

The US Patent System After the Leahy-Smith America Invents Act

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☞ Patents; United States

After many years of debate, the United States has adopted the Leahy-Smith America Invents Act (AIA). The AIA is the most significant overhaul of the US patent system in more than half a century, and moves the American system closer to the European system (with some notable exceptions). As the AIA's various provisions roll out over the 18 months following its enactment, it will significantly change many aspects of the US patent system (e.g. determining priority date, scope of prior art, USPTO proceedings and joinder of parties in litigation) while leaving other key issues (e.g. damages and venue) largely untouched and ripe for further judicial development. This comment examines the practical effects of the AIA's main provisions, particularly with regard to litigation with patent trolls and with competitors.

Background

Since 2005, patent reform has been introduced each year in the US Congress, and in 2011 both the Senate and the House of Representatives introduced patent reform legislation. On September 8, 2011, the Senate voted to approve the House version of one of the proposed Bills, H.R. 1249. On September 16, 2011, President Obama signed the Leahy-Smith America Invents Act into law, stating: "This much-needed reform will speed up the

patent process so that innovators and entrepreneurs can turn a new invention into a business as quickly as possible." That same day, Ambassador João Vale de Almeida, head of the EU delegation to the United States, welcomed the United States to the first-to-file world, praising the shift as a harmonisation that would "provide a boost to the international business community".

The extent to which the AIA speeds up the patent process, aids entrepreneurs or boosts the international community remains to be seen. But, as its various provisions take staggered effect over 18 months following its enactment, the America Invents Act (AIA) will significantly change some aspects of the patent system, while leaving other key issues largely untouched and ripe for further judicial development.

First inventor to file

Perhaps the most significant shift implemented by the AIA in the US patent system will be moving from the current first-to-invent system to a first-inventor-to-file (FITF) regime, effective for all patent applications with effective filing dates on or after March 16, 2013, which is 18 months after enactment. Supporters of this shift claim that it will increase the certainty of issued patents and reduce the extent and cost of litigation over who was first to invent. In particular, it has the potential to decrease the evidentiary burden on inventors to keep detailed records and reduce the need for subjective inquiries into an inventor's state of mind. It also stands to reduce incentives to delay filing, thereby speeding up the system. Moreover, moving the US system towards harmonisation with the "first-to-file" regime of most other nations will simplify and reduce the cost of gaining international patent protection.

At the same time, moving to FITF will not fully align the US regime with other nations' patent systems. Although the new US regime is already widely being referred to as first-to-file, the differences between new US system and the first-to-file system in place in Europe and most other major patent jurisdictions will emerge as regulations are promulgated and new procedures come into effect.

Specifically, the AIA introduces a new "derivation proceeding" of limited scope to resolve disputes over the first filer's status as the true inventor. This may apply primarily in cases of theft or misconduct. It also bears potential similarity to interference proceedings under the current first-to-invent system, though of a much narrower scope. However, there are fewer subjective evidentiary issues in derivation proceedings than in interference practice. The ultimate function and effective scope of derivation proceedings will be one detail affecting how closely aligned the new US system ultimately will be with that of Europe.

³³ *Telstra v Phone Directories* (2011) 90 I.P.R. 1 at [93]–[94] (Keane C.J.); [120]–[126] (Perram J.); and [178]–[179] (Yates J.).

³⁴ *Telstra v Phone Directories* (2011) 90 I.P.R. 1 at [127] (Perram J.).

* The views expressed herein are solely those of the authors and should not be attributed to Orrick, Herrington & Sutcliffe LLP or its clients. The authors express their appreciation for the help of their colleagues Monte Cooper and Clifford Michel.

Although the AIA's scale of changes remains to be seen, and may depend on the details of regulations promulgated by the USPTO, some likely effects include:

- it may reduce incentives to delay filing, thereby speeding up the system overall;
- focused and well-resourced non-practising entities (so-called “patent trolls”) may be able to implement mass filing and may beat inventors in the race to file, putting the burden on inventors to bring derivation proceedings; and
- smaller companies and startups will need to begin filing earlier to secure a priority date, and so will have to invest in patent prosecution at an earlier phase.

