

Testimony of
Mary E. Doyle

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Senior Vice President and General Counsel
Palm, Inc. Sunnyvale, California
before the Senate Committee on the Judiciary regarding
"Patent Reform: The Future of American Innovation"
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Chairman Leahy, Senator Specter and Members of the Committee, my name is Mary Doyle and I am Senior Vice-President and General Counsel of Palm, Inc., headquartered in Sunnyvale, California. I thank the Committee for the opportunity to testify on behalf of Palm and as a member of the Coalition for Patent Fairness in support of the "Patent Reform Act of 2007." We believe this legislation will greatly enhance the ability of Palm and other companies like ours to innovate and to compete globally.

It has been nearly ten years since Congress passed the Intellectual Property and Communications Omnibus Reform Act of 1999. That act addressed inequities in the United States patent system by implementing several reforms, among them, mandatory publication of patent applications after eighteen months and increased third party participation in reexamination proceedings. The only other significant patent reform effort in recent decades resulted in the passage of the Hatch-Waxman Act of 1984, subsequently amended, which addressed issues of concern to the pharmaceutical industry. Despite revolutionary developments in technology and the emergence of global markets, however, the patent statutes have otherwise remained largely untouched since 1952 - and the patent damages statute since 1946.

Palm and many others believe it is time to take stock of the U.S. patent system once again, and to ensure that it is working in a fair and balanced way for American innovators across all industries. In our view, the provisions of S.1145 accomplish that goal. We commend Chairman Leahy, Senator Hatch and other sponsoring Members of this Committee for developing legislation over the past two Congresses that seeks to reconcile the interests of all stakeholders in the U.S. patent system to reach a fair and balanced result.

Mr. Chairman, as you requested I will address the issues you have indicated will be a focus of this hearing, but I also would like to share our views on two additional issues -apportionment of damages and limitation of willful infringement claims -both of which Palm and the Coalition for Patent Fairness (Coalition) believe will be essential to any successful effort at patent reform.

Palm and the Coalition support interlocutory appeal to the U.S. Court of Appeals for the Federal Circuit (Federal Circuit) from Markman rulings, and the revision of venue laws to discourage forum shopping, both provided for in S.1145. We also believe the proposed post-grant review

procedures are a fair and reasoned response to ongoing problems in the patent system and the historical underinvestment in the work of the U.S. Patent and Trademark Office (PTO). In addition, we strongly support Chairman Leahy's and Senator Hatch's effort to provide guidance to the courts regarding the measure of damages for infringement and to establish a more rigorous legal standard for imposition of triple damages upon a finding of willful infringement.

Before delving into these issues in greater detail, I thought it might be useful to the Committee for me to share something of Palm's everyday experience with the patent system. I hope this brief snapshot will provide the Committee a greater understanding of why Palm and a myriad of other interested parties - ranging from financial services firms to energy companies to family farmers - are urgently seeing these reforms of the patent law and process.

Palm's Experience

As the head of the legal department for a mobile computing company, I have seen first hand the challenges that have developed under our patent system, and how abuses have exploded. It now takes as long as four years for a patent to issue on an application reflecting today's innovations. The continued backlog of patent applications at the PTO speaks clearly to the need for a renewed commitment of resources to the system we rely on every day to protect our competitive advantage as a nation of innovators. At the same time, the number of patent infringement claims we face as an industry has grown exponentially.

We, like many others, have also been subject to the threat of monumental damages awards -- the likes of which RIM faced in the NTP litigation -- and have agreed to license patents at rates that greatly exaggerate the contribution of the patented invention. Palm and other members of the Coalition attribute this phenomenon in significant part to forum shopping, the disparity among damage measures applied by our country's courts and the low hurdle to imposition of triple damages for willful patent infringement. For these reasons, Palm adds its voice to the call for immediate patent reform.

Palm, Inc. is a \$1.6 billion high technology company, founded in 1992 and headquartered in the heart of Silicon Valley. Today, millions of Americans rely on Palm devices, including Palm@Treo™ smartphones and Palm handheld devices for their daily mobile computing needs. Palm has long looked to the protections afforded by the U.S. patent, trademark and copyright laws to safeguard its substantial investment in intellectual property and to preserve its competitive advantage. Our products are protected by over 250 U.S. patents. We have nearly double that number of patent applications pending and, as we expand our global reach, have continued to accelerate our patent filings worldwide.

