

IMPROVING THE PATENT SYSTEM TO PROMOTE AMERICAN
INNOVATION AND COMPETITIVENESS

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Testimony of
Kevin T. Kramer
Vice President and Deputy General Counsel
Intellectual Property
Yahoo! Inc.

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“Improving the Patent System to Promote American Innovation and Competitiveness”
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Chairman Goodlatte, Ranking Member Conyers, and members of the Committee, thank you for convening this hearing and for inviting me to testify today about reducing the impact of abusive patent litigation on American innovation, job creation and economic growth. Thank you also for listening to so many innovators and entrepreneurs, and addressing so many of our concerns and recommendations in the excellent legislation you have put forward.

Today I will address our experience at Yahoo with patent assertion entities and some of the common sense reforms that we think would make a difference. In particular, I discuss below the proposed reforms related to clarifying when prevailing parties can be awarded attorneys’ fees, establishing presumptive limits on discovery, requiring heightened pleading, identifying the real-parties-in interest and joining them to the litigation, and limiting discovery pending claim construction in cases.

First, a little bit of background about me and about my company.

Introduction

Yahoo was one of the early pioneers of the World Wide Web and today serves more than 800 million Internet users around the world. We are a global technology company focused on making the world’s daily habits inspiring and entertaining. We provide a variety of products and services, many of them personalized, including search, content, and communications tools—all daily habits for hundreds of millions of users, on the Web and on mobile devices. The majority of our product offerings are available in more than 45 languages in 60 countries.

Yahoo is a founding member of The Internet Association, a trade group representing the fastest growing sector of the US economy—the Internet. Through The Internet Association, we have been working with fellow Internet companies to discuss abusive patent litigation and its harm to the economy with the public and local businesses. Internet companies have been disproportionately targeted by Patent Assertion Entities or “PAEs,” which many refer to as “patent trolls.” Through The Internet Association, we have built a consensus on common sense legislative solutions to eliminate the unfair burden PAEs place on our economy.

The Internet community looks to the members of this Committee and the Congress to act now on bipartisan legislation to remove this great economic burden from the Internet industry and other hard working businesses in your districts.

I came to Yahoo in 2009 to run intellectual property litigation after many years in private practice litigating patent cases. Prior to that, I litigated cases for the US Patent and Trademark Office as a trial attorney in the USPTO Solicitor's Office. I also previously worked at the World Intellectual Property Organization helping to administer the Patent Cooperation Treaty.

As a patent litigator, I understand the need for companies and individuals to assert their intellectual property rights in a responsible and respectful manner in order to protect their investments in innovation. However, I believe that the current system is being abused. I'm here today to tell you about Yahoo's experiences with Patent Assertion Entities and why Yahoo believes that changes are needed to restore balance to the system and discourage abuse.

Our Experience With Patent Litigation Abuse

First, let me make clear that Yahoo believes in patents and the patent system. We believe that patents have a positive role to play in society: they promote innovation, encourage investment, enable entrepreneurship and facilitate employment. In fact, we currently have over 1,600 issued United States patents, a substantial portion of which cover software-related inventions. We invest millions of dollars every year in research, development and innovation to advance the technology that underpins our services and the Internet. Our patents help protect that investment against the unauthorized use of our inventions by competitors. Simply put, we value our patents, participate in the system, and generally believe that the patent system works well for its intended purpose.

However, the current patent litigation system is out of balance. Growing and systematic abuse has led to increasing waste, inefficiency and unfairness. The historical trend of litigation illustrates the problem well. For example, from 1995, when Yahoo was founded, through 2006, Yahoo had between two to four defensive patent cases on its active docket at any given time. In stark contrast, since the beginning of 2007, Yahoo has had between 20 to 25 cases on its active docket at any given time. That is a tenfold increase in patent litigation.

This dramatic increase in patent litigation is not unique to Yahoo. Patents covering inventions applicable to the Internet are litigated nine times more often than other types

of patents.¹ Accordingly, the dockets of many of our peer companies in the Internet industry have dramatically risen in the last six years.

