

Testimony of

Chuck Fish

Vice President and Chief Patent Counsel
Time Warner, Inc.
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VICE PRESIDENT & CHIEF PATENT COUNSEL
TIME WARNER INC.

BEFORE THE

UNITED STATES SENATE
COMMITTEE ON THE JUDICIARY
SUBCOMMITTEE ON INTELLECTUAL PROPERTY

RECOMMENDED PATENT IMPROVEMENTS

June 14, 2005

Chairman Hatch, Senator Leahy, and Members of the Committee, it is an honor to have the opportunity to appear before you today to discuss recommended improvements to our nation's patent laws. My name is Chuck Fish, and I am Vice President and Chief Patent Counsel of Time Warner Inc.

The patent system as it exists today touches Time Warner's diverse businesses in many ways and works well in a variety of contexts. There are several areas, however, where improvements are sorely needed. The patent remedies environment, which is the subject of today's hearing, is one of the most important. As a large and diverse media company, Time Warner has an enormous and unique interest in the maintenance of strong intellectual property protections in all contexts. We believe that creators and innovators must have the fruits of their intellectual endeavors protected lest this country lose its edge in exporting valuable products like our entertainment and technology products and services.

That strong commitment to intellectual property protection and, in particular today, a strong and enforceable patent system in this country is wholly compatible with repairing a remedy system that has begun to reward not innovation, but hiring tenacious lawyers. Indeed, it is critical that the remedial aspects of the patent law and their judicial application strike the right balance in today's complicated marketplace.

To illustrate problems in the current remedy system, imagine a company (either a large or small company) that brings an exciting new information service to market. The company has invested tens of millions of dollars in research, equipment, marketing, etc. and may have negotiated license arrangements on a variety of patents needed for the service. Then, without warning, the company is hit with a patent infringement suit by another patent owner the company was previously unaware of who owns a patent that relates to a small part of the overall service. The patent owner demands as damages a portion of the monthly fee charged to subscribers for the overall service, including the new information service. In addition, the patent owner asks for an injunction, which would prevent the company from providing the service at all merely as a way to gain leverage and increase the likelihood of a favorable license fee. Thus, the new service can be essentially paralyzed until the patent dispute is resolved.

Certainly, if the patent is valid, and the company truly infringes the patent, a broad range of remedies including the issuance of an injunction may well be justified. However, as is increasingly the case, if the patent is invalid, or the company does not infringe the patent, the array of remedies brought into play through such a lawsuit cannot be justified. The company faces the threat of multi-million dollar damages far higher than the value of the patented component, as well as the threat of having to withdraw the service. The results and the relief in such cases are often unpredictable. Even winning these nuisance lawsuits can cause major damage to a large company, and can bankrupt a small company. In the end, most companies settle with the patent owner rather than run the risk of litigating.

Consumers are the real losers, as they either pay the price of the litigation through increases in retail prices, or, in many cases, are never offered the new service.

We have been following proposals for revision of the patent system that have been circulating in Congress with great interest, and continue to evaluate new ideas to improve the patent system. Like many others, we believe that there are three groups of issues that need to be addressed in order to improve the functioning of the patent system. First, the PTO needs to be adequately and consistently funded. Many criticisms are unfairly directed against the PTO. In the recent past, the PTO has been given an enormous task but highly inadequate funding to do its job. We appreciate the work done to make sure the PTO has the resources it needs in this fiscal year, and urge that adequate funding continue so that the laudable programs of Assistant Secretary Dudas and the professionals at the PTO can bear fruit.

Second, to insure the long term viability of the patent system, and the continuation of the benefits it has historically brought to our nation, patent quality needs to be addressed. In this area, improvements we support include limits on abuse of continuation practice, meaningful post grant opposition procedures, publication of all patent applications, and improved ability of the public to submit prior art during prosecution. We recognize that many who support improving the quality of issued patents have concerns about some of the proposals in this area, and agree with them that it is important to retain both substantive and procedural fairness for patentees while fixing the problems.

Third, with respect to patent injunctions and damages, the subject matter of today's hearing, we believe the following changes would address substantial problems in current patent law. We also believe these changes are fair to all and achievable.

