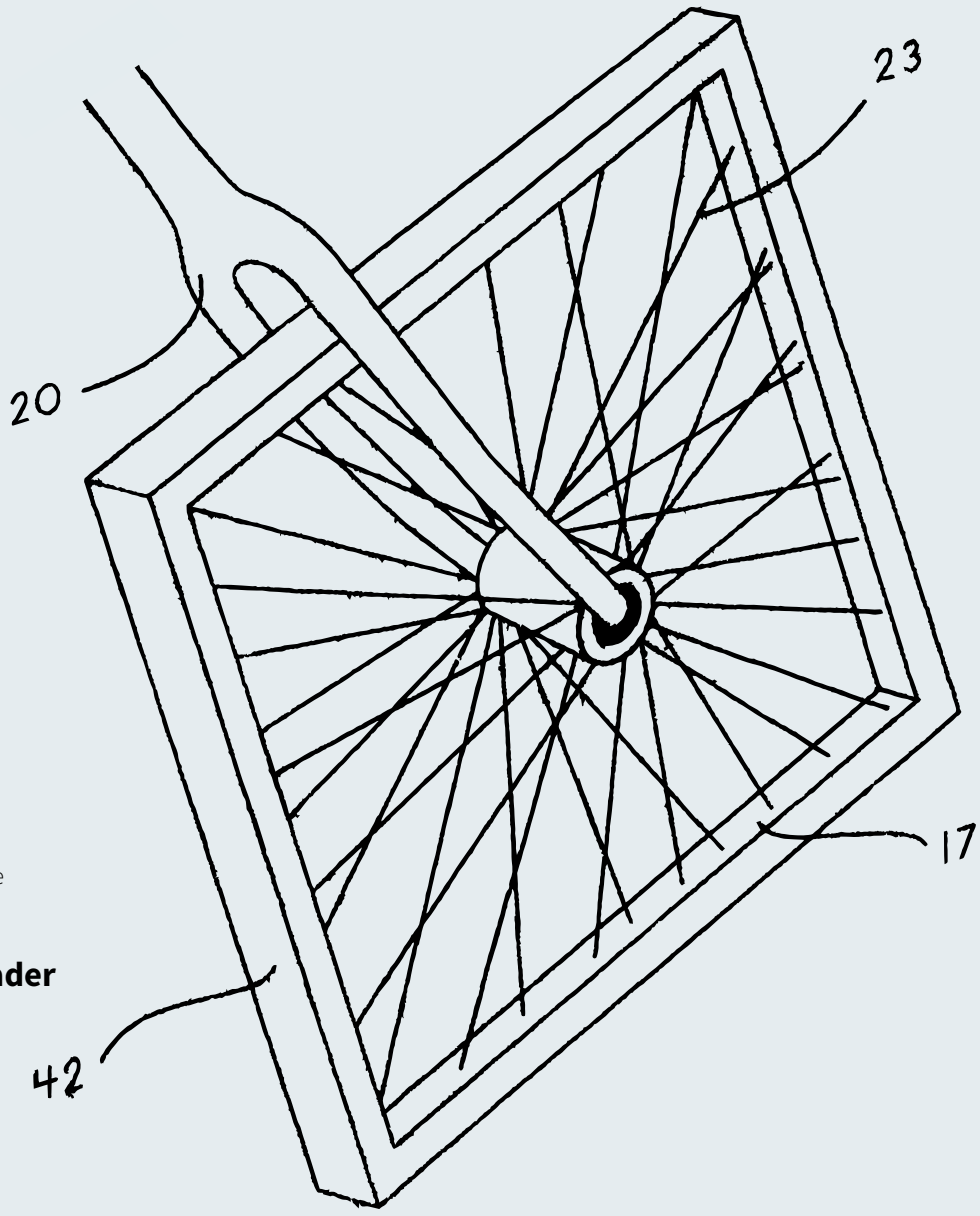
START ME UP

Challenges to the U.S. patent system, judicial activism, and the need for litigation reform

A discussion with Chief Judge Rader of the United States Court of Appeals for the Federal Circuit



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Chief Judge Randall R. Rader
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Randall R. Rader became Chief Judge for the Federal Circuit in 2010 after 20 years of serving on the Federal Circuit. During that time, he wrote many important opinions on patent damages, and his dedication to intellectual property (IP) law has made him one of the leading thinkers and speakers on the subject.

