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Mr Chairman, and Members and Staff of the Subcommittee.

Thank you for this opportunity to share Newegg's experiences and perspectives on the pernicious phenomenon known as patent trolling with all of you, and with the American people. Patent trolling is unfortunately a growing and uniquely American problem that was estimated to have cost the American economy over $80B in 2011 in legal fees, settlements, lost productivity and stifled entrepreneurism, due to loopholes in the patent laws. The cost is likely substantially more today.

The vast, vast majority of proceeds from this activity does not go to inventors, a few of whom are commonly trotted out by patent trolls to justify their unproductive activities; rather, it lines the pockets of lawyers and investors looking for easy money based on exploiting deficiencies in our legal system. American businesses and consumers, who ultimately pay higher prices for products and services subjected to patent trolling, need relief from Congress, and soon.

Before proceeding further, I'd like to submit for consideration that solutions to patent trolling should not focus on the *form* of the party asserting a patent, but on the *activity* itself—**abusive patent assertion**. Any entity or individual can be a patent troll by abusively asserting patents. I believe that *any* individual or any type of entity who (1) asserts bad quality patents, or (2) asserts patents to extract premium payments because defendants need to avoid the high cost of litigation, is a troll. Patent trolls take advantage of substantive and procedural deficiencies in law to extract a tax on all of society. Everyone pays the toll of the troll, even when they are not directly paying. Parties who abusively assert patents, then, are **Abusive Patent Asserters (APAs)** and that is the term I think should be used in place of any of the euphemisms that APAs are trying to get people to use, like Non-Practicing Entity (NPE) or Patent Assertion Entity (PAE), to confuse debate and stall reform.

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I am the Chief Legal Officer for Newegg.com, an internet retailer. We are members of the Consumer Electronics Association (CEA), which represents the interests of over 2,000 members of the innovation industry in Washington and runs the Consumer Electronics Show (CES), the largest showcase for technology products in the world.

We're a common but uniquely American success story, founded by four immigrants in 2000 to sell electronics products online. We are now the second largest online only retailer, after Amazon.com, with

about $2.75B in sales in 2012, and we proudly employ almost 1,000 Americans in three, and soon to be four, states. We have always been profitable in a notoriously low margin business, and we are able to achieve profitability by keeping our costs down—I work in a cube in a warehouse, we serve Folger's coffee in our office, and everywhere I go, I fly coach. Our growth has been achieved by focusing on treating our customers like family—we take that objective very seriously. We consistently garner some of the highest customer satisfaction ratings in both online retail and in retail generally. Our founder and 90% stockholder, Fred Chang, believes that making money should and will be the natural byproduct of doing right by our customers, and that is why we rely very heavily on repeat business, and word-of-mouth referrals, to grow. We have grown every year since we were founded.

Upon joining Newegg in 2005, I was surprised to get a number of demand letters asserting that we infringed someone's patents, and demanding a license payment, because we don't really make anything. Newegg is a retailer, buying products containing IP from innovative companies, and selling them to end user customers who appreciate technology products. The demand letters were most often vague and the patents asserted against us covered common, obvious and ubiquitous functionalities used by every e-commerce web site, like the "shopping cart," drop down menus, search boxes, and the like, that could be coded for any number of ways and which were often covered by many different patents.

In one instance, a corporate patent troll sent us a demand letter claiming we infringed 6 of their patents. After being told that our outside counsel had indicated that we did not infringe on any valid patent claims in those 6 patents, the troll told us that they had thousands of patents, that we likely infringed something, and to pay up. Many, if not most of the demand letters will declare that the entity is the owner/holder of either patents or patent portfolios, without much if any analysis as to why the alleged infringer actually infringes. They will allude to the high cost of litigation and suggest that it makes sense to "resolve" the issue early by having the infringer pay money take a license. These letters may reference other companies who have taken such "licenses" to add credibility to a demand. For a small company that gets such a letter, the only practical path is to pay up, and serially. Patent trolls and their contingency fee lawyers view small companies as sheep to be sheered every couple of months. These demand letters can be crippling to a startup.

Trolls generally "only" want an amount representing "small %" of all of a target's sales or profits, despite contributing NOTHING to anyone's success. It is important to keep in mind that a "license" from a troll for a naked patent, i.e. a patent that is not used as a basis for a useful product or service offered by the troll, does not help a company or entrepreneur build or grow their business—it only confers the right to not be sued or harassed on that specific patent.

