New York Law Journal
SERVING THE BENCH AND BAR SINCE 1888
WWW.NYLJ.COM
An ALM Publication
VOLUME 253—NO. 70
TUESDAY, APRIL 14, 2015

ANTITRUST TRADE AND PRACTICE

Expert Analysis

'Patent Assertion Entities'— Efficient Market Participants or 'Trolls'?

By Shepard Goldfein

And James Keyte

On March 17, 2015, the Federal Trade Commission approved a final order barring a Patent Assertion Entity (PAE) from using deceptive tactics when asserting patent rights.[1] While this marks the first time that the FTC has used its consumer protection authority against a PAE, the FTC has long sought to better understand PAEs—in fact, a two-year-long study on the PAE industry is slated to be completed by the end of this year.

PAEs, also referred to by many as "patent trolls," are firms that aggregate patents but do not create products based on those patents. Instead, the PAE business model involves collecting license fees and pursuing patent infringement actions against alleged infringers in order to generate revenue. For some, PAEs are an efficient way in which certain non-practicing entities (NPEs)—universities, smaller innovators and the like—can exploit and protect legitimate patent rights.[2] Others maintain that PAEs are intellectual-property extortionists that, through sham litigation, can stunt innovation and economic growth, which is contrary to the purposes of both U.S. antitrust and patent laws.

In addition to the FTC, Congress and the judiciary have responded to the growing presence of PAEs, both through lawmaking and, in some instances, recognizing antitrust claims filed against some PAEs that attempt to assert patents. While the potential anticompetitive effects of PAEs in broad terms may not be discernable until the FTC's study is released at the end of this year, there is a growing body of individual actions addressing the viability of antitrust principles to restrict the power of these entities.

The FTC Study

In 2013, the FTC proposed a Section 6(b) study that will, in the words of FTC Chairwoman Edith Ramirez, "expand the empirical picture on the costs and benefits of PAE activity." Recognizing the lack of available data on non-public PAE activity, the study, which is not aimed at enforcement, seeks to garner information about PAEs' organizational structures, the types of patents PAEs hold, how PAEs acquire patents and patent assertion activity by PAEs.[3] Broken into two parts, the first part of the study will consist of a broad analysis of the PAE business model, while the second part will present a comparative case study of how PAEs have asserted intellectual property rights in the wireless communications industry. The empirical investigation involved sending information requests to 25 PAEs with different organizational models and assertion strategies, while the focused case study involved sending information requests to 15 PAEs in the wireless communications sector.

Although the study is not slated to be released until the end of this year, enforcement and reform have not been put on hold pending the study's completion. Federal and state agencies, as well as legislators, have acted in accordance with FTC Commissioner Julie Brill's recent statements that agencies should "act expeditiously to take whatever enforcement actions are warranted to stop inappropriate PAE abuse," and that patent reform bills pending in Congress appear to be proceeding apace.[4]

SHEPARD GOLDFEIN *and* JAMES KEYTE *are partners at Skadden, Arps, Slate, Meagher & Flom.* JUSTINE HAIMI, *an associate at the firm, assisted in the preparation of this column.*

FTC Final Order

Most recently, on March 17, 2015, the FTC voted unanimously to approve a final order prohibiting MPHJ Technology Investments, LLC (MPHJ), a PAE, from using deceptive tactics when asserting patent rights. Specifically, MPHJ is barred from making false or misleading representations that a patent has been licensed in substantial numbers or at particular prices, or that a lawsuit will be initiated and that such a lawsuit is imminent.[5]

In its draft complaint, the FTC alleged that MPHJ violated FTC Act §5(a) by conducting "deceptive acts or practices in or affecting commerce." MPHJ bought patents relating to network computer scanning technology and then sent over 16,000 letters claiming patent infringement to small businesses. In the first round of these letters, MPHJ stated that many other companies opted to pay a specific license fee. Eventually, MPHJ sent letters threatening a patent infringement suit and attached a complaint, despite the fact that MPHJ was not prepared to nor intended to initiate infringement litigation.

