

Prepared Statement of Philip S. Johnson,  
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On Behalf of the  
Coalition for 21<sup>st</sup> Century Patent Reform

Before the

United States Senate  
Committee on the Judiciary

On

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and Recent Court Decisions”

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**Executive Summary**  
**Statement of Philip S. Johnson,**  
**Chief Intellectual Property Counsel,**  
**Johnson & Johnson**

The primary focus of patent reform should be job growth. Congress should change our patent laws to ensure that meritorious inventions are uniformly accorded patent protection. The resulting patents should be promptly and reliably enforceable against infringers, and result in damages awards that fairly compensate for the unauthorized uses made of the patented inventions. Because the R&D investments made in reliance on the patents dwarf the costs associated with their filing, maintenance and enforcement, the principal objective of patent reform should not be on saving administrative costs, but on changes that will stimulate R&D investment. Collectively, these changes will stimulate job growth.

S. 515 is an excellent first step towards achieving these goals. The 21st Century Coalition **supports**, subject to certain technical amendments, the provisions in S. 515 that would: adopt the first-inventor-to-file principle (Section 2); expand the grounds for *inter partes* reexamination to include statements of the patent owner in prior proceedings – but not challenges on the basis of prior use and sale (Section 5); expand the opportunity for the public to submit publications to the USPTO (Section 7); and, permit interlocutory appeals – but only from denied, dispositive summary judgment motions where not duplicative of earlier appeals (Section 8); and permit the Director to set fees if accompanied by statutory protection limiting their use to the USPTO (Section 9).

The Coalition **opposes** the provisions relating to willful infringement as unnecessarily retarding, and perhaps disrupting, the orderly case law development of the objective recklessness standard as contemplated by *In re Seagate* (Section 4), and the provisions relating to venue as unnecessary in view of recent judicial developments facilitating the transfer of cases to districts with substantial contacts with the cause of action and as unfair to patent owners (Section 8).

As to reasonable royalty patent damages, the 21<sup>st</sup> Century Coalition believes that the case for remedial legislation has not been made. The sizes of patent damages awards have been relatively stable for many years, and typically barely cover the costs of litigation. At the very least, the Coalition believes it would be best to await the anticipated decision in *Lucent v. Gateway*, and/or the outcome of the study proposed in Section 18 of H.R. 1260, before considering such changes to our patent laws.

As Chairman Leahy has suggested, one promising future approach may be to enact appropriate “gate keeper” language. Any approach to reasonable royalty damages that would redefine the invention to be less than that to which the inventor has proven he/she is entitled, such as an “essential elements” approach, would amount to just another version of “prior art subtraction,” and would be grossly unfair to inventors.

## **Prepared Statement of Philip S. Johnson**

Mr. Chairman and distinguished Members of the Committee: I thank you for the opportunity to testify on various aspects of patent law reform, and recent court decisions that may affect the advisability of enacting certain provisions contained in S. 515. Although I am active in a number of professional organizations with interests in patent law reform, including Advamed, the American Intellectual Property Law Association, PhRMA, BIO and the Intellectual Property Owners Association, I am appearing today in my capacity as Chief Intellectual Property Counsel of Johnson & Johnson, and as a representative for the Coalition for 21<sup>st</sup> Century Patent Reform ( the “21<sup>st</sup> Century Coalition”).

### **I. Personal/Corporate/Coalition Introduction**

By way of introduction, I am a registered patent attorney with 35 years of experience in all aspects of patent law. In addition to drafting and prosecuting patent applications, I have tried patent cases to both judges and juries, and have advised a wide variety of clients in many industries ranging from semi-conductor fabrication to biotechnology. Over the course of my career, I have represented individual inventors, universities, start-ups, and companies of all sizes. In January of 2000, I left private practice to join Johnson & Johnson as its Chief Patent Counsel.

Johnson & Johnson is a family of more than 200 companies, and is the largest broad-based manufacturer of health and personal care products in the world. Collectively, Johnson & Johnson companies represent this country’s largest medical device business, its third largest biotechnology business, its fourth largest pharmaceutical business, and very substantial consumer, nutritional, and personal care businesses. Johnson & Johnson companies employ approximately 118,000 people. Johnson & Johnson’s companies are research-based businesses that rely heavily on the U.S. patent system and its counterpart systems around the world.

The 21st Century Coalition is a broad and diverse group of nearly 50 corporations including 3M, Caterpillar Inc., Eli Lilly, General Electric, Procter & Gamble and Johnson & Johnson. For more than 100 years, our Coalition’s companies have played a critical role in fostering innovation. We invest billions of dollars annually on research and development to create American jobs and improve lives. Representing 18 different industry sectors including manufacturing, information technology, consumer products, energy, financial services, medical device, pharmaceutical, and bio-technology, our Coalition advocates for patent reforms that will foster investment in innovation and job creation.

As the manufacturers and marketers of thousands of products, the freedom to make and sell products in view of the patents of others is always a concern to our Coalition’s members. They therefore routinely review thousands of patents during their product development processes, make appropriate design changes to avoid the patents of others and/or obtain appropriate licenses or legal opinions prior to launching their products. Our member companies also become involved in patent litigation. Most of these litigations involve competitors or would-be competitors, although some involve

non-manufacturing patentees. Johnson & Johnson's companies, for example, find themselves to be defendants about as often as plaintiffs.

The 21<sup>st</sup> Century Coalition's interest in patent law reform is to insure that the patent system fairly rewards those who contribute to our society through the invention and development of new and useful products and processes. A fair, efficient and reliable patent system will continue to stimulate the investment in innovation that is necessary in today's technologically complex world to create the new products and processes that will lead to better lives for Americans and the rest of the world. In addition, the best promise for preserving and enhancing our place in an increasingly competitive global marketplace will be to stimulate U.S. investment in research-based industries.

## **II. The Primary Focus of Patent Reform Should Be Job Creation**

As Chairman Leahy correctly recognized upon the introduction of S. 515,

Patent reform is ultimately about economic development. It is about jobs, it is about innovation, and it is about consumers. All benefit under a system that reduces unnecessary costs, removes inefficiencies, and holds true to the vision of our Founders that Congress should establish a national policy that promotes the progress of science and the useful arts.