Along with the increase in numbers, Yahoo has seen a decrease in the substantive merits of the cases filed against it. A few examples help to illustrate the point. In one case, brought by a patent troll called Bright Response, the patent-in-question described ways to process incoming electronic messages, such as emails and voice messages. However, Bright Response overstretched the meaning of its patent claims and accused Yahoo's paid search advertising of infringement. Moreover, the asserted patent was based on a provisional application which explained that the claimed invention had already been in public use more than one year prior to the filing of that application. Thus, the patent, by its own admission, was invalid, yet Bright Response pursued the case all the way through trial anyway. Needless to say, Yahoo prevailed as the jury found the patent both invalid and not infringed. In another case brought by a patent troll called Eolas, Yahoo was successful in obtaining a jury verdict of invalidity of two asserted patents, only to see Eolas continue to assert those same patents against others in the Internet industry.

In yet another case, brought by a patent troll called Portal Technologies, the patent described a method for easily updating the information on a public kiosk. However, Portal overstretched the meaning of its patent claims in an attempt to cover the My Yahoo product, which offers personalized web pages for individual users and is the exact opposite of a public kiosk. Finally, in a case brought by a patent troll called API, the patent disclosed a computerized method for conducting automobile diagnostic tests, yet API overstretched the meaning of the claims in an attempt to cover Yahoo's application programming interfaces. We decided to settle both the Portal and API cases because of the expected costs of defense.

In our view, these types of cases should never have been brought in the first place. They are attempts to overstretch the scope of patent claims or knowingly assert invalid patents. As such, they are not substantially justified and impose a needless burden on the courts, our company, and our industry.

That burden is heavy. For example, every time a complaint is filed against Yahoo, it typically takes about two years to resolve and costs several million dollars. If the case actually goes to trial, it typically lasts at least another year and costs several million dollars more. All of this time and money represents lost opportunity. The time and money spent defending against abusive patent litigation could be more productively spent on jobs, on new products, equipment, or other investments.

The high cost of patent litigation means that settlement is almost always the least costly option, and the patent trolls know it. In fact, according to a study by Lex Machina,

¹ John R. Allison, Emerson H. Tiller, Samantha Zyontz, Tristan Bligh, *Patent Litigation and the Internet*, STANFORD TECH. L. REV. 3, 7 (2012).

approximately 75% of these cases settle, so the trolls know they have a virtually guaranteed payoff, for virtually no upfront investment or preparation. They have lawyers on contingency. They function without office space or overhead, and operate with very little in the way of investment or cost. As a result, they tend to be very profitable. Because they are profitable, more and more entrants are drawn into this business model, and more and more cases are being filed.

Without reform, our patent litigation docket will likely increase further over time, increasing costs and decreasing our ability to devote our time and money to more productive uses, such as jobs and investments in new products and equipment.

The PTO's Role in Reform

One idea that is typically discussed as part of the patent reform debate is the notion that improving patent quality will solve the problem. While improving patent quality is a worthy goal, it will not solve the problem, particularly for software patents and the Internet industry. The reason is that software development is an iterative, ongoing, evolutionary process that takes place on laptops, desktops, and servers around the world. And that work typically does not find its way into patents or printed publications that the examiners at the PTO can easily access. As a result, the hard-working examiners at the PTO will never have all of the art needed to comprehensively examine every software patent application.

Consistent with this reality, the law already recognizes that the PTO is not omniscient and never will be. In fact, the Patent Act provides that issued patents are entitled only to a presumption of validity and gives defendants the ability to challenge patent validity in the context of patent infringement cases.

Any attempt to cure the problem of abusive patent litigation should recognize that the PTO cannot do everything and that it should not be expected to, particularly with respect to the Internet industry.

Companies Have a Role to Play

One issue that does not get discussed as much as it should is the role that defendants play in the system, particularly large corporate defendants who are often the target of patent troll litigation. What can companies do themselves to help resolve the problem of abusive patent litigation?

Yahoo does several things to shape the landscape as best that it can. First, we defend ourselves zealously and try cases when we must. For example, we have had four trials in the Eastern District of Texas in the last five years. We have been fortunate to win

three of those cases at trial and win the other on appeal. But we cannot try all of the cases that are brought against us.

Second, we look to participate as a friend of the court in other significant cases before the United States Court of Appeals for the Federal Circuit or the United States Supreme Court. We hope that explaining our history and experience in patent troll cases will help shape the development of the law in a positive way.

Third, we act responsibly when prosecuting our own patents before the USPTO. We do not believe that every minor incremental advancement is a patentable invention because, in our experience, software engineers are highly skilled people whose very job it is to solve problems and advance the art. As a result, we have pursued fewer applications than we otherwise might have and published more papers instead.