Require Meaningful Proof Before Awarding Increased Damages in Patent Suits. Under current law, a finding of willfulness entitles the patent plaintiff to multiply its damages up to treble damages. As Judge Dyk's partial concurrence in *Knorr Bremse v. Dana* noted, the current standard is inappropriate in view of the settled law of punitive damages. Willfulness has a very different meaning in patent law than in traditional tort law, and increased damages are routinely awarded in patent cases. In contrast, in other litigation, increased damages are awarded only where parties have clearly acted reprehensibly or egregiously. Moreover, to fend off possible willfulness allegations, companies must go to the expense of hiring patent counsel to produce exculpatory opinion letters. As courts have noted, such letters are only useful when they are wrong - after a defendant has been found to infringe - despite the letter's stated belief that he did not infringe. Willfulness accusations arise in almost every patent case, and inject great uncertainty as to the ultimate outcome. Allegations of willful infringement lead to substantial increases in discovery and trial costs, because they are difficult to dismiss at the summary judgment stage, and appear to produce very little benefit to the system.

Moreover, as the FTC noted in its 2003 report, *To Promote Innovation*, the overbreadth of the willfulness standard in current law introduces unnecessary uncertainty, raises risks, and reduces efficiency because it discourages parties from reading others' patents and from planning non-infringing business models.

For all these reasons, the Patent Act should be amended so that the purpose behind increased damages, to punish those who have acted with disregard for the law, is actually the predicate for willfulness damages being imposed.

There are many proposals that attempt to amend the willfulness standard. We support all proposals that bring patent law into compliance with other litigation standards, and increase damages only in cases where parties have acted egregiously. In particular, we support requiring that willfulness be established through clear and convincing proof of actual, substantive, written notice to the defendant, deliberate copying of a patented product knowing it to be patented, or continued infringement not colorably distinguishable from activities previously judged to infringe.

Conform Patent Damages to the Reality of Multiple Patents Covering Products. The current law requires that patentees who succeed in litigation receive damages fully adequate to compensate for the infringement. We support this standard for all owners of intellectual property, but note that in the patent area the elements of damages have been expanded by the courts far beyond the patented contribution to the public. Especially in the areas of complex computer and communication systems there can be many hundreds of patents covering a product or service. For example, there are more than 400 patents that are essential to produce a DVD. And others have commented on the hundreds of patents typically related to a computer operating system or a PC. Yet the patent law remains mired in a nineteenth century paradigm of essentially "one patent, one product." As a result, the courts have been required to create and modify complicated patent specific damage rules to give effect to the statutory purpose and underlying policy. Thus, in litigation and negotiation, legitimate patentees, as well as those who would twist the patent litigation system for private advantage despite potential harm to the public, routinely urge that the measure of their damages must encompass any remotely relevant revenue of the defendant.

Time Warner supports reforming patent damages law by explicitly directing the courts to begin their damages analysis for combination inventions by focusing on the incremental value attributable to the patented invention. When the accused product or service involves a complicated system incorporating many public domain and patented contributions, full compensation to the patentee should not usually involve apportioning value unrelated to his or her

invention.

Fix the Patent Injunction Imbalance. Today, as a matter of course in patent litigation, the prevailing plaintiff is entitled to an injunction and the availability of such an equitable remedy is a key part of being able to protect our nation's intellectual property. The problem with today's system comes not in the availability of injunctions but in the application of that remedy over the last fifteen years. Due to changes in the way that courts consider irreparable harm, individuals and companies who do not innovate or put products into the market, but rather buy up paper patents and try to extract large license fees, have been able to shift the equities in the patent environment in a way that makes little sense.

Thus, any patent owner can hold a company hostage by seeking an injunction and threatening to stop the company from operating part of its business. Instead of following traditional principles of equity and requiring a weighing of the equities in patent cases, the Federal Circuit has required district courts to presume irreparable harm in all cases. To make matters worse, this presumption is essentially an irrebuttable one because the Federal Circuit has rejected nearly all attempts to rebut that presumption and discounted hardship to the defendant or the public.

As a result, a patent owner can obtain an injunction, regardless of whether he or she is in fact irreparably injured, regardless of whether the patent owner makes a competing product, and regardless of whether his or her invention is a major or a minor part of the defendant's product or service that is enjoined. Therefore, patent lawsuits frequently place core aspects of a defendant's business in jeopardy of being shut down if the plaintiff prevails. While large companies like Time Warner may be able to absorb some of these costs, one only need to look at patent cases over the last several years to see that small companies simply cannot.