The Chairman's focus is the correct one. Patent reform should focus principally on stimulating the private sector to invest in economic development and job growth. All other considerations should be secondary

Johnson & Johnson's companies are good examples of the relationship of the patent system, and patents, to jobs and job growth. Johnson & Johnson conservatively estimates that 60,000 of its full time jobs depend on the patent portfolios of its companies' 8,000+ U.S. patents (and their foreign counterparts). **Stated differently, we estimate that, on average, each U.S. patent results in, preserves and protects the jobs of, 7.5 employees per year, or, over its 20-year life, 150 job-years.** This estimate does not take into account the jobs of countless others at suppliers, distributors and retailers involved in the research, manufacture, distribution and sale of our products that indirectly depend in whole or in part on our patent rights.

Over the past three years, Johnson & Johnson companies' patent filings have averaged about 1,200 original applications each year. During that time, our companies have been awarded approximately 500 U.S. patents per year by the United States Patent and Trademark Office ("USPTO"). This 42% rate is very close to the current USPTO allowance rate, which is down from over 70% just a few years ago. During these same years, Johnson & Johnson companies have invested \$22.4 billion in R&D, averaging about \$7.5 billion per year, or \$6.2 million in R&D for each patent application filed, and \$15 million for each patent granted. Needless to say, these research and development expenditures have resulted in the direct employment of thousands of people throughout the United States in very good jobs with excellent benefits.

As these numbers reflect, the R&D investments stimulated by the patent system dwarf the costs directly associated with the filing, maintenance and enforcement of patents. Accordingly, in considering changes to the patent system, the primary concern should not only be on the costs of filing or enforcing patents, but on what effect changes to the system might have on R&D investment, and thus jobs and job growth.

As explained below, Johnson & Johnson believes that appropriate patent reforms will maintain current jobs and create new jobs by continuing to encourage private sector R&D investment. Proposed changes that increase the likelihood that meritorious inventions will receive patent protection, and that resulting patents may be reliably enforced against infringers to promptly recover fair compensation should be favored, as these changes will have the greatest impact on stimulating R&D investment and job growth.

### **A. The Causal Relationship Between Patent Protection and R&D Investment**

Johnson & Johnson companies are rational decision makers when it comes to deciding whether and how much to invest in R&D. When deciding whether or not to make, or to continue making, an investment in any given project, many factors are taken into account, including the cost of the project, the technical risk and likelihood of success of the project, the expected cost saving or product enhancement to be achieved, and the expected return on investment. In determining the expected return on investment, a critical element is the likelihood that meaningful patent protection will be accorded to deserving inventions resulting from the project, the degree and duration of exclusivity that resulting products or processes will enjoy, and the likelihood that the involved patents will either be respected by competitors, or promptly and successfully enforced in the event of infringement. When such projections indicate that the return on investment exceeds a threshold commensurate with the risk involved, the investment is, or continues to be, made. When it does not, the project is not begun, or is cancelled.

Johnson & Johnson's companies, and many other manufacturing companies like it, are now finding that the current economic crisis is reducing the likelihood that reasonable returns on investment can be achieved for many of their ongoing R&D projects. For that reason, our companies, and many others like us, have made the painful decision to lay off thousands of employees involved in R&D and other product-related areas.

Simply put, rational business people cannot justify investing in R&D unless the size of the "carrot" and the likelihood of getting the carrot justify the cost of trying to get the carrot. Unfortunately, since the economic crisis is shrinking the size of the carrot, so too are the amounts being spent to get the carrot.

The patent system has a direct effect on both the size of the carrot and the likelihood of getting the carrot. Changes in the patent system that will increase the size of the carrot and/or the likelihood of getting the carrot will cause business planners to invest more in R&D, while those that result in decreases will have the opposite result.

## **B. How S. 515 May Impact Jobs**

Whether the net effect of S. 515 will be to stimulate or retard job growth will depend largely upon its evolution as it is considered by Congress and enacted into law. The current provisions of S. 515 supported by the 21<sup>st</sup> Century Coalition will either be neutral to, or tend to stimulate job growth. With further work, the remaining provisions may be drafted to do the same. Accordingly, there is an historic opportunity for S. 515 to enhance the value of patents and stimulate investment to produce immediate and long lasting job growth.

Coalition members view our current economic conditions as analogous to the economic malaise of the 1970's. Begun as Carter administration initiatives, in the early 1980's Congress passed several bipartisan bills to enhance the value and enforceability of patents, including the Bayh-Dole Act<sup>1</sup> and the Federal Courts Improvement Act of 1982, creating the Court of Appeals for the Federal Circuit.<sup>2</sup> The reaction of the private sector was immediate and dramatic – investment in R&D substantially increased, and a sustained period of prosperity followed. In the Coalition's view, the 111<sup>th</sup> Congress now has a similar opportunity....and its timing couldn't be better.

As in the 1980's, the focus of S. 515 should be on making changes that will encourage R&D investment. Were they able to justify to themselves, and to their investors, that such additional expenditures would make sound business sense, the 21<sup>st</sup> Century's companies have both the wherewithal and the desire to hire back thousands of laid off workers, and many more. To do this in this economic environment, however, will require legislation that will ensure these companies that deserving inventions stemming from their R&D expenditures will receive prompt, high quality examination by the USPTO, and that the patents that the USPTO issues will provide a firm foundation on which to build a growing business. Just as no one would build a house on land whose title could be challenged over and over again, businesses need to be able to count on an extended period of quiet title to their patents if they are to make the kinds of investments in them on which future growth is to be founded.

Many of the provisions already contained in S. 515, such as those relating to the adoption of a first-inventor-to-file system and improved patent examination procedures, should prove to be beneficial to long-term investment and job growth. As Chairman Leahy and Senator Hatch appropriately recognized in their introductory statements, additional work remains to be done on a number of other important issues, particularly reasonable royalty damages. The 21<sup>st</sup> Century Coalition is confident that many of these provisions can be improved so that enactment of S. 515 will drive job creation by improving the reliability of achieving the patent reward, and by preserving its value.