As the first-inventor-to-file system goes into effect, new rules concerning the scope of prior art and the grace period will concurrently come into place to determine the initial validity of patents. For example, the AIA significantly revises the current classifications of prior art set forth in 35 USC §102, such as eliminating the prior one-year general grace period but only on printed publications, public use, sale or availability, collapsing the prior distinction between activities of the inventor and of others (apart from the disclosure exemption), and expanding the public use bar from domestic to global use. One area of substantial controversy is the scope of the new one-year grace period for the inventor's own disclosures. Ambiguity as to what constitutes disclosure is likely to foster litigation over the coming years, with the USPTO's definition of “disclosure” and other related regulations also playing a role.

The grace period and scope of prior art are also areas of continuing discontinuity with the EU law, which gives no grace period except for limited exceptions. Although earlier efforts at US patent reform over the past few years have contemplated making the US adoption of first-to-file contingent upon the reciprocal adoption by the European Union and Japan of some form of grace period, this reciprocity condition was not adopted in the AIA. Another difference concerns prior art provisions. In the United States, for example, confidential sales are now prior art, whereas in Europe they are not. In the United States, a public prior use is prior art unless it falls under the inventor's disclosure exception. In the European Union, prior public use is prior art, unless confidential. As the United States moves towards harmonisation with the EU, Japan and other first-to-file patent systems, disparities in the scope of prior art will remain a challenge for businesses and practitioners.

Patent litigation

Joinder of parties

The AIA introduces a new litigation “joinder” rule, effective as to all actions commenced on or after the date of enactment, which represents a significant change to

the ground rules of US patent litigation practice. For a variety of reasons, some plaintiffs had previously adopted the strategy of suing many defendants in the same suit, even though the only relation between the defendants was that they had been accused of infringing the same patent. This created economies of scale for plaintiffs, from court costs to discovery and drafting filings, as well as efficiencies for courts able to centralise the management of sometimes voluminous factual material and leverage a single, consistent claim construction.

But sprawling multi-party suits have also been a staple strategy used by plaintiffs to maintain actions in a jurisdiction where a defendant is not located or headquartered. Suing many geographically dispersed defendants, along with at least one within the jurisdiction, allowed a plaintiff to argue that no single forum would be convenient for all defendants. Faced with this argument, the court may determine that transferring a case from the plaintiff's chosen forum would not create greater aggregate convenience. This plaintiff's strategy has been particularly successful where many of the defendants had their headquarters in Europe or Asia, and therefore could not claim that any other US domestic venue represented a more appropriate choice.

Although the new joinder rule will not go so far as to create a “one defendant, one lawsuit” norm, as some have called it, it will serve to substantially limit plaintiffs' ability to bring large multi-party lawsuits where the defendants bear no relation other than allegedly infringing the same patent. Under the AIA, in order to join parties, defendants must be either jointly and severally liable or the infringement must arise from the same transaction(s) or occurrence(s) (such as where all the defendants are sued for practising an industry standard) and have common questions of fact. This will change the habits of NPEs who had sued many defendants that are unrelated except for having infringed the same patent.

The AIA's new joinder rule will eliminate at least some of the economies of scale derived from multiple defendant suits and lead to new strategies from plaintiffs and perhaps to new managerial approaches from resource-strapped courts. Plaintiffs accustomed to naming multiple defendants may begin filing simultaneous suits against various parties in disparate jurisdictions. This may be followed by co-ordination of proceedings, such as claim construction, through the United States' unique Judicial Panel on Multidistrict Litigation, in the manner of *In re Katz Interactive Call Processing Litigation*. In his floor statement, Senator Kyl commented on Congress's intent that plaintiffs not attempt to circumvent the new joinder provisions by using consolidation procedures for trial. Another potential practice that may emerge is plaintiffs suing representative defendants in individual actions, and then pursuing licensing agreements with those implicated by the suit.

