually on his death bed before he was finally given the rights and the royalties for that, I think it amounted to just $.02 or $.03 a windshield wiper.

Now, the Committee was not able to complete its work, but we made significant progress and I hope we can build on that. I think we can look at what we did with the Leahy-Smith act. We did that because Senators and stakeholders, Senators of both parties, House Members of both parties, and stakeholders joined together to find solutions.

Abusive practices by bad actors are a discredit to our strong patent system. It is in no one's interest they continue.

So, the real world accounts we have heard from the New England Federal Credit Union, the Printing Industries of America, some of the businesses who will testify today illustrate the impact of abusive practices.

Mr. Chairman, I will put my whole statement in the record, but I think this is—Senator Cornyn and I worked on—I want Senator Cornyn to know I am talking about him.

Chairman GRASSLEY. Senator Cornyn.

Senator LEAHY. Senator Cornyn and I worked on—I was complimenting you, I was complimenting you. There will probably be a recall petition in Texas for you now because—.

Senator CORNYN. You have my full attention.

Senator LEAHY. But Senator Cornyn and I worked hard on this—a number of us did.

I think we can find—and it is not going to be easy—we can find a solution, but the stakeholders themselves are going to have to work. Nobody is going to get everything they want, but we can get a better situation than what we have today.

Thank you, Mr. Chairman.

[The prepared statement of Senator Leahy appears as a submission for the record.]

Chairman GRASSLEY. Thank you.

To accomplish something in the Senate, we have to have bipartisan support and I think the fact that the leadership of Senator Schumer——

Senator SCHUMER. Thank you for mentioning me.

Senator LEAHY. I was about to mention you next, but I was trying to be bipartisan, because, I mean, everybody hears about you every single day, every single hour.

[Laughter.]

Senator LEAHY. If I had half the fame the Senator from New York has.

Chairman GRASSLEY. You see what happens when you say one word, "Schumer."

[Laughter.]

Chairman GRASSLEY. Anyway, Senator Schumer and Senator Leahy do not always agree with Senator Cornyn and me and Senator Lee, but there is a good-faith effort to work on legislation that can be bipartisan. Senator Coons is involved in it, as well, because he has a bill of his own in, and maybe there are other bills in, as well.

Now, I would like to introduce the panel. We start with Brad Powers, general counsel, KINZE Manufacturing, Williamsburg, Iowa, and that is a leading manufacturer of agricultural machinery in the United States. KINZE happens to be quite a success story.

Jon Kinzenbaw, where the word KINZE comes from, started the company in 1956 with a few dollars in his pocket, a small bank loan and a knack for fixing farm machinery. Since then, Mr. Kinzenbaw has been named inventor of 19 patents for KINZE and the company itself owns many others. Today KINZE employs nearly 1,000 people in Iowa.

Prior to joining KINZE, Mr. Powers worked on IP litigation, licensing and portfolio management at the law firm of McKee, Voorhees and Sease. I understand your family is with you and I welcome them, assuming they get here.

I would like to introduce everybody before you testify.

We have Hans Sauer, deputy general counsel for intellectual property of the Biotechnology Industry Organization, a trade association representing over 1,100 biotechnology companies and research institutions. At BIO, Mr. Sauer advises boards of directors and various departments on patent and other IP matters. He has 20 years' professional in-house experience in that industry.

Steven Anderson is vice president and general counsel for Culver's Franchising System located in Prairie du Sac, Wisconsin, famous for its butter burgers and frozen custard. But I can suggest to you that I like the pork tenderloin better. Culver's has 538 restaurants, 22 of them in States—including over 30 locations in my home State of Iowa, and employs 20,000 people. Mr. Anderson at Culver's is responsible for overseeing all legal matters involving the corporation, including its intellectual property. Prior to Culver's, Mr. Anderson worked as a lawyer at Murphy Desmond.

Then, Dr. Michael Crum, vice president for—I did not mean to skip you. We will get to you in just a minute.

Dr. Crum, vice president for economic development and business engagement at Iowa State University. Dr. Crum has been a faculty member, College of Business, ISU, since 1980. He led the initiative to create the Office of Economic Development and Industry Relations, which helps organizations connect with research, technical, and business expertise of the university.

I suppose I have got to mention that you know Iowa State is in the big dance.

Senator LEAHY. Is that right?

Chairman GRASSLEY. Yes, that is right. And also the University of Northern Iowa and also the University of Iowa. So, let us get them all in.

We have Krish Gupta, senior vice president and deputy general counsel at EMC Corporation, located in Hopkinton, Massachusetts. EMC is the world's leading developer and provider of information infrastructure technology.

Mr. Gupta has 20 years' experience working in patent law. At EMC, he has worldwide responsibility for intellectual property law and technology licensing matters.

He oversees EMC's IT portfolio of over 5,100 U.S. patents, a portfolio that has earned that company recognition by the Wall Street Journal as the eighth most innovative IT company.

Mr. Powers, would you start out, please?

STATEMENT OF BRAD POWERS, GENERAL COUNSEL, KINZE MANUFACTURING, INC., WILLIAMSBURG, IOWA

Mr. POWERS. Thank you, Chairman. Chairman Grassley, Ranking Member Leahy, and Members of the Judiciary Committee, I am Brad Powers, general counsel of KINZE Manufacturing. On behalf of Jon and Marcia Kinzenbaw, KINZE Manufacturing, we are honored to have the opportunity to present testimony today about the profound negative impacts of abusive patent assertions on our company, innovation, and our economy.

KINZE Manufacturing is a leading manufacturer of planters in the United States. But it did not start that way. In 1956, Jon Kinzenbaw was 21 years old. With $5 in his pocket, a small bank loan and a gift for fixing farm equipment, he opened a one-man welding shop in Victor, Iowa.

Jon has been named the inventor for 19 patents and our company holds many more. Jon's first patented invention was a plow that the farmer could adjust from the comfort of his tractor. Shortly thereafter, Jon invented a single-axle grain cart. Probably most notable was the rear-folding planter that Jon invented in 1975.

After that, the company grew quickly. KINZE today impacts Iowa factory workers, as well as farmers and small business owners throughout the country. KINZE is still privately held by the Kinzenbaw family and has employed up to 1,000 people in the State of Iowa, manufacturing high-quality agricultural equipment, providing farmers with the tools they need to help feed the world.

Our products are distributed through a network of independently owned dealers located in agricultural States throughout the country.

Now, KINZE is built on innovation and relies upon a strong and healthy patent system to continue to deliver that innovation to our farmers. KINZE has asserted its patents against our competitors. We have defended ourselves from allegations by competitors and we have taken three patent cases to trial.

Litigation is a part of the process and when that litigation is with merit, we accept this. Unfortunately, patent assertion entities take unfair advantage of the patent system and today threaten its health.

In 2012, KINZE experienced the impact of a patent assertion entity firsthand when Clear With Computers sued KINZE, alleging infringement of two of its patents.

Now, unlike KINZE, Clear With Computers does not employ any factory workers, it does not help American farmers, and it makes no products. What it does do is it makes lawsuits. It has filed over 60 patent cases since 2008.

Clear With Computers argued that KINZE's website violated the company's patents for an electronic proposal preparation system and an electronic proposal preparation system for selling computer equipment and copy machines.

In short, the complaint alleged that KINZE infringed these patents by allowing users to search for products and filter search results. This suit cost us many hours of time and significant legal fees before we were ultimately able to resolve the dispute.

Now, that experience has had a lasting impact on KINZE. Farmers rely on access to the latest technology to help them get more out of every acre while reducing their costs and protecting their soil. But KINZE's contract negotiations with suppliers and service providers now routinely include discussions of allocations of liability in the event of patent assertion.

These additional negotiations require resources and delay research, development and production of new products, slowing farmers' access to key technology. We are spending more time and effort developing contracts and have less time and effort to spend on developing the new inventions that will make farming more productive and efficient.

This allocation of IT liability also limits KINZE's ability to work with small companies. Smaller companies, because of their limited resources, are hesitant to provide indemnification for IT liability.

As a result, many smaller companies must decide whether to sign an agreement and accept the risk of defending baseless suits or not accept the work at all.

Now, in the beginning, patent assertion entities seemed to focus on web-based software. This is what KINZE saw with Clear With Computers. But unfortunately, the problem seems to be spreading beyond this limited domain.

By way of example, companies like Cisco Systems have seen this type of issue in areas such as electronic equipment. Now, as you can imagine, the planters used today have come a long way since Jon's first folding planter back in 1975. New technology lets farmers precisely target inputs, such as fertilizer and insecticide, reducing their costs and also benefiting our environment. This technology includes high-tech electronics, GPS location, and cutting-edge software.

As this technology moves to the field, it is no stretch of the imagination to believe the assertion entities will follow. The patent system, which was designed to foster innovation and bring the fruits of American creativity to everyone, has been thrown off balance by a few bad actors taking advantage of the high cost and uncertainty of litigation. Congress must step in to restore this balance and KINZE is ready and eager to be part of that effort.

Thank you, once again, for giving the Kinzenbaws and KINZE the opportunity to talk on this critical issue. As you consider the

legislation to address the very real threat posed by these patent assertion entities, we strongly encourage you to consult representatives from all industries, including agricultural manufacturing.

Improving our patent system is a vital and ongoing process and we thank you for your commitment to seeking the right balance between providing incentives for innovation and protecting American businesses from the high cost of illegitimate patent litigation.

Thank you.

[The prepared statement of Mr. Powers appears as a submission for the record.]

Chairman GRASSLEY. Thank you, Mr. Powers.

Mr. Sauer?

STATEMENT OF HANS SAUER, PH.D., DEPUTY GENERAL COUNSEL FOR INTELLECTUAL PROPERTY, BIOTECHNOLOGY INDUSTRY ORGANIZATION, WASHINGTON, DC

Mr. SAUER. Chairman Grassley, Ranking Member Leahy, and Members of the Committee, thank you, again, for the opportunity to testify here today. I am deputy general counsel for intellectual property at the Biotechnology Industry Organization, on whose behalf I testify today.

In my previous experience before BIO, I worked in a number of drug development programs at several biotech companies over the course of 20 years, first as a scientist and later as a patent lawyer. As is common in the biotech industry, the companies where I worked are now gone and the stroke and Parkinson's disease drug programs on which I worked failed after tens of millions of dollars of investment.

The majority of today's biotech companies face serious similar odds. Approximately 80 percent of BIO's member companies are small and have yet to bring a product to the market, and thus their research and development work is funded through massive private sector high-risk investment which, on average, amounts to more than $2 billion, fully capitalized, for a new biotech medicine. This investment must be sustained over many years; sometimes decades.

Without strong, predictable and enforceable patents, rational investors would stop investing in these possible new therapies and take their money elsewhere. Patents are thus critical to the biotech business model, not to use them for litigation, but to secure the partnerships and investment which our companies need to develop new therapies, new crops, and new biofuels.

As Congress considers legislation to curb misuses of the patent system, it must ensure that innovative companies remain able to protect their own businesses against patent infringement by others. And in scrutinizing dubious practices by some patent holders, Congress should not overlook abuses by others who seek to undermine the patent system for similarly illegitimate reasons.

Unfortunately, misuse of the patent system against patent holders or licensees is also a real and growing problem. In particular, the PTO's inter partes review, IPR system, of administrative patent challenges is undermining the value of predictability of patent rights and long-held, investment-backed expectations. This is because this new system stacks the deck against patent owners in

ways Congress did not intend, leading to patent invalidation rates far exceeding those seen in district court litigation involving similar types of patents and similar grounds for challenges. These disproportionate kill rates invite unintended abuses and predatory practices.

For example, questionable entities are approaching biotech companies with threats of dragging their key patents into IPR proceedings in the patent office unless substantial payments are made. And recently, The New York Times reported on an investment scheme in which a hedge fund first takes a short position in the stock offer by a pharmaceutical company and then files an IPR challenge against that company's key patents to drive down the company's stock.

Biotech companies are vulnerable to such manipulation because they tend to be small, derive most of their revenue from only one or two products, and have just a handful of very valuable patents protecting these products.

The first company to be targeted by this hedge fund strategy was a small biotech company whose main product is an innovative treatment that helps patients with multiple sclerosis walk better. On the day that the IPR challenge was filed, this company lost more than $150 million of market capitalization during the course of a single afternoon.

Such cynical strategies not only damage the value of companies working on cures, but hurt those who are eagerly waiting for such cures.

To prevent such abuse, Senators Coons, Durbin and Hirono have introduced S. 632, the STRONG Patents Act, which BIO supports, as a complement to other ongoing legislative considerations.

