

Statement for the Record
House Judiciary Committee
Subcommittee on Courts, Intellectual Property, and the Internet
“Examining Recent Supreme Court Cases in the Patent Arena”

The *American Bankers Association*; *American Insurance Association*; *The Clearing House Payments Company L.L.C.*; *Credit Union National Association*; *Financial Services Roundtable*; *Independent Community Bankers of America*; *National Association of Federal Credit Unions*; and *National Association of Mutual Insurance Companies* appreciate the opportunity to submit this statement for the record in connection with the February 12, 2015, hearing before the House Committee on the Judiciary Subcommittee on Courts, Intellectual Property, and the Internet.

The Federal Circuit’s 1998 decision in *State Street Bank & Trust Co. v. Signature Financial Group, Inc.*¹ created a flood of poor quality business method patents and a cottage industry of business method patent litigation.²

In response to the poor quality of business method patents, the federal judiciary has written numerous decisions attempting to reign in business method patents. The Supreme Court’s recent decision in *Alice Corp. Pty. Ltd. v. CLS Bank Int’l* is arguably the most significant. In *Alice*, the Supreme Court established that a patent claim directed to an abstract idea implemented on a generic computer is not patentable subject matter under 35 U.S.C. § 101 (hereinafter “§ 101”).³

As a result of *Alice*, there are a substantial number of business-method patents that are invalid under current law.⁴

¹ 149 F.3d 1368.

² Douglas L. Price, *Assessing the Patentability of Financial Services and Products*, 3 J. High Tech. L. 141, 155 (2004) (“The fallout from *State Street* has created a gold-rush mentality toward patents and litigation in which companies ... gobble up patents on anything and everything It is a mad rush to get as many dumb patents as possible.”(citations and internal quotation marks omitted)); John R. Thomas, *The Patenting of the Liberal Professions*, 40 B.C. L. Rev. 1139, 1160 (1999) (“After *State Street*, it is hardly an exaggeration to say that if you can name it, you can claim it.”); Krause, *supra* at 101 (*State Street* “opened up a world of unlimited possession to anyone quick enough to take a business method and put it to use via computer software before anyone else.”).

³ *Alice Corp. Pty. Ltd. v. CLS Bank Int’l*, 134 S. Ct. 2347, 189 L. Ed. 2d 296 (2014).

⁴ See, e.g., Professor Mark Lemley of Stanford Law School stated that “I don’t think it’s all software patents, but I guess what I would say is a majority of the software patents being litigated right now, I think, are invalid under *Alice*.” (<http://www.ipwatchdog.com/2014/09/04/the-ramifications-of-alice-a-conversation-with-mark-lemley/id=51023/>). Erich Spangenberg, founder of IPNav, recently expressed his view that “the combination of the AIA and recent Supreme Court decisions, especially *Alice*, have had the effect of wiping out billions of dollars of value in patents, especially software patents. If some of the more recent 101 (what is patent eligible) decisions are upheld, we are only beginning to understand what *Alice* means.” (<http://www.ipnav.com/blog/erich-spangenbergs-patent-predictions-for-2015/>). Professor David Hricik of Mercer University School of Law commented that “I’ve been reading a lot of law professor views, and several (if not many) think software patents are dead, or largely so. . . . My guess is *Alice* is going to cause us all to bang our heads, stub our toes, and wander through Wonderland for many years to come.” (<http://patentlyo.com/hricik/2014/06/which-mushroom-alice.html>).

Currently, there are only two ways to get rid of business method patents that are invalid under § 101: (i) litigation in federal district court (“District Court”) and (ii) the covered business method (“CBM”) review proceedings before the United States Patent and Trademark Office’s (“USPTO”) Patent Trial and Appeal Board (“PTAB”).