Regardless of how courts interpret the new joinder provisions, the overall shift represents the end of an era for multi-tentacled, multi-party patent suits, of which one final testament is the flurry of September 15, 2011

activity, as in the Eastern District of Texas, where more than 20 patent suits were filed, including cases naming Microsoft, Samsung, Nokia, Google, HTC, LG and others as defendants.

Prior commercial use defence

Another change that will have a significant impact on litigation practice is the expansion in the AIA of the “prior commercial use” defence, effective immediately as to any patent issued on or after the date of enactment. It allows as a defence to a claim of infringement for any prior commercial use by the defendant of a claimed process within one year of the effective filing date of the patent. The defence was previously applicable only to business method patents. While the scope and definition of “commercial use” will likely be tested in court, the examples included in the statute, such as pre-marketing regulatory review, suggest a potential broad scope. So, too, as does Senator Kyl’s floor statement that the defence will be available “[s]o long as use of the product is integrated into an ongoing commercial process, and not merely fleeting or experimental or incidental to the enterprise’s operations”. The prior commercial use defence will also apply to internal commercial processes, tools and devices used inside a closed shop, and substances that are exhausted by the manufacturing process and prove useful in defending products, such as software, that are not necessarily visible or publicly known, apart from those falling under the exemption for federally funded university patents. As a broader business strategic concern, the availability of this defence will relieve existing tension between competing incentives to patent a process or protect it as a trade secret, demonstrating one way in which the AIA will have broad effects on the ecosystem of intellectual property management.

Other changes affecting litigation

Advice of counsel and wilfulness

The closest the AIA comes to reform of damages law is its unequivocal elimination of a plaintiff’s ability to rely on the defendant’s failure to seek advice of counsel as proof of wilfulness. While it essentially codifies 2007 opinion by the Federal Circuit in *In re Seagate*,¹ this legislative intervention will create greater certainty that will prevent courts, as some have done, from nevertheless considering a defendant’s failure to seek opinion of counsel as one piece of relevant evidence in the context of a broader willfulness determination.

¹ *In re Seagate* 497 F.3d 1360, 1371 (Fed. Cir. 2007).

² *Forest Group Inc v Bon Tool Co* 590 F. 3d 1295 (Fed. Cir. 2009).

False marking

The AIA will greatly limit false marking suits, which have increased precipitously in the past few years, especially after the Federal Circuit’s 2009 opinion in *Forest Group Inc v Bon Tool Co*,² that found a per article fine of up to \$500 in false marking actions. This opinion resulted in a boom of qui tam suits brought by many plaintiffs seeking high damages. The AIA will basically eliminate qui tam lawsuits, in which damages-motivated private parties serve as public attorneys general. Under revised 35 UDC §292, the only parties with standing to sue for false marking will be the United States (which may recover the per article fine) or one who has suffered a competitive injury (who may recover compensatory damages).

The AIA also eliminates civil liability for marking a product with an expired patent number, if the patent number covered the product. Further, the AIA will allow “virtual marking” in place of marking on the product itself or packaging, in which patent holders may substitute the patent number with a website address, if the website contains a list of patents covering the article.

Best mode

As of the AIA’s enactment, the best mode defence in patent litigation is eliminated. This change was intended to bring American patent practice into harmony with Europe and other countries that do not require the disclosure of the best mode of practising the invention. Previously, a defendant could invalidate a US patent on the grounds that the inventor failed to disclose the best mode. Oddly, the best mode statutory requirement is not eliminated wholesale, just invalidation in litigation of a patent based on the lack of best mode. The statutory requirement that the inventor disclose the best mode remains as a condition for filing for patent protection. This means that in prosecution, it still matters. However, its elimination as a litigation strategy may stand to alter the long-term consequences of less robust disclosures of the best mode, and thereby change the emphasis given to this aspect of the inventor’s disclosure incentives. As the EU patent system does not have an equivalent of the best mode requirement, this elimination is one more step towards harmonisation, doing away with what had been a potential trap for the unwary or less experienced patent prosecutors in the United States.