BIO encourages this Committee to develop a legislative package that will curb abusive patent practices, including the abuse of the IPR system, and to do so through a balanced and targeted approach.

We believe consensus can be achieved on a big range of issues, such as enhancing transparency of patent ownership and enforcement, curtailing unfair practices in the sending of demand letters, addressing how patents can be enforced against blameless end users and consumers of infringing products that were sold by others, and making the IPR system a more balanced one.

→ double check, sounds weird

We remain concerned, however, that proposals for more systemic patent litigation changes presently sometimes lack this requisite balance.

Concepts such as enhanced pleading requirements, mandatory stays of merits discovery, and joinder of third parties for the purpose of collecting attorney fee awards are one-sided and go too far in restricting the ability of patent owners to enforce the patents.

→ ignore highlight

The reintroduction of the Innovation Act in the House of Representatives relies on a dramatically shifted landscape, this debate over the right balance. Court decisions, conference changes in the judicial conference, PTO actions, and legislative and enforcement activities over the past few years have changed the dynamics and the results have been a substantial decline in such suits since this Committee last considered broad patent litigation reforms.

"result has been"

These changes reinforce the need to ensure that any additional changes do not swing the pendulum too far. We are optimistic that targeted and balanced solutions that address the practices of entities who unfairly enforce and who unfairly attack patents can be achieved.

Thank you for your attention and this opportunity. I look forward to answering your questions.

[The prepared statement of Mr. Sauer appears as a submission for the record.]

Chairman GRASSLEY. Thank you, Mr. Sauer.

Mr. Anderson?

STATEMENT OF STEVEN E. ANDERSON, VICE PRESIDENT AND GENERAL COUNSEL, CULVER FRANCHISING SYSTEM, INC., PRAIRIE DU SAC, WISCONSIN

Mr. ANDERSON. Chairman Grassley, Ranking Member Leahy, and Members of the Judiciary Committee, I am Steve Anderson, vice president and general counsel of Culver Franchising System, Inc.

Thank you for the opportunity to testify about the impact of abusive patent litigation practices on Culver's restaurants. Culver's has been a family business from the very beginning, opening its first restaurant in Sauk City, Wisconsin, in 1984, offering cooked-to-order butter burger hamburgers, with fresh frozen custard, that remain the hallmark to this day.

We currently have 538 restaurants, all but seven of which are franchised, serving our customers in 22 States, and those restaurants employ more than 20,000 people. We are experts in delivering great food with warm hospitality to guests. We are not experts in the fields of technology or patent law.

Restaurants in the U.S. account for an estimated $709 billion in annual sales and serve 130 million hungry customers every day. Restaurants create meals and restaurants create jobs. However, most restaurants are small businesses, like our franchisees, and operate on very thin margins. We simply cannot afford to litigate patent infringement lawsuits and we lack the technical expertise to evaluate the merits of technology patent claims. This makes restaurants prime targets for patent trolls.

In the past few years, Culver's has been the recipient of two demand letters and one lawsuit from patent trolls. Each entity claimed to own the rights to basic technology used by many restaurants. In the lawsuit, it was a nutritional calculator on our website and in one demand letter it was the use of shortened lengths and time content in text messages. The third instance, another demand letter, I cannot address since the resolution of this demand included a confidentiality agreement that forbids further public discussion.

As general counsel for Culver's, there is nothing that I dread more than receiving a patent demand letter. They are broadly drafted form letters to offer nothing on the validity of the patent, exactly what the alleged violation may be, and whether or not we were actually infringing upon that patent. These trolls are happy to tell us that we are welcome to test their claims in litigation, knowing that a trial is cost prohibitive, with typical attorney's fees

"that"?

of well over $1 million, and too much of a burden for our business to undertake.

These trolls strategically offer an alternative of the licensing fee that is a mere $250,000 to $500,000. This demand amount has nothing to do with the value of the technology, but is instead offered as a less-expensive alternative to litigating. And although we do not know if the patent is valid, let alone whether we were indeed infringing upon it, this form of extortion is very effective and, in most cases, the recipient of this type of demand letter pays the demand.

Moreover, the money we spend dealing with these demands have to come from somewhere. We must divert it from other places in our business that might be productive and profitable and instead use it to placate trolls.

Patent trolls strategically target their demands against the end user, who is a customer of the technology and has limited knowledge of the technology or patents around it, rather than the producers and sellers of the technology. We cannot insure against such claims and we cannot rely on technology providers to indemnify us for the cost of these risks.

As a result, we have resorted to avoiding the use of technology wherever possible or only purchasing from large-enough companies to protect us against patent claims.

Other small businesses suffer as we are not buying the services from them because we cannot afford to risk another patent demand letter.

When Culver's receives a troll demand letter, we have lost, because by simply receiving that letter, it will cost us a minimum of $100,000 in legal fees and licensing payments. I know this from my own experiences, as well as from speaking to many other companies.

I urge you to consider every useful change that could increase transparency and shift the economic incentives away from trolls making baseless claims. In particular, we at Culver's urge you to consider three improvements.

First, we believe that increased demand letter transparency would be very effective. Second, clear and complete pleading standards for suits that are filed would have a positive effect in the same way that the transparent demand letters would. Third, it is crucial that the suits against the customer are stayed while suits against the manufacturer proceed.

With these changes, patent assertion entities would be required to be more open and target the appropriate parties first, which would put everybody on the same level playing field in terms of information and resources.

Thank you, once again. We urge Congress to pass meaningful reforms so that Culver's and other restaurants can spend more funds on jobs and services that benefit the American economy and less on payments to patent trolls.

[The prepared statement of Mr. Anderson appears as a submission for the record.]

Chairman GRASSLEY. Thank you, Mr. Anderson.

Dr. Crum?

STATEMENT OF MICHAEL R. CRUM, D.B.A., VICE PRESIDENT FOR ECONOMIC DEVELOPMENT AND BUSINESS ENGAGEMENT, IOWA STATE UNIVERSITY, AMES, IOWA

Dr. CRUM. Thank you, Chairman Grassley, Ranking Member Leahy, and Members of the Judiciary Committee, for this opportunity to testify on such an important topic.

I am Mike Crum and I serve as vice president for economic development and business engagement at Iowa State University.

On behalf of Iowa State, I am pleased to offer this testimony, which is endorsed by the six major higher education associations and councils that collectively represent the majority of our Nation's research universities.

Universities depend on the U.S. patent system to protect the legitimate intellectual property rights of individual university inventors and large companies alike. Patents provide universities with the means to ensure that the many discoveries resulting from our research are transferred to the private sector where those discoveries can be turned into innovative products and processes that power our economy, create jobs, and improve our quality of life.

At my home institution of Iowa State University, technology transfer has led to numerous and diverse technologies that have had a major impact locally, nationally, and globally.

A few of the more prominent examples include a critical algorithm for the fax machine, the vaccine for the PED virus that has really threatened our State's hog industry, the patented lead-free solder that has been licensed by some 60 companies globally, with roughly 70 percent of the electronics worldwide containing this solder, and hybrid corn which just this year was named by the Association of University Technology Managers as one of the 40 most important inventions by a university.

Iowa State pulls in over $300 million annually in external funding to support the research that is conducted by our students and faculty. University economic development units provide business and technical assistance to more than 4,000 Iowa companies each year. One of our centers alone generated an impact totaling over $1.7 billion, with more than 25,000 jobs added or retained over the last 5 years.

Between 2010 and 2014, the three State of Iowa regent universities, the University of Northern Iowa, Iowa State and University of Iowa, demonstrated that they do more than just being good at basketball, as the Chairman noted.

During that 5-year period, we generated more than 1,000 invention disclosures, 767 patent applications, and we were responsible for the execution of 472 licenses and options, including 183 to companies in Iowa.

Additionally, our faculty and students launched 190 start-ups supported by over $24 million in outside funding.

The ability of our university's technology transfer operations to achieve the types and magnitudes of societal benefits that I just described is critically dependent on a strong patent system. Without robust patent protections, licensees and venture capitalists will not take on the significant risks associated with investing in and developing our inventions. Strong patents are particularly essential for

the small, often undercapitalized start-up companies built upon university discoveries.

Indeed, patents are often the most critical assets of these start-ups and small businesses. To be able to gain a foothold in often well-developed markets, such companies must be able to assert their patent rights effectively.

It is also crucially important for universities and their licensees to be protected from potentially crippling abusive patent litigation practices. We recognize that abuse of patent litigation practices are a corrosive assault on the Nation's patent system and must be forcefully countered.

We also believe strongly, however, that any changes to the patent system should be scrutinized carefully for their unintended and undesirable consequences.

Many of the proposed changes do have an adverse impact on the ability of patent holders to protect their intellectual property rights. For instance, mandatory fee shifting and involuntary joinder are especially troubling to the university community. These provisions would make the legitimate defense of patent rights excessively expensive and risky. They would impede the ability of universities to forge mutually beneficial agreements with potential licensees and venture capitalists.

Proposals for heightened pleading, discovery limitations and increased disclosure would also, in our opinion, do more harm than good. Heightened pleading would add unnecessarily to the burden of filing infringement cases. Discovery limitations would preclude cases where broader discovery would lead to more efficient resolution of those cases, and new disclosure requirements would require information that could violate confidentiality agreements, thereby chilling venture capital investments.

In closing, universities recognize that abusive patent practices are real and they are harmful. We contend that an approach involving carefully targeted legislation developed in the context of the changing landscape created by recent judicial and administrative actions can effectively combat abusive patent practices while maintaining the capacity of our robust patent system.

Again, we appreciate this opportunity today to present our perspective and we sincerely want to continue to work with the Committee and Congress in constructing legislation that supports the innovation and economic competitiveness for the benefit of the Nation and its citizens.

Thank you.

[The prepared statement of Dr. Crum appears as a submission for the record.]

Chairman GRASSLEY. Thank you, Dr. Crum.

Mr. Gupta?

STATEMENT OF KRISH GUPTA, SENIOR VICE PRESIDENT AND DEPUTY GENERAL COUNSEL, EMC CORPORATION, HOPKINTON, MASSACHUSETTS

Mr. GUPTA. Chairman Grassley, Ranking Member Leahy, and Members of the Committee, I am Krish Gupta, senior vice president and deputy general counsel for EMC Corporation. I am honored to testify today on the critical need for patent litigation reform.

EMC is a global leader in cloud computing and has a keen interest in a strong and balanced patent system that protects and promotes innovation and one that cannot be exploited by abusive litigation tactics.

We look to the U.S. patent system to protect our innovations and the jobs that result from them. EMC and its affiliates hold more than 9,000 issued U.S. patents and patent applications.

At EMC, I have worldwide responsibility for IP law, including patent litigation. In my 20 years in this field, I have witnessed firsthand how our patent system has undergone transformation, but not always for the better.

Abusive patent litigation has swept our country, diverting billions of dollars from economic growth and innovation to battling frivolous suits filed by abusive litigants.

Since 2005, EMC has been sued by patent assertion entities, or PAEs, more than 35 times and has never been found to have infringed. A typical PAE suit involves a shell company with secret backers created solely to file suits. The complaint is often vague and provides little information about the specific infringement allegations.

Shortly thereafter, PAEs try to pressure us into settlement by demanding thousands of documents and emails during discovery, most of which are irrelevant to the suit and costly to produce.

As a matter of principle, we do not settle frivolous suits. Yet, defending those suits has been extremely expensive, costing over $10 million in 2014 alone, and this does not include the substantial disruption to our business, requiring our employees to shift their attention from designing new products and growing the business to sitting in depositions or going to court. And EMC is not alone in this regard.

Most impartial observers agree abusive patent litigation harms innovation and the economy as a whole. In 2014, more than 5,000 new patent lawsuits were filed, the third highest count ever.

Some have suggested that recent Supreme Court decisions and administrative processes at the PTO either reduce or negate the need for Congress to act.

As a practitioner who spends most of his time on patent litigation matters, I disagree. Only Congress can comprehensively address abusive patent litigation practices.

In *Highmark* and *Octane*, the Supreme Court loosened the standard by which district courts have valued what qualifies as an exceptional case for the award of attorney's fees while granting them greater discretion to make this determination. However, *Highmark* and *Octane* have had no meaningful impact.

In the first 9 months since these decisions, motions for fees have been granted only 4 percent more often than they were in the 2 years before these cases and at least one highly experienced and respected judge with a large patent caseload has stated that he does not see *Octane* changing what he would have determined was appropriate for an award of attorney's fees.

We, therefore, support legislation that includes a balanced fee-shifting provision with meaningful fee recovery. These provisions

would discourage the filing of frivolous suits and the use of abusive litigation tactics by imposing financial accountability.

