

2016

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Recommended Citation

Hon. Paul R. Michel, *Judicial Litigation Reforms Make Comprehensive Patent Legislation Unnecessary as Well as Counterproductive*, 14 Nw. J. TECH. & INTELL. PROP. 131 (2016).
<https://scholarlycommons.law.northwestern.edu/njtip/vol14/iss1/6>

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10th Annual Northwestern University Journal of Technology and Intellectual Property Symposium Key Note Address

Judicial Litigation Reforms Make Comprehensive Patent Legislation Unnecessary as Well as Counterproductive

The Honorable Paul Redmond Michel

Chief Judge of the United States Court of Appeals for the Federal Circuit (2004–2010)

ABSTRACT

The patent system provides the necessary incentives for continuing investments in invention, fostering economic growth, creating new jobs and increasing America's competitiveness in the global marketplace. In fact, innovation is now our only competitive advantage. Intellectual property, particularly patents, now constitutes nearly 80% of the value of most corporations. But the innovation eco-system is under heavy stress due to five converging hurricane-force winds, all intersecting in just the last two or so years: the impact of the new reviews authorized by the America Invents Act, invalidating most challenged patents; six landmark Supreme court decisions, particularly three casting doubt over the validity of countless patents that may now be deemed ineligible to even have been considered for patentability; the Judiciary's changes last December in the Rules of Civil Procedure on pleadings and discovery; vigorous case management procedures in local patent rules and individual judge's standing Orders; and the Patent Pilot program for volunteer judges to specialize in patent cases. Although the system is struggling to adjust and recover, investment incentives, patent values, patent licensing and patent sales are all down. Can company stock values be far behind? Will growth stagnate? Nevertheless, Congress, concerned about abuses by some irresponsible patent owners known as "trolls", threatens to impose a series of new restrictions on the enforcement of all patents, no matter how clearly valid and infringed. They would make defending patent rights still more expensive, more difficult, more disruptive, slower, and less certain. If enacted, these bills would further impair an already weakened patent system, further depressing investments and "progress in science and the useful arts", which the Constitution mandates Congress to support with the patent system. Small businesses, start-ups, universities, research institutes, hospitals and individual inventors would be hardest hit. Yet, these very institutions create most new jobs and most new technologies. But their interests and those of 99% of the companies in America go largely unheard in a Congress besieged by a few dozen very large, very rich and very angry companies, mostly Silicon Valley mega IT companies, demanding relief from patent suits. How did this tragedy happen and what you can do about it is the subject of this address.

¶1 Good evening, everyone, and thank you for being here for the closing act of this dramatic day. Congratulations to the Journal for putting on a conference of extremely high quality. I was privileged to sit through a very good portion of it. I was highly impressed by the high quality of all the speakers, the selection of topics, the interchange among panelists with different perspectives and different levels of expertise. It was a great event, and it's all the more impressive that it's the tenth in a row. I hope that next year you will repeat this very fine event, and anyone who was involved will be privileged to be here as I was today.

¶2 I want to speak with you briefly tonight about a circumstance that faces us that may not be as clear in our vision as perhaps it needs to be. It's my thesis that the country, our country, is today at a crossroads, and that the patent system is imperiled. It's been said that we are now an innovation nation. Indeed, you could say that practically from the founding we were an innovation nation. After all, we started as a very poor, very backward, totally agrarian economy, overshadowed by the great powers of Europe, and, over the ensuing decades and centuries, we became the most highly industrialized, most wealthy, and the most technologically advanced civilization on the planet. So, I don't shrink from the description that others give to this country as being the innovation nation. In fact, it is not only highly industrialized and advanced technologically, but it has become more dependent than ever on intellectual property as the driver.

¶3 When I was born, the vast majority of the assets of nearly every American company were physical, tangible, real property: inventory, raw materials, factories, and so forth. Today, for most companies, the vast majority of their assets are intangible, mostly intellectual property, and most of that is patent portfolios. It has been documented that there are 40 million American workers who are employed by IT - pardon me - IP intensive companies and industries. If we look at the global perspective, our key to being competitive globally with all of our rivals and trading partners is our technological leadership. So, IP has become for our country the key to economic growth, global competitiveness, job creation.