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<sup>1</sup> University and Small Business Patent Procedures Act, Pub. L. No. 96-517 (1980)

<sup>2</sup> P.L. 97-164 §165, 96 Stat. 50 (1982)

### **III. Improving the United States Patent and Trademark Office**

The first priority of patent reform should be to improve the completeness of patent examination and the quality of patents that issue. These reforms focus on properly financing the Patent and Trademark Office, simplifying the patentability standards and their application, and expanding public input in the decision to grant a patent. They have garnered broad support from stakeholders and represent an achievable core of needed reforms to improve the operation of the USPTO. While these reforms may not immediately create jobs, they hold directly address the twin problems of an unacceptably large backlog of pending applications and the public's perception that some patents granted by the USPTO are of low quality. Improvements in patent quality should also improve the reliability of patent protection and the downstream efficiency of enforcement proceedings.

#### **A. Improvements to Guarantee the USPTO Financial Resources**

Additional improvements that should be considered for inclusion in S. 515 are those that provide additional financial resources to the USPTO. For example, the adoption of two linked proposals contained in Sections 9 and 15 of S. 1145 as reported by this Committee in the 110<sup>th</sup> Congress could significantly improve USPTO. Section 9, continued in Section 9 of S. 515, would give the USPTO the authority to set its fees by regulation, tailoring the fees to better reflect the extent of the effort needed to thoroughly examine patent applications. The necessary corollary, missing from S. 515, is the creation of a revolving fund from which the USPTO could finance its operations. Such a fund would assure that the USPTO could use the fees that it collects to fund the work for which those fees were paid, and it would allow the USPTO to engage in strategic planning over the course of multiple fiscal years secure in the knowledge that it had a predictable source of funding.

Many of the quality and pendency problems confronting the USPTO, and the subsequent litigation that the grant of questionable patents can generate, can be directly traced to the diversion of USPTO fee revenues from 1992 through 2004 to fund other, unrelated government operations. Cumulatively, this diversion resulted in a loss of more than \$750 million in fees paid by patent and trademark applicants for the processing of their applications. As a result, the USPTO was unable to hire the examiners it needed for a decade and has therefore had enormous difficulty hiring, training, and retaining the number of skilled examiners needed to catch-up and cope with the ever increasing number of patent application filings.

While the Congress has permitted the USPTO to retain essentially all of its user fees for the last four fiscal years, users of the patent system recognize that there is nothing to prevent the return of this devastating practice, a prospect that could more likely materialize in the current Federal budget deficit situation. The beginning steps taken by the USPTO to address its quality and pendency issues—made possible by its being appropriated all of its fee revenues—demonstrate the importance of a permanent end to this possibility. The USPTO must have such protection in order to intelligently plan for and meet the multitude of challenges it faces – its users who pay the fees deserve no less.



## **B. International Harmonization Provisions**

An essential step identified by the National Academies' Board on Science, Technology, and Economic Policy ("NAS")<sup>3</sup> for improving the US patent system is the elimination of the subjective elements in US patent law. The elimination of these subjective elements would improve the operation of the USPTO, benefiting all constituencies, by promoting patent quality, simplifying the administration of the patent law, and facilitating the ability of the USPTO to work cooperatively with other patent offices to address the global backlog.

### **1. First-Inventor-To-File**

The cornerstone of these harmonizing changes is the proposal to adopt the first-inventor-to-file principle contained in Section 2 of S. 515. It will significantly simplify the patent law, provide fairer outcomes for inventors, speed final determinations of patentability, and reduce overall costs for procuring patents. With the accompanying changes that bring objectivity to the determination of what information can be used to assess the patentability of an invention, the adoption of the first-inventor-to-file principle would allow the United States to join the world patent community and make patentability determinations on objective criteria using publicly available information. The public could more readily assess the patentability of granted patents and avoid costly litigation.

### **2. “Best Mode” Harmonization**

One recommendation of the NAS that does not appear in S. 515 is the elimination of the requirement for applicants to “set forth the best mode contemplated by the inventor of carrying out his invention.” The NAS noted that much of what is wrong with the enforcement of patents can be traced to the prevalence of so-called “subjective elements” such as “best mode” in patent litigation. Questions such as “What constitutes a mode of carrying out an invention? Was one mode thought by the inventor to be better than the rest when the patent application was filed? “Were details of such best mode sufficiently disclosed in the patent application? We believe that a convincing case has been made that simply eliminating the “best mode” requirement from the patent statute is appropriate. The public’s interest in having a complete patent disclosure is readily achieved by the requirements that the patent fully describe the claimed invention and contain all the information needed to make and use the invention.

### **3. Orderly Transition Period for First-Inventor-To-File**

Before leaving the harmonizing topic, there is one technical problem in S. 515 that I would like to bring to your attention. The effective date provision contained in Section 13(a) of S. 515 would appear to apply the first-inventor-to-file principle to all applications issuing more than 12 months after the date of enactment. This approach is simply not feasible, as the decision to file, the preparation of the patent application itself, its filing and its examination should all be performed knowing the patentability rules that will apply to its grant. Such an important transformation needs to be made in an orderly

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<sup>3</sup> Merrill, Levin, and Myers, “A Patent System for the 21st Century”, Committee on Intellectual Property Rights in the Knowledge-Based Economy, Board on Science, Technology, and Economic Policy, National Research Council, National Academies <http://www.nap.edu/html/patentsystem/0309089107.pdf>

manner to give USPTO, inventors and the patent profession time to properly engineer its implementation. In our opinion, it would be best to first apply the changes of S. 515 to original patent applications filed more than one year after enactment.

### **C. Public Input Into the Patent Examination Process**

Another way to improve the quality of patent applications is to allow members of the public to provide timely input into the examination process. We are pleased to see the inclusion in S. 515 of Section 7 expanding the opportunity for the public to submit information to the USPTO. Allowing the public to submit information to patent examiners working on individual patent applications, together with concise descriptions of its relevance, will help ensure that all relevant information will be considered before a patent is issued. This provision will contribute to our long-standing objective to have the USPTO conduct a quality examination the first time, before a patent is granted, obviating the need to rely on post-grant clean-up procedures. The public and patent applicants alike will benefit from the grant of more reliable patents based on more thorough and complete examination that this procedure will offer.