Resolving disputes at the USPTO

An overall goal of the AIA is to provide earlier, quicker and less costly routes to challenge patents and resolve disputes. To this end, the AIA establishes several new proceedings (such as post-grant review), and alters several others (such as inter partes and ex parte re-examination review). Proponents claim that funnelling challenges into

post-grant proceedings will decrease the amount of litigation, weed out weak patents and improve clarity and certainty of existing patents. At the same time, these changes have the potential to foster greater congestion at the USPTO, lead to a proliferation of challenges to patents of independent inventors and small entities and increase early-stage costs associated with a patent.

The new pre-grant submission procedures, effective September 14, 2012, increase the opportunity for third-party involvement in examination because any party may submit prior art references with statements of relevance for the examiner's consideration while an application is pending. Although this stands to help bring prior art to the attention of the USPTO, it is not without strategic implications for third-party submitters who may generate examiner findings with respect to a submission that are unfavourable and entitled to deference in subsequent proceedings.

A key new proceeding will be post-grant review, under which a patent may be challenged by any non-owner during the nine months after grant or issuance, on any grounds that would be available in district court litigation. This represents a much broader scope than existing re-examination procedures. Significantly, unlike EU opposition proceedings, post-grant review will entail some discovery, as well as greater discretion for the parties to terminate the proceeding through settlement.

Parties who choose to challenge a patent through post-grant review will be estopped from raising in civil litigation or ITC proceedings any issue that was raised or could have been raised in post-grant review. No such estoppel provision attaches in EU oppositions. Also available will be an automatic stay of district court litigation that is filed after a post-grant review and does not seek injunctive relief.

Inter partes review will replace existing inter partes re-examination and will be limited to grounds of anticipation or obviousness based on prior art patents or publications under a "reasonable likelihood that the requestor would prevail with respect to at least [one] of the claims challenged" standard. It will be available after the nine-month post-grant review window has expired, or after termination of an actual post-grant review. A final new proceeding will be supplemental examinations, which will largely replace current ex parte re-examination practice and can be used to consider, reconsider or correct information believed to be relevant to any patent issued before or after September 16, 2012. This will likely limit challenges based on inequitable conduct.

In practice, post-grant proceedings may funnel much potential litigation into the USPTO or lead some challengers to wait, challenge through inter partes review and then litigate, rather than give up their ability to seek recourse in the courts. It may also lead new challengers to emerge who might otherwise have settled, not sued, or sought challenge under previously existing PTO procedures. The availability of new proceedings, in short, will no doubt alter the environment for handling disputes, but not all of its effects will necessarily reduce costs or

the duration, number or intensity of disputes. Although less costly than litigation, expanded post-grant proceedings also have the potential to multiply proceedings, drive up costs, increase complexity, expand bureaucracy, increase the backlog and make it harder overall for at least some companies to obtain patents. It may decrease costs associated with a patent overall, but it will create expenses at an earlier phase, which will especially affect smaller companies.

Overall, changing the cost profile of a broad challenge has the potential to effect profound changes on the allocation of activity between the USPTO and District Courts. It will be interesting to observe how disputants' strategies and preferences lead them to use the new mechanisms will unfold over the next half-decade.

Pragmatic concerns flow from the AIA's underlying assumption of a high level of monitoring. But, if a company is to make effective use of post-grant review, it will have to implement a thorough and costly patent monitoring programme in order to track applications and challenge them within the nine-months of grant or issuance. This may be conceivable in some industries, such as biotechnology, involving a smaller number of key patents but less so for high tech companies.

Eliminated and curtailed patentable subject-matter

The AIA installs a special new programme for challenging business method patents and eliminates some types of patents outright.