Since going public early in 2001, Palm has been subject to an increasing flurry of patent assertions and patent litigation. Of the sixteen lawsuits pending against the company during this period, all but three were launched by licensing companies; and, though Palm's principal place of business is in California and its state of incorporation is Delaware, none of these cases was first filed in California, only four were first filed in Delaware, and six (all in the last two years) were brought first in what are referred to as "magnet jurisdictions."

Palm has been successful to date in resolving all matters before trial, either upon summary judgment or through settlement negotiations. That's the good news. The bad news, however, is that these results come at the expense of Palm's investment in its business, where with each \$1M spent on litigation we could instead employ as many as ten entry level software engineers for a year.

The cost of patent litigation today is many times that of other intellectual property litigation with similar amounts at risk, such as copyright litigation. Reportedly, the median cost of defending a major patent case is approximately \$4.5 million.¹ In Palm's experience, multi-defendant patent litigation may cost each defendant (and particularly the relatively smaller defendants) less, but single defendant litigation, particularly cases that have been appealed multiple times to the Federal Circuit, can cost more than double the reported average without ever reaching trial.

We also face the prospect of much larger damage awards than in previous years. For example, prior to 1990 there had been only one patent damage award in history larger than \$100 million; but between 1990 and 1999, there were thirteen such awards. And that trend has continued with 21 such awards between 2000 and 2005, including one recent astronomic damages award against Microsoft of \$1.52 billion.²

The settlement calculus derived from the high cost of litigation and the risk of an unprecedented damages award, not to mention an award of triple damages, is clearly weighted in favor of the patent holder. It should not be surprising, then, that an industry of patent speculators has grown up almost overnight.

Palm also routinely receives patent assertions, generally delivered in the guise of "invitations to license." Vaguely worded and generally unsubstantiated by claim charts or otherwise, these letters by themselves may expose the recipient to triple damages for willful patent infringement. Invitations to license may in some cases be coupled with what we call the "thwack" factor, named for the sound a large stack of patents makes when it hits the negotiations table. The "thwack" factor is credited with discouraging the recipient of a letter from undertaking the not insubstantial cost to do an initial infringement and invalidity analysis, all because, once one patent is knocked out of contention, another patent lines up to take its place.

Often, the offer to license is phrased in terms of a percentage royalty based on the total selling price of Palm products, even when the scope of the patent or patents extends to only a relatively insignificant feature of the device. The risk of triple damages, the "thwack" factor and uncertainty as to the measure of damages that a court will apply often convinces many a recipient to achieve the best settlement it can under the circumstances and avoid the cost and aggravation of litigation. While we and many others successfully navigate these waters daily, there is no question that the license fees paid to patent owners big and small, powerful and emerging, with products or without, is unjustifiably inflated to reward not the innovator, but the litigator who takes maximum advantage of the current inequities in our patent system.

Here is one recent example. Last year we were approached by a patent aggregator with an offer to license a number of patents it contended implicated a component in our products. This component was available from a number of suppliers, all with significant financial resources,

who are in a far better position than Palm to understand the merits of the patent infringement claims, and to determine the validity of the patents involved.

Still, the aggregator chose to approach Palm and other system vendors. In the course of our discussions, we learned that the aggregator had sued to enforce its patents in a magnet jurisdiction. Our further discussions await the resolution of that litigation, but this much is clear: We have been approached rather than our supplier because the aggregator believes it can attach a royalty, not just to the value of the allegedly infringing component, but to Palm's entire product offering. In the eyes of a licensing entity, this gaming behavior is likely perceived as entirely rational in a world where there are few checks and balances on launching speculative claims, demanding high ransom settlements, or threatening legal actions in preferred jurisdictions where it is difficult if not impossible to predict the measure of damages that will be applied. But to an outsider, this behavior is non-intuitive, unfair to both the system vendor and the supplier, and an example of how an unbalanced patent system can distort the market in ways not anticipated or intended by the American patent laws.

Key Issues

Turning next to a discussion of each proposed reform, we will share our thoughts concerning venue, interlocutory appeals from Markman rulings and the structure of postgrant review. We will also discuss two other reforms that we together with the Coalition for Patent Reform strongly favor - apportionment of damages and limiting claims of willful infringement.

As a preliminary matter, I would first like to emphasize our belief that S. 1145 would improve patent quality and restore fairness and balance to the way patent disputes are resolved in our courts. I should add that it does all this while maintaining patentees' rights and their ability to derive meaningful economic value from their intellectual property. Nothing in the bill would prevent patent holders from having their day in court and obtaining reasonable royalties from those that would infringe on their patents.

