

1 THE IMPACT OF ABUSIVE PATENT LITIGATION PRACTICES ON
2 THE AMERICAN ECONOMY

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WEDNESDAY, MARCH 18, 2015

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United States Senate,

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Committee on the Judiciary,

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Washington, DC

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The Committee met, pursuant to notice, at 10:02 a.m.,

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Room 226, Dirksen Senate Office Building, Hon. Charles E.

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Grassley, Chairman of the Committee, presiding.

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Present: Senators Hatch, Cornyn, Lee, Flake, Perdue,

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Tillis, Leahy, Feinstein, Schumer, Durbin, Whitehouse,

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Klobuchar, Franken, Coons, and Blumenthal.

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1 OPENING STATEMENT OF HON. CHARLES E. GRASSLEY, A U.S.
2 SENATOR FROM THE STATE OF IOWA, CHAIRMAN, COMMITTEE ON
3 THE JUDICIARY

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5 Chairman Grassley. [In progress] and in particular,
6 the destructive tactics of so called patent trolls. This
7 practice of patent trolling has hit businesses both big
8 and small across all industries and is having a harmful
9 effect on the economy.

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

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

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

25 Patent trolls, however, are entities that engage in

1 abusive and deceptive tactics to assert poor quality
2 patents against businesses already utilizing technologies
3 as common as wireless e-mail, digital video and Internet.
4 They use overly broad patents to allege infringement
5 against companies that are simply engaging in normal
6 business activities or have bought a technology, product
7 or service from a vendor, many times buying that right
8 off the shelf.

9 They send out intentionally evasive and misleading
10 blanket demand letters and employ overly aggressive
11 litigation practices to extort settlements. They
12 frequently hide behind patent holding subsidiaries,
13 affiliates and shells of operating companies in order to
14 escape scrutiny.

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

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

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

3 We will be hearing from three witnesses today about
4 their experiences with and the impact of abusive patent
5 litigation tactics. These witnesses represent businesses
6 from different industries. Two of these companies have
7 patent portfolios, while one company does own patents.

8 Yet, their conclusion is the same -- patent troll
9 abuse is counterproductive to our Nation's economic
10 growth.

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

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

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

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

11 [The letters referred to follow:]

12 *****COMMITTEE INSERT*****

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

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

10 They maintain that recent Supreme Court decisions are
11 on pleading standards, fee shifting and patent quality,
12 as well as actions by the Federal Trade Commission and
13 the U.S. Patent and Trademark Office have largely taken
14 care of all these issues and comprehensive legislation
15 then is unnecessary.

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

20 I do not dispute that we should preserve patent
21 rights and valid patent enforcement rules. We do need to
22 strike the right balance, but Congress should act
23 decisively if we want to alleviate the problems that are
24 harming businesses both big and small. This will
25 strengthen our patent system, benefit inventors,

1 businesses and consumers. So here we are, back at it
2 again in this Congress.

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

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

14 [The prepared statement of Chairman Grassley appears
15 in the appendix.]

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

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

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4 Senator Leahy. Thank you very much, Mr. Chairman.

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

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

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

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

21 Website owners have faced costly litigation for using
22 basic software in e-commerce. So what happens, instead
23 of using patents to drive new creation, bad actors have
24 held up main street businesses and innovative companies
25 to extort financial settlements.

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

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

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

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

24 Now, the Committee was not able to complete its work,
25 but we made significant progress and I hope we can build

1 on that. I think we can look at what we did with the
2 Leahy-Smith act. We did that because Senators and
3 stakeholders, Senators of both parties, House members of
4 both parties and stakeholders joined together to find
5 solutions.

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

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

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

17 Chairman. Senator Cornyn?

18 Senator Leahy. and I worked on--I was
19 complimenting you, I was complimenting you. There will
20 probably be a recall petition in Texas for you now
21 because--.

22 Chairman. You have my full attention.

23 Senator Leahy. Senator Cornyn and I worked on -- I
24 was complimenting you.

25 Senator Cornyn. Excuse me?

1 Senator Leahy. I was complimenting you. There will
2 probably be a recall petition in Texas for you now.

3 Senator Cornyn. You have my full attention.

4 Senator Leahy. But Senator Cornyn and I worked hard
5 on this, a number of us did.

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

11 Thank you, Mr. Chairman.

12 [The prepared statement of Senator Leahy appears in
13 the appendix.]

14 Chairman Grassley. Thank you.

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

18 Senator Schumer. Thank you for mentioning me.

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

22 [Laughter]

23 Senator Leahy. If I had half the fame the Senator
24 from New York has.

25 Chairman Grassley. You see what happens when you

1 say one word, Schumer.

2 [Laughter]

3 Chairman Grassley. Anyway, Senator Schumer and
4 Senator Leahy do not always agree with Senator Cornyn and
5 me and Senator Lee, but there is a good faith effort to
6 work on legislation that can be bipartisan.

7 Senator Coons is involved in it, as well, because he
8 has a bill of his own in and maybe there are other bills
9 in, as well.

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

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

22 Prior to joining KINZE, Mr. Powers worked on IP
23 litigation, licensing and portfolio management at the law
24 firm of McKee, Voorhees and Sease.

25 I understand your family is with you and I welcome

1 them, assuming they get here.

2 I would like to introduce everybody before you
3 testify.

4 We have Hans Sauer, Deputy General Counsel for
5 Intellectual Property of the Biotechnology Industry
6 Organization, a trade association representing over 1,100
7 biotechnology companies and research institutions.

8 At BIO, Mr. Sauer advises boards of directors and
9 various departments on patent and other IP matters. He
10 has 20 years' professional in-house experience in that
11 industry.

12 Steven Anderson is Vice President and General Counsel
13 for Culver Franchising System located in Prairie du Sac,
14 Wisconsin, famous for its butter burgers and frozen
15 custard. But I can suggest to you that I like the pork
16 tenderloin better.

17 Culver's has 528 restaurants, 22 of them in States --
18 including over 30 locations in my home State of Iowa, and
19 employees 20,000 people.

20 Mr. Anderson at Culver is responsible for overseeing
21 all legal matters involving the corporation, including
22 its intellectual property.

23 Prior to Culver, Mr. Anderson worked as a lawyer at
24 Murphy Desmond.

25 Then Dr. Michael Crum, Vice President for -- I did

1 not mean to skip you. We will get to you in just a
2 minute.

3 Dr. Crum, Vice President for Economic Development and
4 Business Administration at Iowa State University. Dr.
5 Crum has been a faculty member, College of Business, ISU,
6 since 1980. He led the initiative to create the Office
7 of Economic Development and Industrial Relations, which
8 helps organizations connect with research, technical and
9 business expertise of the university.

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

12 Dr. Crum. Is that right?

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

16 We have Krish Gupta, Senior Vice President and Deputy
17 General Counsel at EMC Corporation, located in
18 Hopkington, Massachusetts. EMC is the world's leading
19 developer and provider of information infrastructure
20 technology.