This recent judicially-created patent injunction doctrine has a number of harmful effects. First, it creates a litigation imbalance between plaintiffs and defendants that distorts the purpose of the Patent Act. The mere threat of an injunction produces a disproportionate in terrorem effect. Plaintiffs are able to assert far-fetched claims and extract settlements with the threat of stopping a company that is already in the marketplace from using a technology that is part of its product or service offering. In the vast majority of cases (most which never go to trial), companies that have not infringed pay what amounts to protection money to avoid the draconian threat of disruption of their businesses. Second, the doctrine permits a patent-holder to obtain (or to threaten to obtain) an injunction against an entire business model even when the patented item is a small element of the defendant's product or service offering. Third, the doctrine disproportionately rewards entities that own but do not practice patents because they can pursue litigation, threatening to shut down another company, without risk that the same strategy will be applied to them. Fourth, the doctrine is highly problematic in areas where, due to constraints on its resources, the PTO has been unable to maintain patent quality because plaintiffs with improperly issued patents can stop companies who have legitimately brought products and services to market from providing them to consumers.

The net result of this doctrine is substantial uncertainty that harms small companies that are in the marketplace every bit as much as big companies. In fact, in some situations, small promising companies could actually be put out of business by a patent owner because they do not have the funds to fight an expensive lawsuit. In either situation, consumers end up losing as well, because they ultimately pay the costs of lawsuits and decreased competition. The injunction problem is of concern to Time Warner because predictability is very important to us as we invest in items that we know consumers want, such as new content delivery systems to bring our content to consumers, innovative cable technologies, and exciting new possibilities for AOL users.

As we said earlier, we believe that injunctions are an important and essential part of the patent system. And we believe strongly that only parties who will be actually irreparably harmed should be able to receive an injunction following a finding of patent infringement, and that patent holders will be able to establish irreparable harm easily in many situations.

Level the Playing Field for Patent Litigants on Validity Issues. Currently, issued patents receive a strong presumption of validity. To invalidate a patent, a defendant must prove by "clear and convincing" evidence that the patent should have never been issued. In practice, this means that a defendant must prove that it is absolutely clear that the patent should have never been issued. All too frequently, this standard unfortunately cannot be squared with the current state of our patent system. Although the PTO has made great strides with the extremely limited resources it has been given, most recent reports recognize the inadequate quality of examination in the PTO and the resulting recent poor quality of issued patents. Thus, it is often the case that patents do not deserve a strong presumption of validity.

Given the inefficiency inherent in increasing numbers of expensive validity contests over increasingly weak patents (especially in the software and business method areas), it is important to level the playing field now. We thus propose that, to invalidate a patent, a party relying on prior art not considered by the PTO must prove by "a preponderance of the evidence" that the patent is invalid -- in other words a 51% probability that the patent should have never been issued. This is fair, especially considering that when a patent is in litigation, thousands of hours and millions of dollars may be spent on examining whether it should have been issued. This intense scrutiny should be given at least the same amount of weight as the effort of the PTO to issue a valid patent, especially in light of the fact that on average

an examiner is typically given less than 30 hours to decide whether to issue a patent.

Require the "Loser Pays Rule" for Patent Infringement Suits. Patent litigation is extremely expensive, involving high expert witness fees, attorneys fees and extensive discovery. However, the cost of such litigation often falls disproportionately on defendants. Even when they win, defendants will usually pay over a million dollars in fees to prove that a single patent is invalid. Currently, even with (rarely imposed) Rule 11 sanctions, there is a gap in disincentives to deter a patent owner that wishes to launch a nuisance patent infringement lawsuit. Even when the patent owner is not justified in his actions, defendants are stuck with the tremendous cost of defending the lawsuit. As patent litigation is almost entirely contested between commercial entities (increasingly commercial entities that exist solely for the purpose of threatening or pursuing patent litigation), we believe there is no justification for continuing a system biased in favor of plaintiffs. Some type of fee shifting mechanism would go a long way to ensuring that litigation is a last recourse, rather than a first option, as occurs all too frequently today.

We believe that adoption of our recommendation would provide a stimulus to decrease the incidence of patent litigation, and increase negotiated (and hopefully therefore more efficient) resolution of patent disputes.

Other Proposed Reforms. Other reforms to the patent litigation system, including repealing Section 271(f) of the Patent Law, providing additional alternatives to expensive litigation, and venue reform, may also be worthy of consideration. Overall, however, we believe that the goal should be to return patent litigation to the mainstream of business litigation and restore traditional balance to patent-specific rules, while respecting the important role that the patent system plays in our economy and the rights of patent owners. We also believe that patent litigation reform can have a near term impact in alleviating patent quality problems while the processes in the PTO are being upgraded for the long haul.

Conclusion. Thank you for the opportunity to testify. We believe the proposals I've described are important reforms that would make the U.S. patent system much fairer and more reasonable for all parties. In providing this testimony, we hope to stimulate a discussion regarding the best way to reform problems in patent law, including patent litigation. We know that much remains to be done to turn these recommendations into proper legislative proposals, and would be delighted to work with this Subcommittee to help in any way we can.