1. CBM Review is Substantially More Efficient than District Court Litigation for Disposing of Business Method Patents Now Invalid under *Alice*

Litigation over whether business method patents are invalid under *Alice* places a substantial monetary burden on U.S. courts and the U.S. economy. CBM is the only viable tool for quickly, efficiently and cost-effectively eliminating covered business method patents that are invalid under *Alice*. Without CBM, the federal judiciary is the only vehicle for the Supreme Court’s direction in *Alice* to be applied to currently issued business method patents. *Inter Partes* Review (“IPR”) does not allow for a determination as to whether the patent is invalid under § 101.⁵ While Post-grant Review (“PGR”) does allow review under § 101, PGR is not available for the more than 45,000 business method patents that have already issued.⁶ Moreover, leaving the post-*Alice* clean up to the federal judiciary is contrary to Chairman Goodlatte’s opening remarks: “On the patent quality front, I strongly believe that the PTO should not simply be in the business of granting patents and leaving the mess created for the courts and Congress to fix”

The efficiency of having an administrative proceeding to rule on the invalidity of business method patents under *Alice* is evidenced by the time and cost savings of CBM as compared to District Court litigation. CBM review proceedings are statutorily required to be complete within eighteen months.⁷ In contrast, the median time to trial for patent litigation cases in District Court takes about 66% longer (thirty months total).⁸ Moreover, an administrative review option has allowed District Courts to utilize stays to more efficiently manage judicial resources and reduce litigation costs. In fact, District Courts are staying about 70% of their cases in favor of CBM review.⁹

Not only are CBM reviews substantially faster, they are also much less expensive than District Court litigation. In 2013, companies spent over \$4.7 billion in legal costs to defend

⁵ See 35 U.S.C. § 311(b) (“A petitioner in an inter partes review may request to cancel as unpatentable 1 or more claims of a patent only on a ground that could be raised under section 102 or 103 and only on the basis of prior art consisting of patents or printed publications.”)

⁶ See P.L. 112-29, § 6(f)(2)(A) (PGR shall only apply to patents issued under the first to file rules); 35 U.S.C. § 321(c) (“A petition for post-grant review may only be filed not later than the date that is 9 months after the date of the grant of patent or of the issuance of a reissue patent (as the case may be).”)

⁷ See P.L. 112-29, § 18(a)(1) (CBM “shall employ the standards and procedures of, a post-grant review”); 35 U.S.C. § 324(c); 35 U.S.C. §326(a)(11) (final decision must be made within 1 year of institution of proceeding).

⁸ Chris Barry et al., *2014 Patent Litigation Study: As Case Volume Leaps, Damages Continue General Decline*, PricewaterhouseCoopers (July 2014) (available at http://www.pwc.com/en_US/us/forensic-services/publications/assets/2014-patent-litigation-study.pdf).

⁹ See <http://interpartesreviewblog.com/statistics-stays-view-ipr-cbm-proceedings/>

against patent suits brought by non-practicing entities.¹⁰ The median patent litigation cost for cases proceeding through trial range from \$2,000,000 to \$5,500,000 where the damages at-risk exceed \$1,000,000.¹¹

In stark contrast, the USPTO estimated that the cost of preparing a petition for CBM review to be about \$61,000.¹² This is still extremely expensive for small financial institutions, especially when the PTO's filing fees and post-institution fees are considered. However, it remains much cheaper than the alternative of litigating in District Court. Furthermore, a typical budget for a patent suit in District Court is 600% more than that of an IPR, which mirrors the activities of a CBM proceeding.¹³

Because the onus for dealing with erroneously issued patents that are invalid under § 101 already falls on the shoulders of innocent businesses, it is critical to maintain CBM review as a faster, cheaper and more efficient alternative to District Court litigation.¹⁴ Without CBM, there is no administrative proceeding in which to determine the validity of tens of thousands of issued business method patents under *Alice*.

