



## Setting the Record Straight on Patent Reform

### *Avoiding Unintended Consequences That Would Impact Threaten Entrepreneurial Ecosystem*

NVCA supports patent reform legislation that will target abusive behavior, but is concerned that legislation under consideration will create unintended consequences that discourage investment in innovative startups. H.R. 9, and to a lesser extent S. 1137, contain provisions that will raise the cost and risk of patent litigation for all companies, making it harder for startups to enforce their patent rights against entrenched competitors or to defend themselves in patent cases brought by those competitors or even by larger Non-Practicing Entities (NPEs). NVCA stands ready to work with all stakeholders to solve the issue of abusive patent litigation, but we must be careful not to do so at the expense of the next generation of American inventors and companies.

A patent is only as strong as the owner's ability to enforce it, if necessary, and respect given by others to that ability. NVCA believes that current patent reform efforts run the risk of impairing both of these parameters, thus making it more difficult to invest in patent-reliant startups. Further, making it more difficult for startups to defend their patent rights will have an adverse impact on entrepreneurship, making it more difficult for a potential entrepreneur to leave a steady job to pursue the risky venture of founding a new company in an industry dominated by entrenched incumbents who may be emboldened to infringe on the patents of that startup.

**Fee Shifting** – Fee shifting works as a deterrent to abusive behavior only when it is properly targeted at abusive behavior. If the provision is written too broadly, as in both H.R. 9 and S. 1137, the risk of fee shifting will discourage small companies from engaging in patent litigation against a larger competitor irrespective of the merits of their position. For larger entities, legal expenses are simply the cost of doing business, but for startups and other small companies the cost of legal expenses cannot be taken for granted and could lead to bankruptcy. Large corporations typically outspend startups in litigation by multiples, a fact that converts fee shifting into a hammer to be wielded against startups and other small businesses in any patent dispute.

The fee shifting provision in H.R. 9 is effectively mandatory for most patent cases. The language requires that fees be shifted to the prevailing party unless the losing party can demonstrate affirmatively that all of its arguments during litigation were reasonable in both law and fact – a most difficult burden for any losing party to satisfy. S. 1137 also contains an overly broad standard that will shift fees in too many cases where a good faith litigant doesn't prevail. Given the probabilistic nature of all litigation and the highly uncertain outcome of patent cases in particular, it is essential to confine fee shifting to cases of frivolous or abusive litigation and to give the trial judge discretion in the award of fees.

**Joinder** – For investors in companies bankrupted by fee shifting, H.R. 9 would pierce the corporate veil and allow recovery of fees from that company's investors. The corporate structure of American business, because it isolates investors from liability claims if a company goes into bankruptcy, is one of the fundamental building blocks of an industrial economy. This provision in H.R. 9 will have the practical effect of increasing the risk of investing in startups beyond the total amount invested, threatening capital investment in patent-reliant startups.

**Discovery** – Mandatory discovery stays will increase the cost of patent litigation by giving infringers significant opportunities to create delays and to continue infringing. H.R. 9 and S. 1137 create a one-size-fits-all approach that includes detailed procedures for handling patent cases, and both bills will create major opportunities for a large corporation to make cases more expensive for a small company.

**Pleadings** – The detailed pleading requirements in H.R. 9 and S. 1137 would impose requirements that far exceed what is necessary for the efficient administration of a patent case. This will create opportunities and incentives for large defendants to continue infringing while they harass startups with unnecessary motions to the court.

**Estoppel** – The language in the two bills would remove a phrase from the estoppel provision in the IPR and PGR provisions of the America Invents Act. This will allow large corporations to attack the patents of a smaller entity twice by using some of their prior art and sandbagging additional prior art until a court trial.