In *Iqbal* and *Twombly*, the Supreme Court addressed the level of specificity required in a complaint. With the Judicial Conference recommending the elimination of Form 18, it is expected that *Iqbal* and *Twombly* will apply to patent pleadings, as well. However, these cases do not set forth bright-line rules for patent litigation, which is a specialized area of the law.

Without clear standards in patent cases, many courts will undoubtedly continue to allow vague pleadings. Furthermore, uniform and clear pleading standards would impose no new burden on good-faith plaintiffs who will have already conducted proper due diligence.

We also support legislation that would reasonably limit discovery before claim construction to ensure that it is focused on issues that actually matter. Further, requiring the requesting party to cover the cost of unnecessary discovery would limit the extent to which it can be used as a bargaining chip to extort a settlement.

These three areas, fee shifting with accountability, pleading specificity and discovery, require legislative intervention. The Judiciary cannot bring about the prompt solution that Congress can structure to ensure consistency and predictability.

EMC believes legislation must be enacted to restore accountability and balance back into the world's premier patent system and to alleviate the unfair burdens that PAEs are able to put on hardworking companies that are the lifeblood of our economy.

Thank you and I look forward to your questions.

[The prepared statement of Mr. Gupta appears as a submission for the record.]

Chairman GRASSLEY. Thank you, Mr. Gupta.

We will have 5-minute rounds for questions. I would like to first start with you, Mr. Gupta and Mr. Powers. I will not repeat the number of patents that you have said your company has.

You have just heard two of the witnesses express concerns about legislative proposals to strengthen pleading, discovery and allow for more fee shifting.

Do you believe that these provisions will diminish the value of patents and harm the ability of patent holders to enforce their patent rights and get investment backing and are these concerns justified?

I will start with you, Mr. Gupta.

Mr. GUPTA. Thank you for the question, Senator. No, I do not believe that these concerns are justified. Patent holders who bring meritorious actions should not be concerned with these provisions. The real effect will be felt by those shell companies who buy patents with secret backers and file vague complaints and then attempt to use the unbalanced and asymmetric discovery burdens to extort settlements.

Pleading specificity, for an example, can only help focus a case early on and with, at least, some clear understanding of what is being accused of infringement and why. In fact, I think specific pleadings will actually help plaintiffs in that we will eliminate a lot of motion practice in terms of specificity of complaints as to whether they satisfy *Iqbal* and *Twombly*.

In discovery, I believe that focused discovery helps both plaintiffs and defendants. Defendants also, if they—if there are some well-heeled defendants who might try to bury plaintiffs with unnecessary and burdensome discovery, some sort of rational discovery, phased discovery proposition is beneficial to both. And the proposals that I have seen also include judicial flexibility, so the judges have discretion.

And last, without some financial accountability, where the risk is not entirely shifted onto defendants, we cannot target or reduce the abuses that we feel in the system and we need accountability in the form of fee shifting for the prevailing party, with an ability to collect those fees.

Chairman GRASSLEY. For your answer, Mr. Powers, do not be repetitive of him, but anything you want to add.

Mr. POWERS. Thank you, Chairman Grassley. No, it would not impact our ability to assert our patents and we largely echo what Mr. Gupta with EMC said.

What I would add is that having done these types of investigations myself both in my capacity at KINZE and as a patent litigator, this is just part of your normal homework. If you are filing a patent lawsuit, you should have done everything you can to obtain the accused infringing product, look at it, develop the claim charts and figure out what really is the case.

So, this should be Patents 101.

Chairman GRASSLEY. For Mr. Gupta, critics of patent reform argue that recent Supreme Court decisions on pleadings of patent fee awards and patent quality have substantially reduced the need for congressional action on abusive patents.

Do you believe the Supreme Court decisions are adequate in terms of deterring abusive and deceptive patent litigation tactics?

Mr. GUPTA. I do not. But I do believe that these Supreme Court decisions have helped clarify certain areas of patent law. None of these decisions go to the core issues of patent litigation abuse. None of these decisions require disclosure of claims that are being asserted, what products are being accused of infringement.

They do not require that the theory of infringement be explained in any way to the defendant. There is nothing in these decisions that reduce the burden and expense of discovery. And these decisions do not make fee shifting the default and certainly there is no mechanism provided by these decisions to ensure that fees can be collected.

reduces?

Chairman GRASSLEY. And then my last question will have to be for Mr. Anderson and Mr. Powers. I would like to explore in more detail the cost of patent troll abuse.

Can you provide some perspective as to the amount of resources your companies have had to devote to fighting off frivolous patent infringement? Has it changed the way you do business? Has there been an impact on the innovative research or development or expansion? Is there a downstream impact, particularly, obviously, on consumers?

Start with you, Mr. Anderson and probably ask for short answers because my time is about up. Go ahead.

Mr. ANDERSON. In terms of the financial impact, we spend hundreds of thousands of dollars and for us that is a big number. I am

hearing some big numbers at the table here, but for us that is a large number.

But what is more troubling is the fact that it really affects the way in which we do business.

Our business as a franchiser is there to support the franchisees, drive business to their businesses and help them succeed.

We are shying away from technology because we cannot afford to play in that world. So, we are not engaging in the technology that our guests want, our franchisees want. When we do look at technology, we are only looking at that from larger companies.

We would love to give the business to the small entrepreneur, but those small entrepreneurs cannot fight the fight. So, we really have backed off the technology and when we do, it has gone to the larger provider.

Chairman GRASSLEY. Mr. Powers?

Mr. POWERS. Thank you, Chairman. With KINZE, there has been a financial cost, but probably the more disturbing cost is, like Mr. Anderson said, the cost on small businesses, their inability to go ahead and play in the big space and be able to bring their technology to market through manufacturers like KINZE.

As a result, the small business suffers, the farmers suffer, and ultimately we all suffer.

Thank you.

Chairman GRASSLEY. Now, I go to Senator Leahy and then after Senator Leahy will be Senator Hatch. I am going to step out just for a minute.

Senator LEAHY. Thank you, Mr. Chairman.

Mr. Anderson, listening to what you are saying, you sound very almost exactly like what I have heard from a lot of businesses and people in my own State of Vermont, people's opinion I respect greatly.

→ take out?

There is one bipartisan solution that Senator Lee and I worked on and that made clear that it is a deceptive trade practice to send misleading demand letters.

We have also authored a customer stay provision. It helps customers who are targeted simply for using a product they purchased off the shelf. And we got broad bipartisan consensus, Senator Lee and I did, for those two provisions.

I think they are essential components of a comprehensive patent troll bill.

Would these solutions be important in what work you do, the customer stay provision and the deceptive trade practice provision?

Mr. ANDERSON. Absolutely. They would be a step in the right direction.

Senator LEAHY. Mr. Powers, I was looking over—preparing for this. There is a KINZE tractor dealership in St. Albans, Vermont. That is up in the northwest corner of our State. It is a heavy agriculture area. But I also know that they are susceptible to being targeted by patent trolls.

Do you agree with Mr. Anderson that the provisions, just to begin with, there will be other provisions, of course, but the ones that Senator Lee and I worked on, would be helpful?

Mr. POWERS. Thank you for the question, Senator. KINZE believes that all measures taken to help stop trolls are good and we welcome them.

Specifically regarding the customer stay provision, I believe is what you asked.

Senator LEAHY. Yes.

Mr. POWERS. We also support the customer stay provision.

Senator LEAHY. Thank you. I am thinking of the restaurants and all. We have not just franchises, but small operations, coffee shops, sandwich stores, and one of the things to get people in is to provide Wi-Fi and stuff like that, and then suddenly they get a demand letter, well, there is this component of it, they get a demand letter. And the question is do they just turn it off or pay the demand letter?

I think some of the people making these demands do not realize you are dealing with individuals—not huge corporations, you are dealing with individuals who work every day to try to make a living.

Mr. Sauer, you raised concerns about abuses of the post-grant review programs that were in the America Invents Act. Those were created to improve patent quality.

I am troubled by some of the behavior you have described, and I was reading your testimony earlier. But we have to have AIA programs as a strong tool for patents to be reviewed by experts.

What do you see as most important of the things you suggested? And can you reassure us it would not undermine the efficacy of the AIA programs?

Mr. SAUER. Yes, Senator. Thank you for that question. The AIA programs, as you rightly point out, were intended as a tool for patent quality enhancement and as a faster and more affordable alternative to district court litigation.

So, as such, these proceedings were created as something that the Patent Office had never done before. Before, they had always examined patents and now they are adjudicating disputes where two parties come in, present their case, and the administrative patent judges, just like judges in district court, are supposed to decide who is right and who is wrong.

And because it is such a trial-like proceeding, we feel strongly that these trials in the Patent Office should have some of the same procedural protections and have the same legal standards that otherwise apply in district court.

So, for example, our particular concerns relate to the way patent claims are interpreted in these proceedings, that patent claims should be interpreted the same way whether it is in district court or in the Patent Office.

The ability to amend claims, which was granted by the AIA, should be more meaningful, and the Patent Office, just as a matter of course, do not allow them really. In two and a half thousand proceedings that have been requested, the Patent Office permitted amendments maybe three times.

does ←

So, there are a couple of ways in which we think these proceedings could be calibrated for some of the protections that are available in district court, because they are like litigation, and that will encourage much more confidence in these proceedings.

Senator LEAHY. Thank you.

Mr. Gupta, do you agree?

Mr. GUPTA. I believe that the IPR proceedings and the post-grant proceedings in general have been very successful. We have filed 19 IPR petitions ourselves and seven of our patents have been challenged using these petitions, and we think that this mechanism has been a very successful mechanism.

People have questioned the high success rate, but what is not typically apparent is that a petitioner makes a very careful decision before they choose to file an IPR petition because of the collateral estoppel effect. And unless there is slam-dunk prior art, people usually do not file petitions.

And it is no surprise that with that strength of prior art, when it goes before the board, that the success rate is high.

Senator LEAHY. Thank you very much. Thank you, Mr. Chairman.

Chairman GRASSLEY. Thank you, Senator Leahy.

Senator Hatch.

Senator HATCH. Thank you, Mr. Chairman.

I believe everyone here agrees it is way past time to do something about patent trolls and to combat them. Last Congress, we began the legislative process to fix this mess and I am optimistic that we will pass patent troll legislation this year.

I have been talking about the problem of patent trolls since 2005 when Senator Leahy and I first began work on the now America Invents Act.

Patent trolls are an unnecessary drain on our economy and our Nation's innovation. An effective legislative approach will include many elements, but in my mind, two are absolutely essential.

First, mandatory fee shifting is the best way to discourage patent litigation and abusive cases which should never have been brought, or defended in the first instance. Fee shifting should not be left primarily to the judge's discretion.

Second, any viable legislation must ensure that those who successfully defend against abusive patent litigation and are awarded fees actually will get paid.

There must be a mechanism to ensure the recovery of fees will be possible even against judgment-proof shell corporations or companies.

Mr. Chairman, whatever we do, it must work and we must not support a bill that fails to provide an effective deterrent against patent trolls at all stages of the litigation.

Now, let me just ask you, Mr. Gupta, a question. Do you agree the Supreme Court's decision in *Highmark* and *Octane Fitness* do nothing to ensure the recovery of fee awards from insolvent shell corporations? → does? did?

Mr. GUPTA. Yes, Senator. Thank you for the question. I do agree. *Highmark* and *Octane* provide no remedy in terms of recovery of fees.

Senator HATCH. When I introduced the Patent Litigation Integrity Act in October 2013, the general counsel of your company wrote to me and said, quote, "By requiring a party to demonstrate that they or a third party have the ability to pay potential fees or explain why they wouldn't, a bonding or similar accountability pro-

vision ensures that the fee-shifting provision has the intended effect of curbing frivolous and baseless patent litigation," unquote.

Now, I am sure you agree with me that we need to curb frivolous and baseless patent litigation, but do you also agree with me that having an effective recovery-of-award mechanism is critical to achieving this goal?

Mr. GUPTA. Yes, Senator. I absolutely agree with that. And I think it is necessary because, as we found out, these shell companies are very creative about how they game the system and we absolutely need a recovery mechanism to ensure that when fees are shifted they can be recovered.

Senator HATCH. Yes. They sue and then run.

Mr. GUPTA. Yes.

Senator HATCH. And leave you holding the bag after countless expenses.

I am concerned about patent quality. I want to ensure that the U.S. Patent and Trademark Office issues the highest quality patents possible. Now, do you believe that allowing the USPTO to apply the broadest reasonable interpretation to patent claims allows them the greatest ability to get rid of bad patents?