¶4 So, what's the problem? Well, the problem is that there's been so much change in the last 15 months, just a little over a year, 15 months, that the system, the patent system, is in a hurricane wind, and it's not clear whether it's going to survive or not. Already patent portfolio values are falling, and they may fall much farther because of some of these changes, and I'll give a few examples in just a moment. Now, if portfolio values fall and they're the majority of the assets of most companies, what might happen to the stock value of those companies? What might happen to their employees? Are we at risk of an endless recession because of the collapse of IP values that may occur?

¶5 So, some of the changes, of course, are very well known to all of you, but maybe a few are not so well known. First and foremost, the America Invents Act, passed in 2011 and partly effective in 2012, fully effective in March of 2013, but only now beginning to be fully felt as the post-grant review proceedings on validity are being decided by the patent office in a cycle that takes about 18 months. So, there's a lag of almost two years. So, that's why only now, in 2014 and early 2015, we are beginning to see the full impact. And it's very dramatic. They expected that they might have 400 a year, and they're now being filed at four times that rate. There are nearly 3000 such proceedings pending today.

¶6 So, that's part of it, but those numbers are the least dramatic. The institution rate of requested post-grant reviews, inter-party reviews and covered business method patent

reviews - so I'll just say IPRs for inter-party reviews - the institution rate is upwards of 80 percent, and the invalidation rate is also about 80 percent. And, in fact, in over 90 percent of the cases at least some of the claims were invalidated, even if others survived. So, it's a very potent, very robust way to challenge validity, and much faster and cheaper than district court. That's very good. But, the main point is that the impact is huge, and its full measure has yet to be taken. So, that's the first big change of recent months.

¶7 Secondly, the Supreme Court, in just its last term, the term that ended in June of 2014, decided six major patent cases, the most in any Supreme Court term since the 1870s. You know the cases: *Alice*, *Octane*, *Highmark*, *Nautilus*, *Akamai*, and the rest. Very important cases. The full impact, again, not completely clear, but major impact for sure. Beyond that, the judiciary itself has been in a state of great flux.

¶8 The Judicial Conference of the United States, the governing body of the federal judiciary, has made major changes. The infamous patent complaint "form 18" is being abolished, and that means that the rigors of the Supreme Court's decision in *Twombly* will now kick in and govern every patent complaint being filed. Discovery rules are being changed in a very major way, which should be good to save money, and time, and disruption of companies. But, again, the important thing is not whether we think the changes are ideal or whatever, but they're big. And they all intersect with other changes.

¶9 So, the Supreme Court cases are the second source of change. The Judicial Conference: third source of change. With us tonight is former Chief Judge James Holderman from the Northern District of Illinois. He is famous for many things, but one of which is that his district pioneered having what we informally call "local patent rules" to guide, and manage, and constrain excesses in patent litigation, and, on top of that, he's been the lead steer in the patent pilot program with national influence over the techniques used by district judges all over the country in the 94 districts to try to more fairly, more efficiently, more accurately handle patent infringement and related cases. That's another big change, and, again, still in progress, the full impact not yet seen.

¶10 The fifth source of major change is the district courts themselves in these 94 districts. Some twenty-five have local patent rules, as the Northern District of Illinois does. And in many other districts, even though they don't have district-wide rules, individual judges have extremely elaborate, detailed scheduling orders and general orders that guide, and constrain, and structure the forward-progress in patent infringement cases. These are all major reforms. Revolutionary, if you go back five or ten years. So, a lot has been happening at the district court.

¶11 So, that's where we are right now. So, what's next? Well, Congress is poised to do a second round of major patent reform legislation. H.R.9 is a bill that is likely to pass the House shortly, and then go over to the Senate. It has many interesting provisions in it. They're ostensibly aimed at curbing abuses by so-called patent trolls, but they apply to all cases, to all defendants, all technologies, all industries. And they have an important potential impact.