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

25 He oversees EMC's IT portfolio of over 5,100 U.S.

1 patents, a portfolio that has earned that company
2 recognition by the *Wall Street Journal* as the eighth most
3 innovative IT company

4 Mr. Powers, would you start out, please?

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

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

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

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

24 After that, the company grew quickly. KINZE today
25 impacts Iowa factory workers, as well as farmers and

1 small business owners throughout the country. KINZE is
2 still privately-held by the Kinzenbaw family and has
3 employed up to 1,000 people in the State of Iowa,
4 manufacturing high quality agricultural equipment,
5 providing farmers with the tools they need to help feed
6 the world.

7 Our products are distributed through a network of
8 independently owned dealers located in agricultural
9 states throughout the country.

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

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

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

23 Now, unlike KINZE, Clear With Computers does not
24 employ any factory workers, it does not help American
25 farmers, and it makes no products. What it does do is it

1 makes lawsuits. It has filed over 60 patent cases since
2 2008.

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

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

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

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

1 efficient.

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

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

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

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

23 As this technology moves to the field, it is no
24 stretch of the imagination to believe the assertion
25 entities will follow. The patent system, which was

1 designed to foster innovation and bring the fruits of
2 American creativity to everyone, has been thrown off
3 balance by a few bad actors taking advantage of the high
4 cost and uncertainty of litigation. Congress must step
5 in to restore this balance and KINZE is ready and eager
6 to be part of that effort.

7 Thank you once again for giving the Kinzenbaws and
8 KINZE the opportunity to talk on this critical issue. As
9 you consider the legislation to address the very real
10 threat posed by these patent assertion entities, we
11 strongly encourage you to consult representatives from
12 all industries, including agricultural manufacturing.

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

18 Thank you.

19 [The prepared statement of Mr. Powers appears in the
20 appendix.]

21 Chairman Grassley. Thank you, Mr. Powers.

22 Mr. Sauer?

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1 STATEMENT OF HANS SAUER, DEPUTY GENERAL COUNSEL FOR
2 INTELLECTUAL PROPERTY, BIOTECHNOLOGY INDUSTRY
3 ORGANIZATION, WASHINGTON, DC
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5 Mr. Sauer. Chairman Grassley, Ranking Member Leahy,
6 and members of the Committee, thank you again for the
7 opportunity to testify here today. I am deputy general
8 counsel for intellectual property at the Biotechnology
9 Industry Organization, on whose behalf I testify today.

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

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

1 years, sometimes decades.

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

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

17 Unfortunately, misuse of the patent system against
18 patent holders or licensees is also a real and growing
19 problem. In particular, the PTO's inter-parties review,
20 IPR system, of administrative patent challenges is
21 undermining the value of predictability of patent rights
22 and long-held investment-backed expectations. This is
23 because this new system stacks the deck against patent
24 owners in ways Congress did not intend, leading to patent
25 invalidation rates far exceeding those seen in district

1 court litigation involving similar types of patents and
2 similar grounds for challenges. These disproportionate
3 kill rates invite unintended abuses and predatory
4 practices.

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

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

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

25 Such cynical strategies not only damage the value of

1 companies working on cures, but hurt those who are
2 eagerly waiting for such cures.

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

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

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

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

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

1 patents.

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

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

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

18 [The prepared statement of Mr. Sauer appears in the
19 appendix.]

20 Chairman Grassley. Thank you, Mr. Sauer.

21 Mr. Anderson?

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

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5 Mr. Anderson. Chairman Grassley, Ranking Member
6 Leahy, and members of the Judiciary Committee, I am Steve
7 Anderson, Vice President and General Counsel of Culver
8 Franchising System, Inc.

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

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

22 Restaurants in the U.S. account for an estimated \$709
23 billion in annual sales and serve 130 million hungry
24 customers every day. Restaurants create meals and
25 restaurants create jobs. However, most restaurants are

1 small businesses, like our franchisees, and operate on
2 very thin margins. We simply cannot afford to litigate
3 patent infringement lawsuits and we lack the technical
4 expertise to evaluate the merits of technology patent
5 claims. This makes restaurants prime targets for patent
6 trolls.

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

17 As general counsel for Culver's, there is nothing
18 that I dread more than receiving a patent demand letter.
19 They are broadly drafted form letters to offer nothing on
20 the validity of the patent, exactly what the alleged
21 violation may be, and whether or not we were actually
22 infringing upon that patent. These trolls are happy to
23 tell us that we are welcome to test their claims in
24 litigation, knowing that a trial has cost prohibitive,
25 with typical attorney's fees of well over \$1 million and

1 too much of a burden for our business to undertake.

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

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

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

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

1 claims.

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

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

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

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

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

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

6 [The prepared statement of Mr. Anderson appears in
7 the appendix.]

8 Chairman Grassley. Thank you, Mr. Anderson.

9 Dr. Crum?

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1 STATEMENT OF MICHAEL R. CRUM, VICE PRESIDENT FOR ECONOMIC
2 DEVELOPMENT AND BUSINESS ENGAGEMENT, IOWA STATE
3 UNIVERSITY, AMES, IOWA.

4

5 Dr. Crum. Thank you, Chairman Grassley, Ranking
6 Member Leahy, and members of the Judiciary Committee, for
7 this opportunity to testify on such an important topic.

8 I am Mike Crum and I serve as Vice President for
9 Economic Development and Business Engagement at Iowa
10 State University.

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

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

25 At my home institution of Iowa State University,

1 technology transfer has led to numerous and diverse
2 technologies that have had a major impact locally,
3 nationally, and globally.

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

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

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

1 During that 5-year period, we generated more than
2 1,000 invention disclosures, 767 patent applications, and
3 we were responsible for the execution of 472 licenses and
4 options, including 183 to companies in Iowa.

5 Additionally, our faculty and students launched 190
6 startups supported by over \$24 million in outside
7 funding.

8 The ability of our university's technology transfer
9 operations to achieve the types and magnitudes of
10 societal benefits that I just described is critically
11 dependent on a strong patent system. Without robust
12 patent protections, licensees and venture capitalists
13 will not take on the significant risks associated with
14 investing in and developing our inventions. Strong
15 patents are particularly essential for the small, often
16 undercapitalized startup companies built upon university
17 discoveries.

18 Indeed, patents are often the most critical assets of
19 these startups and small businesses. To be able to gain
20 a foothold in often well developed markets, such
21 companies must be able to assert their patent rights
22 effectively.

23 It is also crucially important for universities and
24 their licensees to be protected from potentially
25 crippling abusive patent litigation practices. We

1 recognize that abuse of patent litigation practices are a
2 corrosive assault on the Nation's patent system and must
3 be forcefully countered.