In Newegg's case, the trolls who hit us offered to settle for, initially, high six to low seven figures, to "help us" avoid the exorbitant cost of defense. Most of our co-defendants settled, sometimes for substantial amounts. Not being a seasoned patent litigator or patent attorney, I didn't know better than to ask some basic questions, and soon realized that patent trolling was a complete scam. Settling with trolls to avoid the cost and inconvenience of litigation might save a little money on the front end, but would encourage more and more lawsuits. Settling would Feed the Beast.

Newegg was and is a high revenue business that would naturally be targeted by many scam artists, including patents trolls, as a deep pocket defendant. Since our margins were and are low, however, we simply could not afford to serially cut settlement checks the way other large revenue companies with high margins could. We also couldn't spend what our competitors spent to defend ourselves. As a result, I spent a lot of time and effort on every means to lower defense costs without compromising quality and to preserve our trial option. We used boutique law firms, we pulled a lot of e-discovery review and production work in-house, we used alternative fee arrangements that rewarded defense counsel with incentives for achieving great results, and we took risk by going to trial.

I was very nervous when that first jury in one of our cases in the Eastern District of Texas came out of deliberations in our 2010 shopping cart lawsuit. The jury could have awarded the troll, Soverain Software, $34M and royalties. They didn't, and on appeal to the Federal Circuit, we invalidated all 3 patents asserted, and reversed the whole $2.5M award. In 2011, we invalidated another cornerstone patent asserted by a corporate troll, and another in 2012 owned by Kelora Systems. Despite being sued or threatened over 30 times, we have never lost a patent suit after appeal. While we are about to go to trial next week against TQP, one of many shell companies controlled by notorious patent abuser Erik Spangenberg, in Marshall, Texas, next week, trolls largely don't sue Newegg anymore. They have far too many easier victims.

Unfortunately, we are the exception instead of the rule. Other patent troll victims, especially small companies and startups, do not have the resources to fight. Most large companies settle as well because it is cheaper to do so—the typical cost of defense, without using Newegg's cost-control methods, runs between $3-5M per lawsuit. The overwhelming majority of patent troll lawsuits settle, even when asserted patents are of terrible quality or when a defendant likely does not infringe, because of the high financial cost, and logistical burdens of defense.

Although our strategy of resisting frivolous lawsuits appears to be bearing fruit, we remain committed to helping reform patent law. As a practical matter, we do so because even if we are not directly hit by trolls, we are still paying. We pay every time vendors who settle with trolls charge us more, or when technology suppliers force us to sue them to get them to stand behind the IP rights they have sold or licensed to us when a troll sues us. Strategically, for a company that has built a business as the advocate for the end user technology customer, we continue to fight because the ultimate cost of patent trolling gets passed on to end user consumers, who cannot buy as many technology products.

As a matter of principle, we stay engaged in the fight because not long ago, we were a small company and could not possibly have launched if our programmers (already working in a dark and dingy warehouse because the proverbial garage was too expensive) had to look over their shoulders and pay money every time they wrote a line of code, which is exactly what abusive patent asserters want everyone to do. Finally, we stay in the fight because it is simply the right thing to do. We view it as our corporate duty and obligation.

Patents are legal monopolies, granted under a visionary piece of legislation to spur innovation that would **benefit society**. The Patent Act was not passed to reward extortionists who have identified and

are taking advantage of loopholes in the patent laws to force honest, hardworking businesspeople and entrepreneurs, to pay premiums to avoid the cost of litigation. It was passed to **benefit society**. Those who abuse patents do not deserve windfall profits simply because our legal system disadvantages defendants in patent cases, and contains little or no recourse for those defendants and no consequence for abusive patent asserters. Not curtailing abusive patent assertion allows inequity to perpetuate and will competitively disadvantage the American economy compared to the economies of countries that are not burdened with abusive patent litigation.

Congress must step in. Common sense steps can be taken to increase the cost of abusively asserting patents, and to allow small companies and startups to innovate without fear. Provisions included in HR 3309, the Innovation Act, would be a great start.

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Thank you again for the opportunity to testify. I would be happy to answer any questions you might have, and to provide what assistance I can to the Committee's work.