MPHJ had attempted to bar the FTC investigation, filing a declaratory judgment suit claiming that the FTC was violating its First Amendment rights under the Noerr-Pennington doctrine.[6] But the U.S. District Court for the Western District of Texas dismissed MPHJ's suit, stating that "a determination of whether MPHJ's various letters were a 'sham' would require the Court to usurp the fact-finding responsibility of the FTC."[7] MPHJ ultimately agreed to a settlement with the FTC in November 2014.

Both the New York and Vermont Attorneys General have sued MPHJ for violations of their state antitrust statutes, focusing as well on conduct that may be named as sham litigation. While the Vermont case is ongoing, New York Attorney General Eric Schneiderman secured a "groundbreaking settlement" requiring that MPHJ make a good-faith effort to determine whether companies may actually be infringing its patents before contacting them and prohibiting MPHJ from trying to hide its identity.[8] Industry observers caution, however, that MPHJ's tactics may be too egregious for the settlement agreements to serve as guidance for future PAE enforcement.

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Antitrust Counterclaims

On the private litigation front, in *Intellectual Ventures I LLC v. Capital One Financial Corp.*[9] and *Intellectual Ventures I LLC v. Toshiba Corp.*,[10] Intellectual Ventures (IV), a PAE holding a portfolio of approximately 80,000 patents, brought patent infringement suits against Capital One and Toshiba. Both defendants brought antitrust counterclaims, which have found initial acceptance by the courts.

Having been sued for infringement of IV's financial-services-related patents, Capital One sought to amend its answer to add three antitrust counterclaims—monopolization under Sherman Act §2, attempted monopolization under §2, and unlawful asset acquisition under Clayton Act §7. To prove its §2 claims, Capital One alleged that IV controlled 100 percent of the relevant market, defined as IV's portfolio of 3,500 patents related to the financial services industry. The court for the District of Maryland agreed that IV's "inescapable" financial-services portfolio was a distinct market, because banks like Capital One have no choice but to buy a license from IV or face endless, meritless litigation.

Further, the court held that Capital One adequately alleged that IV willfully acquired monopoly power, because IV owned no patents relating to financial services until those patents were already in place and employed by the banking industry. The court differentiated between IV's ex post patent aggregation and procompetitive patent aggregation by operating companies, finding that IV's patent accumulation created portfolios that allowed IV to tax productive commercial use of existing technology. In assessing the plausibility of a Clayton Act §7 violation, the court refused to assess the effect of each individual patent acquisition, but rather looked to the cumulative effects of IV's patent acquisitions. The court stated that, although IV's "first 10, or 100, or 1,000 patent acquisitions did not violate §7….at some point, the acquisitions…created a monopoly and crossed the line to actionable under §7." Because all three antitrust counterclaims in the court's view were adequately alleged, the court granted Capital One's Motion to Amend.

In another patent assertion attempt, IV sued Toshiba for infringement of patents in its semiconductor portfolio. Like Capital One, Toshiba asserted that the relevant market for a monopolization claim was IV's portfolio of 3,700 semiconductor patents and that IV controlled a 100 percent market share. Toshiba also alleged that IV's monopoly power resulted from "careful planning and execution of an unlawful scheme" rather than a superior product, business acumen, or historic accident. Further, Toshiba's complaint stated that IV actively acquired patents to attack existing products, obfuscated its patent holdings through an extensive network of over 2,000 shell companies (while refusing to disclose the contents of its semiconductor portfolio), and relied upon the threat of repeated sham lawsuits to extract monopoly rents.

The court for the District of Delaware stayed any counterclaims involving the validity of IV's portfolio until the traditional patent claims of infringement and invalidity are decided. Yet, antitrust counterclaims based on the numerosity and value of IV's patent portfolio and its alleged improper exercise of that portfolio were not stayed. Allowing those counterclaims to proceed on a bifurcated schedule from the patent infringement case, the court stated that the issues Toshiba presented were "sound in antitrust law."