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

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

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

1 capital investments.

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

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

16 Thank you.

17 [The prepared statement of Dr. Crum appears in the
18 appendix.]

19 Chairman Grassley. Thank you, Dr. Crum.

20 Mr. Gupta?

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1 KRISH GUPTA, SENIOR VICE PRESIDENT AND DEPUTY GENERAL
2 COUNSEL, EMC CORPORATION, HOPKINGTON, MASSACHUSETTS

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4 Mr. Gupta. Chairman Grassley, Ranking Member Leahy,
5 and members of the Committee, I am Krish Gupta, Senior
6 Vice President and Deputy General Counsel for EMC
7 Corporation. I am honored to testify today on the
8 critical need for patent litigation reform.

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

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

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

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

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

7 Shortly thereafter, PAEs try to pressure us into
8 settlement by demanding thousands of documents and e-
9 mails during discovery, most of which are irrelevant to
10 the suit and costly to produce.

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

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

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

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

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

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

18 We, therefore, support legislation that includes a
19 balanced fee-shifting provision with meaningful fee
20 recovery. These provisions would discourage the filing
21 of frivolous suits and the use of abusive litigation
22 tactics by imposing financial accountability.

23 In Iqbal and Twombly, the Supreme Court addressed the
24 level of specificity required in a complaint. With the
25 Judicial Conference recommending the elimination of Form

1 18, it is expected that Iqbal and Twombly will apply to
2 patent pleadings, as well. However, these cases do not
3 set forth bright line rules for patent litigation, which
4 is a specialized area of the law.

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

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

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

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

1 Thank you and I look forward to your questions.

2 [The prepared statement of Mr. Gupta appears in the
3 appendix.]

4 Chairman Grassley. Thank you, Mr. Gupta.

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

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

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

16 I will start with you, Mr. Gupta.

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

25 Pleading specificity, for an example, can only help

1 focus a case early on and with at least some clear
2 understanding of what is being accused of infringement
3 and why. In fact, I think specific pleadings will
4 actually help plaintiffs in that we will eliminate a lot
5 of motion practice in terms of specificity of complaints
6 as to whether they satisfy Iqbal and Twombly.

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

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

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

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

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

8 So this should be patents 101.

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

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

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

24 They do not require that the theory of infringement
25 be explained in any way to the defendant. There is

1 nothing in these decisions that reduce the burden and
2 expense of discovery. And these decisions do not make
3 fee shifting the default and certainly there is no
4 mechanism provided by these decisions to ensure that fees
5 can be collected.

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

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

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

18 Mr. Anderson. In terms of the financial impact, we
19 spend hundreds of thousands of dollars and for us that is
20 a big number. I am hearing some big numbers at the table
21 here, but for us that is a large number.

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

24 Our business as a franchiser is there to support the
25 franchisees, drive business to their businesses and help

1 them succeed.

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

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

11 Chairman Grassley. Mr. Powers?

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

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

20 Thank you.

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

24 Senator Leahy. Thank you, Mr. Chairman.

25 Mr. Anderson, listening to what you are saying, you

1 sound very almost exactly what I have heard from a lot of
2 businesses and people in my own State of Vermont,
3 people's opinion I respect greatly.

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

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

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

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

17 Mr. Anderson. Absolutely. They would be a step in
18 the right direction.

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

25

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

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

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

10 Senator Leahy. Yes.

11 Mr. Powers. We also support the customer stay
12 provision.

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

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

25 Mr. Sauer, you raised concerns about abuses of the

1 post-grant review programs that were in the America
2 Invents Act. Those were created to improve patent
3 quality.

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

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

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

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

23 And because it is such a trial-like proceeding, we
24 feel strongly that these trials in the Patent Office
25 should have some of the same procedural protections and

1 have the same legal standards that otherwise apply in
2 district court.

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

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

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

19 Senator Leahy. Thank you.

20 Mr. Gupta, do you agree?

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

1 very successful mechanism.

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

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

11 Senator Leahy. Thank you very much. Thank you, Mr.
12 Chairman.

13 Chairman Grassley. Thank you, Senator Leahy.

14 Senator Hatch?

15 Senator Hatch. Thank you, Mr. Chairman.

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

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

24 Patent trolls are an unnecessary drain on our economy
25 and our Nation's innovation. An effective legislative

1 approach will include many elements, but in my mind, two
2 are absolutely essential.

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

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

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

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

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

22 Mr. Gupta. Yes, Senator. Thank you for the
23 question. I do agree. Highmark and Octane provides no
24 remedy in terms of recovery of fees.

25 Senator Hatch. When I introduced the Patent

1 Litigation Integrity Act in October 2013, the general
2 counsel of your company wrote to me and said, quote, "By
3 requiring a party to demonstrate that they or a third
4 party have the ability to pay potential fees or explain
5 why they wouldn't, a bonding or similar accountability
6 provision ensures that the fee shifting provision has the
7 intended effect of curbing frivolous and baseless patent
8 litigation," unquote.

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

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

19 Senator Hatch. Yes. They sue and then run.

20 Mr. Gupta. Yes.

21 Senator Hatch. And leave you holding the bag after
22 countless expenses.

23 I am concerned about patent quality. I want to
24 ensure that the U.S. Patent and Trademark Office issues
25 the highest quality patents possible. Now, do you

1 believe that allowing the USPTO to apply the broadest
2 reasonable interpretation to patent claims allows them
3 the greatest stability to get rid of bad patents?

4 Mr. Gupta. I do agree with that, Senator. And the
5 standard was recently reviewed by the Federal Circuit in
6 KaZUo and the Federal Circuit agreed that that was the
7 proper standard. It is the standard that the Patent
8 Office has been using for hundreds of years. That has
9 been used for reexaminations and reissues and is indeed
10 the standard that ought to be applied.

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

16 Senator Hatch. Thank you, sir.

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

25 Why should we not expect significant changes in the

1 application of section 285 when the judge who oversees
2 the most patent cases in the country has said that Octane
3 Fitness will not change the calculus for him or his
4 colleagues?

5 Mr. Sauer. Senator, yes. Far be it for me to
6 comment on Judge Gilstrap's pronouncement. What we are
7 aware of is, and it is very early in the process,
8 preliminary numbers did show that there was, after the
9 Octane Fitness case, an uptick both in motions that were
10 brought for QP recovery and for the months following what
11 seemed like an increased grant rate, actually, a
12 significantly higher grant rate of these motions.

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

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

25 Senator Hatch. The Chairman has allowed me to ask

1 one further question, Mr. Sauer. You mentioned in your
2 written testimony that the joinder provision in the
3 House's Innovation Act would create additional
4 encumbrances for patent-owning innovators. How would it
5 do this?