Finally, we act responsibly when selling patents. Our policy has been to sell patents only to operating entities rather than to non-practicing entities. We do not want our patents to be obtained by a troll and irresponsibly asserted against others in the Internet industry.

But this is a slow and inefficient way to solve some of the problems with the patent litigation system. More comprehensive, common sense reforms are needed to bring balance to the system, particularly reforms that enable companies to more easily defend themselves from abusive litigation.

Common Sense Reform Is Needed

We believe that Congress is best positioned to make a meaningful difference by instituting several common sense reforms that level the playing field and bring greater transparency into patent litigation.

On this front, we are extremely encouraged by Chairman Goodlatte's bipartisan bill, which contains most, if not all, of the reforms that we have been advocating for the past year. Thank you and your colleagues for your efforts and your straightforward approach to addressing a significant problem.

In addition, we know that many members of this committee have introduced thoughtful legislation, all of which seek to remedy a real problem. Please know that we very much appreciate your attention and the effort.

We think the Innovation Act is right on track with proposals that bring more balance and transparency to the system. In particular, we would like to highlight the proposals regarding attorneys' fees to prevailing parties, establishing limits on discovery, requiring heightened pleading, transparency regarding the real-parties-in interest and joining those parties to any litigation, and limiting discovery pending claim construction.

1. Clarify When Prevailing Parties Can Recover Fees

Perhaps the most beneficial thing Congress can do to bring balance to the system is to clarify the fee-shifting provision that exists in current law. We appreciate the Innovation Act addressing this important issue.

The concept of fee-shifting is not new or radical. In fact, the Patent Act has included fee-shifting in Section 285 since 1952. The current standard for awarding fees is that the case must be “exceptional.” However, pursuant to case law, winning defendants must typically prove that a losing plaintiff’s case was both objectively baseless and brought with bad faith. As a result of this very strict two-prong standard, it is nearly impossible for winning defendants to recover their attorneys’ fees. In fact, it has been reported that winning defendants recover their fees in less than one percent of cases.²

A good illustration of how difficult it is for winning defendants to recover their fees is the case that Bright Response brought against Yahoo. In that case, the provisional application on which the patent was based admitted that the claimed invention had been in public use more than one year before the filing date of the application. Therefore, the patent was invalid. Any responsible plaintiff should have conducted its due diligence prior to filing and understood this basic defect in the patent. In our view, Bright Response’s assertion of that patent was not justified and the case should have been considered exceptional given this admission in the provisional application. Despite the fact that the jury quickly invalidated the patent on the ground of public use, the district court denied Yahoo’s request for attorneys’ fees under the strict two-prong standard that has evolved for determining whether a case is exceptional.

Because that standard is so difficult to satisfy, and because winning defendants rarely are awarded their fees, the current statute presents an insignificant restriction on troll litigation and how it is conducted. Without that threat of fees, there is no disincentive for plaintiffs to file weak cases or, worse yet, bring weak cases to trial. Congress providing clarity as to when courts should shift fees will force patent plaintiffs to act more responsibly during litigation and when contemplating whether to file suit at all.

2. Establish Presumptive Limits on Discovery

There is no dispute that discovery is a vital part of the legal process. However, discovery without limits is susceptible to abuse. Because placing sensible, presumptive limits on discovery will help level the playing field of litigation between patent trolls and corporate defendants, we support the Innovation Act’s provisions on this point.

² According to LegalMetric, a company providing statistical analyses of federal court cases, attorney fees are granted in only about 1% of all patent cases that are filed, with plaintiffs (typically the patent owners) being almost twice as likely as defendants (typically the accused infringers) to win a contested fee motion.

Our experience in patent cases may help to shed light on why presumptive limits are necessary. In a typical troll case, we are asked to provide *hundreds of thousands of pages of documents*, including emails from *anyone* with relevant information, their attachments to those emails, such as word processing documents, spreadsheets, and presentations. The processing of that electronically stored information costs money, and for typical defendants, the more information processed for discovery, the more costly given both processing fees and time for attorney review. Despite all of this cost and production, emails and their attachments do not typically describe how our products perform or why. As a result, in the four trials that we have had, relatively few emails or electronic documents get introduced as exhibits. Certainly, in my experience, *less than one percent* of the electronic documents that get produced actually get used at trial.