Mr. GUPTA. I do agree with that, Senator. And the standard was recently reviewed by the Federal circuit in *Kaz USA* and the Federal circuit agreed that that was the proper standard. It is the standard that the Patent Office has been using for hundreds of years. That has been used for re-examinations and reissues and is indeed the standard that ought to be applied.

And this is the agency that we think has the highest competence when it comes to granting of patents. If they want to revisit or reexamine their work, it is only fair that they be able to do it with the same standard that they used in the first place.

Senator HATCH. Thank you, sir.

Now, Mr. Sauer, you said there has been significant judicial developments in fee shifting that will impact fee awards. Yet Judge Rodney Gilstrap of the Eastern District of Texas, the judge who oversees the most patent cases in the country, said last week that the Supreme Court's ruling in *Octane Fitness* would not significantly alter the standard he uses for deciding whether to grant fees under Section 285 of the Patent Act.

Why should we expect significant changes in the application of Section 285 when the judge who oversees the most patent cases in the country has said that *Octane Fitness* will not change the calculus for him or his colleagues?

Mr. SAUER. Senator, yes. Far be it for me to comment on Judge Gilstrap's pronouncement. What we are aware of is, and it is very early in the process, right? So preliminary numbers did show that there was, after the *Octane Fitness* case, an uptick both in motions that were brought for key fee recovery and for the months following what seemed like an increased grant rate, actually, a significantly higher grant rate of these motions.

Whether or not that is currently tapering off, I think, is subject to debate. Everybody in the community is closely watching this. So, whether or not it will lead to more fee awards I think is a little bit up in the air, but we do see a leveling off, I think at this point that should, at least be taken into account by this Committee.

These cases are widely viewed as very significant and I am kind of surprised that now that they have been done and decided after so much briefing, their significance is being downplayed by those who ask for more mandatory fee shifting and less judicial discretion.

Senator HATCH. The Chairman has allowed me to ask one further question, Mr. Sauer. You mentioned in your written testimony that the joinder provision in the House's Innovation Act would create additional encumbrances for patent-owning innovators. How would it do this?

Mr. SAUER. We are very concerned about the joinder provisions. Senator, yes, it would create encumbrances as introduced in the House in the sense that that provision works by first sending out notices, menacing notices, if you will, at least, so they will be perceived by these business partners of the patentee who could potentially be put on the hook after the litigation is over for their fee award.

So, that is a big concern that is of particular concern to biotech because we work in an ecosystem of licensors, licensees, small businesses, universities. There is a lot of concern about provisions that work after the fact, if you will, but that are premised on notice that is being sent out at the beginning of the lawsuit.

People are very worried about interference with ongoing business relationships that will come from that. And if the target is to target shell companies, we do not think everybody should be put through the process.

Senator HATCH. Thank you. Thank you, Mr. Chairman.

Chairman GRASSLEY. Senator Feinstein.

Senator FEINSTEIN. Thank you very much, Mr. Chairman.

Mr. Anderson, I thought, well stated the problem with demand letters. Mr. Anderson, I just quickly want to read your written statement: "These types of settlement demands can be crippling to small business, but the attorney's fees required to fight the lawsuit might be 10 times as much. So, in most cases, defendants will choose to settle regardless of the extent of their use or the merits of the patent claim."

That is a bingo moment. I found that out firsthand with the ADA—the Disabilities Act, the Americans with Disabilities.

I am in Riverside County and I talked to a group of the Chamber of Commerce, which is a lot of small businesses and many minority businesses, and a group came up to me and said there were these attorneys that sent them demand letters if their "No Parking" sign was in the wrong place, if a trash barrel obstructed part of an entry, whatever it was, and it said that for $10,000, we will not sue.

A lot of them were struggling to pay that. Well, we took a good look at it and the result was that the State legislature passed a bill, Senate Bill 1186, Governor Brown signed it, and essentially it required demand letters to contain specificity as to the wrong alleged.

It prohibited such letters from containing a request to demand money or an offer or agreement to accept money, and, third, prohibiting such letters from stating any specific potential monetary liability.

Do you believe something like that should be in a Federal law?

Mr. ANDERSON. Thank you, Senator. I certainly do, and we have had similar experiences to what you expressed and the first demand letter that we received we brought to our ad agency, who is responsible for the technology.

The demand letter was written so broadly that they did not know what to do with it and the quote was, "This is an amazingly broad letter and we have no idea what they are asserting."

So, it is a problem and it needs to be fixed.

Senator FEINSTEIN. Thank you.

Does any witness disagree with Mr. Anderson's statement?

[No response.]

Senator FEINSTEIN. There being none, for the record. So, I thank you. I would like to move on.

I am sympathetic to the plight of businesses who suffer from abusive discovery requests from patent trolls and recognize that this often creates a one-sided situation and a pressure to settle a case.

As we all know, sometimes discovery is necessary in a legitimate lawsuit. But, does any witness disagree that discovery can be needed for a purpose, such as establishing that the court has jurisdiction over the case and the parties? Does anyone disagree with that?

[No response.]

Senator FEINSTEIN. Good. How would witnesses, you, propose to structure appropriate discovery limitations that make sure the need for legitimate actors to enforce lawful patents is protected? Who would like to begin?

Mr. Gupta?

Mr. GUPTA. Thank you, Senator, for that question. Clearly, in patent litigation there is a sequence to how certain things happen.

A very important aspect of patent litigation is the Markman hearing. And in a Markman hearing, a plaintiff and the defendant will submit their proposals around what an invention actually means and the judge will construe those claims.

What that does is early on you get to focus the case, if the Markman is done early. So, the plaintiffs know what claims they want to proceed with. The defendants then know what type of prior art they need to look for; and often the defendants also then know and the plaintiffs know what products can potentially be accused of infringement.

Focusing discovery, for example, in a way, before Markman, to eliminate any unnecessary and burdensome discovery on things such as sales to customers or licensing agreements with customers or the number of customers, documents and product specifications for pretty much every product that a particular company can offer.

It is wasteful and can be addressed in ways by phasing discovery and also by shifting some of the discovery burden so that core discovery can be paid for by the party that is required to respond, but non-core discovery is paid by the party requesting such discovery.

Senator FEINSTEIN. That is actually very helpful.

Does anyone have a comment to make on that? Mr. Sauer, you raised your hand.

Mr. SAUER. Thank you, Senator. Yes. I actually agree with a lot of what Mr. Gupta says. Our concern really is that the bill, at least

the one that we see introduced in the House, H.R. 9, does not do that.

The bill, H.R. 9, would require in some way to prospectively limit discovery to only what is necessary for claim construction at a time when the parties do not know what is going to be necessary for claim construction.

Senator FEINSTEIN. You like what Mr. Gupta said.

Mr. SAUER. I like what Mr. Gupta said, that there should be a nationally uniform process indeed for the development of information on both sides of the case to make clear what the party's theory of the case is, what evidence backs up the party's theory of the case, and that should lead to a Markman hearing.

I encourage the Committee to look through local patent rules that are in use in a number of district courts that are actually able to get to this claim construction hearing with a bilateral process where parties disclose to each other the information that backs up their contentions and get to a Markman hearing with 9 to 12 months uniformly in this court.

I think that would really help and it would curb the unfocused discovery that is a problem in a number of district courts.

Senator FEINSTEIN. Does anybody disagree with what Mr. Gupta or Mr. Sauer have just said?

[No response.]

Senator FEINSTEIN. Good. I will move on to universities. In the last patent bill——

Chairman GRASSLEY. This will have to be the last question.

Senator FEINSTEIN. I will be fast. Thank you, Mr. Chairman.

The problem always comes in patent revision between universities and small inventors being on one side and the others—the bio, pharma, tech on the other side. It is very hard for me.

I come from a State with a very large and well-known public university system. It leads universities nationwide in the number of patents each year and a substantial part of its revenue is derived from patents. And we graduate thousands of engineers every year.

How would you prevent that from happening? And what is the importance of strong patent protection for universities and small inventors? Mr. Crum?

Dr. CRUM. Yes. I am not sure I have an answer for that. That is part of the balance that needs to be struck.

Senator FEINSTEIN. Right.

Dr. CRUM. And as I hear the conversation around the table, as we talk to small companies that are licensing our technology, just the uncertainty, the risk that they may incur in the loser paying, for example, even if they are convinced that they have a strong case, one loss like that can be devastating to them financially and we are just concerned that it may curb and present a significant barrier to their access to judicial review of those.

Senator FEINSTEIN. I think my time is up. Thank you very much.

Chairman GRASSLEY. I have been kind of liberal on the time. I think we are going to have to stick to 5 minutes, if it does not irritate anybody. Otherwise, we will not get done today.

Senator Cornyn.

Senator CORNYN. Thank you, Mr. Chairman. I never thought of you as liberal.

[Laughter.]

Senator CORNYN. But thank you for your generosity. Thank you for having this hearing. This is an important part of the table setting, I think, for consideration of patent reform legislation.

We got close last year, but it did not happen. So, I am optimistic that we will be able to make progress this year and if there is one word that I guess I have heard all of you use, it is balance.

We need to recognize there are certainly legitimate rights that should be litigated and decided in court, but on the other hand, there is also legal extortion, shaking down people who cannot defend themselves and using that money then to file other frivolous litigation.

Last Congress, I introduced the Patent Abuse Reduction Act, which has several core components, many of which you have talked about already. It requires plaintiffs to plead the substance of their claim; puts lawsuit beneficiaries on the hook for abusive patent litigation from which they profit; and brings fairness to the discovery process; and, finally, shifts responsibility for litigation abuse to the abuser.

I personally am of the view that unless we have an adequate fee-shifting mechanism in the legislation, it is not worth doing. So, I feel very strongly about that.

Mr. Sauer, I think you mentioned some concern about the fee-shifting provision. Perhaps you are referring to the House legislation which has a presumption, and I wonder if you would have any kinder remarks to make about a system that was not presumptive.

Mr. SAUER. I believe I would. And so, to clarify for the Committee, our concern, as it was expressed by our smaller members, because we also have larger members who are more accepting of a fee-shifting provision, our concern was that the House bill would establish what, in the view of our smaller members, would be a true loser pays system, where under the normal American system, ordinarily each pays their own and it is up to the winner to explain why the loser should have to pay.

The House bill would flip that burden and the burden would be on the loser to explain why they should not have to pay.

As we see it, your bill, Senator Cornyn, especially after it went through negotiations in this Committee with staff during the last Congress, that work product we understand was trending away from these concerns that we have expressed in our testimony and we would be interested to see how it develops further, if we had had an opportunity. Maybe we will have one to take it back up.

Senator CORNYN. Well, that remains a work in progress here on this Committee and we are working closely with the Chairman and the Ranking Member and Senator Schumer, in particular, but really all Members of the Committee, to try to address that.

I know there have been some—we have not talked very much about the importance of a pleading requirement. Mr. Gupta, maybe you can address this. The legislation that we have filed requires that the claimant or the plaintiff actually explain in the lawsuit what their patent is and how it got infringed.

Do you think that is an unreasonable thing to ask and what is the problem of the status quo?

Mr. GUPTA. Thank you, Senator. I certainly do not think that is a problem. In fact, in meritorious actions that are initiated by patent holders, there is enough diligence that is done prior to the action being filed where that information should be available to the patent holder in the first place.

Businesses, lawyers, reputable businesses, they go through a review process before any patent action is filed to ensure that they have complied with the Rule 11 obligations, their obligations to ensure that they are not asserting frivolous claims.

And so requiring a basic amount of information about the claims that are allegedly infringed, how the infringement occurs and the claims that are being asserted is a very low burden on good faith plaintiffs.

Senator CORNYN. Thank you. I was struck—and this was something Mr. Sauer said about the post-grant review process, but a case in particular where a hedge fund shorted that company's stock before filing a claim.

I guess if the claim is successful, then the patent should have never been issued. Then they would be vindicated. But I just wonder if the same potential for abuse exists in the litigation context. I would imagine it does.

So, what would happen, for example, Mr. Powers, to your company if a hedge fund decided to file a patent infringement lawsuit and then shorted your stock? How would you see that and what would that do to your ability to function?

Mr. POWERS. Thank you for the question, Senator. Being a privately held company, that is not a concern that we have to deal with.

Senator CORNYN. Okay. Let me ask Mr. Anderson. You are a publicly held company, are you not, sir?

Mr. ANDERSON. No, we are not. We are private.

Senator CORNYN. Well, imagine, with me.

[Laughter.]