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

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

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

25 Senator Hatch. Thank you. Thank you, Mr. Chairman.

1 Chairman Grassley. Senator Feinstein?

2

3 Senator Feinstein. Thank you very much, Mr.

4 Chairman.

5 Mr. Anderson I thought well stated the problem with
6 demand letters.

7 Mr. Anderson, I just quickly want to read your
8 written statement. "These types of settlement demands
9 can be crippling to small business, but the attorney's
10 fees required to fight the lawsuit might be 10 times as
11 much. So in most cases, defendants will choose to settle
12 regardless of the extent of their use or the merits of
13 the patent claim."

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

17 I am in Riverside County and I talk to a group of the
18 Chamber of Commerce, which is a lot of small businesses
19 and many minority businesses, and a group came up to me
20 and said there were these attorneys that sent them demand
21 letters if their no parking sign was in the wrong place,
22 if a trash barrel obstructed part of an entry, whatever
23 it was and it said that for \$10,000, we will not sue.

24 A lot of them were struggling to pay that. Well, we
25 took a good look at it and the result was that the State

1 legislature passed a bill, Senate Bill 1186, Governor
2 Brown signed it, and essentially it required demand
3 letters to contain specificity as to the wrong alleged.

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

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

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

14 The demand letter was written so broadly that they
15 did not know what to do with it and the quote was this is
16 an amazingly broad letter and we have no idea what they
17 are asserting.

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

19 Senator Feinstein. Thank you. Does any witness
20 disagree with Mr. Anderson's statement?

21 [No response]

22 Senator Feinstein. There being none for the record.
23 So I thank you. I would like to move on.

24 I am sympathetic to the plight of businesses who
25 suffer from abusive discovery requests from patent trolls

1 and recognize that this often creates a one-sided
2 situation and a pressure to settle a case.

3

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

9 [No response.]

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

14 Mr. Gupta?

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

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

23 What that does is early on you get to focus the case,
24 if the Markman is done early. So the plaintiffs know
25 what claims they want to proceed with. The defendants

1 then know what type of prior art they need to look for,
2 and often the defendants also then know and the
3 plaintiffs know what products can potentially be accused
4 of infringement.

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

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

17 Senator Feinstein. That is actually very helpful.

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

20 Mr. Sauer. Thank you, Senator. Yes. I actually
21 agree with a lot of what Mr. Gupta says. Our concern
22 really is that the bill, at least the one that we see
23 introduced in the House, H.R. 9, does not do that.

24 The bill, H.R. 9, would require in some way to
25 prospectively limit discovery to only what is necessary

1 for claim construction at a time when the parties do not
2 know what is going to be necessary for claim
3 construction.

4 Senator Feinstein. You like what Mr. Gupta said.

5 Mr. Sauer. I like what Mr. Gupta said, that there
6 should be a nationally uniformed process indeed for the
7 development of information on both sides of the case to
8 make clear what the parties' theory of the case is, what
9 evidence backs up the parties' theory of the case, and
10 that should lead to a Markman hearing.

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

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

21 Senator Feinstein. Does anybody disagree with what
22 Mr. Gupta or Mr. Sauer have just said?

23 [No response.]

24 Senator Feinstein. Good. I will move on to
25 universities. In the last patent bill --

1 Chairman Grassley. This will have to be the last
2 question.

3 Senator Feinstein. I will be fast. Thank you, Mr.
4 Chairman.

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

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

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

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

20 Senator Feinstein. Right.

21 Dr. Crum. And as I hear the conversation around the
22 table, as we talk to small companies that are licensing
23 our technology, just the uncertainty, the risk that they
24 may incur in the loser paying, for example, even if they
25 are convinced that they have a strong case, one loss like

1 that can be devastating to them financially and we are
2 just concerned that it may curb and present a significant
3 barrier to their access to judicial review of those.

4 Senator Feinstein. I think my time is up. Thank
5 you very much.

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

10 Senator Cornyn?

11 Senator Cornyn. Thank you, Mr. Chairman. I never
12 thought of you as liberal.

13 [Laughter]

14 Senator Cornyn. But thank you for your generosity.
15 Thank you for having this hearing. This is an important
16 part of the table setting I think for consideration of
17 patent reform legislation.

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

22 We need to recognize there are certainly legitimate
23 rights that should be litigated and decided in court, but
24 on the other hand, there is also legal extortion, shaking
25 down people who cannot defend themselves and using that

1 money then to file other frivolous litigation.

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

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

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

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

1 to explain why the loser should have to pay.

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

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

13 Senator Cornyn. Well, that remains a work in
14 progress here on this Committee and we are working
15 closely with the Chairman and the Ranking Member and
16 Senator Schumer, in particular, but really all members of
17 the Committee to try to address that.

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

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

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

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

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

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

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

25 So what would happen, for example, Mr. Powers, to

1 your company if a hedge fund decided to file a patent
2 infringement lawsuit and then shorted your stock? How
3 would you see that and what would that do to your ability
4 to function?

5 Mr. Powers. Thank you for the question, Senator.
6 Being a privately-held company that is not a concern that
7 we have to deal with.

8 Senator Cornyn. Okay. Let me ask Mr. Anderson.
9 You are a publicly-held company, are you not, sir?

10 Mr. Anderson. No, we are not. We are private.

11 Senator Cornyn. Well, imagine with me.

12 [Laughter]

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

20 Mr. Anderson. I cannot really answer that, Senator.

21 Senator Cornyn. I imagine it would be pretty
22 devastating.

23 Mr. Sauer?

24 Mr. Sauer. A very quick observation. Yes. So I
25 think settlement pressures can be terrible, I think,

1 especially for smaller businesses.

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

10 In IPR proceedings, the patents go down approximately
11 80 percent of the time or only 20 percent come out. So
12 we believe that the markets react probably more strongly
13 to IPR proceedings because they just see these statistics
14 with higher kill rates than what is available in the
15 district courts, and it is great for people who bet
16 against patents when they have a proceeding like that
17 where the statistics bear that out.

18 Senator Cornyn. Mr. Chairman, thank you for your
19 generosity in terms of the time. I would just say I
20 think we need to also recognize that when frivolous
21 patent litigation is filed, it exacts a cost not just on
22 the company, the defendant, and extracts perhaps a
23 nuisance settlement, it also can have a dramatic impact
24 on the shareholders of that publicly-held company and
25 basically constitute legal extortion and, of course, have

1 much broader impact on the people who own the shares in
2 that company.

3 Thank you.

4 Chairman Grassley. Now, Senator Schumer? I am
5 going to ask Senator Lee if he will chair while I take a
6 couple appointments in my office.

7 Senator Schumer?

8 Senator Schumer. Thank you, Mr. Chairman.

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

11 [Laughter]

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

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

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

1 Although the deal was elusive at the time, I am
2 confident that with renewed bipartisan effort and energy,
3 we will get this done in the Congress.

4 The witnesses before us advocating for reform
5 represent an important cross-section of the economy. We
6 have a large tech company, a family farm manufacturer, a
7 small business restaurant franchise company.