In January 2013, Chief Judge Rader was the Bench of Honor at the FTI Consulting In-House IP Counsel Forum. The forum brings together senior in-house counsel and invited federal judges to debate current issues around intellectual property litigation.

While there, Chief Judge Rader took time out to talk with Christopher Gerardi, Senior Managing Director and Co-leader of the Intellectual Property group at FTI Consulting.

The In-House IP Counsel Forum

The FTI Consulting Intellectual Property group hosts the In-House IP Counsel Forum twice a year in New York exclusively for senior in-house intellectual property counsel. The forum brings together senior in-house counsel from various industries and invited federal judges, among them judges participating in the Patent Pilot Program. At the forum, participants debate current issues and promote knowledge sharing about intellectual property litigation. In 2013, we will extend the forum to other cities in the United States.

Christopher Gerardi: Chief Judge Rader, in your keynote speech at the Intellectual Property Owners' 2012 annual conference, you delivered a blunt and impassioned warning about the future of the U.S. patent system. You said the next generation of Americans could inherit a patent system weaker and less conducive to innovation than at any time in the country's history. Why do you say that?

Chief Judge Rader: There has been a concerted effort to attack some of the fundamental principles of the patent system. Its detractors attack it for things it is not intended to do. They attack it as a healthcare pricing policy or as a manufacturer's protection policy or as a competition guarantee. It's meant to be none of those. The patent system is intended to spur innovation and invention; to incentivize research and development. Another thing it's blamed for is inefficient litigation. But the patent system is not intended to be a litigation improvement system either.

Gerardi: Who are the cynics to whom you refer?

Rader: There is a broad coalition. There are academics who make their career by finding fault in market

Christopher Gerardi

systems and economic growth. And then there are companies manufacturing a product or providing a service that would like to corner innovation in their space. They like to think that they alone will make the advances for the next generation. Therefore, when inventions emerge from universities or clinics or individual inventors outside the corporate system, that inconveniences companies, and they attack the patent system.

But their model of innovation is never going to happen again. It was a magnificent process for the era of Thomas Edison when he brought together the greatest engineers and thinkers of his time. They sat together in one little warehouse and invented everything for the world. Nowadays, because of communications and

Chief Judge Rader

other modern technologies, you have kids in Bangalore, researchers in Chengdu and startup companies in Düsseldorf all contributing to the advancement of technology. Even the brightest minds at the biggest corporations — Microsoft, Cisco and Intel, for instance — cannot corner innovation anymore. It happens worldwide, and the companies that succeed will be those that recognize cooperation as the best form of competition.

Gerardi: How do you respond to those who advocate what they believe is a more reasonable set of reforms; for instance, eliminating software patents or clamping down on non-practicing entities that accumulate patent portfolios so they can file lawsuits?

Rader: There's a definite need for litigation reform. We need to make it less expensive and more efficient to resolve marketplace disputes. That will be achieved through reduced discovery expense, speedier trials and earlier valuations — for tort and products liability, as well as for the patent system. We have a real responsibility to serve better. With regard to the patent system, we need to quickly identify inventions that deserve a greater degree of protection and weed out those that may have a marginal impact and don't deserve the time and effort they can consume. That way, we can make the system work for its purpose, which is to incentivize research and development and encourage investment in the long-term growth of innovation and the economy. The biggest problem here is what I perceive to be litigation blackmail. A party will assert an infringement claim on an incremental invention and demand for it millions or billions of dollars. Successfully defending that claim will cost more than the settlement value; thus, the defendant capitulates. There are business models built on this principle. Companies buy patents cheaply, assert them far beyond their worth and then settle at less than the cost of defense. That's not a problem with the patent system as much as it's a problem with the litigation system, and we need to address this. Let me explain why it's not the patent system's problem. The patent system says you can have improvement patents, which are not cataclysmic breakthroughs — they're just incremental advances. We need to identify those incremental steps and distinguish them from the pioneering, major steps, which deserve more protection in return for their significant contributions to our economy. And that is where the difficulty lies: achieving a valuation at an early stage that would let us separate the most deserving cases from the less so.