### **IV. Expanded *Inter partes* Reexamination Proceedings**

The 21<sup>st</sup> Century Coalition supports Section 5 of S. 515, subject to eliminating its provisions relating to prior use or sale. The provisions of Section 5 of S. 515 closely track the *inter partes* reexamination provisions contained in Section 6 of HR 1908 as passed by the House in 2007. Unfortunately, S. 515 dramatically expands the grounds upon which an *inter partes* reexamination may be instituted to include on evidence that the claimed invention was in public use or on sale in the United States more than one year prior to the application for patent. In particular, S. 515 amends paragraph (1) of Section 301 to allow the citation of such evidence.<sup>4</sup>

The Coalition for 21<sup>st</sup> Century Patent Reform has consistently opposed adding “prior public use or sale” to *inter partes* reexaminations because in this procedural setting patentees will be disadvantaged if such issues may be raised many years after a patent has granted. Challengers and patent owners should be given a full and fair opportunity to oppose and defend patents on a neutral playing field, preferably before the patentee has invested heavily in developing the invention. Adding prior public sale or use arguments in reexaminations proceedings initiated many years after the alleged acts took place, without guaranteeing the right of the patent holder to take discovery and cross examine witnesses, does not provide a fair proceeding for patent owners. This new avenue of challenge is neither appropriate nor acceptable.

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<sup>4</sup> H.R. 1260 accomplishes the same objective by adding a new paragraph (3) to Section 301 to allow the citation of “documentary evidence that the claimed invention was in substantial public use or sale in the United States more than 1 year prior to the date of the application for patent in the United States.” The language in H.R. 1260 further enhances the subjectivity of such evidence by specifically stating that the public use must be “substantial,” a requirement not found in the Senate language.

## **V. Patent Damages: A Solution In Search of a Problem?**

No patent reform proposal has engendered more controversy than that relating to patent damages.<sup>5</sup> We are grateful to several Senators (and their staffs) who have participated in many hours of stakeholder discussions concerning patent damages issues, and appreciate the willingness of the sponsors of S. 515 to continue working to achieve a consensus on these issues.

### **A. Available Data Indicates Damages Awards Are Appropriate**

In the 21<sup>st</sup> Century Coalition's view, the case has yet to be made that any reform in patent damages law is needed.<sup>6</sup> Contrary to critics' assertions of just a few years ago, the number of patent litigations in this country is at least leveling-off, if not declining.<sup>7</sup> Overall, patentees have had an overall success rate of only 36% over the last 13 years. When they do win, median patent verdicts have been fairly constant since 1995, even trending downward in 2008.<sup>8</sup> These winning verdicts, if ultimately sustained, are barely enough to cover attorneys' fees in most of these cases, much less to compensate patent owners for the infringement that has occurred.

Recent experience shows that of the 2,700 cases filed each year, fewer than 5 led to verdicts in excess of \$100 million. Experience also shows that few if any of these verdicts survive post judgment review and appeal. A prime example is the *Alcatel-Lucent v Microsoft* verdict of \$1.5 billion that was touted in the last Congress as *the* reason for patent damages reform, even though it was later promptly and finally vacated.

Nor have the advocates for a change demonstrated that these few large awards are disproportionate to the damage caused to the patent owner on account of the infringement. Companies in our Coalition, like other big businesses, have many products whose yearly sales are in the hundreds of millions or even billions of dollars. When infringement damages are awarded with respect to a multi-year infringement involving such a product, it should come as no surprise that the proper damages award may be in the range of tens, if not hundreds, of million dollars. Size alone, without reference to the

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<sup>5</sup> William C. Rooklidge and Alyson G. Barker, "Reform of a Fast-Moving Target: The Development of Patent Law Since the 2004 National Academies Report,"

[http://www.patentsmatter.com/issue/pdfs/20090205\\_rooklidge\\_barker.pdf](http://www.patentsmatter.com/issue/pdfs/20090205_rooklidge_barker.pdf)

See also Scott Shane, The Likely Adverse Effects of an Apportionment-Centric System of Patent Damages, [http://www.mfgpatentpolicy.org/images/Appportionment\\_of\\_Damages\\_Adverse\\_Effects\\_Jan14\\_09.pdf](http://www.mfgpatentpolicy.org/images/Appportionment_of_Damages_Adverse_Effects_Jan14_09.pdf) (Jan. 14, 2008).

<sup>6</sup> Recognizing that insufficient data exists on patent damages, Section 18 of H.R. 1260 proposes that such a study be conducted.

<sup>7</sup> Aron Levko, Principal, PricewaterhouseCoopers, FTC Hearing on "The Evolving IP Marketplace – The Remedies," February 11, 2009 <http://www.ftc.gov/bc/workshops/ipmarketplace/feb11/docs/alevko.pdf>

<sup>8</sup> There is no empirical evidence to support the claim that damages awards are out-of-control. Indeed, several studies have found that damages awards are not increasing. A recent PriceWaterhouseCoopers study concluded "The annual median damages award since 1995 has remained fairly consistent, when adjusted for inflation." Professor Paul Janicke from the University of Houston Law Center recently testified before the FTC that the median damages award in a patent case is \$5-6 million, and if the cases where the patent owner loses (which happens in 64% of cases) are included, the median drops to less than \$2 million.

magnitude and duration of the infringement, and the nature of damage caused thereby, does not indicate that the damages award was in any way inappropriate.