Markman Hearings

We strongly support the efforts in S. 1145 to provide for interlocutory appeal of a Markman claim construction ruling to the Federal Circuit. Claim construction is a fundamental predicate to the dispute; it goes to the heart of the legal sufficiency of any patent infringement case. Not until a patent claim is construed is it possible to establish whether infringement has occurred, whether the patent is invalid and whether it makes more sense to pursue litigation or settle the case. This foundational claim construction process, if conducted early in the litigation, also considerably narrows discovery, motion practice and the related expense. In short, claim construction affects all aspects of the case.

Currently, there is wide variation among courts in the scheduling of Markman hearings. In many cases, an accused infringer can wait for two years or more from the start of litigation just to learn the court's interpretation of the patented claims. Yet, even then, there is often no final resolution because claim construction rulings are so frequently reversed by the Federal Circuit.

Let me offer a case in point. Palm recently prevailed in a piece of litigation in which the patent holder sought a claim interpretation that would include a Palm device, such as a Treo smartphone, within the meaning of the word "card." The district court construed the claim favorably to Palm, and then granted Palm's subsequent motion for summary judgment. On the patent holder's appeal to the Federal Circuit, the district court's claim construction was reversed. On remand, the trial court conducted a second Markman hearing, once again construing the word "card," this time in conformity with the decision of the Federal Circuit, but again to Palm's advantage. Summary judgment was granted to Palm a second time, and was sustained on the second appeal to the Federal Circuit. There is now no question that Palm's devices are not "cards." The cost of this litigation and two trips to the Federal Circuit? \$3.5M.

This litigation and many others like it would be far less costly if an interlocutory appeal from the Markman ruling were permissible.

Venue

Most on this Committee are doubtless familiar with traditional notions of federal jurisdiction and venue. Generally, venue addresses the question of which among the federal courts with subject matter and personal jurisdiction is most convenient for the conduct of a case.

The current law on venue in patent cases provides that venue is proper either where the defendant resides or where the defendant has committed acts of infringement and has a regular place of business. However, when the definition of the word "resides" as applied to venue for corporate defendants was amended by the Congress in 1988, a corporation was presumed to reside wherever it was subject to personal jurisdiction. As a result, virtually any company whose products are sold nationwide is subject to patent litigation in any jurisdiction in the country.³

Liberalization of the venue statute imposes a costly burden on businesses like ours that must collect evidence and witnesses and travel to remote jurisdictions to try complex patent cases over a period of weeks or months. It is also apparent to us that this change in the statute worked a perverse mischief, encouraging forum shopping. If patent holders may bring suit anywhere in the country, courts with speedy dockets or famously generous verdicts will almost certainly attract their attention. It is no wonder that "magnet jurisdictions" arise.

We believe, consistent with traditional venue concepts, that a lawsuit should be resolved in a forum that has a real and meaningful connection to the underlying claim and the parties, and that venue standards should preclude "gaming the system." One way to achieve this objective is to further refine the language in S.1145 to ensure that claims are heard in a location that has tangible nexus, either to the defendant's headquarters or to a place it conducts significant operations. Such a change will discourage forum shopping and the resulting inconsistencies in jurisprudence.

Post-Grant Review Procedures

Under current law, a patent may be challenged in a number of ways at any time during the life of the patent: through a court proceeding, such as a declaratory judgment action, or through an inter partes or ex parte reexamination. The notion that a patent now enjoys "quiet title" and that a post-

grant system with a second window would be unprecedented, is simply incorrect. Furthermore, effective post-issuance administrative review procedures are widely available in other countries.

The proposed post-grant review process in S. 1145 is an evolution of the interpartes procedure that has been in place for years. The principal differences between the proposed post-grant review process and the current reexamination process are the greater availability of limited discovery, the narrower scope of estoppel, the assignment of an administrative law judge to preside over post-grant reviews rather than a patent examiner and the ability to base a challenge on evidence that is not in the form of an issued patent or printed publication. While these differences are not trivial, it is clear that the changes would merely alter the existing reexamination procedures to allow for a more meaningful review.