For example, any "strategy for reducing, avoiding, or deferring tax liability" is deemed to be "prior art", effective immediately as to any application pending on or failed after date of enactment, with "tax liability" defined as any liability for tax under federal, state, local or foreign law. USPTO has granted about 160 such patents since the 1998 *State Street* case, which will be unaffected. About the same number were pending at the time of enactment, all of which will be deemed prior art and therefore invalid. Also eliminated were patents on a claim "directed to or encompassing" a human organism, effective upon enactment as to all applications filed after the enactment, as well as all applications pending on the date of enactment. In the life sciences context, the meaning and scope of "directed to or encompassing" will likely be a source of litigation.

Under the Transitional Program for Covered Business Method Patents, parties will be able to challenge any business method patent other than patents for technological inventions. In essence, this establishes a post-grant review to challenge business method patents, effective one year after enactment and to last for an eight-year period. Unlike the general post-grant review, it is not limited to nine-month period following grant or issuance. Any business method patent will be challengeable by one sued or charged with infringement of a covered BMP, with the scope of prior art being art showing that the invention was known or used by others

in this country, or patented or described in a printed publication in this or a foreign country. One potentially problematic area is the scope of “technological inventions”, which remains to be defined by USPTO regulation. This will affect the likelihood of data processing patents, which represent a substantial percentage of business method patents, falling under the transitional programme.

Provisions absent from the AIA but under judicial development

The only explicit venue reform to emerge from the AIA is a minor industry-specific fix preventing the use of an ATM to establish jurisdiction, of importance only to financial institutions and those who sue them. Given the AIA’s lack of any sweeping provision in this area, continued change of venue law will likely come from the courts.

Another area conspicuous in its absence from the AIA is reform of the law concerning damages. Proposed procedures in prior years included:

1. expanding judges’ authority over damages assessment as “gatekeepers”;
2. a requirement that damages bear a relation to a patent’s specific contribution in relation to prior technology;
3. a ban on enhanced damages where liability is a close call; and
4. mandatory bifurcation of liability and damages at trial.

These types of damages limitations could afford litigants greater clarity on the value of a patent and how much money is at stake in a given litigation, and also potentially save the costs of expansive discovery on damages evidence until after determination of liability. Courts have recently been active in this area, reining in expert reports and the applicable royalty base, ending the 25 per cent rule and making other gestures towards limiting the often huge and unpredictable patent damages awards. The development of patent damages will continue to come from the courts.

Fees and funding

The backlog at the USPTO has grown steadily over the past six years, with about 700,000 applications awaiting examination. The USPTO’s proposed solution was an increase in hiring of examiners, including those with training in specialist fields, and investment in upgrading information technology. At the same time, the USPTO is a net donor of funds to Congress, taking in far more in fees than it spends in operating costs, with about 10 per cent of USPTO fees diverted to Congress annually, a total of about \$800 million.

Early versions of the Bill, including the Senate version passed in June 2011, proposed giving the USPTO more autonomy to set its fees and to control the funds it takes

in. But the reigning political and economic environment in the first half of 2011, and concomitant furore over the debt ceiling, put a narrow focus on the federal budget, and so USPTO funding took on an intense political significance. Ultimately, the USPTO will gain certain fee-setting authority, but its funding will be appropriated through Congress.

Overall, most patent-related fees will increase by about 15 per cent. At the same time, smaller entities are receiving fee reductions to make the process less costly, with substantially reduced filing fees applicable immediately to “micro entities” and “small entities”. The new system will have a “prioritized examination” procedure available with an initial limit of how many may be granted per year.

The USPTO does have fee-setting authority under the AIA and has a year to promulgate regulations, including those addressing fees. This could be critical given all of the new office actions that have been created. The bureaucratic complexity and therefore cost of implementing the AIA will be considerable, including the need to keep several systems working at once as the transition takes place, new systems come into effect and holdover proceedings under the old system continue for years into the future.