Senator CORNYN. Imagine, Mr. Anderson, you are a publicly held company and a hedge fund shorts your stock and then generates a patent infringement lawsuit against you. What would go through your mind? What sort of pressures would that bring to bear on a publicly held company to settle that lawsuit even though it was a frivolous lawsuit? I realize it is a hypothetical.

Mr. ANDERSON. I cannot really answer that, Senator.

Senator CORNYN. I imagine it would be pretty devastating.

Mr. Sauer?

Mr. SAUER. A very quick observation. Yes. So, I think settlement pressures can be terrible, I think, especially for smaller businesses.

The reason why I believe the stock markets might react differently is that know statistically when patents are challenged in district courts on the same grounds that are available in the Patent Office IPR proceeding, they go down approximately 45 percent of the time in district court. That is the invalidation rate for these reasons: patent and written publication to have prior art.

In IPR proceedings, the patents go down approximately 80 percent of the time or only 20 percent come out. So, we believe that the markets react probably more strongly to IPR proceedings because they just see these statistics with higher kill rates than what

is available in the district courts, and it is great for people who bet against patents when they have a proceeding like that where the statistics bear that out.

Senator CORNYN. Mr. Chairman, thank you for your generosity in terms of the time. I would just say, I think we need to also recognize that when frivolous patent litigation is filed, it exacts a cost not just on the company, the defendant, and extracts perhaps a nuisance settlement, it also can have a dramatic impact on the shareholders of that publicly held company and basically constitute legal extortion and, of course, have much broader impact on the people who own the shares in that company.

Thank you.

Chairman GRASSLEY. Now, Senator Schumer.

I am going to ask Senator Lee if he will Chair while I take a couple appointments in my office.

Senator Schumer.

Senator SCHUMER. Thank you, Mr. Chairman.

First, I would like to congratulate Mr. Anderson on his public offering. I hope your stock does very well.

[Laughter.]

Senator SCHUMER. I want to thank Senator Cornyn for working closely with me in trying to come up with a bipartisan solution, and Senators Grassley and Leahy for helping us put that all together. We are feeling pretty good about it.

And it is not the first time that we are coming together to discuss the problem of patent trolls. I am sure it will not be the last.

Last spring, as you know, our Committee spent several months in heated and bipartisan negotiations. But our goal remains the same and that would help us club the trolls once and for all without harming legitimate inventors and innovators who rely on a robust patent system.

Although the deal was elusive at the time, I am confident that with renewed bipartisan effort and energy, we will get this done in the Congress. The witnesses before us advocating for reform represent an important cross section of the economy. We have a large tech company, a family farm manufacturer, a small business restaurant franchise company. → sounds weird

But I want to spend a moment focusing on those who have really animated my personal interest in this debate, the small technology start-ups that are energizing the New York economy every day.

Mr. Gupta talks a little about this in his testimony. He notes that patent trolls are a problem for large companies, but they are a larger problem for start-ups who will lose investors and easily be driven out of business by patent trolls.

I have heard about this. Good companies, they come in, they get extorted, they say we are going to file a lawsuit against you unless you give us half a million dollars, and they do not have it. And this is the lifeblood of America, these new companies.

So, I feel so strongly about this—not just from a national point of view, but from a New York point of view.

delete? In a letter our Committee received from 140 venture capitalists who invest in technology companies backs this up. Engine Advocacy has pointed out 82 percent of troll activity targets small and medium businesses; 55 percent of troll suits are filed against start-ups

with revenues of less than $10 million because they know those people cannot afford a long, lengthy lawsuit, which the Patent Office, now the patent law now, not only sanctions, but blesses.

The trolls are smart. They know these small companies cannot afford to litigate even if they are in the right, so they are more likely to settle. It is those start-ups that are in the front of my mind throughout this debate and will continue to be my lodestar.

A patent reform bill needs to meaningfully address the needs of these start-ups to earn my vote. In many ways, patent troll legislation, as all of us on this Committee have learned, is like a Rubik's Cube. You need to turn and twist all the parts properly so we are really fixing the problem, but also protecting those who are not part of the problem, who are represented by two witnesses here today.

It is very hard to do. That is why it has taken a long time. It is not ideological as much as it is trying to solve the problem without creating negatives that might outweigh the benefit of solving the problem.

Well, the good news is, I think we are in a good place. Senator Cornyn and I worked out agreements. Senator Leahy asked me to get involved, which I did, I was happy to do. And I believe that the compromise Senator Cornyn and I came up with remains a positive framework for bipartisan cooperation.

In fact, I see patent reform as a little oasis of bipartisan cooperation in what many of us worry is a desert of partisanship these days. So, I want to continue to work with Senator Cornyn, Chairman Grassley, Ranking Member Leahy, on putting together a package that is fair and meaningful and protects patent holders while eliminating the leverage that bad actors currently exercise in the patent system.

So, Mr. Gupta, you mentioned in your testimony that the biggest impact on patent trolls is on smaller start-up firms. Can you elaborate on that point? What reforms would be most significant in protecting those companies?

Mr. GUPTA. Thank you for the question, Senator.

I have cited some research from reputable universities and the conclusion is unanimous that impacts investment. It also impacts their ability to hire people on focused research and development and it is a big distraction for these companies.

The biggest challenge they have is that patent litigation is so expensive right now—and not only that, but the risks are so asymmetric that defendants really do not have the ability to get their day in court.

To get to trial, the data that I have cited, the average time to trial now is almost 3.5 years, 1,220 days.

Senator SCHUMER. It is a crazy system.

Mr. GUPTA. So, most small companies do not have the financial wherewithal to actually get their day in court.

Senator SCHUMER. So, let me, before my time expires or expires any longer, ask you one more question.

You have talked about the importance of post-grant administrative review with the PTO. Can you explain the effect that the changes in the STRONG Act, which my dear colleagues have introduced, but I disagree with, would have on your ability to utilize those proceedings to weed out poor-quality patents?

Mr. GUPTA. A particular proposal around claim amendment is a reasonable proposal that I think we could work around. However, for example, one suggestion is that there should be a different panel that ought to consider the—make the institution decision and a different panel should look at the final decision or be responsible for the final decision. That does not seem to be a practical solution.

In district court litigation today, for example, we do not say that if a judge rules on a motion to dismiss adversely, that we get a different judge for the rest of the trial.

In Patent Office prosecution, we do not say, for example, that if a patent examiner rejects the claims of a patent in a first office action, that the second office action be considered by a different examiner.

So, I think there are various aspects that are not practical. And this was a system that was designed to lead to a quick, efficient way to have the Patent Office, the body that granted the patents in the first place, simply revisit their work.

So, they should have the rulemaking authority. The Federal circuit looked at the process and has blessed it, in my words, and I think it is too early to tinker with this. The Patent Office is actually asking for comments from practitioners, litigators, the public. They are expected to issue quick fixes in the next few months and final rules by the end of the year. We should let this process play out.

Senator SCHUMER. Well, thank you.

And I just want to say, Mr. Chairman, I am optimistic that Senators Grassley, Leahy, Cornyn, and I can come up with a bipartisan solution that will actually pass the Senate this year.

Thank you.

Senator LEE [presiding]. Thank you. Thanks to all of you for being here today. This is a very important issue.

The way I can tell that it is an important issue has a lot to do with what I see at town hall meetings. This is an issue that just a few years ago was very rarely discussed outside of the sort of wonky circles that we see inside of Washington.

But this is something that has now become important to people not just on K Street or on Wall Street, but on main streets throughout America. I hear about it routinely from small business owners across my State and from throughout the country.

It is a subject that we need to pay more attention to and there is a lot of enthusiasm on this Committee for patent reform, which, I think, has now become indispensable for American businesses, large and small, who want to be able to operate and grow without fear of extortion from patent trolls; for example, unscrupulous entities who will send your small business a letter accusing you of infringing one of their asserted patents, with the Wi-Fi router you happen to use in your small business, perhaps allowing your customers to access it while in your store.

But in this demand letter, although you are told that you are infringing, you are not told how you are infringing and you are threatened with litigation and you receive a demand for payment.

Last Congress, this Committee worked hard to pass patent reform legislation that would crack down on abusive practices in patent litigation. Senator Leahy and I worked together on a bill called the Patent Transparency and Improvements Act that would have attacked the problem of demand letter abuse and would have protected businesses like retailers who use equipment manufactured by someone else from having to immediately defend against infringement claims.

Meanwhile, Senators Grassley and Cornyn proposed important reforms to address the way patent cases are tried. Their reforms were designed to make the business model of these patent trolls unprofitable and to give parties the incentives to conduct efficient litigation in patent infringement cases and to, of course, hold them accountable when they impose unreasonable burdens on each other.

I am hopeful that this year we will succeed in uniting these reforms and that we will finally pass legislation so desperately needed by American businesses, both big and small.

Mr. Anderson, in your testimony you describe some of your experiences with abusive patent infringement demand letters. How does a business like yours decide whether or not to pay up on a demand letter?

In other words, do you try to evaluate the merits of the infringement allegations against you or are you more likely to try to size up the size of the demand and weigh it against the inevitable cost of litigation?

Mr. ANDERSON. The routine is, I try to gather—thank you, Senator—as much information as I can, but ultimately we end up in the same place. We cannot afford to litigate one of these cases. There is too much unknown information out there. And so, ultimately we know that we are going to enter into a license agreement. The question is, can we negotiate that price down a little bit?

But as I said in my earlier testimony, the price has nothing to do with the technology. The technology may be something that really does not drive business and may not be worth much to us, but somebody alluded to earlier that maybe you could just stop using the technology.

That does not matter because you are still responsible for past use. So, at that point in time, the demand is not going to go much—down very much if you cease using that technology.

So, it is just a question of trying to reduce my outside attorney's fees with the IP attorney and reduce the licensing fee. But that is where we end up.

Senator LEE. If you had to identify just one reform or, say, one small list of two or three reforms that would help alleviate this problem, what would that or what would those reforms be?

Mr. ANDERSON. Senator, it would be difficult to narrow it down to one or two or three. We are looking for comprehensive reform. The more that you can do for us, the better.

This really is crippling to our business and it is steering us away from technology, which, as I said before, our customers want, our franchisees want, and we really would like to give business to the small innovator.

Senator LEE. Would it help, separate and apart from what other reforms might be helpful, would it also help if Congress somehow channeled the FTC's enforcement activities toward going after demand letter abuse?

Mr. ANDERSON. Certainly that would be one step that would be helpful.

Senator LEE. And I assume you see a lot of demand letter abuse in your line of work based on your description earlier.

Mr. ANDERSON. Yes, we do.

Senator LEE. How many of those do you get in a typical year, if you feel comfortable sharing that?

Mr. ANDERSON. Patent troll demand letters, we received two and we have—we are the defendant in a lawsuit. But I have reached out to other restaurants and retailers and this is common practice across the industry.

Senator LEE. All right. I see my time has expired.

Senator Durbin.

Senator DURBIN. Thank you, Senator Lee. And thank you to the panel for being here.

The first major patent reform in the modern era was in 1952. We waited 59 years before we tackled it again in 2011 and then we decided to wait 3 years to go after it again.

I am concerned about that. Why would we return so quickly to something enshrined in the Constitution and critical to the development of the American economy? And the explanation was given by my colleague from New York. We are out to club the trolls. That is what this is all about.

Who are these trolls? You visualize a gnomish little ambulance chaser threatening litigation, mischief, and harassment, trying to extort money when they have no legitimate claim.

Well, perhaps that is what some think a troll to be. We asked the Government Accountability Office what percentage of patent litigations are filed by non-participating entities; in other words, companies that do not make things, companies that just sue people.

Incidentally, that could be a university that came up with some research that led to patent which is licensed in favor, and they said of all the patent litigation filed, they would put the non-participating entities, the trolls, at a maximum of 20 percent.

That means out of every five lawsuits filed in patent litigation, the Government Accountability Office says, one out of five could be a troll.

So, what we are talking about are changes that are going to affect 80 percent of patent litigation, which most of us believe is totally legitimate. It is not just about clubbing the trolls. We are clubbing the filers of patent litigation and that includes a lot more than just mischievous little gnomish figures.

In fact, if you take a look at the group that opposes H.R. 9, which is the only stated position now for reform by Congressman Goodlatte, listen to who is included in the opposition to this reform effort that we have been hearing about. Listen to the opponents and tell me if you think these are ambulance chasers.

The Association of American Universities. Dr. Crum, that might include your school. The Biotechnology Industry Organization; the Medical Device Manufacturers Association; the National Venture

Capital Association; PhRMA; and, a group which represents 200,000 American scientist and engineers. Ambulance chasers? I do not think so.