The Innovation Act

On the legislative front, the bipartisan Innovation Act, which addresses many of the issues cited by the FTC, Capital One, and Toshiba, was introduced on Feb. 5, 2015, to address abusive patent litigation.[11] If passed, the act would require, among other things, plaintiffs to disclose who owns a patent before litigation—so that PAEs cannot hide behind shell companies—and to explain in their pleadings why a suit is being brought. The act would also require courts to determine patent validity early in the litigation process and judges to award attorney fees to victims of frivolous patent lawsuits.

Passed by a vote of 325-91 in the House of Representatives last session, the Innovation Act did not clear the Senate, where a similar bill is now pending with an exemption for colleges and universities. Unlike last session's bill, the Innovation Act now contains some concessions, including a carve-out for pharmaceutical patents and a possible provision for stays pending patent review. The Innovation Act is currently in the Judiciary Subcommittee on Courts, Intellectual Property, and the Internet.

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Going Forward

While the few courts addressing PAEs appear to be taking a fairly aggressive stance under the antitrust laws, the FTC continues to pursue a methodical and fact-based approach to assess the procompetitive and potentially anticompetitive effects of the evolving PAE business model. But in some sense the train has already left the station. Thus far, state and federal investigations have successfully constrained the ability of PAEs to use deceptive tactics to coerce licenses from alleged infringers. Perhaps more interestingly, federal courts are exercising quite a bit of analytical flexibility in upholding antitrust counterclaims that are not dependent on the validity of a PAE's patents, and go at lengths to squeeze these cases into traditional monopolization or "sham litigation" frameworks.

Despite the effective use of antitrust laws in these cases, however, extrapolation to PAE regulation or general hostility from the courts at large may be too speculative at this point; both successful agency enforcements against individual PAEs and the few antitrust counterclaims that have been upheld thus far arguably have focused on particularly egregious conduct rather than more subtle strategies and contexts that are likely to emerge. But this only highlights the importance of the FTC's upcoming study, which at a minimum, should offer broader insight into the factual basis for taking any particular side in the ongoing PAE debate and facilitate future congressional lawmaking and agency regulation of the PAE industry.

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2. Chairwoman Edith Ramirez, Competition Law & Patent Assertion Entities: What Antitrust Enforcers Can Do, Computer & Communications Industry Association and American Antitrust Institute Program, Washington, D.C. (June 20, 2013); Commissioner Joshua Wright, What Role Should Antitrust Play in Regulating the Activities of Patent Assertion Entities?, Dechert Client Annual Antitrust Spring Seminar, Philadelphia, Pa. (April 17, 2013).
3. FTC Comment Request, 79 Fed. Reg. 28,715 (May 19, 2014).
4. Melissa Lipman, "Patent Troll Study Shouldn't Slow Reforms, FTC's Brill Says," LAW360 (Jan. 29, 2015), http://www.law360.com/articles/616680/patent-troll-study-shouldn-t-slow-reforms-ftc-s-brill-says.
5. MPHJ Technology Investments, LLC, Decision and Order, FTC File No. 142 3003 (March 13, 2015).
6. *E.R.R. Presidents' Conference v. Noerr Motor Freight*, 365 U.S. 127 (1961); *United Mine Workers of America v. Pennington*, 381 U.S. 657 (1965).
7. *MPHJ Technology Investments, LLC v. FTC*, No. W-14-CV-011 (W.D. Tex. Sept. 16, 2014).
8. Melissa Lipman, "Patent Troll Case May Herald More Antitrust Probes," LAW360 (Jan. 22, 2014), http://www.law360.com/articles/611945http://www.law360.com/articles/502702/patent-troll-case-may-herald-more-antitrust-probes.
9. No. PWG-14-111, 2015 WL 898146 (D. Md. March 2, 2015).
10. No. 13–453–SLR, 2015 WL 1476708 (D. Del. March 20, 2015).
11. The Innovation Act, H.R. 9, 114th Cong. (2015).