In contrast, in the typical case, what is needed to assess whether a Yahoo product infringes a patent claim is the source code for that product or feature at issue. In fact, in each of the three trials where our infringement was at issue (one trial only covered invalidity of the plaintiffs' patents), our source code was a central part of the case.

As a result of this experience, it makes practical sense to presumptively limit discovery in the first instance to core documents. In fact, we applaud the prior effort of the United States Court of Appeals for the Federal Circuit on this point. That court had previously issued a model order that district courts could use to help alleviate the burdens in troll litigation by placing presumptive limits on discovery.

In addition, we believe that it makes practical sense for the Judicial Conference to develop rules that will allow for additional discovery "if such party bears the reasonable costs, including reasonable attorney's fees, of the additional document discovery" as proposed in the Innovation Act. Such rules should help to encourage all parties in litigation to act more responsibly by focusing the case on those things that matter to the outcome of the litigation.

3. Require Genuine Notice Pleading

Another meaningful reform would address the insufficient complaints that are filed in patent cases, and we support the Innovation Act's provisions on this point.

Again, our experience may help to shed light on the problem. More often than not, when a complaint is filed against Yahoo, we are left guessing as to the scope of the case. Since 2007, 70 patent cases have been filed against Yahoo. A review of those complaints reveals that only 11 of these cases -- just 16% -- identified the asserted claims of the patents. Because patent claims are what is infringed, and not patents, it is insufficient to identify only the asserted patent and not the asserted claims of that patent. Furthermore, although 52 of the complaints against us identified at least one accused product, only 21 identified the accused feature within the product that was alleged to have infringed. Because asserted patents are typically much narrower in

scope than one of our products, such as Yahoo Sports, Finance or News, the relevant information is the accused feature, and that is only provided about 30% of the time. Finally, only three patent complaints against us since 2007 provided both asserted claims and accused features of products. Thus, only in about 4% of our cases do we have genuine insight at the pleading stage into what those cases are about. In the other 96% of cases, we must guess.

But guessing has its consequences. Without knowing the asserted claims and the accused features of products, it is very difficult for us to begin to defend ourselves. For example, it is difficult to identify potentially relevant witnesses in order to institute hold notices to prevent inadvertent document destruction. It is difficult to determine what the potential non-infringement arguments might be in any given case. Without knowing, we need to wait months down the road until sometime during discovery when plaintiffs are required to provide infringement contentions or expert reports in order to learn what the case is really about. Accordingly, not providing the necessary information at the beginning of a case in the complaint slows down the litigation and makes it inefficient and expensive for both parties.

There is no reason that patent plaintiffs cannot be more detailed in their complaints and identify both asserted claims and the accused features of the defendants' products at issue. Right now, Rule 11 of the Federal Rules of Civil Procedure requires plaintiffs to conduct adequate pre-filing investigations prior to filing complaints. These investigations should include a comparison of the asserted patent claims to the accused products. Given that plaintiffs typically do this work anyway, it is not a burden to require more than bare-bones pleading in a patent complaint.

In fact, complaints filed in the International Trade Commission under Section 337 are often very detailed, including the identification of asserted claims and a detailed comparison of those claims to the features of the products at issue. If complainants before the ITC can plead patent cases with particularity, there is no reason not to expect the same from plaintiffs in district court cases.

Further, we believe that filing a complaint comes with a social responsibility. When filing, plaintiffs are asking the levers of government to act on their behalf, including judges, juries, clerks, and administrative staff. Plaintiffs absolutely have the right to come to court seeking justice for their perceived injuries. However, they should be fully prepared when they do so and be fully encouraged to focus the litigation from the outset. In the patent context, this means providing more than just simple notice that they have a patent and there is a lawsuit. Rather, as proposed in the language of the Innovation Act, this means "identification of each claim" of the patent allegedly infringed, and "identification of each accused apparatus, product, feature, device, method, system, process, function, act, service, or other instrumentality ... alleged to infringe the claim."

We believe that these common sense proposals in the Innovation Act will help to streamline litigation, and therefore, they deserve our support.