Critics from some large technology companies nonetheless contend that damages reform is needed because their fears that erratic or spurious awards will be granted cause them to settle their cases at higher amounts than are fair. This contention is hard to vet, as settlement terms are normally private, and entered at a fraction of the damages that would be assessed were the case to proceed to judgment. At least one commentator, however, has pointed out that few of these settlements are material to the accused infringer.<sup>9</sup>

### **B. The Litigation Abuse Problem: Is a “Loser Pays” System The Solution?**

More commonly, proponents of patent damages reform complain that they are assaulted with baseless actions accusing their best selling products with infringement, and that the sole purpose of most of these actions is to coerce a settlement in an amount less than it would take to mount a successful defense. We have sometimes encountered this problem, which is unique to patent cases because the cost of a patent defense is so expensive that a settlement of a million dollars or more may be cheaper than the alternative. In our view, this problem stems from the common failure to award attorneys fees in patent cases. As a result, such conduct is encouraged, while the bringing of meritorious actions that might not recover enough to offset the litigation costs involved is unfortunately discouraged. One possible solution to this problem would be for the Committee to consider amending S. 518 to reinstate the “loser pays” provision that Senators Leahy and Hatch proposed in S. 3818.<sup>10</sup>

### **C. Juries Are Being Appropriately Instructed on Damages Issues**

Contrary to the opinions of some, our experience is that judges and juries are not left at sea in ascertaining damages in patent cases. To the contrary, extensive discovery is permitted into opposing parties’ damages contentions, extensive expert reports are exchanged, and both damages-related witnesses and experts are deposed at length. Motions to exclude improper testimony are permitted and considered both before and during trial, and improper evidence is routinely excluded. To the extent it is not, the aggrieved party may preserve its objection for appeal. Juries hear only admissible evidence and testimony, including explanations from qualified experts for both sides, as to value of the use made of the invention, and the base and rate of a fair royalty to be paid for that use. Jury instructions are proposed and negotiated by both sides, and any objections to those instructions may be preserved for appeal. Within the limits of those instructions, skilled trial lawyers for both sides are given ample time to explain their damages positions in closing argument, and the court’s instructions are diligently administered. Following trial, either party may move for judgment notwithstanding the verdict, or for a new trial if the verdict is against the clear weight of the evidence.

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<sup>9</sup> Pat Choate, “The Patent Reform Act of 2007: Responding to Legitimate Needs or Special Interests? The “Patent Fairness” Issue An Analysis,” suggesting that over the period 1995-2006, reported patent settlements for companies in the Coalition for Patent Fairness averaged one ninth of one percent (0.11 percent).

<http://www.innovationalliance.net/files/CPF-Patent%20Reform%20Act%20Analysis%2010-30-2007.pdf>

<sup>10</sup> Section 5(b), S. 3818, 109<sup>th</sup> Congress.

Were district courts not generally discharging their duties in the area of patent damages, one would expect critics to have pointed to large numbers of appeals to the Federal Circuit where aggrieved defendants complained that the foregoing procedures were not being followed, or that reversible error occurred. They have not. To the contrary, the public record demonstrates that damages issues are raised in relatively few patent appeals, and then seldom with respect to any of the procedural errors that one would expect were the criticisms espoused reflected in actual experience. See [www.patstats.org](http://www.patstats.org) (compare, for example, the 374 appellate rulings on literal infringement issues to only 22 for reasonable royalties for the 2000-2004 time period).

#### **D. Potential Value of “Gate Keeper” Provisions**

While our experience in patent litigation does not suggest that district court judges fail to hear appropriate motions to exclude inappropriate evidence, or to exclude damages claims that are unsupported by substantial evidence, some critics continue to contend that their experience is to the contrary. As Chairman Leahy has mentioned, one appropriate response to this perception may be to enact so-called “gate keeper” language that would ensure that courts or juries consider only those damages contentions that are cognizable at law and supported by substantial evidence. Such language, originally suggested during the so-called Feinstein-Specter meetings, appears to have garnered widespread stakeholder support, and thus should be considered as an alternative to the damages language now included in S. 515.

#### **E. Addressing Damages Involving a Small System Component**

In addition to the foregoing, concerns continue to be expressed that there is an undue risk that damages will be oversized when the invention is a feature that is added to a larger system of which the feature is but a small part. In the context where the patent owner is a non-practicing patentee not otherwise active in the field, there appears to be widespread stakeholder agreement that any reasonable royalty damages awarded should be commensurate with the value added by using the invention. Nonetheless, after years of trying, no substantive language has been proposed that has gained widespread support. We believe that this failure to agree stems from a misunderstanding of the difference between the function of the patent claims to *define* the invention, and the methodology used to *value* that invention.

##### **1. The Nature and Role of Patent Claims: To Define the Invention**

To understand the difference, it is first necessary to understand the nature and role of the numbered “claims” that appear at the end of every issued U.S. patent. In order to gain patent protection for their inventions, inventors are required to meet certain strict disclosure requirements relating to the inventions they wish to protect. In particular, every patent application must include a “specification” that contains

a written description of the invention, and of the manner and process of making and using it, in such full, clear, concise, and exact terms as to enable any person skilled in the art to which it pertains, or with which it is most nearly connected, to

make and use the same, and shall set forth the best mode contemplated by the inventor of carrying out his invention. 35 U.S.C. 112 (1<sup>st</sup> para.)

In addition to meeting these “written description” and “enablement” requirements, every patent application must

conclude with one or more claims particularly pointing out and distinctly claiming the subject matter which the applicant regards as his invention.

A claim may be written in independent or, if the nature of the case admits, in dependent or multiple dependent form. 35 U.S.C. 112 (2<sup>nd</sup> & 3<sup>rd</sup> paras.)

These patent claims, as interpreted in view of the description in the specification and the knowledge of a person skilled in the art, are the focus of the patent examination process. Upon approval or allowance by the Patent and Trademark Office, claims serve as the operating definitions of what is actually patented.

Most commonly, the original patent claims submitted with a patent application are not allowed in their original forms. During the patent examination process, each claim is carefully reviewed to ensure that it is adequately supported by the specification (that the invention it claims is both properly described and enabled), that it is sufficiently definite (that it particularly points out and distinctly claims the invention), that it seeks to cover subject matter of the kind that may be patented, that it is novel, and that it was not “obvious at the time the invention was made to a person having ordinary skill in the art to which said subject matter pertains.”<sup>11</sup> Most commonly, Patent Examiners find that an applicant’s originally proposed claims fail to meet one or more of these statutory requirements, and accordingly reject them in one or more “Office Actions” that are issued during the patent examination process. Applicants are allowed to file “responses” to such Office Actions, which may amend or rewrite the patent claims, submit additional evidence relevant to the patentability determination, explain how the claims should properly be interpreted, and/or explain why the stated grounds for the rejection of the patent claim(s) are unfounded. Most often, this back and forth process will result in a final decision on allowance after two Office Actions, although in a minority of cases, additional reviews and/or appeals will be needed before a final patentability conclusion is reached.