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

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

17 I have heard about this. Good companies, they come
18 in, they get extorted, they say we are going to file a
19 lawsuit against you unless you give us \$.5 million, and
20 they do not have it. And this is the lifeblood of
21 America, these new companies.

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

24 In a letter our Committee received from 140 venture
25 capitalists who invest in technology companies back this

1 up. Engine Advocacy has pointed out 82 percent of troll
2 activity targets small and medium businesses; 55 percent
3 of troll suits are filed against startups with revenues
4 of less than \$10 million because they know those people
5 cannot afford a long, lengthy lawsuit, which the Patent
6 Office, now the patent law now not only sanctions, but
7 blesses.

8 The trolls are smart. They know these small
9 companies cannot afford to litigate even if they are in
10 the right, so they are more likely to settle. It is
11 those startups that are in the front of my mind
12 throughout this debate and will continue to be my
13 loadstar.

14 A patent reform bill needs to meaningfully address
15 the needs of these startups to earn my vote. In many
16 ways, patent troll legislation, as all of us on this
17 Committee have learned, is like a Rubic's cube. You need
18 to turn and twist all the parts properly so we are really
19 fixing the problem, but also protecting those who are not
20 part of the problem, who are represented by two witnesses
21 here today.

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

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

7 In fact, I see patent reform as a little oasis of
8 bipartisan cooperation in what many of us worry is a
9 desert of partisanship these days.

10 So I want to continue to work with Senator Cornyn,
11 Chairman Grassley, Ranking Member Leahy on putting
12 together a package that is fair and meaningful and
13 protects patent holders while eliminating the leverage
14 that bad actors currently exercise in the patent system.

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

19 Mr. Gupta. Thank you for the question, Senator.

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

25 The biggest challenge they have is that patent

1 litigation is so expensive right now and not only that,
2 but the risks are so asymmetric that defendants really do
3 not have the ability to get their day in court.

4

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

8 Senator Schumer. It is a crazy system.

9 Mr. Gupta. So most small companies do not have the
10 financial wherewithal to actually get their day in court.

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

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

19 Mr. Gupta. A particular proposal around claim
20 amendment is a reasonable proposal that I think we could
21 work around. However, for example, one suggestion is
22 that there should be a different panel that ought to
23 consider the -- make the institution decision and a
24 different panel should look at the final decision or be
25 responsible for the final decision. That does not seem

1 to be a practical solution.

2 In District Court litigation today, for example, we
3 do not say that if a judge rules on a motion to dismiss
4 adversely, that we get a different judge for the rest of
5 the trial.

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

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

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

23 Senator Schumer. Well, thank you. And I just want
24 to say, Mr. Chairman, I am optimistic that Senators
25 Grassley, Leahy, Cornyn and I can come up with a

1 bipartisan solution that will actually pass the Senate
2 this year.

3 Thank you.

4

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

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

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

18 It is a subject that we need to pay more attention to
19 and there is a lot of enthusiasm on this Committee for
20 patent reform, which I think has now become indispensable
21 for American businesses, large and small, who want to be
22 able to operate and grow without fear of extortion from
23 patent trolls; for example, unscrupulous entities who
24 will send your small business a letter accusing you of
25 infringing one of their asserted patents, with the wi-fi

1 router you happen to use in your small business, perhaps
2 allowing your customers to access it while in your store.

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

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

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

24 I am hopeful that this year we will succeed in
25 uniting these reforms and that we will finally pass

1 legislation so desperately needed by America businesses,
2 both big and small.

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

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

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

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

24 That does not matter because you are still
25 responsible for past use. So at that point in time, the

1 demand is not going to go much -- down very much if you
2 cease using that technology.

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

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

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

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

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

23 Mr. Anderson. Certainly that would be one step that
24 would be helpful.

25 Senator Lee. And I assume you see a lot of demand

1 letter abuse in your line of work based on your
2 description earlier.

3 Mr. Anderson. Yes, we do.

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

6 Mr. Anderson. Patent troll demand letters, we
7 received two and we have -- we are the defendant in a
8 lawsuit.

9 But I have reached out to other restaurants and
10 retailers and this is common practice across the
11 industry.

12 Senator Lee. All right. I see my time has expired.

13 Senator Durbin?

14 Senator Durbin. Thank you, Senator Lee. And thank
15 you to the panel for being here.

16 The first major patent reform in the modern era was
17 in 1952. We waited 59 years before we tackled again in
18 2011 and then we decided to wait 3 years to go after it
19 again.

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

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

5
6 Well, perhaps that is what some think a troll to be.
7 We asked the General Accountability Office what
8 percentage of patent litigations are filed by non-
9 participating entities; in other words, companies that do
10 not make things, companies that just sue people.

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

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

19 So what we are talking a bout are changes that are
20 going to affect 80 percent of patent litigation, which
21 most of us believe is totally legitimate.

22 It is not just about clubbing the trolls. We are
23 clubbing the filers of patent litigation and that
24 includes a lot more than must mischevious little gnomish
25 figures.

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

7 The Association of American Universities. Dr. Crum,
8 that might include your school. The Biotechnology
9 Industry Organization; the Medical Device Manufacturers
10 Association; the National Venture Capital Association,
11 PhRMA; and, a group which represents 200,000 American
12 scientist and engineers. Ambulance chasers? I do not
13 think so.

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

25 As you look at this story and step back from this

1 little gnomish figure, the patent troll, it starts to
2 look at lot differently.

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

6

7 Mr. Gupta. \$24 billion.

8 Senator Durbin. So what would \$10 million -- what
9 percentage would \$10 million in legal fees be of your \$24
10 billion revenue?

11 Mr. Gupta. And that is just outside counsel,
12 Senator. The disruption to our business in terms of the
13 number of people who get involved.

14 In one particular case, we had a star engineer devote
15 10 percent of his time. We had to get 100 people
16 involved in looking for documents that go back so far
17 that we do not even have electronic records for them.

18 Senator Durbin. The calculation, incidentally, is
19 not four-tenths of 1 percent of their revenues, it is
20 four-100th percent of their revenues that were spent.

21 I would say that you probably have nuisance lawsuits
22 in a lot of areas that amount to as much, if not more.

23 But I do sympathize with, Mr. Anderson, your company
24 and I do eat butter burgers; and, Mr. Powers, with your
25 company. And we have got a lot of farmers in our State

1 that use your company's inventions.

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

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

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

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

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

23 But it is the innovation is coming at the -- where we
24 transfer our technologies to those who can take it to
25 market and do something wonderful with it.

1 And precisely as you said, it is those companies --
2 and we deal with big companies, too. They are big,
3 innovative partners of ours. But it is those small
4 companies that are at risk here.