¶12 There's presumptive fee shifting to whichever side loses, not based on the case being frivolous, just based on being unsuccessful. A great many patent cases are very close. You can't even predict who's going to win. But whoever loses could be on the hook for not only 3 to 10 million dollars of their own costs and lawyers' fees, but the same amount for the other side's costs and lawyers' fees. There's a great potential, I think, that that may

deter many people with valid patents that are actually being infringed from feeling that they can afford to get justice in the United States because of that potential impact.

¶13 The bill also requires very detailed fact pleading that would make Charles Dickens turn in his grave. Complaints will have to be hundreds of pages long, have thousands of facts in them, and, if any fact is left out, the complaint is dismissible. So, then what happens? Well, if it's dismissed with prejudice, the patent owner's out of luck permanently. If it's dismissed without prejudice, probably more likely, then they'll be a revised complaint filed and we'll start all over again. So, a lot of wheel spinning, perhaps. But, in any event, a significant development.

¶14 There also are provisions in the Goodlatte bill, H.R.9, to delay discovery, an attempt to save costs, but it also adds delay. Delay is already a huge problem in patent cases, very often 5 to 10 years to get a final outcome in a patent infringement case. So, this will add cost and delay, as will the other provisions. And there are major provisions also to stay patent cases with regard to certain accused infringers, so-called "customer stays", but the way it's drawn it applies to lots of people other than end-users or final customers. So, very major provisions.

¶15 In my view, and I don't necessarily suggest it's the only view or even the best view, but in my view, the general drift of these provisions would be to hurt the chances of almost all patent owners and to help almost all accused infringers. It would tend to benefit very rich parties and disadvantage parties who are not very rich, whatever the nature of the case may be. It would be particularly hard on a set of players in the overall complex patent system: small businesses, middle size businesses, emerging companies, start-ups, universities, research institutes, and individual inventors. And, ironically, those very institutions create more net new jobs than the big companies do, but they're the ones who would get hurt by H.R.9 the way I access it.

¶16 So, who benefits? Very rich companies, very big companies, particularly the giant IT companies in Silicon Valley, about a dozen major companies. We all know them. We buy their products. They're great products. I'm a customer myself. I am not denigrating these companies. But, they have a very specific economic interest and great, great power. And their power in Washington has escalated vastly in the last several years.

¶17 Some other industries are quite important here. Biopharma and manufacturing sector companies, I think, would be very much hurt by this bill. So, ironically, it favors the companies that mainly outsource jobs from the US, and it hurts the manufacturing companies that make things here in the United States and employ fellow citizens.

¶18 So, there are a lot of controversies about this. I'm not here to condemn the bill or try to make converts, but really just to point things out so that you can think and perhaps act. Our diplomatic corps, headed by our trade representative, has been hard at work for many years to try to get certain foreign countries to respect IP rights, particularly IP rights of American firms. So, we are pressing hard with China, India, Brazil, Russia, and many other countries to have them strengthen their IP rights, but meanwhile we're weakening our IP rights here. So, they say to our diplomats, "Hey, why should we strengthen our IP regime when you're weakening yours? You're hypocritical." This is not credible. So, we've made the job of those officials more difficult already and the H.R.9 would make them vastly more difficult still.

¶19 One of the other things the bill does, which I consider at least highly questionable, if not absolutely horrible, is to severely limit the discretion of federal judges. The

management of individual lawsuits, individual infringement cases, is inherently a judicial function. It really only can be done by the judge in the room, people like Judge Holderman, here with us tonight. But Congress has been importuned by powerful special interests, who have spent astounding amounts of money, to greatly restrict the discretion of federal judges – on stays, on fee shifting, on the management of cases in many respects. I think it's highly questionable and probably will be quite counterproductive.