The Venture Capital Association takes a look at Congressman Goodlatte's bill and writes us a letter. Here is what they say: "We're concerned that H.R. 9, if enacted as written, will have a chilling effect on investment in patent-intensive companies and will make it far more difficult, risky and expensive for emerging companies to enforce their patents, an essential part of the patent right. Further, H.R. 9 will raise the cost and risk of confronting smaller companies trying to defend against patent litigation brought by larger competitors."

This—as you look at this story and step back from this little gnomish figure, the patent troll, it starts to look a lot differently.

Mr. Gupta, you spoke in your testimony about EMC spending $10 million in 2014 on frivolous patent litigation. What were the revenues of EMC in 2014?

Mr. GUPTA. $24 billion.

Senator DURBIN. So, what would $10 million—what percentage would $10 million in legal fees be of your $24 billion revenue?

Mr. GUPTA. And that is just outside counsel, Senator. The disruption to our business in terms of the number of people who get involved. In one particular case, we had a star engineer devote 10 percent of his time. We had to get 100 people involved in looking for documents that go back so far that we do not even have electronic records for them.

Senator DURBIN. The calculation, incidentally, is not four-tenths of 1 percent of their revenues, it is four-hundredths percent of their revenues that were spent. It doesn't suggest to me that EMC is being crippled. I would say that you probably have nuisance lawsuits in a lot of other areas that amount to as much, if not more.

But I do sympathize with, Mr. Anderson, your company and I do eat butter burgers; and, Mr. Powers, with your company. And we have got a lot of farmers in our State that use your company's inventions.

And I do know that harassment does take place. That is why I am cosponsoring Senator Coons' bill. We want to go after the real abusers in this, but we do not want to put a chilling effect on the patent system.

Honest to goodness, there are going to be small patent holders who are going to have to get up and fight the big boys who are abusing their patent rights. And when we start throwing in loser pays, most of them are going to walk away and say we just lost it.

We have lost something that is a property right enshrined in the Constitution and something that is as critical to the future of the American economy as small- and medium-sized businesses.

Dr. Crum, every major university in Illinois has written to me saying, "Oppose this patent reform." Every one of them. Tell me why the universities are speaking out against something that many have characterized as just clubbing the trolls.

Dr. CRUM. Thank you, Senator. I think it would be hard to improve on what you just articulated. I think you really hit a lot of it.

Much of our concern is for our partner companies, as we transfer our technologies to those who can take it to market and do something wonderful with it.

And precisely as you said, the concern is for those small companies—though we deal with big companies, too. There are big, innovative partners of ours, too. But it is those small companies that are at risk here.

We do not disagree with going after the abusers. We absolutely are in line with that because we see the impact. But for small companies, it is the fear that even if they are right, there is so much uncertainty and risk in going to litigation, and none of these companies are litigious. They do not have staffs or resources to do that.

We try to help them, but we also are not geared for that. We do not want to put money into litigation. We want to put it into research and innovation.

Senator DURBIN. And back into the GAO report: 80 percent of patent litigation not being filed by trolls, being filed by small- and medium-sized patent holders who are many times fighting the big boys. And H.R. 9, the Goodlatte loser pays approach, is going to have a chilling effect on their efforts to protect their property rights and these ideas and their ability to assert those rights in our court of law.

This so-called reform is about a lot more than clubbing trolls.

Thank you, Mr. Chairman.

Senator LEE. Thank you.

Senator Tillis.

Senator TILLIS. Thank you, Mr. Chair.

Actually, Dr. Crum, let me come to you first. Can you give me a sense—I am from North Carolina. I have got N.C. State-Chapel Hill, Duke. They do a lot of great work there and they apply for a lot of patents.

What is unique to the university setting versus, say, the private sector that is doing fundamentally the same thing outside of a university setting? What is unique to your concern or are there any unique considerations?

Dr. CRUM. Thank you for the question. It is a very good question.

I think that there are many similarities in what we do, obviously. I think maybe, again, if you are taking a look at the kind of research that we do, that research is being performed largely by large companies, large private companies.

They do have deeper pockets, but litigation is not where they want to put their resources and it should not be where they have to put their resources if it is frivolous, but they, at least, have that ability.

Senator TILLIS. I was trying to get a sense—in North Carolina, the Research Triangle, we have a lot of smaller companies that would probably be more resource strapped than the university, quite honestly.

Dr. CRUM. Absolutely.

Senator TILLIS. So, I am trying to get a better idea for those types of companies and why they are different and unique.

Dr. CRUM. Why they are different? I missed the point. Why they are different and unique from——

Senator TILLIS. From the university, the concerns and priorities for any kind of reform that we would pursue.

Dr. CRUM. Maybe I should address that by saying what our priorities are, what our mission is. We view our mission as research, discovery, and creating knowledge that we then move to the marketplace via partner companies.

Thus, our concern is the impact on those companies that we work with, because we are not as good at technology commercialization as the private sector. We understand that.

So, we are focusing our efforts, our resources on the research and then transferring that technology.

But we have concerns, too, because the university can be subject to litigation. But much of our concerns are with our partners, particularly those small firms that we have talked about and the startups.

Maybe I am missing your point. I am sorry if I am.

Senator TILLIS. No, and I can follow up.

Mr. Gupta, I have a question. I know you mentioned the worldwide revenues for EMC. What was your profit last year?

Mr. GUPTA. That is a good question. Several billion.

Senator TILLIS. But the base really needs to be on your profits, not on the cost to produce.

Then, the next question is, do you know roughly what your R&D budget was?

Mr. GUPTA. About $3 billion last year.

Senator TILLIS. About $3 billion. So, again, I worry about the amount of money spent on these matters at the expense of innovation. Whether you are a university, whether you are a small business, whether you are a large business, you all create technologies that keep America at the forefront. I see this as eroding money that can be put to a better and higher purpose. Thank you for that.

I have a question, in general. We did patent troll legislation in North Carolina, thought it was going to be a no-brainer. It is not. I was the Speaker of the House there when we started moving it. We had everybody coming in with their concerns.

Since I have been up here, I have heard about everybody is for some sort of change, except for the kind of change that would harm them, which is why we probably could raise a hand and get 10 different groups in here for a different kind of reform.

I particularly heard concerns raised between the pharmaceuticals industry and the high-tech industry and I get the sense that one kind of likes the devil they know. The other one thinks that there needs to be some fundamental changes.

Can you all give me some sense of what the crux of the issue is? I will just leave it to those who want to volunteer their own perspective, and maybe we can start with Mr. Gupta and then we will come down there.

Mr. GUPTA. Thank you for the question, Senator. I think you are absolutely right that there is a fundamental difference in how the abuses in the system are viewed.

Fortunately for the pharmaceutical industry, they have not been targeted by abusive litigation tactics. Unfortunately, our industry seems to draw most of the attention and——

Senator TILLIS. Are you aware of the report that was issued—I do not recall the professor's name at Harvard—that is saying it is just a matter of time where the pharmaceuticals industry will be next?

As these folks continue to raise money and they can expand their field of play, I do not think any industry should think that they are somehow going to be protected from it over time if we do not do something about it.

I am sorry to interrupt you.

Mr. GUPTA. I could not agree more with you, Senator. I am aware of that study and I think, as we found out, these shell companies are very creative about figuring out where is the next pocket of money they can chase. And pharmaceutical companies and biotech companies are highly profitable and I am sure it is just a matter of time.

Senator TILLIS. Mr. Chair, if you do not mind, I would like to hear from a couple of others, if I may. The gentlemen down here.

Mr. SAUER. Well, thank you. Our sense is within BIO, because we have so many large and small members that the divide—I think more unambiguously thoughts between large companies and small companies. On many of these issues, we have large, robust PhRMA companies who feel that they will be able to weather a lot of changes in the law and a lot of developments, whereas 80 percent of our members are small companies who are much more concerned about what is going on, whether they are biotech or in other areas.

A quick word about whether PhRMA will be next as targets for patent trolls. We, too, are aware of that particular study. We have discussed it at length within our membership and for reasons that take too long, we cannot validate hardly any of it. I think we do not share that particular concern because our landscape is somewhat different than what was presented in this study.

A quick word on what the proposed legislation would actually do. Everybody agrees that small companies deserve more protection against unfair assertion.

Our members, most of which are small companies, are quite concerned, though, that legislation that has been introduced will not do anything for them, at least to the extent they need to defend their own businesses against patent infringement.

For example, provisions like enhanced pleading, the motion practice that would be enabled by that is not for these small companies to use. Impleader practice for joining parties, they do not need to do that.

What we should be doing is treat demand letters like any other consumer scam. I think in States, your State bill, I think, takes the right approach. Whether it should happen at the State level is one question, but I think a lot of people and policymakers have caught onto that that is a very important starting point.

We need to regulate demand letters and make sure that they give proper information. And we need to do other steps like protect consumers of products and end users of products, when it is really the manufacturers of these products who should be defending the lawsuits.

Thank you.

Senator TILLIS. Thank you, Mr. Chair, and thank you for your work on this matter.

Senator LEE. Thank you.

Senator Franken.

Senator FRANKEN. Thank you, Mr. Chairman.

Just one thing that Senator Schumer brought up that I wanted to sort of balance a little bit. He talked about start-ups wanting protections from what you call the trolls.

There is the other side of it, I think, of start-ups and I think the university is—the universities sort of represent this, because he talked particularly about venture capital.

I think venture capitalists—is it not true that very often venture capitalists, when they are investing in a business, a start-up, see the value of the patent even if the business does not make it? And that is the other side of—Senator Schumer seemed to suggest that venture capitalists are on the other side of this issue because they are start-ups and they do not want to be attacked by a troll.

But is it not sort of the other side, too, which is that venture capitalists very often are in this to have the value of the patent even if the business does not work?

I guess I could ask either Dr. Crum or Mr. Sauer.

Dr. CRUM. Let me start. Thanks for the question. I think the venture capitalists view the patent as a very important reason for investing in that company, but the VCs themselves are looking for someone that can take the IP and develop the products and the processes.

So, yes, the patent is extremely important to them and the ability to protect that intellectual property. But if the business goes under, the VCs, even if they are left with ownership of the patent, they still need someone that can then develop that, develop off of that patent.

So, again, I think it still gets back to the question that we need to make sure that the small companies, the start-up companies that are truly innovative, have fair protection of IP.

Senator FRANKEN. Mr. Sauer?

Mr. SAUER. In the small companies where I worked before I joined BIO, we went through this several times, because there is always need for more capital in these companies that burn like tens of millions of dollars per year in biotech.

My experience was that whenever we went out for funding, one of the very first things the analysts would ask for and the venture capital funders would ask for would be what patent portfolio do you have, like what is your platform technology, what are the patents that protect those, can we take a look at those, how were they examined.

So, they went really in depth. It was quite stressful—at the time, I was just a patent agent—for the company to survive such scrutiny.

The scientists had it better, because they just had to talk about the merits of their technology. But when they went into the patent portfolios, because that depended on how much money they were going to give us, there was a lot of pressure from management.

So, I can only validate that at least those VCs who invest in the life sciences are very, very interested in patents and will not fund

a company, by and large, that does not have a meaningful IP portfolio.

Senator FRANKEN. Again, we are talking about balance and I just wanted to kind of balance what Senator Schumer said, because the other side of it seems to be that venture capital is very often invested because of the patent.

But on the other side of it, of course, is—Mr. Anderson, I appreciate your being here to represent the perspective of an American business that has been harmed by bad actors in this sphere, and I know that abusive tactics have harmed Minnesota businesses and there is no question that we need to do more to stop the worst abuses of the system, of the patent system.

At the same time, the patent itself also protects a lot of Minnesota businesses. So, again, I hope we can get this balance right.

Can I ask you to describe to me how Culver approaches a demand letter? Have you ever considered litigating a patent infringement claim or has the cost always been too prohibitive given the size of your company and the capacity to confront such issues? And on the other hand, how much money has Culver spent settling various claims with demand letters?

Mr. ANDERSON. Due to confidentiality, I cannot get into the dollar amounts of the settlement, and you will find that across the industries.

In terms of how I handle it, the first thing I do is contact—I am a solo practitioner in-house and patents, when I came to work for Culver's, I had hardly heard of a patent and, unfortunately, they crept into the restaurant industry.

I check with other in-house counsel and outside counsel to see how these things have played out, but ultimately we cannot afford to litigate.

We are the defendant in one lawsuit. We would have settled but for—we were able to form a joint defense group. So, I was paying one-tenth of every legal fee.

I still paid $100,000 and we were still early in the lawsuit, but if I was not paying one-tenth, $1 million, there is no way we could afford that.