5 We do not disagree with going after the abusers. We
6 absolutely are in line with that because we see the
7 impact. But it is those small companies. It is the fear
8 that even if they are right, there is so much uncertainty
9 and risk in going to litigation, and none of these
10 companies are litigious. They do not have staffs to do
11 that.

12 We try to help them. We are not geared for that. We
13 do not want to put money into litigation. We want to put
14 it into research and innovation.

15 Senator Durbin. And back into the GAO report, 80
16 percent of patent litigation not being filed by trolls,
17 being filed by small and medium size patent holders who
18 are many times fighting the big boys. And H.R. 9, the
19 Goodlatte lower pays approach, is going to have a
20 chilling effect on their efforts to protect their
21 property rights and these ideas and their ability to
22 assert those rights in our court of law.

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

25 Thank you, Mr. Chairman.

1 Senator Lee. Thank you.

2 Senator Tillis?

3 Senator Tillis. Thank you, Mr. Chair.

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

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

12 Dr. Crum. Thank you for the question. It is a very
13 good question.

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

19 They do have deeper pockets and in terms -- I mean,
20 the litigation is not where they want to put their
21 resources and it should not be where they have to put
22 their resources if it is frivolous, but they at least
23 have that ability.

24 Senator Tillis. I was trying to get a sense -- in
25 North Carolina, the Research Triangle, we have a lot of

1 smaller companies that would probably be more resource
2 strapped than the university, quite honestly.

3 Dr. Crum. Absolutely.

4 Senator Tillis. So I am trying to get a better idea
5 for those types of companies and why they are different
6 and unique.

7 Dr. Crum. Why they are different? I missed the
8 point. Why they are different and unique from --

9 Senator Tillis. From the university, the concerns
10 and priorities for any kind of reform that we would
11 pursue.

12 Dr. Crum. Maybe I should address that by saying
13 what our priorities are, what our mission is. We view
14 our mission as the research, discovery and the knowledge
15 that we create getting it to the marketplace.

16 Thus, it is the impact on those companies that we
17 work with, because we are not as good at doing that as
18 the private sector. We understand that.

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

21 So we have concerns, too, because we can be subject
22 to litigation. But a lot of our concerns are with our
23 partners, those small firms that we have talked about and
24 the startups.

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

1 Senator Tillis. No, and I can follow-up.

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

5 Mr. Gupta. That is a good question. Several
6 billion.

7

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

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

12 Mr. Gupta. About \$3 billion last year.

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

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

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

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

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

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

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

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

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

5 I am sorry to interrupt you.

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

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

16 Mr. Sauer. Our sense is within Bio, because we have
17 so many large and small members that the divide -- I
18 think more unambiguously thoughts between large companies
19 and small companies. On many of these issues, we have
20 large, robust pharma companies who feel that they will be
21 able to weather a lot of changes in the law and a lot of
22 developments, whereas 80 percent of our members are small
23 companies who are much more concerned about what is going
24 on, whether they are biotech or in other areas.

25 A quick word about whether PhRMA will be next as

1 targets for patent trolls. We, too, are ware fo that
2 particular study. We have discussed it at length within
3 our membership and for reasons that take too long, we
4 cannot validate hardly any of it.

5 I think we do not share that particular concern
6 because our landscape is somewhat different than what was
7 presented in this study.

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

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

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

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

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

6 Thank you.

7 Senator Tillis. Thank you, Mr. Chair, and thank you
8 for your work on this matter.

9 Senator Lee. Thank you. Senator Franken?

10 Senator Franken. Thank you, Mr. Chairman.

11 Just one thing that Senator Schumer brought up that I
12 wanted to sort of balance a little bit. He talked about
13 startups wanting protections from what you call the
14 trolls.

15 There is the other side of it I think of startups and
16 I think the university is -- the universities sort of
17 represent this, because he talked particularly about
18 venture capital.

19 I think venture capitalists -- is it not true that
20 very often venture capitalists, when they are investing
21 in a business, a startup, see the value of the patent
22 even if the business does not make it? And that is the
23 other side of -- Senator Schumer seemed to suggest that
24 venture capitalists are on the other side of this issue
25 because they are startups and they do not want to be

1 attacked by a troll.

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

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

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

12 So, yes, the patent is extremely important to them
13 and the ability to protect that intellectual property.
14 but if the business goes under, the VCs, even if they are
15 left with ownership of the patent, they still need
16 someone that can develop that, develop off of that
17 patent.

18 So, again, I think it still gets back to the question
19 that we need to make sure that the small companies, the
20 startup companies are truly innovative, have fair
21 protection of IP.

22 Senator Franken. Mr. Sauer?

23 Mr. Sauer. In the small companies where I worked
24 before I joined BIO, we went through this several times,
25 because there is always need for more capital in these

1 companies that burn like tens of millions of dollars per
2 year in biotech.

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

10

11 So they went really in depth. It was quite
12 stressful. At the time, I was just a patent agent -- for
13 the company to survive such scrutiny.

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

19 So I can only validate that at least those VCs who
20 invest in the life sciences are very, very interested in
21 patents and will not fund a company, by and large, that
22 does not have a meaningful IP portfolio.

23 Senator Franken. Again, we are talking about
24 balance and I just wanted to kind of balance what Senator
25 Schumer said, because the other side of it seems to be

1 that venture capital is very often invested because of
2 the patent.

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

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

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

20 Mr. Anderson. Due to confidentiality, I cannot get
21 into the dollar amounts of the settlement, and you will
22 find that across the industry.

23 In terms of how I handle it, the first thing I do is
24 contact -- I am a solo practitioner in-house and patents,
25 when I came to work for Culver's, I had had hardly heard

1 of a patent and, unfortunately, they crept into the
2 restaurant industry.

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

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

9 I still pay the \$100,000 and we are still early in
10 the lawsuit, but if I was not paying one-tenth, \$1
11 million, there is no way we could afford that. That is
12 money, again, that should be going towards helping our
13 franchisees succeed, not paying out to patent trolls.

14 Senator Franken. Well, I guess my time is up, but
15 you aid you cannot tell me because of confidentiality,
16 but my understanding is that does not hold in Senate
17 hearings. Is that not right, Mr. Chairman? No, I am
18 lying. That is not true.

19 [Laughter]

20 Senator Franken. Thank you.

21 Senator Lee. Senator Perdue?

22 Senator Perdue. Thank you, Mr. Chairman. And thank
23 you for being here.

24 I was trained as an engineer. I have been very
25 heavily involved in the tech community in my home State.

1 For the last few years, I have actually been on the
2 board of a high tech startup.

3 So I have seen both sides of this endeavor and it
4 seems to me that the greatest economic miracle in the
5 history of mankind, we have sat here and watched it over
6 the last 70 years in the United States, and it was
7 fundamentally founded on three precepts.

8 In addition to having the best workforce in the
9 history of the world, we have the ability to innovate and
10 we have the ability to form capital and we have the rule
11 of law.