¶20 But the biggest problems with patent litigation – and I mentioned how expensive they are, how many the delays are, how unpredictable they are, how disruptive they are – are other qualities with which you may be familiar. What will the impact of H.R.9 be? It will make every single one of those ills much worse – much more expensive, much slower, much more disruptive, much more unpredictable. Is that really a good direction as a matter of national economic policy or patent policy for us to move in? Why is all this happening? Well, it's been happening because there's been a massive campaign by a very small number of self-interested companies to sell a narrative that most patents are invalid, most patent owners are irresponsible parties – trolls is the term of choice – most lawsuits are frivolous, and most defendants are victims of an extortionate scheme.

¶21 Now there are, of course, abuses in lawsuits. There are frivolous lawsuits filed in every area of law, including in patent infringement cases. So, it's not like there's no problem. The question is what's the size of the problem, what's the nature of the problem, and what are logical and tailored fixes for those problems. My impression from 22 years on the Federal Circuit was that the incidence of frivolous lawsuits, at least the ones I saw, was well under one percent. So, it's a 1 percent problem; 99 percent not a problem. But, of course, I only saw suits that got appealed. So, lots of suits get settled. About 90 percent of the suits filed – 3 to 6 thousand a year – get settled. So, maybe the incidence of frivolous suits in that larger universe is higher. But I doubt it's higher than five percent. Outside, maybe 10 percent. So, it's a 10 percent problem, give or take. So, that means it's 90 percent not a problem. But the legislators in Congress have been persuaded by massive lobbying, massive PR campaigns that it's the norm.

¶22 So, we're in a situation where the Congress has been stampeded by careful lobbying, and campaign contributions, and fundraisers, and bundlers, and massive work by hired PR firms, law firms, lobby firms, and so forth to accept a certain narrative that is a threat to the health of the patent system. But, that's in any event, where we are. You should be comforted by this: many of you will go on to become, and some already are, patent lawyers, IP lawyers, and you'll have lots to do when you get out, and, if this bill passes, you'll have even more to do. There's a saying in Washington that every time Congress passes a new law, it always benefits lawyers and accountants. It may be awful for business people or taxpayers, but it's always good for lawyers and accountants. I'm afraid there's all too much truth in that statement.

¶23 So, then the question is, well, can we do better? Can we have more rational policy-making, can we have it be fact-based, be analytical, be based on reliable statistics, on hard facts and numbers. Well, sure, we could. Those things exist. A lot of the scholars that we heard from today are experts in these areas. Many of you are experts, as well. The larger patent community has all the expertise. So, if policy-makers would listen, they could do a much better job than they seem to be inclined to do right now.

¶24 I spent nine years earlier in life as a staffer in the Senate. This was in the seventies and the eighties, and it is now a totally different place. It is awash in money, it is cynical

beyond belief, it is bitterly partisan, it is highly irrational. It is a very sick institution, I'm sorry to say, as a fellow citizen. You know you can't say these things when you're a federal judge. So, I resigned my lifetime commission, a job I loved and thought I would never leave, because it was the only way I could get back my First Amendment rights. So, I plan on exercising them, including tonight.

¶25 So, what about the Supreme Court? What about the Patent Trial and Appeal Board? The Patent Trial and Appeal Board is this new animal created by the America Invents Act, and it's a very potent tribunal. I think it's now the single most important patent tribunal on earth - more important than the Supreme Court, more important than the Federal Circuit, even more important - Sorry, Jim - than district courts - because almost every case is going to go there first. It's the way station before you can get justice in the district court, it's looking like more and more. Not always, not 100 percent, but a very high rate of granting stays until there's a final result. And it's more efficient. If the patent's going to disappear, why should the overburdened district court spend time and agony struggling with this. So, it's not irrational to stay these cases, but it's important in its impact. Why? Because it adds even more delay, adds even more cost. So, that has impacts on the overall system.

¶26 So, the Patent Trial and Appeal Board: big new player. And the Supreme Court has become a very major player, particularly as regard to patent eligibility. We had a very good panel here today on that. I won't go into the details of that. I will only say that the Supreme Court has now become a major policy-maker in the patent world on a level that was unimaginable to me until the *Mayo* decision just a couple of years ago. And the *Alice* decision basically doubled-down on *Mayo*, so now eligibility is a huge question. There are probably hundreds of thousands of patents that now have a huge cloud over their validity because of the uncertainty. They're not definitely invalid, but they might well be invalid, and no one can tell for sure.