4. Require Transparency of Ownership: Identification of, and Joinder of, The Real-Parties-in-Interest

In most cases, a defendant goes to court knowing who is on the other side. In stark contrast, the PAE model is such that a patent defendant often does not know, beyond the name of a shell corporation plaintiff, who has an interest in the litigation and the patent at issue. Yet this is knowledge that will inform decisions around every facet of a case, including key decisions such as when and whether to settle a case.

Again, our experience plays a role in our viewpoint on this issue. In several cases, settlement has been complicated by the “investors” or “partners” that had a financial interest in a litigation against Yahoo. This often comes to light during mediation or settlement talks when a plaintiff reveals that it cannot accept a lower offer because it would not satisfy unnamed investors in the endeavor. Transparency into the ownership stakes in a patent or in the plaintiff would help to avoid these issues and help to ensure that the parties at the bargaining table are the ones with the power and authority to settle the litigation.

Further, it is worth noting that a patent is a government grant. Like real property or any other government grant, it is reasonable to expect that the government’s records disclose who owns that right. If anything, the expectation should be greater in patent cases given the ability to enforce that right through litigation and the strict liability for infringement.

Finally, there is a fundamental fairness about transparency of ownership that should be considered. In any case, a defendant should be entitled to face their accuser. Absent transparency of ownership, and the ability to join real-parties-in interest to the litigation, a patent defendant may not have that opportunity.

For these reasons, we support the proposals in the Innovation Act to require the disclosure of those who own a financial stake in the patents in lawsuits and the plaintiffs in those lawsuits, as well as those proposals which allow courts to join interested parties such as assignees, those who have a right to enforce or sublicense, and those with a direct financial interest in the patent or patents at issue.

5. Limit Discovery Pending Claim Construction

Finally, another area where Congress can bring meaningful reform is in the staging of events in patent cases. In particular, we support the Innovation Act’s proposal to presumptively limit discovery pending claim construction.

Claim construction represents a decisive point in most patent cases. Once the court construes the claims at issue in the case, the parties have much more clarity as to the issues and the arguments to be litigated, if any. In fact, claim construction can and often is determinative of the issue of infringement. To this point, Yahoo has had numerous cases resolved either on summary judgment or through outright voluntary dismissal by the plaintiff after the district court has issued claim construction.

Given the potential impact of claim construction, it is only logical that it take place early in the case and before any unnecessary discovery is required. In fact, several of our cases have already adopted this type of a schedule, including several that had been filed in the Western District of Texas. The Innovation Act would simply encourage that this common sense approach be adopted more broadly.

Appropriately, the proposal in the Innovation Act allows the district court discretion to expand the scope of discovery when necessary upon motion by a party. Thus, the district court judges would have the flexibility to broaden the scope of discovery during the claim construction phase when the facts of the case warrant. Accordingly, we believe that the proposal in the Innovation Act presents a balanced approach.

6. Additional Comments

Our options for a less expensive alternative to litigation are limited or come attached with drastic consequences. Both Inter Partes Review and Post Grant Review apply estoppel to all issues that could have been raised before the PTO -- potentially erasing the ability to defend a district court action. We applaud the Innovation Act's inclusion of the estoppel correction to the America Invents Act.

The Innovation Act's common sense approach to some of the most vexing legal issues facing American companies represents a tremendous step forward. We look forward to working with you as this bill moves through the legislative process, particularly with respect to the standard for construing claims in PTO proceedings and expanding the scope of the PTO's Covered Business Method review program, which is limited in scope to only those patents used in the practice, administration or management of a financial product or service. We look forward to working with Congress on these issues.

Conclusion

Thank you again to the Committee for your ongoing leadership in promoting American innovation, and for your time today discussing how to reduce meritless patent litigation and restore needed balance to the system.

The bottom line is that abusive practices by patent trolls are harming our economy and the innovation ecosystem. To make the entire system work better we understand that we in the industry need to do our part, but some common sense reforms are needed to make progress in resolving the problem. Only Congress can advance these reforms.

America's intellectual property system and innovative companies need action swiftly. Without reform the problem will not stay the same; the trends show it will only get worse. More cases will be filed, and more resources will be required to defend them -- resources that would be better spent innovating new products or developing new services.

The Innovation Act would make significant strides to restore the desired balance between protecting intellectual property and discouraging abuse. It provides common sense reforms that level the playing field of patent litigation and allow for the level of transparency that both defendants and the courts deserve. We encourage its enactment into law and look forward to working with you as this bill moves through the legislative process.