Chief Judge Rader

Randall R. Rader was appointed to the United States Court of Appeals for the Federal Circuit by President George H.W. Bush in 1990 and assumed the duties of Chief Judge on June 1, 2010. He was appointed to the United States Claims Court (now the U.S. Court of Federal Claims) by President Ronald W. Reagan in 1988. Chief Judge Rader's most prized title may well be Professor Rader.

As professor, Chief Judge Rader has taught courses on patent law and other advanced intellectual property courses at The George Washington University Law School, University of Virginia School of Law, Georgetown University Law Center, the Munich Intellectual Property Law Center, and other university programs in Tokyo, Taipei, New Delhi and Beijing. Due to the size and diversity of his classes, Chief Judge Rader may have taught patent law to a greater number of students than anyone else. He has won acclaim for leading dozens of government and educational delegations to every continent except Antarctica, teaching rule of law and intellectual property law principles.

Gerardi: The Federal Reserve Bank of St. Louis has published a working paper titled "The Case against Patents" in which the authors argue that there is no empirical evidence that patents serve to increase innovation and productivity. I'm guessing you don't agree with the premise of that article?

Rader: These messages are not new. Even Thomas Jefferson criticized Clause 8 of Section 8 of Article 1 of

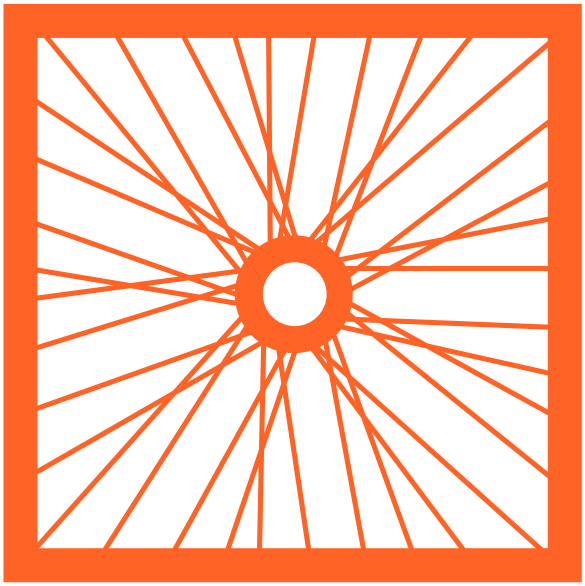
the Constitution of the United States of America. That's the intellectual property clause. But I don't have to get hyper-academic to tell you that if you are subsidizing something, you're going to get more out of it. And that's the purpose of the patent system. It creates a way of subsidizing long-term innovation. All of you [at FTI Consulting] work in a field where the key to establishing new businesses often is having proof of an innovative and meritorious idea. But bankers in Silicon Valley won't give you a mere $50 to start unless you show them some kind of patent protection for it.

Gerardi: Switching gears a little bit, recently you spoke at the New York State Bar Association's Annual Meeting of the Intellectual Property Law Section on judicial and legal activism …

Rader: I speak too much, you know.

Gerardi: and the impact this activism — real or perceived — is having on the practice of IP law. There has been a lot of discussion concerning judges' attempts to curb perceived runaway damages awards and inject some economic reality into them. Is this judicial activism or merely an attempt to enforce the guidance that flows from judicial decisions?

Rader: Section 284 tells us we are to find adequate compensation for infringement of property rights. But compensation is not deterrence. We're not looking for punitive damages; we're not looking to impose penalties on people because they have trespassed on vital property rights. But we are trying to determine what amount would represent adequate compensation. For the infringement, what would the profit have been to the property owner? In other words, what are the actual damages a party has suffered? That gets us into hardcore economics to try and determine the value of an advance to a field of science or technology or medicine. That value helps us distinguish between incremental and major advances. Making such a distinction is a challenging economic task and one that judges tend to supervise more than achieve themselves. They just try to keep the rules very clear.



Gerardi: Do you think that cases should be treated differently depending on the potential exposure; that is, should the court treat a $1 billion case differently from a $1 million case?