Senator FRANKEN. Sure.

Mr. ANDERSON. That is money, again, that should be going towards helping our franchisees succeed, not paying out to patent trolls.

Senator FRANKEN. Well, I guess my time is up, but you said you can't tell me because of confidentiality, but my understanding is that doesn't hold in Senate hearings. Isn't that right, Mr. Chairman?

[Laughter.]

Senator FRANKEN. No, I am lying.

[Laughter.]

Senator FRANKEN. That's not true. Thank you.

Senator LEE. Senator Perdue.

Senator PERDUE. Thank you, Mr. Chairman. And thank you for being here.

I was trained as an engineer. I have been very heavily involved in the tech community in my home State. For the last few years,

I have actually been on the board of a high-tech start-up. So, I have seen both sides of this endeavor.

It seems to me that the greatest economic miracle in the history of mankind—we have sat here and watched it over the last 70 years in the United States—and it was fundamentally founded on three precepts. In addition to having the best workforce in the history of the world, we have the ability to innovate, and we have the ability to form capital, and we have the rule of law.

No other single country that we compete with today has all three of those to the degree that we do.

It seems to me that this abuse that we are talking about here today is threatening two of those three and it really is very serious, but we have got to find a balance. I have got a couple of questions about trying to find that balance, but it just seems to me that there are two objectives here. Obviously, we have got to control the frivolous nature of these lawsuits to protect the start-ups.

In my experience, start-ups need three things: One is, they have to have the innovation; two is, they have got to have the capital; and three is, they have got to survive the first 2 years. And I would bet if you look at this, a lot of these attacks happen in these first 2 years, while angel investors are in there before the venture capital community is involved, and it will scare everybody to death and it will freeze up that early capital, in my opinion.

So, I am concerned about the universities who own the technology. They are trying to transfer the technology and get a license for it, but I am also concerned about the person who is buying the technology and actually trying to commercialize it.

So, Dr. Crum, I would love for you to talk about this transfer process and about the Innovation Act, but also to talk about the specific provisions of the various bills that you believe adversely affect the ability of universities not only to transfer the technology, but also to help these start-ups, because I know you guys and other universities are very involved with angel investors in helping these start-up entities attract capital in the early, early stages of their incumbency.

Dr. CRUM. Thank you. When we have those first conversations with companies about what their needs are, what their goals are, what they are trying to do, we sit down and we work very closely with them. They become a partner. We license the technology to them. We try to help them attract capital.

I talked to the person who runs our IP and tech transfer operation just yesterday and asked if she could give me a few examples of companies for which the patents were absolutely critical to getting capitalization, and she ran through 15 just off the top of her head.

So, you are absolutely right, having the technology, the ability to protect it, is absolutely critical to attracting the capital, no question about that.

And, the second part of your question was?

Senator PERDUE. Well, it seems to me that one of the problems you have is in helping these young entities survive.

Dr. CRUM. Exactly.

Senator PERDUE. And so, the frivolous lawsuit, you see both sides of this equation.

Dr. CRUM. Yes.

Senator PERDUE. I think that you and Dr. Sauer particularly can empathize with these business owners and yet you are protecting the university for their rights as well.

So, there are two sides of this and we have got to find a balance and the way through here, the 20 percent that end up being the frivolous cases. I do not know where Google or Microsoft or Apple might have been in their first few years of development, but if they were caught up in this, they may never have gotten to maturity.

Dr. CRUM. And I think you were asking what things do we see maybe that we would strongly support. I think we have talked about a lot of that already, and a key one is ending the abusive demand letters. As has been discussed, those need to be more narrowly focused, specific, and nonthreatening.

There needs to be recourse against those who are filing those frivolous demands, the trolls.

Also, I think any changes that lead to higher-quality patents, more narrowly scoped, better defined, that would also include some of the mechanisms that were being discussed earlier by the panelists that enable and encourage challenges to patents before litigation occurs.

If we keep out of the courts, I think that is really critical in those first couple years in particular for the start-up companies.

I think there are other things out there. I am not an attorney and I am not as deep into the weeds on the proposals. I think the other panelists here probably are better suited for that.

Senator PERDUE. Dr. Sauer, would you like to answer the second part of that question?

Mr. SAUER. Yes. So, I think the small businesses need protection before large businesses. In this debate, I think we should give precedence for the concerns of small businesses and abuses that they suffer.

To that end, I agree we need to treat demand letters like other consumer scams. We need to get them within the ambit of consumer protection agencies. We need to enhance clarity and transparency in patent enforcement for everybody.

And we could talk and should talk about provisions that protect end users and consumers of product from being sued for using this product that they just bought off the shelf somewhere at retail or bought from somebody else.

I think those are worthwhile proposals. I think there is a lot of consensus that can be reached. Our worry at BIO, again, is that on some level, our small companies they feel there is a bait-and-switch at the same time going on, where there are a lot of systemic litigation reforms being proposed that do not benefit companies that do not want to or cannot litigate.

Small companies tell us, "that is not going to benefit us," like most of the things that are in the litigation reform, but those are for big guys.

The Game of Kings, that is what patent litigation is and the bigger king you are, the more you will be able to leverage the systemic litigation reforms that are being proposed.

So, they fall into two buckets and our members have different views on one versus the other.

Senator PERDUE. Thank you very much. Thank you, Mr. Chairman.

Senator LEE. Thank you.

Senator Coons.

Senator COONS. Thank you, Senator Lee. And I would like to thank Chairman Grassley and Ranking Member Leahy for holding this hearing, and for the witnesses, the broad and representative panel that we have got today, and for your testimony.

This hearing has helped reinforce a valuable lesson that I think we should all keep in mind. How you view patents and patent litigation really depends a lot on where you operate within our wide-ranging economy; whether you are a start-up or a large company, whether you are investing millions or billions of dollars into a research-intensive business model, or providing a service directly to consumers.

Our economy, as a number of Members have commented, remains incredibly successful, and important businesses that cover the whole spectrum of these characteristics have been affected, and we are all better off by retaining the diversity, the innovation, the creativity of the full scope of our country.

We have heard from witnesses, Mr. Gupta from a multi-billion-dollar technology company, Mr. Anderson from a restaurant company, who have both testified to the cost and the disruption of companies, large and small, of demand letters, and of some of the aspects of patent litigation.

But we have also heard from Mr. Powers at KINZE, from Dr. Sauer on behalf of 1,100 companies that are members of BIO, and Dr. Crum from Iowa State, who have all cautioned strongly against overreach and the unintended consequences that could come with litigation reforms that may be hitting on that with a hammer in an effort to club the trolls.

So, while we work to fight abuses of the system, we have to keep in mind that we have to honor and respect the diversity of our economy and the range of sources of innovation.

There is a great deal at stake, not the least of which is our ability to cure diseases, as Dr. Sauer referenced in his introduction, from Alzheimer's to multiple sclerosis to leukemia; our ability to develop new materials, new crops, new biofuels.

It hangs in the balance of whether we overreach in our efforts at reform. Patents are a property right at the very core of the American dream, enshrined in our Constitution, and for generations Americans with little funding or manufacturing capabilities have clung to that patent right which gives them the possibility of taking a chance, of building a new model, of tinkering and solving a problem, and that is the kind of entrepreneurship that has made America great and we need to work to preserve the best of that system and inspire future generations.

So, to address abuses in our patent system, the real abuses that have been described today, yet ensure fairness in post-grant proceedings and a strong patent system, I have introduced the STRONG Patents Act of 2015, along with my colleagues, Senators Durbin and Hirono.

This legislation would ensure that we strengthen the pleading requirements for patent litigation to match the stringent standard currently enforced in other civil litigation.

It empowers the FTC to go after those who send deceptive and abusive letters to extort from large and small businesses, and it tackles some of the recent abuses of the post-grant system at the PTO, described by Dr. Sauer, when a hedge fund can raise hundreds of millions of dollars of investor capital simply by filing a challenge for the purpose of profiting from shorting the stock. And it would end fee diversion to ensure an increase in the quality of the work at PTO.

I look forward to working with my colleagues to enact meaningful reforms that will respect the diversity of business models in our economy.

And if I might, Senator Lee, I would like to submit for the record letters that express support for the approach of the STRONG Patents Act from the National Venture Capital Association, the National Small Business Association, the Biotechnology Industry Association, the Association of American Universities, the Association of Public and Land-Grant Universities, the Medical Device Manufacturers Association, the Pharmaceutical Research and Manufacturers of America, the Innovation Alliance, and the IEEE USA.

I think it is important when we look at the very wide range of folks who have weighed in on behalf of this focused, targeted approach that we respect the range of innovators in our economy.

So, if I might, I think I have time for one question, to Mr. Powers, if I might.

I really appreciate your testimony about the growth of KINZE Manufacturing from a small welding shop to a company that today employs 1,000 people. Your CEO was named the inventor on 19 patents, including, I think, if I remember, the rear folding planter toolbar, which I couldn't describe in any detail if my life depended on it.

But just help us understand how these patents helped KINZE attract investors and compete against larger competitors.

I was struck that, in your written testimony, you said, "we should urge caution on provisions which would create significant hurdles for legitimate inventors seeking to enforce their patent rights, such as blanket fee-shifting provisions. There is a balance to be struck, and"—that word, balance, has been used by most of the Senators who spoke today—"we want to be careful to go far enough to take away the incentives from those who abuse the litigation system, and no farther."

In KINZE's experience, what does that mean? And then I would like to ask other members of the panel if you care to comment: What does it mean to go "no farther" and why is that important given the history of your company and the inventions of your founder?

Mr. POWERS. Thank you for the question, Senator. Starting out with the role of patents in KINZE Manufacturing, Jon has been fortunate enough to be a good enough businessman that he did not need to seek outside investment, just truly a self-made man.

What it did give us the ability to do is to get out in front and commercialize a planter that made farmers' lives much easier, re-

duced the amount of time that they had in the field, and gave them the ability to plant their fields during a very narrow window during the spring. You actually have, roughly, about 2 to 3 weeks where if you can get your crop in during that time, you are going to get peak yields. If rain or other things delay you, the farmer is going to be hurt.

So, that having been said, patents are very important to us and we would like to see a strong patent system.

Turning to the limits—you know, we should go no further than to prevent the patent trolls. KINZE is not in favor of blanket fee-shifting or mandatory fee-shifting provisions. However, we do believe that fee shifting when parties bring baseless litigation would serve as a practical deterrent to those who would go ahead and do abusive patent litigation.

Senator COONS. Thank you, Mr. Powers. And I appreciate KINZE bringing a balanced view to this.

Dr. Sauer, would you just make some comment about how some of the proposals that were discussed today, like a blanket fee shifting or a loser pays system would impact the way that BIO as an ecosystem operates, particularly the smaller and start-up companies you described earlier.

Mr. SAUER. I think it can be well exemplified by perhaps the impleader provisions that are connected to the fee-shifting provisions of the bill. From fee shifting comes concepts of, how do we make sure the loser pays once we have a loser pays system.

The impleader provision, like a few other provisions, exemplifies the ecosystem within which biotech works, which implicates small companies, university licensors, and the like. So, if that system works in a way that implicates not just patent owners who must defend their businesses against patent infringement, but drags their business partners into the litigation as unwilling co-plaintiffs and subjects them to potential liability.

delete?

That makes a big difference on the ability of biotech companies and their licensors to agree on the scope of their business, do licenses and the like.

Senator COONS. Thank you, Dr. Sauer. I can see my time is coming to a close.

Mr. SAUER. I regret that.

Senator COONS. I just wanted to make sure, whether it is a Hawkeye, a Cyclone or a Panther, we had an opportunity to hear from Dr. Crum on behalf of Iowa State and the other inventors and innovators at the university system. Can you just give us a context about the dangers of overbroad patent reform on universities?

Dr. CRUM. Yes. I just would follow up on what Hans was just saying about the involuntary joinder concerns, that is really huge for us, because we could have our university individual faculty and departments pulled into this. And if you want to talk about throwing a wet blanket over innovation: that kind of fear and concern about being pulled into something over which you had no control, because you developed some outstanding technology, that would definitely throw a wet blanket over innovation. That is a real concern for us and it also diverts a lot of resources that we should be putting back into the research enterprise and diverts it to litigation.

Senator COONS. Thank you. I appreciate the entire panel and I appreciate the opportunity to focus on the idea that inventors, innovators, companies large and small, established, private, public, have real concerns about overreach in patent litigation reform and we need to find a balance.

Thank you, Mr. Chairman.