The proposed post-grant review process should lead to better patent quality, which will benefit everyone - patent holders, patent users and consumers. Allowing third parties to institute an administrative proceeding early in the process should also solidify the breadth and applicability of these patents, thereby leading to fewer later challenges. I am also optimistic that the post-grant review will ultimately reduce litigation costs.

For many companies whose products include hundreds, if not thousands of different technologies, a single review process immediately after a patent has issued, is not sufficient. First, the review of even a single patent, let alone all those that might be brought to bear on an integrated product such as a Palm device, is impracticable both from a cost perspective and from an engineering resource perspective. Second, companies often cannot anticipate, at the time a patent is issued, all of the ways that the patent may be interpreted by the patent holder or the courts. In fact, with over 180,000 patents being issued annually in the U.S., patent users often are unaware of an alleged infringement until the patent holder, who has more visibility into the meets and bounds of its patent, threatens a company with court action. For these reasons, Palm and the Coalition favor the proposed "second window."

Apportionment

The complexity and the level of innovation necessary to today's technology products is stunning. For example, there are more than 400 patents that have been claimed to be essential to producing a DVD, tens of thousands of patents that may relate to a single microprocessor and perhaps hundreds of thousands of patents that may relate to a personal computer. In addition, multiple technologies that once may have been incorporated individually into dedicated devices such as televisions, telephones, cameras or music players, are now found on a single integrated device. For example, in March 1996, the original Palm Pilot 1000 personal digital assistant offered four simple features: an electronic address book, calendar, to-do list and note pad. Today, Palm's latest mobile computing device includes not only these four features, but dozens of others including telephony, photography, videography, web browsing, email, text messaging, document processing, and so on.

Despite the increasing complexity of technology products, the courts have strayed from apportionment analyses sanctioned in U.S. Supreme Court cases dating back to the 1850s, often embracing instead the "Entire Market Value Rule," which allows a patent holder to recover a reasonable royalty based on the economic value attributable to an entire product rather than the

allegedly infringing component, feature or function. Courts have chosen in recent years to apply the Entire Market Value Rule in entirely dissimilar situations, leaving the likely measure of damages applicable in any given case open to anyone's guess.

Not surprisingly, confusion regarding the applicable measure of damages can increase by orders of magnitude the damages a patent holder may legitimately seek, providing tremendous incentive to file infringement actions with respect to any aspect of a complex product, no matter how insignificant the contribution of the patented invention. The amount of money potentially at stake in the litigation as a result of this confusion can and does impose huge settlement pressure on defendants, regardless of the strength of the infringement claim.

We believe that the measure of patent damages should consistently reflect the original purpose of a reasonable royalty award, namely, to provide the patent holder with a portion of the profit attributable to the patent as compensation for use of the patented invention, while leaving the infringer with a portion of that profit in return for its business risk, labor and investment,¹ just as royalties reached in real-life negotiations do. Under Federal Circuit precedent, however, the patent holder may receive a royalty far in excess of that contribution, while an infringer need not be left with any profit at all after paying a reasonable royalty. As a result, even where a patent is for a marginal improvement to a product, the reasonable royalty award for infringement can exceed not only the profit attributable to the patented invention but the profit on the entire product.⁶ Such awards fly in the face of the bedrock principle that the purpose of patent damages is to compensate, not to punish.

The language proposed in S. 1145 would help limit excessive royalty awards and bring them back into line with historical patent law and economic reality. By requiring the court to determine as a preliminary matter the "economic value properly attributable to the patent's specific contribution over the prior art", S. 1145 will ensure that only the infringer's gain attributable to the claimed invention's contribution over the prior art will be subject to a reasonable royalty. The portion of that gain due to the patent holder in the form of a reasonable royalty can then be determined by reference to other relevant factors.

Palm also supports codification of the "Entire Market Value Rule" in this legislation, ensuring that the courts will continue to assess damages based on the "entire value" of the product in instances where the claimed invention is the predominant basis for consumer demand for the product.

Willful Infringement

The patent law provides that a court may award up to triple damages and attorney's fees if it finds that the defendant has engaged in "willful" infringement. Although the courts have characterized these extra-compensatory damages as a form of punitive damages, the standard applied to determine whether the defendant acted "willfully" is far lower than what is required to impose punitive damages in other contexts - proof of bad faith or egregious conduct is not required and a patent holder may prevail simply by showing that "a potential infringer ha[d] actual notice of another's patent rights" and failed to satisfy his "affirmative duty to exercise due care to determine whether or not he is infringing."⁸ This standard has the practical effect of shifting the burden of proof to the defendant whenever the patent holder can show that the defendant had

notice of the plaintiffs patent, perhaps only by way of a vague and unsubstantiated "offer to license," as I suggested earlier.