A. CBM Review Has Proven Highly Effective At Evaluating Business Method Patent Invalidity Under § 101

Due to its benefits in terms of time, efficiency, and cost, CBM review has proven to be an effective and favored tool for challenging business method patents that are invalid under § 101. In 2014, the PTAB became the most chosen venue for patent disputes.¹⁵ The success of CBM as a program is evidenced by the broad range of industries that have utilized CBM. Approximately 70% of CBM petitions have been filed by industries other than financial services.¹⁶ Moreover, CBM has been widely embraced as an effective forum to assess invalidity

¹⁰ 2013 NPE Cost Report: High-Level Findings, RPX Corporation (available at <http://www.rpxcorp.com/wp-content/uploads/2014/01/RPX-2013-NPE-Cost-Report---High-level-Findings.pdf>).

¹¹ AIPLA Report of the Economic Survey (2013).

¹² 77 Federal Register 28 (10 February 2012), p. 7086.

¹³ See Tom Engellener, *Comparison of Federal Court, ITC, and USPTO Proceedings in IP Disputes*, January 2014 AIPLA MWI Meeting.

¹⁴ Opponents of making CBM review permanent may argue that defendants can seek early dismissal on § 101 grounds under Rules 12(b)(6) or 12(c) of the Federal Rules of Civil Procedure. Given however, that District Courts may decide that construction of claim terms is required before determining whether the claims are directed to patentable subject matter under § 101, defendants may be forced to engage in costly preparation for District Court claim construction proceedings—including discovery pertaining to claim construction, written briefs, and an oral hearing—as well as unrelated written discovery and document production which often occur in advance of or in parallel with claim construction proceedings. See, e.g., *StoneEagle Services, Inc. v. Pay-Plus Solutions, Inc.*, Case No. 9:13-cv-2240-T-33MAP, Dkt. No. 91 (M.D. Fla. Feb. 9, 2015); *Bancorp Servs., L.L.C. v. Sun Life Assur. Co. of Canada*, 687 F.3d 1266, 1273-1274 (Fed. Cir. 2012) (“We note, however, that it will ordinarily be desirable—and often necessary—to resolve claim construction disputes prior to a § 101 analysis, for the determination of patent eligibility requires a full understanding of the basic character of the claimed subject matter.”).

¹⁵ See *2014 Patent Dispute Report and Analytics*, Unified Patents (available at <http://unifiedpatents.com/2014-patent-dispute-report-and-analytics/>).

¹⁶ Based on a review of filed CBM petitions filed by December 31, 2014 and accessed through the PTAB's Patent Review Processing System (<https://ptabtrials.uspto.gov/>).

under § 101. Indeed, § 101 is the second most frequent grounds used in CBM for invalidation of business method patents.¹⁷ In addition, the prevalence of § 101 challenges in CBM review proceedings demonstrates the continuing existence and assertion of business method patents that are invalid under § 101 and the demand for an administrative proceeding to resolve § 101 issues.

B. Keeping the CBM Program Is Necessary For An Effective Administrative Review of Patents Now Invalid Under *Alice*

CBM review is an efficient and effective means for dealing with a substantial pool of business method patents exposed by *Alice* as invalid under § 101. Pursuant to the sunset provision of the Leahy-Smith America Invents Act (“AIA”), however, CBM review is slated to cease existence in September 2020 with respect to new patent challenges.¹⁸ Without CBM, there will be no administrative procedure in which to address these business method patents now invalid under *Alice*.

With the looming end to administrative review of business method patents based on *Alice*, there is tremendous incentive for holders of business method patents to simply delay assertion and thereby avoid invalidation of their patents through a CBM review proceeding. As September 2020 draws closer, the incentive for delaying assertion in this manner will continue to grow. Such gaming of the system is an unintended consequence of the sunset provision and one that drastically undermines the purpose for creating CBM review.

Letting CBM review proceedings lapse, which is the only available administrative procedure to review business method patents exposed as invalid by *Alice*, will impose a substantial burden on the U.S. court system and the U.S. economy. Accordingly, the existing CBM program should be made permanent.