Once the Patent and Trademark Office has determined that the patent claims are proper in all respects, and after one final search to be sure that the same invention isn’t the subject of any another prior pending application, they are allowed, issue as part of the granted patent, and serve as the definition(s) of what is patented.

Under current law, the scope of a patent’s claims will be reconsidered at the request of any member of the public who files a reexamination request with the Patent and Trademark Office showing that a substantial new issue of patentability exists with respect to one or more of the patent’s claims in view of the disclosure(s) of one or more prior patents or publications.

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<sup>11</sup> See 35 U.S.C. 101, 102, 103 & 112.

Whether or not a patent's claims have been tested in reexamination, their validity and proper interpretation may again be challenged in federal district court by any accused infringer. During such proceedings, the district court judge is required to conduct a so-called "Markman" hearing to interpret the claims to ensure that they are construed consistently with the "intrinsic evidence," which includes the specification as well as all of the back and forth communications (known as the "prosecution history") that led to their allowance. Once such a claim interpretation is rendered, that interpretation is used in connection with decision of all subsequent issues, including any validity challenges, the determination of infringement, and the assessment of patent damages on account of the infringement.

## **2. The Proper Approach to Determining an Invention's Value**

The process of determining the value of the use of an invention by an infringer is quite different than determining the scope and patentability of the underlying invention. In the normal case, reasonable royalty patent damages are determined by looking at what the infringer would have been reasonably willing to pay, and what the patentee would have been reasonably willing to accept, for a license to use of the invention negotiated at the time just before the infringement began. In the normal context, where the patentee and infringer are competitors, or at least have other business interests in the same field, this determination can be complex, as the sales to be made by the infringer may have a substantial negative impact on the sales being made by the patentee, and/or a license may alter or disrupt market dynamics. Accordingly, litigants normally contest reasonable royalty issues by proffering evidence related to one or more of thirteen so-called *Georgia Pacific*<sup>12</sup> factors that have been developed by the courts relating to various business circumstances that could have had an influence on the outcome of the hypothetical negotiation.

Where the patentee is not a practicing entity (and thus does not compete against or have interests in the same field with the accused infringer), the business context is simplified. In such cases, most stakeholders appear to agree in concept that the focus of the reasonable royalty determination should be on the incremental value of using the invention, and that that value should not be artificially inflated or diminished merely because an expanded or contracted royalty base is employed in its calculation. In particular, the business value of using an invention should generally be independent of whether it was claimed broadly or narrowly. For example, if the reasonable royalty for using a patented, variable-speed automobile windshield wiper is one dollar, it should not matter whether the amount is assessed as one dollar per wiper assembly, or one dollar per car. Stated differently, a patentee who has drafted his claim to "an improved car with the [novel] windshield wiper assembly" should not be awarded more than one who drafts his claim only to "an improved [novel] windshield assembly" – the resulting incremental value to an auto manufacturer of using the invention in this example does not vary, nor should the amount of reasonable royalty damages awarded.

## **3. Non-Use, or Non-Infringing Substitute, As a Focus for Comparative Valuation**

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<sup>12</sup> *Georgia-Pacific v. United States Plywood*, 318 F. Supp. 1116 (S.D.N.Y. 1970).

It appears that a promising approach to this reasonable royalty problem, at least for circumstances involving non-practicing patentees with no competitive interests in the field, may be to focus on ascertaining the incremental value to the infringer, at the time just before the infringement began, of using the invention compared to not using it, or to using its closest reasonably available non-infringing substitute, and then determining the fair proportion of that value that should be paid to the patent owner for that use. In the example of the windshield wiper example, the value of the car with the improved windshield wiper may be compared to the car's value without a conventional windshield wiper, and a reasonable royalty that is a fair proportion of the determined incremental value could then be assessed.

#### **4. The Invention Should Not Be Redefined for Damages Purposes**

Unfortunately, proponents of reasonable royalty reform have gone down the wrong track, and appear to be at risk of doing so again, by trying to narrow the definition of the invention for damages purposes. According to this methodology, the definition of patented invention, as set forth in carefully crafted claims approved by the USPTO, would still be used in the validity and infringement phases of a patent enforcement litigation, but not for purposes of assessing fair damages “for the use made of the invention by the infringer,” as is now required by statute. Instead, these proponents would narrow the claimed invention using one or more definitional devices that are plainly intended to reduce inventors’ recoveries so that the royalties will be based on less than what the Patent and Trademark Office agreed to be patentable.

Some such definitional devices suggested during the last Congress included limiting the claimed invention for damages purposes to “its inventive contribution,” its “patentable features,” or, as proposed in S. 515, “the patent’s specific contribution over the prior art.” After extensive discussion and debate, it was recognized in the Senate Judiciary Committee’s report for S. 1145 that the language “specific contribution over the prior art” would have to be amended to address concerns in the patent-using communities. Indeed, in the 110<sup>th</sup> Congress, a number of witnesses and commentators noted that language that would require that a claimed invention be dissected down to less than all of its component parts for damages purposes would (a) systematically under-compensate inventors, and (b) be “toxic” to the progress of other meaningful patent law reform.

#### **5. *Quanta*’s “Essential Features” Language Is Not the Answer**

This year, some have suggested that the claimed invention again be re-defined for damages purposes, this time by reducing it to its “essential elements,” as noted by the Chairman in his introductory remarks for S. 515. This “essential elements” language is borrowed from the recent Supreme Court decision in *Quanta Computer, Inc. v. LG Electronics, Inc.*,<sup>13</sup> which used it in an entirely different context. *Quanta* in fact has nothing to do with determining the proper amount of damages to be awarded for the use made of an invention by an infringer, and by no means authorizes the kind of systematic limitation on patent damages that would result from this proposal.

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<sup>13</sup> 128 S. Ct. 2109 (2008).



