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Articles & White Papers

The Rise of Non-Practicing Entity (NPE) Patent Litigation

July 13, 2013

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The biggest news of this year in the patent industry is probably the dramatic increase in patent litigations filed by non-practicing entities (NPEs). A record 60% of all patent litigations in the past year were filed by NPEs. The entire landscape of patent litigation is being affected by this rise. A serious backlash has occurred among the business community, which has turned to Congress, the Courts and the USPTO to try to stem this tide. President Obama, who praised patents in his 2011 State of the Union address ("No country has more successful companies, or grants more patents to inventors and entrepreneurs."), has now jumped on the bandwagon of frustration by issuing executive actions and legislative recommendations designed to curb abusive patent litigation.

Provisions in the America Invents Act (which was the subject of my three previous newsletters) were supposed to reduce the amount and cost of patent litigation. Unfortunately, to date these provisions seem to be having no noticeable effect on reducing the volume and costs of patent litigation. There are many reasons for the increase in NPE litigation, but you will be hard-pressed to find any articles written about them. Instead, the vast majority of the articles discuss the burden that such lawsuits place on companies and how the USPTO allegedly issues overly broad patents.

The reasons for the rise of NPE litigation are much more complicated than the alleged issuance of overly broad patents by the USPTO. The following trends, which are rarely written about or discussed, are all contributing to the rise of NPE litigation:

i. Many large and valuable patent portfolios have been sold by technology companies in the past five years, some due to bankruptcy (e.g., Kodak, Nortel Networks) and others due to corporate monetization strategies (e.g., large and often financially healthy corporations selling chunks of their own patent portfolios for cash). These portfolios typically wind up in the hands of the highest bidder, which is usually a patent monetization entity. Patents have a limited lifespan so lawsuits will inevitably follow after ownership transfer to bring a return on investment to the acquiring entity. The USPTO has unwittingly accelerated this process by dramatically increasing maintenance fee payments on issued patents, thereby raising the stakes of large companies to dump issued patents from their portfolios. For example, the 12 year large entity maintenance fee has almost doubled since 2007, rising from $3,800 to $7,400 today.

ii. The rise of sophisticated patent monetization entities which seek out and build patent portfolios in strategic growing niche areas of technology, which, in turn, can then be licensed to willing entities who wish to avoid expensive patent litigation, often for less than the cost of such litigation. Unwilling potential licensees are then sued in accordance with the business plan of such entities.

iii. Excess capacity within the commercial litigation industry resulting from a significant drop in the volume of general commercial litigation. Many of the newer lawsuits are being filed by lawyers and law firms that have no history of patent litigation. Likewise, large, general practice law firms are also jumping into such cases, partly to utilize their own excess capacity in this area. Rising damages awards have increased the attractiveness for such law firms to take these cases.

iv. Most large companies are now aggressively increasing the percentage of revenue obtained from “new products” since it is now a well-established fact that average profit margins are significantly higher on new products vs. older products. This inevitably leads to more disputes if the new products incorporate patented technology that competitors cannot successfully invent around. One or more patents cover virtually every new feature in motor vehicles and smart phones. Even the most mundane consumer products like diapers and cleaning supplies (e.g., mops, dusters) are being re-engineered with newly patented technology.

v. Many large and small companies have reduced their R&D expenditures as part of cost-cutting measures and have opted to purchase and/or license their new technology from third parties. By not inventing the technology in their new products, the likelihood of legitimate patent disputes rises dramatically. In most instances, the cost of patent litigation is a small price to pay for the savings in R&D.

None of these trends can be reversed by more stringent patent examining at the USPTO. In fact, stronger patents make for better lawsuits since most NPEs prefer to identify and acquire strong patents that will stand up to validity challenges at the USPTO and in Court challenges.

The purpose of this article is not to defend the rise in patent litigation. The invention industry as a whole clearly suffers when costs are diverted from developing new products to defending patent litigations. However, this is a much more complex issue than the way that it is portrayed in the media, and many of the reasons for the rise in patent disputes are the inevitable result of the accelerating pace of innovation and the changing manner in which technology is brought to the marketplace today.

My advice for clients remains the same on the protection front. Patents are still the only way to protect certain types of innovation, and building patent portfolios around new products and services should always be investigated before patent rights expire as a result of statutory bar deadlines.