C. CBM Review is a Critical Tool for Combating Abusive Demand Letters

Some of the most abusive demand letters allege infringement of business method patents. Recognizing the weakness in these patents, pre-AIA demand letter campaigns often sought settlements slightly less than the cost of litigation. The availability of CBM review has been a major disruptive force. Instead of seeking settlements at less than the cost of litigation, for which a typical budget is 600% more than that of a CBM proceeding, demand letter campaigns involving business method patents now often seek settlements that are less than the cost of a CBM proceeding. Now that a plethora of business method patents have been exposed by *Alice* as invalid under § 101, many campaigns have effectively gone out of business, while others have reduced their settlement expectations even lower.

Permitting the CBM program to expire would increase the viability of abusive demand letter campaigns asserting business method patents that are invalid under § 101. Without the availability of CBM review as a less expensive option for challenging business method patents

¹⁷ Based on a review of CBM decisions through October 30, 2014, § 101 (36%) trailed only obviousness under 35 U.S.C. § 101 (41%) as grounds for successful invalidation of claims in challenged patents.

¹⁸ See 37 C.F.R. §42.300(d)

under § 101, the organizations running these abusive demand letter campaigns will be able to increase the range of their settlement demands about 600% (the difference in cost between CBM review and District Court litigation). Moreover, many targets of abusive demand letter campaigns are small-to-medium-sized businesses that cannot afford to engage in patent litigation in District Court and therefore, absent the availability of CBM review, would have no viable option to challenge an asserted business method patent under § 101.

Accordingly, it is critical that the existing CBM review program be made permanent so as to minimize the harmful effects of abusive demand letter campaigns.

D. CBM Has the Appropriate Safeguards Already Built In To Avoid Abuse While Efficiently Addressing The Effect of *Alice*

Preserving CBM review ensures that there is an efficient, cost-effective alternative to litigation for the review of business method patents exposed as invalid by *Alice*. Preserving CBM review will not subject patent holders to harassment or abuse.

There are numerous unique safeguards built into CBM review to prevent the harassment of patent holders and ensure that only those patents more likely than not to be invalidated are subject to review:

- Patents only become eligible for CBM review when the patent holder threatens or elects to pursue litigation. Only at that point can those parties charged with infringement of an eligible patent petition for review under CBM.
- CBM review requires meeting a high bar for review. A petitioner must establish that it is “more likely than not” that the patent is invalid in order to gain admission into the program.
- A petition for review under CBM can only be filed when PGR is not an option, meaning nine months after the issuance of the patent.
- Once a party charged with infringement files for declaratory judgment they are barred from petitioning for relief under CBM program.
- Petitioner in a CBM proceeding in which a final written decision is issued, is estopped from raising grounds of invalidity in a District Court proceeding that were raised in the CBM proceeding.
- There is no mandatory stay under CBM.
- CBM-eligible patents do not include patents for “technological inventions.”
- Review under the CBM must be completed within one year from initiation of the review and not more than 18 months from the time the petition for review was filed.

2. Conclusion

As a result of the Supreme Court’s decision in *Alice* there are a substantial number of business-method patents that are not valid under current law. CBM review is the only

administrative proceeding in which these patents can be evaluated under *Alice*. In the absence of CBM review, there is no viable option for challenging the validity of these patents on § 101 grounds other than costly and protracted litigation in District Court.

CBM review was established as a pilot program. It has proven highly efficient and highly effective at balancing the rights of patent holders against the need to ensure patent quality. Any effort at addressing abusive patent litigation should be built upon those aspects of the current patent review system that are working well. CBM review is a vital tool for efficiently challenging low quality patents. We urge that any patent legislation going forward make the existing CBM review program permanent. In addition, we urge Congress to give the Director of the Patent and Trademark Office discretion to waive the fees associated with the program for small institutions, as is included in section 9(d)(2) of H.R. 9. Thank you for the opportunity to submit this statement. We would be happy to answer any questions or discuss this issue further with members of the Committee.

Respectfully submitted,

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