*Quanta* deals with the doctrine of patent exhaustion: when in the distribution chain so much of the patented invention has been sold that it would be unfair to allow the patent owner to control (or collect further royalties from) further downstream sales. The Court held that patent rights are exhausted following the authorized sale of components that must be combined with other components in order to practice the method claimed in the patents in that case. In reaching this holding, the Court quoted its 1942 decision in *United States v. Univis Lens Co.*,<sup>14</sup> “where one has sold an uncompleted article which, because it embodies essential features of his patented invention, is within the protection of his patent, and has destined the article to be finished by the purchaser in conformity to the patent, he has sold his invention so far as it is or may be embodied in that particular article.”

In the context in which the Court used the term “essential features” in *Univis*, the term was clearly intended to capture the thought that exhaustion applies where a patentee has sold a product essentially embodying the whole of a patented invention. The court was not attempting to dissect the invention into essential and non-essential features, nor suggesting the use of “essential features” in damages calculations. The Supreme Court in *Quanta* was only saying that, in line with *Univis*, exhaustion applies where a patentee sells a product that embodies essentially all of the features of a claimed invention so that “the only step necessary to practice the patent is the application of common processes or the addition of standard parts.”

*Quanta*’s “essential features” phrase cannot be applied to inventions made up of a combination of prior art elements because subtraction of the common processes or standard parts would leave nothing. For those who argue that the “essential features” phrase would not apply to combination inventions, the reality is that, at some level, all inventions are combinations of old elements. As Chief Judge Markey explained “there ain’t no new elements! Only God makes things out of new elements.... It may be possible to think of a non-combination claim, but it’s very hard. Perhaps chemical claims are meant, but they are usually combinations of chemical elements.”<sup>15</sup> Thus, neither *Quanta* nor *Univis* address the value of the use made of an invention and the “essential elements” phrase should not be used in any damages legislation.

## **6. The Committee Should Await the *Lucent-Gateway* Decision**

One judicial development that may have a substantial impact on the reasonable royalty debate is *Lucent v Gateway*,<sup>16</sup> which is a reasonable royalty damages case now on appeal before the Federal Circuit. Over twenty stakeholders, including Johnson & Johnson, have participated in *amicus* filings in this case, which is likely to be argued in May of this year. It is very likely that the Federal Circuit will address some, if not most, of the damages issues raised in connection with this legislation. Accordingly, this Committee may wish to consider delaying its resolution of the reasonable royalty issues until this case has at least been argued, if not until a decision is rendered, likely as early as this summer.

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<sup>14</sup> 316 U.S. 241, 250-51 (1942)

<sup>15</sup> Howard T. Markey, *Semantic Antics in Patent Cases*, 88 F.R.D. 103 (1980); *Why Not the Statute?* 65 J. PAT. & TRADEMARK OFF. SOC’Y 31 (1983)

<sup>16</sup> *Lucent Techs. Inc. v. Gateway, Inc.*, No. 2008-1485, -1486, -1487, -1495 (Fed. Cir.)

## **VI. Interlocutory Appeals of Markman Rulings Should Be Permitted, But Limited to Certified, Dispositive Summary Judgment Motions**

Section 8 of S. 515 would amend section 1292 of 28 U.S.C. 1292 to permit patent litigants to appeal interlocutory claim construction rulings. Under current law, there are already two ways such Markman rulings may be appealed. The first is by bringing a successful, dispositive summary judgment motion; whereupon the claim construction ruling is reviewed as a matter of right on appeal. The second way, which has been very rarely granted, is to seek certification of the Markman ruling from the ruling district court judge, whereupon the appeal will be heard only at the discretion of the Court of Appeals for the Federal Circuit.

Although Section 8 of S. 515 would give the trial court discretion whether to approve such appeals and, if granted, whether to stay its proceedings during the pendency of such appeal, it would change current law by requiring that the Federal Circuit hear and decide the appeal. Our Coalition believes that this approach is fraught with opportunities for mischief. Such an approach is likely to lead to piecemeal litigation that will clog the docket of the Court of Appeals, slow the timely resolution of patent cases, and, ultimately, reduce the value of the patent award. As stated by Chief Judge Michel

Interlocutory appeals of Markman rulings need no legislative compulsion ... because they already happen. The majority of our appeals are from summary judgments of non-infringement based on claim construction. What would be added are mainly cases where the claim construction is not dispositive, which hardly seems efficient. Greater cost and delay will follow when everyone agrees costs and delays need to be reduced.<sup>17</sup>

Moreover, where the case involves the alleged invalidity of a patent, and/or where factual disputes exist as to the nature of the alleged infringement, our experience is that further proceedings, including trial, are normally needed to develop the issues. For this reason, and because patent cases normally involve the assertion of multiple claims raising many issues of interpretation, many Markman rulings are not case dispositive. Moreover, it is not infrequent for district court judges to modify their claims construction rulings during the course of the case, as they become more familiar with the technology at issue and better appreciate the context, significance and potential ambiguities of their initial interpretations.

Although previously rarely granted (as previously noted), there are signs that this may be changing. On February 6, 2009, the Federal Circuit granted permission in *Shire LLC v. Sandoz* for Sandoz to pursue an interlocutory appeal under 28 U.S.C. § 1292(b) concerning the effect of a prior district court Markman ruling.<sup>18</sup>

For these reasons, and because it would compound and delay already-complex patent litigation, we do not favor giving litigants an unfettered right to bring interlocutory appeals on all claims construction rulings. Nonetheless, if a right of interlocutory appeal

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<sup>17</sup> "A Strong Patent System," remarks by Paul R. Michel, Chief Judge, U.S. Court of Appeals for the Federal Circuit, before the Association of Corporate Patent Counsel, January 28, 2009 [http://www.patentmatter.com/issue/20090128\\_michel\\_acpc.htm](http://www.patentmatter.com/issue/20090128_michel_acpc.htm)

<sup>18</sup> *Shire LLC v. Sandoz*, Miscellaneous Docket No. 893, (Fed. Cir. 2009).

is to be given, it should be limited to appeals from denials of potentially case-dispositive summary judgment motions based on the interpretation of one or more of the patent claims in issue. Moreover, such appeals should not proceed unless the district court believes that the evidentiary record is sufficiently developed to fairly support the appeal, the ruling is sufficiently final as to be unlikely to be modified in ensuing proceedings, one or more issues to be appealed is outcome determinative, and an immediate appeal would otherwise further the interests of justice. Finally, if such an interlocutory appeal is taken, the appellant should not be permitted to institute a second appeal as to any claim construction issue that was raised or could have been raised. By including these important limitations, district courts will maintain control of the management of their cases, and those claim construction issues that are appealed will be of sufficient importance to merit the time and attention of the Federal Circuit.