¶27 So, what do you do if you're a business owner? What do you do if you're an investor? What do you do if you play some other role in this large, complex system? Not only is the Supreme Court making broad policy, but it's doing so, as far as I can see, based on guesses and based on assumptions. So, for example, in the *Mayo* case - Justice Breyer writes for a unanimous court that, Section 103 can't do the job. Section 101 is "better established", he said. We need to depend on it, not Section 103, 112, 102, the other key provisions of the patent code. Pure guess. He also says that, if we don't constrain eligibility, patents will deter more innovation than they're promoting. Pure assumption. I don't know of any evidence that in any way really supports that view. It might be true. I doubt it, but it might be true. But he had no basis for saying that. He just said it because he's on the Supreme Court, eight justices agreed with him. It's the law of the land; we have to live with it. But it's not so constructive in my opinion.

¶28 Consider this problem. The phrase that's used in the *Alice* case, and the predecessor *Mayo* case, *Bilski* and *Myriad* are also important, of course, but we don't need to make it more complicated, let's just stick with *Mayo* and then *Alice* applying it in all technologies. So, they talk about abstract ideas. How do you define an abstract idea? How abstract is too abstract? This, as far as I can tell, is totally subjective. So, how can you have consistency? Think of the people who have to implement that standard, of what's too abstract? Or some of the other things - what adds "significantly more"? Another magic phrase. What limitations add significantly more to a claim that has in it one of these implied exceptions that the Supreme Court has pulled out of nowhere. It's not in the Patent Act,

the four categories. Nothing in there by way of exceptions. Certainly nothing in there about abstract ideas, laws of nature, natural phenomena, etc. They just made it up.

¶29 Now, maybe it's good policy. I doubt it, but maybe it's good policy. But it's made up, and it's not administrable. Think of who has to implement these vague, subjective, indeterminate standards. 8,300 engineers and scientists, mostly very young, who are the patent examiners in the patent and trademark office; 650 federal trial judges; 16 Federal Circuit judges; tens of thousands of private attorneys and business decision makers. With so little predictability and such subjective standards, it's all in the eye of the beholder. How can anybody make any prediction? How can anybody administer this regime in a way that's consistent? I think the results will be wildly inconsistent, from examiner to examiner, judge to judge, appellate judge to appellate judge. So, I think we have chaos. Maybe it can get fixed. Not so clear how - how we got there I won't go into, but it was a very tortured course. So, Alice double-downed on *Mayo*, *Mayo* revived *Flook*, which had been overruled by *Dier*. So, the logic of this is a little bit hard for me to follow, but maybe I'm just not up to Supreme Court standards of figuring things out.

¶30 In any event, in my new life I spend a lot of time talking to business people and union leaders, investment people, money managers, and so forth. You know what they all say? Just give me certainty. I can live with a bad rule. I can live with a horrible rule. I can live with a good rule. But I can't live with - because I can't plan, I can't make rational decisions - with this massive uncertainty. So, in eligibility, we have massive uncertainty. In fee shifting, we have massive uncertainty. And so on in some of these other areas, too. So, I'm not sure we're moving in a good direction if we enact this H.R.9, or what some people refer to as the Goodlatte bill.

¶31 Well, is there any hope in sight? Yes, you are all experts in some degree or fashion or another. In the United States Senate, there is one expert. Only one. It happens that a new junior Democratic Senator from the state of Delaware used to be, in his former life, a chief patent counsel at the famous DuPont chemical company. He actually understands the patent system. He is the only one in the entire Congress who understands it. Well, he recently sponsored a bill, co-sponsored quite proudly by Senator Durbin from this fine state, and I must say Senator Durbin wasn't a chief patent counsel at any major industrial company the way Senator Coons was, but Senator Durbin has done his homework. Maybe he talked to Judge Holderman. I don't know. Senator Durbin has learned the patent system, and he's a co-sponsor of this bill.