Chairman GRASSLEY [presiding]. Well, without objection, the material that Senator Coons wanted put in the record will be made a part of the record.

[The information appears as submissions for the record.]

Chairman GRASSLEY. And quite frankly, I believe it would be Senator Whitehouse would have priority, if you want it.

Senator WHITEHOUSE. Thank you, Chairman. I will be brief and I will yield to my extremely distinguished colleague, Senator Blumenthal, very shortly.

I just want to make the point that I think we have a really significant opportunity to pass a significant piece of legislation.

If people will rein in their ambitions for ulterior purposes being achieved through this, I think the key areas have been addressed, in large part, in Senator Coons' legislation, then I think there is agreement. I think we could pass that very quickly if people did not want to add extraneous things.

The areas where I hear from Rhode Islanders that I particularly want to focus on are making sure that a plaintiff is a real plaintiff and there are not shell and sham plaintiffs that are allowed to exist; that patents that were written at a time when people did not understand the internet or other things and need to be reviewed, there is an ability to review those patents rather than to have them be weapons in the hands of trolls; that the abuse of demand letters, which has become a scandal, be controlled, and that we focus the litigation between the patent holder and the person who is actually using, in the ordinary sense of the word, the patented technology—not the florist or the grocer who is using the end product.

And I think if we can agree on those four things—and for the record, I see an awful lot of heads nodding here—we have a bill that we can pass.

But if we want to add, you know, abortion provisions to human trafficking bills, and if we want to add running around in national security WRDA dam and hydroelectric sites with firearms to bills that protect sportsmen, and if we want to add tort reform to this bill, then we are going to end up with unnecessary fights. And I hope we can go forward with that.

I'd like to read into the record what Brown University says, which is a very, very important player in our Rhode Island ecosystem.

Brown University President Christina Paxson says that "the bill in the House of Representatives, H.R. 9, the Innovation Act, goes far beyond what is needed to curb abusive patent practices. Of particular concern are very broad mandatory fee shifting and involuntary joinder provisions. I urge you to oppose efforts to add broad provisions like these to any Senate patent troll legislation."

And Brown has a lot of patents. URI has a lot of patents.

Our university signed another letter that I would like to read from into the record. In fact, I think every State represented on this Committee has a university on this list that signed this letter, except maybe Utah. I think they are the one exception.

But every other State represented on this Committee has signed this letter and it says that "mandatory fee shifting and involuntary joinder are especially troubling to the university community because they would make the legitimate defense of patent rights excessively risky and thus weaken the university technology transfer process, which is an essential part of our country's innovation and entrepreneurial ecosystem."

So, I hope with universities like that making the point that if we focus on what is really the problem, we can get something done.

In that spirit, I hope we can move significant bipartisan legislation. And my plaudits again to Senator Coons for the scope that he has provided. I have not signed onto that bill yet because I am not—I am in the same neighborhood that he is in, if I am not exactly down to the same street and mailbox.

But I really think that is the way to proceed, Mr. Chairman, and adding extraneous fights to things where we can go forward on a bipartisan basis I do not think is helpful.

So, I hope we can go forward in that spirit, and I will leave with that comment.

Chairman GRASSLEY. Thank you, Senator Whitehouse.

Now, Senator Blumenthal.

Senator BLUMENTHAL. Thanks, Mr. Chairman, and thanks for holding this hearing on a supremely important topic where I think there is broad consensus that abuses need to be stopped and inventiveness and creativity encouraged. And the great enemy of constructive change has been overreaching.

My colleague, Senator Whitehouse, referred to it as overbroad ambitions, but I think it is overreaching in terms of what proponents have sought to accomplish. And we need to respect what is happening in the real world where circumstances are changing.

The Supreme Court has changed the law. The *Octane Fitness* decision, which makes it significantly easier for the prevailing party to get attorney's fees in patent cases, the *Nautilus* decision, which required more specificity in patent claims, the *Alice* decision, and the very likely development in the Judicial Conference abolishing Form 18, these are changed circumstances that we need to respect because they are having some results.

And likewise, for me, as a former law enforcer, the great question here is how can existing law be used more effectively. The mantra in the legislature always is there ought to be a law or a new law. But if existing law, let alone new law, is unenforced, it is dead lettered, it is useless.

So, the Federal Trade Commission ought to be using existing law. Federal officials ought to be following the lead of State attorneys general, who are going after deceptive or misleading practices under the good old consumer protection laws. Fraud and deception in some of the letters that are sent widely perhaps can be pursued under existing law.

So, I would like to know from this panel what existing laws can and should be enforced more aggressively to pursue this problem and who ought to be doing it.

Mr. GUPTA. Senator, I can take a shot at it, if you would like.

I think, first off, it is not really about labeling the actor. If it is a large company, a small company, a university, if they initiate abusive litigation, unmeritorious claims, there has to be a remedy available to those that are subject to it.

So, requiring that pleadings be specific to state with clarity what the defendant is accused of having done wrong seems to be a fundamental principle that everyone should be able to agree to. And right now you stated that the Judicial Conference has recommended that Form 18 be abolished. At least Form 18 gave us a form that we knew that we had to be able to comply with.

With Form 18 being abolished, we are being asked to refer to *Iqbal* and *Twombly*, which are not patent cases and which all the guidance that those two cases provide is to say that you need to state enough facts to show that you plausibly——

Senator BLUMENTHAL. Well, State attorneys general are taking more action under existing laws.

Mr. GUPTA. Yes.

Senator BLUMENTHAL. Why not encourage law enforcers to use those existing laws more aggressively and effectively? Apparently, all of these developments are having some effect because the numbers of patent cases has diminished. You would agree with me on that point. Mr. Sauer made that point in his testimony.

Mr. GUPTA. I would respectfully sort of disagree in that the last 3 months of data that we have from December, January, and February, if you look at the same period the previous year, the litigation numbers are up again.

So, we do not know whether that was a temporary modest dip in 2014, but certainly the data that we have from January and February of this year suggest that the numbers are up again relative to the same time——

Senator BLUMENTHAL. Do you agree, Mr. Sauer?

Mr. SAUER. I think the more robust data show—if we compared, let us say, the whole year last year to the year before, the year was down almost 20 percent over the year before. So, we can wait until the end of this year and see what the numbers show.

What we are not seeing is skyrocketing or the sky is falling or other strident rhetoric what would support that.

With respect to your question about which existing laws could be enforced, I would add to your list, veil piercing—corporate veil piercing. This is not the first time the law encounters shell corporations and undercapitalized paper entities. But they are well-established principles. Veil piercing is difficult, but the corporate form is very important. But it is not that judges are unfamiliar with companies who set up paper entities behind which they hide. So, the law is not helpless against these kinds of events.

Senator BLUMENTHAL. Mr. Gupta, from what we have seen, I think we can agree, and I do not want to make too much of the data that exists, but I think we can agree that the trend is heading in the right direction. And if that is so, shouldn't we be cautious about legislating in an area where circumstances are changing and

the courts are developing new law in the wake of the United States Supreme Court opinions?

Mr. GUPTA. As I stated, Senator, I am not sure that 2014 was not a one-time——

Senator BLUMENTHAL. Well, shouldn't we wait until we know what is actually happening in the courts on the ground in the real world?

Mr. GUPTA. Unfortunately, the Supreme Court decisions that we have discussed today, none of them address the issue of reduction of discovery expenses or unreasonable discovery. Those decisions do not provide us with any guidance in terms of how specific pleadings need to be, and how a defendant is notified as to what is it that it is accused of infringing.

Senator BLUMENTHAL. I know that the Supreme Court has not dealt with the whole problem for all time, but in terms of framing solutions when circumstances seem to be changing, shouldn't we target those solutions to the problems that are causing the abuses and target them narrowly in very limited ways, especially since the facts on the ground—and facts are stubborn things—seem to be changing and perhaps going in the right direction?

Mr. GUPTA. I agree, Senator, which is why I think we have been a proponent of very specific reform targeted at pleadings, something that the courts are not looking at, and discovery reform, something that the courts are not looking at, and also an ability to recover fees.

Supposed to be repeated?

Now, the Supreme Court decision says that the prevailing party—it says nothing about the defendant—so, a prevailing plaintiff is actually now better able with a fee shifting—I am sorry—with the fee-shifting proposal says that the prevailing party would be entitled to their fees. So, it helps plaintiffs and defendants. In fact, a small plaintiff without the ability to hire a lawyer could actually now get a contingency attorney who knows that even when the damages are small in a case, they have an upside because they can get their fees recovered.

So, these are areas where we want targeted reform because the Supreme Court does not have anything on their docket today that would address those issues.

Senator BLUMENTHAL. My time has expired. Thank you, Mr. Chairman.

Chairman GRASSLEY. This will end the hearing, but before you get up, I want to thank you, once again, for a good discussion on a very controversial issue. I do not think it is controversial that things need to be done in this area, but it is somewhat controversial even in my own State between various interests.

We are going to have to find common ground, particularly in the Senate, to get a bill through the United States Senate. We are open to hearing everybody's point of view. But we thank all of you very much for your fine testimony.

I have questions I am going to submit for the record and for the benefit of the other Members of the Committee the record will be open for a week for questions to be submitted for answer in writing, and particularly from Members that could not be here to participate in oral questions, I am sure you will get some questions.

So, we would appreciate very much your response to those written questions.

Thank you very much. The meeting is adjourned.

[Whereupon, at 12:24 p.m., the hearing was adjourned.]

[Additional material submitted for the record follows.]

APPENDIX

Additional Material Submitted for the Record

Witness List

Hearing before the
Senate Committee on the Judiciary

On

"The Impact of Abusive Patent Litigation Practices on the American Economy."

Wednesday, March 18, 2015
Dirksen Senate Office Building, Room 226
10:00 a.m.

Mr. Brad Powers
General Counsel
KINZE Manufacturing, Inc.
Williamsburg, IA

Mr. Hans Sauer
Deputy General Counsel for Intellectual Property
Biotechnology Industry Organization
Washington, D.C.

Mr. Steven E. Anderson
Vice President and General Counsel
Culver Franchising System, Inc
Prairie du Sac, WI

Dr. Michael R. Crum
Vice President for Economic Development and Business Engagement
Iowa State University
Ames, IA

Mr. Krish Gupta
Senior Vice President and Deputy General Counsel
EMC Corporation
Hopkinton, MA

Prepared Statement by Senator Chuck Grassley of Iowa
Chairman, Senate Judiciary Committee
At a hearing entitled:
"The Impact of Abusive Patent Litigation Practices on the American Economy"
March 18, 2015

We're here today to discuss the topic of patent litigation abuse, and in particular, the destructive tactics of so-called "patent trolls." This practice of patent trolling has hit businesses both big and small across all industries, and it's having a harmful effect on the economy. Patent litigation abuse imposes high costs on American businesses. It wastes resources that could instead be utilized for research, development, job creation and economic growth. It undermines the innovation and creativity that patents are supposed to protect.

Patent assertion entities focus on buying and asserting patents, rather than on developing or commercializing patented inventions. Now I want to make clear that licensing one's patent is not in itself a bad thing. Inventors and patent owners, including universities, often aren't in a position to commercialize their patented inventions – but they certainly have the right to protect their intellectual property against infringers.

Patent trolls, however, are entities that engage in abusive and deceptive tactics to assert poor quality patents against businesses already utilizing technologies as common as wireless email, digital video streaming and the internet. They use overly broad patents to allege infringement against companies that are simply engaging in normal business activities or have bought a technology, product or service from a vendor, many times right off the shelf. They send out intentionally evasive and misleading blanket demand letters, and employ overly aggressive litigation practices to extort settlements. They frequently hide behind patent holding subsidiaries, affiliates and shells of operating companies in order to escape scrutiny.

Frivolous patent lawsuit filings have increased over the years, and they rarely have merit. But the extent of the problem is actually much worse because most cases don't reach merits judgment stage. Patent trolls strategically set their royalty demands below litigation costs to entice companies to settle rather than run the risk of expensive and risky patent litigation. Many companies don't have the expertise or resources to litigate these cases, so most of the time they have no choice but to submit to this patent extortion. This, in turn, drives up costs which many times are passed on to consumers.

We'll be hearing from three witnesses today about their experiences with, and the impact of, abusive patent litigation tactics. These witnesses represent businesses from different industries. Two of these companies have patent portfolios, while one company doesn't own patents. Yet their conclusion is the same – patent troll abuse is counterproductive to our nation's economic growth.

The United States should remain at the forefront of technology, innovation and creativity. Patents and the U.S. patent system are a significant component of the American tradition of opportunity, invention and innovation. But we shouldn't allow bad actors to bring the entire system down.