The current willfulness standard has several negative effects. To avoid a finding of actual notice of a patent, some companies now instruct their employees to avoid reading patents and patent applications. That is behavior opposite of what the patent system was intended to encourage. The historical success of Silicon Valley is based not only on the creation of revolutionary new products, but also on the evolution of old ideas. Fundamental to the revolution and evolution of innovation is learning from what others have done in the past.

Once a company does learn of the existence of the plaintiffs patent, it may seek to satisfy its duty of care by obtaining an opinion of counsel that the patent is invalid or not infringed by the company, or both. But reliance on that opinion typically triggers a pre-trial disclosure obligation, which in turn may result in a broad waiver of the attorney-client privilege - requiring disclosure of other materials prepared by the defendant's attorneys, even materials relating to the infringement litigation itself. There is little incentive to take this risk.

Given the ease of proving willful infringement, the opportunity to reap windfall triple damages, and the conundrum that a willfulness claim causes for defendants, it is not surprising that such claims are asserted frequently in patent litigation. One study found that they were asserted in more than ninety percent of all cases.⁹ In addition to the ill effects already discussed, these claims provide patent holders with increased leverage in settlement negotiations. Defendants face considerable pressure to settle even unjustified claims because a huge monetary judgment can result from a loss on the merits.

Given these concerns, we applaud the sponsors of S. 1145 for language that will address this inequity and help restore balance to the patent litigation process.

Summary

To summarize, Palm relies on the patent system to protect its key innovations, its design freedom, and its most valuable intellectual property. We believe that Congress should establish a level playing field that provides greater predictability and balance to the patent system for both plaintiffs and defendants in infringement cases, and pledge to continue to work with you, Chairman Leahy and Senator Hatch, and your colleagues, to ensure that the patent system again provides an effective incentive for innovation and promotes American competitiveness around the globe.

I would be happy to address any questions you may have.

I American Intellectual Property Law Association, Report of the Economic Survey, at 23 (2005) (median cost for cases with more than \$25 million at issue).

² William O. Kerr and Gauri Prakash-Canjels, Patent Damages and Royalty Awards: The Convergence of Economics and Law, in *les Nouvelles*, June, 2003, at 83; Internet Patent News Service & Source Translation and Optimization Co., Table of Patent/copyright infringement lawsuits/licensing awards, at <http://www.iplaw-quality.com/economic/awards.htm>.

3 Improving Federal Court Adjudication of Patent Cases: Hearings Before the Subcomm. On Courts, the Internet and Intellectual Property, 109th Congress (Oct. 6,2005) (testimony of Kimberly A. Moore, Prof. of Law, George Mason University School of Law), at 6.

4 Georgia-Pacific Corp. v. United States Plywood Corp., 318 F. Supp. 1116,1122 (S.D.N.Y. 1970) ("[T]he very definition of a reasonable royalty assumes that, after payment, the infringer will be left with a profit.").

5 See, e.g., Monsanto Co. v. Ralph, 382 F.3d 1374,1384 (Fed. Cir. 2004) ("[A]lthough an infringer's anticipated profit from use of the patented invention is among the factors to be considered in determining a reasonable royalty, . . . the law does not require that an infringer be permitted to make a profit." (citation omitted))

6 See, The Patent Reform Act of 2007, Hearing on H.R. 1908 Before the Subcommittee on Courts, the Internet, and Intellectual Property, 110th Cong. (statement of John R. Thomas, Professor of Law, Georgetown University Law Center at 3-5) (April 26,2007) (discussing ten examples in which excessive royalty awards have been granted).

7 Pall Corp. v. Micron Separations, Inc., 66 F.3d 1211,1223 (Fed. Cir. 1995) ("[T]he purpose of compensatory damages is not to punish the infringer, but to make the patentee whole.").

8 Knorr-Bremse Systeme Fuer Nutzfahrzeuge GmbH v. Dana, 383 F.3d 1337, 1343 (Fed. Cir. 2004) (Dyk, J.,concurring in part and dissenting in part) (citation and internal quotation marks omitted).

9. Kimberly A. Moore, Empirical Statistics on Wilful Patent Infringement, 14 Fed. Cir. B.J. 227,232 (2004).