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

14 It seems to me that this abuse that we are talking
15 about here today is threatening tow of those three and it
16 really is very serious, but we have got to find a
17 balance.

18 I have got a couple of questions about trying to find
19 that balance, but it just seems to me that there are two
20 objectives here, obviously. We have got to control the
21 frivolous nature of these lawsuits to protect the
22 startups.

23 In my experience, startups need three things. One is
24 they have to have the innovation, two is they have got to
25 have the capital, and three is they have got to survive

1 the first t years. And I would bet if you look at this,
2 a lot of these attacks happen in these first 2 years,
3 while angel investors are in there before the venture
4 capital community is involved, and it will scare
5 everybody to death and it will freeze up that capital, in
6 my opinion.

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

12 So, Dr. Crum, I would love for you to talk about this
13 transfer process and about the Innovation Act, but also
14 to talk about the specific provisions of the various
15 bills that you believe adversely affect the ability of
16 universities not only to transfer the technology, but
17 also to help these startups, because I know you guys and
18 other universities are very involved with angel investors
19 in helping these startup entities attract capital on the
20 early, early stages of their incumbency.

21 Dr. Crum. Thank you. When we have those first
22 conversations with companies about what their needs are,
23 what their goals are, what they are trying to do, we sit
24 down and we work very closely with them. They become a
25 partner. We license the technology to them. We try to

1 help them attract capital.

2 I talked to the person who runs our IP and tech
3 transfer operation just yesterday say could you just give
4 me a few examples of the companies that the patents were
5 absolutely critical to getting capitalization, and she
6 ran through 15 just off the top of head.

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

10 And the second part of your question was?

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

14 Dr. Crum. Exactly.

15 Senator Perdue. And so the frivolous lawsuit, you
16 see both sides of this equation.

17 Dr. Crum. Yes.

18 Senator Perdue. I think you and Dr. Sauer
19 particularly can empathize with these business owners and
20 yet you are protecting university for their rights as
21 well.

22 So there are two sides of this and we have got to
23 find a balance and the way through here. The 20 percent
24 that end up being the frivolous cases, I do not know
25 where Google or Microsoft or Apple might have been in

1 their first few years of development, but if they were
2 caught up in this, they may never have gotten to
3 maturity.

4 Dr. Crum. And I think you were asking what things
5 do we see maybe that we would strongly support, that we
6 think -- I think we have talked about a lot of that
7 already, and that is ending the abusive demand letters.
8 I think we had a conversation about those need to be more
9 narrowly, specific, nonthreatening.

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

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

17 If we keep out of the courts, I think that is really
18 critical in those first couple years in particular for
19 the startup companies.

20 I think there are other things out there. I am not
21 an attorney and I am not as deep into the weeds on the
22 proposals. I think some of the colleagues here probably
23 are better suited for that.

24 Senator Perdue. Dr. Sauer, would you like to answer
25 the second part of that question.

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

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

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

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

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

25 The Game of Kings, that is what patent litigation is

1 and the bigger king you are, the more you will be able to
2 leverage the systemic litigation reforms that are being
3 proposed.

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

6 Senator Perdue. Thank you very much. Thank you,
7 Mr. Chairman.

8 Senator Lee. Thank you. Senator Coons?

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

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

22 Our economy, as a number of members have commented,
23 remains incredibly successful and important businesses
24 that cover the whole spectrum of these characteristics
25 have been affected and we are all better off by retaining

1 the diversity, the innovation, the creativity of the full
2 scope of our country.

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

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

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

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

25 It hangs in the balance of whether we overreach in

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

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

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

19 It empowers the FTC to go after those who send
20 deceptive and abusive letter to extort from large and
21 small businesses, and it tackles some of the recent
22 abuses of the post-grant system at the PTO, described by
23 Dr. Sauer, when a hedge fund can raise hundreds of
24 millions of dollars of investor capital simply by filing
25 a challenge for the purpose of profiting from shorting

1 the stock. And it would end fee diversion to ensure an
2 increase in the quality of the work at PTO.

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

6 And if I might, Senator Lee, I would like to submit
7 for the record letters that expres support for the
8 approach of the Strong Patents Act from the National
9 Venture Capital Association, the National Small Business
10 Association, the Biotechnology Industry Association, the
11 Association of American Universities, the Association of
12 Public and Land Grant Universities, the Medical Device
13 Manufacturers Association, the Pharmaceutical Research
14 and Manufacturers of America, the Innovation Alliance,
15 and the IEEE USA.

16 [The letters referred to follow:]

17 *****COMMITTEE INSERT*****

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Senator Coons. 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 could not 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 you written testimony you said, "We should urge caution on provisions which would create

1 significant hurdles for legitimate inventors seeking to
2 enforce their patent rights, such as blanket fee shifting
3 provisions.

4 There is a balance to be struck, and that word,
5 balance, has been used by most of the Senators who spoke
6 today. We want to be careful to go far enough to take
7 away the incentives from those who abuse the litigation
8 system and no farther.

9 In KINZE's experience, what does that mean? And then
10 I would like to ask other members of the panel.

11 What does it mean to go no farther and why is that
12 important given the history of your company and the
13 inventions of your founder?

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

19 What it did give us the ability to do is to get out
20 in front and commercialize a planter that made farmers'
21 lives much easier, reduced the amount of time they had in
22 the field, and gave them the ability to plant their
23 fields during a very narrow window during the spring.
24 You actually have, roughly, about 2 to 3 weeks where if
25 you can get your crop in during that time, you are going

1 to get peak yields. If rain or other things delay you,
2 the farmer is going to be hurt.

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

5 Turning to the limits -- you know, we should go no
6 further than to prevent patent trolls. We should go no
7 further than to prevent the patent trolls.

8 KINZE is not in favor of blanket fee shifting or
9 mandatory fee shifting provisions. However, we do
10 believe that fee shifting when parties bring baseless
11 litigation would serve as a practical deterrent to those
12 who would go ahead and do abusive patent litigation.

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

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

20 Mr. Sauer. I think it can be well exemplified by
21 perhaps the impleader provisions that are connected to
22 the fee shifting provisions of the bill. From fee
23 shifting comes concepts of how do we make sure the loser
24 pays once we have a loser pay system.

25 The impleader provision, like a few other provisions,

1 exemplifies the ecosystem within which Biotech works,
2 which indicates small companies, university licensors and
3 the like.

4 So if that system works in a way that implicates not
5 just patent owners who must defend their businesses
6 against patent infringement, but drags their business
7 partners into the litigation as unwilling co-plaintiffs
8 and subjects them to potential liability.

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

12

13 Senator Coons. Thank you, Dr. Sauer. I can see my
14 time is coming to a close. I just wanted to make sure,
15 whether it is a Hawkeye, a Cyclone or a Panther, we had
16 an opportunity to hear from Dr. Crum on behalf of Iowa
17 State and the other inventors and innovators at the
18 university system.