Rader: This is somewhat controversial. We have a fundamental sense of American fairness that everybody deserves equal access to the court systems and the justice system; small company, big company, individual or group, it doesn't matter. We try to give them all equal access. But in reality, we judges have to recognize that we have hundreds of cases on the docket, and every minute or hour we spend on one of those is time we're not spending on the others. Therefore, efficiency is critical to our form of service as well. If we can devote hours or days to the cases that deserve more time, that's a form of efficiency.

Gerardi: If we should give extra attention to cases that have greater value, do you look at value as relative or absolute? For example, compare a small manufacturing company defending a case with $20 million of exposure with a Fortune 500 company involved in a case with $100 million of exposure. In absolute dollars, it's $20 million vs. $100 million. But that $20 million may bankrupt the small company, whereas the $100 million exposure of the Fortune 500 company merely represents a rounding error.

Rader: Well, you realize that question is not going to have an answer. It urges us to learn more about each case and apply the facts as judiciously as we can. We must

understand the impacts of each case on the parties. On the other hand, for patent law in particular, there is a cumulative effect on the economy that can't be ignored just because a large corporation can absorb the loss and carry on with business. Cumulatively, over the whole economy, that might cost multitudes of jobs and greater actual economic harm than if that one small company had gone out of business because of its infringement. In other words, there's no answer. As judges, we take each case on an individual basis. We give it our best time and attention. We, however, recognize that we have, say, 300 additional cases on our docket, and we need to provide an efficient way to resolve them so those disputes do not encumber the economy.

Gerardi: There is a perception that damages awards are becoming oversized, and there has been an increase in the number of successful Daubert challenges precluding damages experts. How do you respond to those who say that generalized methodologies for calculating damages, such as the Georgia-Pacific factors, lead to inconsistent and unreliable results?

Rader: Georgia-Pacific is neither a test nor a methodology. It is a laundry list of potential sources of evidence. It never was intended to be anything other than that. And if you'll allow me to point my finger for a moment, these Georgia-Pacific factors are vastly abused by the legal community. Let me tell you how that is so. The self-endowed experts will say: "Well, there are 15 factors, and five of them favor my result; three of them are neutral; and the other seven are against my opponent. So the total is — we win!" That's using a laundry list as a test, which is wrong. I'd love to see us put the Georgia-Pacific standard in its proper, very limited context. It's a source of information, not a measure of value.

Gerardi: What else is on your mind with respect to damages reform? What other areas do you think need to be carefully evaluated by damages experts in cases?

Rader: I would like to see greater reliable economic proof. I understand this is a proposition that often runs counter to some of the things I said a moment ago about making litigation more efficient. It tends to add cost upfront as you analyze the market and identify the actual contribution of a small component to a larger system or machine. However, I view that as an investment in efficiency — as a way to streamline the system and get accurate results, which, in the long run, is what we're trying to accomplish.

Gerardi: One of the questions that many in-house attorneys deal with is patent quality and what the PTO [United States Patent and Trademark Office] is doing about it. Is there anything the court can do to reasonably influence the PTO?

Rader: It's not our job to do the work of the executive branch or the Patent and Trademark Office. We judges administer the resolution of cases that come to us. We are very aware of patent quality each time we deal with a case involving enablement or obviousness. We try to influence the level of disclosure in patent documents and the attention given to the legal standard for invention. But I don't think we're trying to dictate to the PTO how it does its job.

Gerardi: Last question, and I think this probably is going to be the toughest one of all: Aside from your day job of being the front man for the United States Court of Appeals for the Federal Circuit, you're also the front man for the band De Novo. And I will say you do a mean Mick Jagger impersonation. If you were going to take one Rolling Stones song as the anthem for the Court of Appeals for the Federal Court, what would it be?

Rader: That's easy: "Start Me Up." I wanted to avoid "Honkey Tonk Woman" and "Satisfaction."

Gerardi: I would have guessed "Time Is on My Side." Chief Judge Rader, thank you for taking time to talk with us today.

Rader: Thank you. These are important questions, and we need to get people focused on them. ■

***"Start Me Up" is the name of a well-known song made famous by Mick Jagger and the Rolling Stones in 1981.**

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