## **VII. Legislative Action on Willfulness Is No Longer Needed**

The 21<sup>st</sup> Century Coalition opposes the willfulness provision of Section 4 of S. 515, as the Federal Circuit's recent decision in *In re Seagate*<sup>19</sup> abandoning the former "duty of care" standard in favor of the higher "objectively reckless" standard obviates the need for any further legislation at this time.

First, the willfulness provision contained in S. 515 is a carry over of a provision written to establish a safe harbor from liability that might have existed in a "duty of care" environment. It proposes, for example, to establish a good faith state of mind defense, even though, as the Federal Circuit explains in *Seagate*,

The state of mind of the accused infringer is not relevant to this objective inquiry. If this threshold objective standard is satisfied, the patentee must also demonstrate that this objectively-defined risk (determined by the record developed in the infringement proceeding) was either known or so obvious that it should have been known to the accused infringer.<sup>20</sup>

Moreover, in determining whether an accused infringer "acted despite an objectively high likelihood that its actions constituted infringement of a valid patent," courts must consider "both legitimate defenses to infringement claims and credible invalidity arguments . . . ,"<sup>21</sup> provisions not addressed in the current proposal. Accordingly, the potential exists that S. 515 may be interpreted as altering the law of *Seagate*, rather than codifying it.<sup>21</sup>

Second, while the Federal Circuit set forth the objectively reckless standard in *Seagate*, the court explicitly recognized "that the term [reckless] is not self-defining" and that future cases are needed to "develop the application of this standard." Thus, to enact legislation at this point would likely interfere with the orderly development of important case law that will elucidate the practical considerations to be met in applying this standard.

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<sup>19</sup> *In re Seagate Tech., LLC*, 497 F.3d 1360, 1371 (Fed. Cir. 2007), *cert. denied*, 2008 U.S. LEXIS 2153 (2008).

<sup>20</sup> *See id.*

<sup>21</sup> *See id.*; *Black & Decker, Inc. v. Robert Bosch Tool Corp.*, No. 2007-1243, 2007-1244, 2008 U.S. App. LEXIS 207, at \*\*18 (Fed. Cir. Jan. 7, 2008).

Third, as an immediate and direct result of *Seagate*, district courts have begun routinely dismissing claims of willfulness from cases before they reach the trial stage, thus suggesting that undue allegations of willfulness are no longer the problem they once were. In the Coalition's view, the best course under these circumstances would be for Congress to exercise legislative restraint in deference to the progress made on this issue by the courts, recognizing that there will be time for further legislative action, should subsequent developments indicate such a need.

### **VIII. Legislative Action Regarding Venue Is No Longer Needed and As Proposed Would Be Unfair**

The 21<sup>st</sup> Century Coalition opposes the provisions of Section 8 relating to venue, because this provision is no longer necessary in view of recent judicial decisions, and in any event would unfairly discriminate against patent owners.

Section 8 of S. 515 is presumably directed at prohibiting plaintiffs from filing cases in the Eastern District of Texas, which has been criticized by some as a pro-plaintiff forum. If such a remedy were ever needed, several developments now appear to have made it unnecessary. First, there was a 17% decline in filings in the Eastern District in 2008, perhaps due to its mounting case backlog. Second, the Fifth Circuit's recent decision *In re Volkswagen of America, Inc.*,<sup>22</sup> which was promptly followed by the Federal Circuit's decision *In re TS Tech Corp.*,<sup>23</sup> appears to have remedied the venue shopping problem by holding that cases must be transferred to locales where there is a considerable nexus to the forum, such as to those *fora* where the witnesses and evidence may be found.

Should the Committee opt to retain a provision on venue, the Coalition urges that the language be balanced so that it recognizes a patent owner's legitimate interest in bringing an infringement action in the district where it performs its research, development, manufacturing, or other commercialization of the involved technology, or where its relevant evidence or witnesses are located. For example, although the language of Section 8 allows patent-owning individuals, universities and nonprofit organizations to file suit where they reside, corporate defendants are denied such rights, and must bring suit in a district permitted under one of the preceding subsections specifying where defendants may be sued. Not only is this dichotomy unfair to corporate patent owners, but it is unduly overreaching to address the real root of the perceived venue problem that has spurred the calls for reform – cases being brought in purportedly pro-plaintiff venues that lack any substantive connection to any party's activities or to the evidence relating to the case.

The rationale for recognizing a plaintiff's home district as an appropriate venue for bringing a patent infringement action exists for corporate plaintiffs as well as individuals, universities and nonprofit organizations. Given the high costs and burdens associated with patent litigation, for many corporate plaintiffs, geographic convenience is

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<sup>22</sup> See *In re Volkswagen of America, Inc.*, 545 F.3d 304 (5th Cir. 2008).

<sup>23</sup> *In re TS Tech Corp.*, 551 F.3d 1315 (Fed. Cir. 2008) (granting a writ of mandamus holding that Eastern District of Texas clearly abused its discretion in denying a motion to transfer patent infringement case to Southern District of Ohio )

a primary concern. They prefer to bring suit in their home districts, where their witnesses, documents and other information typically are located. Moreover, for many corporate patent owners, their home forum typically is the place where they often have invested in research, development and commercialization of the patented technology. Their interests in protecting those investments in their home districts should not be ignored in favor of an accused infringer's interests in litigating in its home court. Nearly every patent infringement action presents geographical inconvenience to one party or the other; and in our view, a venue rule that imposes that inconvenience on a corporate patent owner in all cases is neither fair nor justifiable.

## **IX. Conclusion**

Johnson & Johnson and the Coalition for 21<sup>st</sup> Century Patent Reform appreciate the invitation to provide our views to the Committee on these and other patent reform proposals, and look forward to working with the Committee on this bill to bring it to successful passage.

3/8/09