19 Can you just give us a context about the dangers of
20 over-broad patent reform on universities?

21 Dr. Crum. I just would follow-up on what Hans was
22 just saying about the involuntary joinder concerns, that
23 is really huge for us, because we could have our
24 university individual faculty departments pulled into
25 this. And if you want to talk about throwing a wet

1 blanket over innovation, that kind of fear and concern to
2 be pulled into something over which you had no concern,
3 develop some outstanding technology, that is throwing a
4 wet blanket over innovation. That is a real concern for
5 us and it also diverts a lot of resources that we should
6 be putting and try to put back into the research
7 enterprise diverts it to litigation.

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

14 Thank you, Mr. Chairman.

15 Chairman Grassley [presiding]. Without objection,
16 the material that Senator Coons wanted put in the record
17 will be made a part of the record.

18 Quite frankly, I believe Senator Whitehouse would
19 have priority, if you want it.

20 Senator Whitehouse. Thank you, Chairman. I will be
21 brief and I will yield to my extremely distinguished
22 collage, Senator Blumenthal very shortly.

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

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

7 The areas where I hear from Rhode Islanders that I
8 particularly want to focus on are making sure that a
9 plaintiff is a real plaintiff and there are not shell and
10 sham plaintiffs that are allowed to exist; that patents
11 that were written at a time when people did not
12 understand the Internet or other things and need to be
13 reviewed, there is an ability to review those patents
14 rather than to have them be weapons in the hands of
15 trolls.

16 The abuse of demand letters, which has become a
17 scandal be controlled, and that we focus the litigation
18 between the patent-holder and the person who is actually
19 using, in the ordinary sense io the word, the patented
20 technology. Not the florist or the grocer who is using
21 the end product.

22 And I think if we can agree on those four things --
23 and for the record, I see an awful lot of heads nodding
24 here, we have a bill that we can pass. But if we want to
25 add abortion provisions to human trafficking bills and if

1 we want to add running around in national security, Werda
2 dam and hydroelectric sties with firearms to bills that
3 protect sportsmen.

4 And if we want to add tort reform this bill, then we
5 are going to end up with unnecessary fights. And I hope
6 we can go forward with that.

7 I would like to read into the record what Brown
8 University say, which is a very, very important player in
9 our Rhode Island.

10 Brown University President Christina Paxson says that
11 the bill in the House of Representatives, H.R. 9, the
12 Innovation Act, goes bar beyond what is needed to curb
13 abusive patent practices.

14 Of particular concern are very broad mandatory fee
15 shifting and involuntary joinder provisions. I urge you
16 to oppose efforts to add broad provisions like these to
17 any Senate patent troll legislation.

18 And Brown has a lot of patents. URI has a lot of
19 patents. Our university signed another letter that I
20 would like to read from into the record. In fact, I
21 think every State represented on this Committee has a
22 university on this list that signed this letter, except
23 maybe Utah. I think they are the one exception. But
24 every other State represented on this Committee has
25 signed this letter.

1 It says that mandatory fee shifting and involuntary
2 joinder are especially troubling to the university
3 community because they would make the legitimate defense
4 of patent rights excessively risky and thus weaken the
5 university technology transfer process, which is an
6 essential part of our country's innovation and
7 entrepreneurial ecosystem.

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

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

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

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

23 Chairman Grassley. Thank you, Senator Whitehouse.

24 Now, Senator Blumenthal?

25 Senator Blumenthal. Thanks, Mr. Chairman, and

1 thanks for holding this hearing on a supremely important
2 topic where I think there is broad consensus that abuses
3 need to be stopped and inventiveness and creativity
4 encouraged. And the great enemy of constructive change
5 has been overreaching.

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

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

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

25 So the Federal Trade Commission ought to be using

1 existing law. Federal officials ought to be following
2 the lead of State Attorneys General, who are going after
3 deceptive or misleading practices under the good old
4 consumer protection laws. Fraud and deception in some of
5 the letters that are sent widely perhaps can be pursued
6 under exiting law.

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

10 Mr. Gupta. Senator, I can take a shot at it, if you
11 would like.

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

17 So requiring that pleadings be specific to state with
18 clarity what the defendant is accused of having done
19 wrong seems to be a fundamental principle that everyone
20 should be able to agree to.

21 And right now you stated that the Judicial Conference
22 has recommended that Form 18 be abolished. At least Form
23 18 gave us a form that we knew that we had to be able to
24 comply with.

25 With Form 18 being abolished, we are being asked to

1 refer to Iqbal and Twombly, which are not patent cases
2 and which all the guidance that those two cases provide
3 is to say that you need to state enough facts to show
4 that you plausibly --

5 Senator Blumenthal. Well, State Attorneys General
6 are taking more action under existing laws.

7 Mr. Gupta. Yes.

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

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

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

23 Senator Blumenthal. Do you agree, Mr. Sauer?

24 Mr. Sauer. I think the more robust data show -- if
25 we compared, let us say, the whole year last year to the

1 year before, the year was down almost 20 percent over the
2 year before. So we can wait until the end of this year
3 and see what the numbers show.

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

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

16 Senator Blumenthal. Mr. Gupta, from what we have
17 seen, I think we can agree, and I do not want to make too
18 much of the data that exists, but I think we can agree
19 that the trend is heading in the right direction. And if
20 that is so, should we not be cautious about legislating
21 in an area where circumstances are changing and the
22 courts are developing new law in the wake of the United
23 States Supreme Court opinions?

24 Mr. Gupta. As I stated, Senator, I am not sure that
25 2014 was not a one-time --

1 Senator Blumenthal. Well, should we not wait until
2 we know what is actually happening in the courts on the
3 ground I the real world.

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

11 Senator Blumenthal. I know that the Supreme Court
12 has not dealt with the whole problem for all time, but in
13 terms of framing solutions when circumstances seem to be
14 changing, should we not target those solutions to the
15 problems that are causing the abuses and target them
16 narrowly in very limited ways, especially since the facts
17 on the ground, and facts are stubborn things, seem to be
18 changing and perhaps going in the direction.

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

24 Now, the Supreme Court decision says that the
25 prevailing party, it says nothing about the defendant.

1 So a prevailing plaintiff actually now better able
2 with a fee shifting -- I am sorry -- the fee shifting
3 proposal says that the prevailing party would be entitled
4 to the fees. So it helps plaintiffs and defendants. In
5 fact, a small plaintiff without the ability to hire a
6 lawyer could actually now get a contingency attorney who
7 knows that even when the damages are small in a case,
8 they have an upside because they can get their fees
9 recovered.

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

13 Senator Blumenthal. My time has expired. Thank
14 you, Mr. Chairman.

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

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

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

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

10 Thank you very much. The meeting is adjourned.

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

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