¶32 Now, I'm not here to sell the bill. I'm not their PR guy. But I think it's a very useful counterpart to the very anti-patent bill sponsored by Congressman Goodlatte or Chairman Goodlatte. And I've studied the bill. I think there are a lot of things in it that are quite good. I'm not going to try to sell it tonight, but it has the virtue of trying to focus in a very laser-like way on the actual problem - the abusive lawsuits that do exist, the bad conduct during the course of lawsuits that does happen, whether it's 2 percent, 10 percent, who knows what. Whatever it is, it's not good. It needs to be curtailed. This bill pinpoints by behavior, not the status of the party, what the countermeasure is. It seems to me that's on the right track. I hope it will be taken seriously. And I hope that some serious debate will arise within the Senate. It's probably hopeless within the House at this point. They'll overwhelmingly again pass the Goodlatte bill. I think that's pretty much a foregone conclusion. It doesn't have to be, it shouldn't be, but it probably will be. So, the hope of a more rational process and perhaps a better outcome lies primarily in the Senate.

¶33 So, what does this all have to do with you? Actually, it has everything to do with you. And here's why: the entire stampede to greatly weaken patent rights in the United States has been promulgated by fewer than 30 companies. Most of them are in Silicon Valley. A couple Wall Street banks, one company in Texas, one company in Idaho, but just about everyone else is in a small section of California that we refer to as Silicon Valley. So, 30 companies, give or take a few. In the United States today, we have over 200,000 commercial corporations. If we exclude the little ones and we only talk about the ones that have at least 100 employees, there are 30,000. So, we have 30 out of 30,000 stampeding to Congress to get what will serve their bottom line at the expense of the other – you can do the math – 29,970. That seems a little bit disproportionate. That seems a little out of kilter, at least to me.

¶34 So, again, come back to the question. What does that have to do with you? Well, what it has to do with you is, you're part of a university and I'm happy to report, if you don't already know it, that your university president, of the whole university, not just the law school, signed a letter with other big ten university presidents saying to Congress, "Wait a minute. Don't wreck the patent system. Yes, deal with abuses, but in the process, don't wreck it for everybody else." Seemed like a good step.

¶35 Everybody who cares about having an effective, successful, fair, non-abusive patent system should raise their voice because Congress will listen if the silent 99 percent stops being silent. You could write a one-sentence letter to Congress – all of them, the ones on the judiciary committee, your local Senators or House members, any way you want to do it. It doesn't have to be a law review article. It just has to be a statement of caution, a statement of interest, a statement of concern. Those of you who are connected to companies or law firms, you can work through those entities. Those of you who are merely individual citizens, like I am now – a private citizen. I was misdescribed today as a public citizen. I will accept the idea that I am a public scold and a public nuisance, but I'm not sure I'm a public citizen. I think I'm a private citizen. But, anyway, that's just terminology.

¶36 So, we have this odd circumstance in this country where a very tiny number of individual people and corporations with enormous resources so dominate the politics, and not just the politics on Capitol Hill, but what's written in the major media is highly dominated by major money interests of a very small number of players. So, my friends in Silicon Valley – Google, Cisco, the rest, you know all of the suspects – they have spent untold sums in a 10-year campaign, not only to lobby Congress, which they're entitled to do. It's in the Constitution, we should all do it – petition the government for redress of grievances, they have every right to do it, they should do it. If I were they, I would do it, too. But, if the rest of us are silent, there's no balance, there's no counter-story, there's no correction of false or inflated or exaggerated statements. So, that's why it's so important for the rest of us to speak up.

¶37 Now, you didn't come here to get an assignment – I'm not your professor – but I do think anybody who has any knowledge or concern about the intellectual property regimes, particularly the patent system in this country, needs to be concerned. It's hard enough to get it right if you have all the facts on the table and you act logically and rationally and analytically. If you act only from PR and big money, you're almost sure to get it wrong. That's the problem in Congress today. So, I'm hoping that all of you will decide to become soldiers in the army to try to have rational, healthy, job-promoting patent policy in the United States. Thank you very much.