

Testimony of

Mr. Andrew Cadel

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Introduction

Chairman Hatch, Ranking Member Leahy, and members of the Subcommittee, my name is Andrew Cadel. I am a Managing Director, Associate General Counsel and Chief Intellectual Property counsel at JP Morgan Chase and I am pleased to testify today on behalf of The Financial Services Roundtable and BITS, which are affiliated financial services trade associations.

The Financial Services Roundtable (www.fsround.org) represents 100 of the largest diversified financial services companies providing banking, insurance, and investment products and services to American businesses and consumers. Member companies participate through their chief executive officer and other senior executives nominated by the CEO. Roundtable member companies account directly for millions of jobs.

BITS (www.bitsinfo.org) was created in 1996 to foster the growth and development of electronic financial services and e-commerce for the benefit of financial institutions and their customers. BITS provides intellectual capital and addresses emerging issues where financial services, technology and commerce intersect. BITS's Board of Directors is made up of the Chairmen and CEOs of twenty of the largest U.S. financial services companies, as well as representatives of the American Bankers Association and the Independent Community Bankers of America.

As you know, the financial services community is intensely interested in patent quality and litigation issues, and is grateful that you are considering these matters.

It is, perhaps too easy and convenient to place the entire burden for patent quality on the staff of the U.S. Patent and Trademark Office ("PTO"). We believe that Commissioner Dudas and his staff continue to perform admirably to overcome the challenges facing the PTO including reducing the backlog of pending applications. However, the fact remains that over 800,000 applications¹ are pending at the PTO and Examiners are unable to spend enough time to provide a meaningful examination on complex applications.² As a result, patent quality has suffered, and patents of dubious quality threaten to injure inventors, licensors, licensees and to disrupt lawful economic activity.

My testimony will cover needed improvements in the areas of patent quality, including our strong support for disclosure of relevant prior art, a post-grant opposition proceeding with two windows, and an interlocutory appeal of Markman rulings. I also want to emphasize our support for needed changes in the litigation landscape including appellate procedures and the ways in which damages are calculated.

¹ U.S. PATENT AND TRADEMARK OFFICE , PERFORMANCE AND ACCOUNTABILITY REPORT FISCAL YEAR 2004, available at www.uspto.gov/web/offices/com/annual/2004/060405_table5.html (last visited April 27, 2005).

² FEDERAL TRADE COMMISSION, TO PROMOTE INNOVATION: THE PROPER BALANCE OF COMPETITION AND

PATENT LAW AND POLICY, A REPORT BY THE FEDERAL TRADE COMMISSION, October 2003, at 5.

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The system for granting and adjudicating patents can be improved by (1) creating a meaningful opposition proceeding with two windows, (2) establishment of an interlocutory appeal for Markman rulings, and (3) ensuring that meaningful prior art is disclosed to the PTO early in the application process. In addition, there are various other provisions that can be adopted which will make our patent system an effective and efficient mechanism that fosters economic growth.

Opposition Proceeding

The PTO proposed a post-grant review of patent claims in its 21st Century Strategic Plan that was released in 2002. We strongly support establishment of an opposition proceeding with two windows.

With respect to the first window, we recommend that the opposition procedure allow the public to petition the PTO to cancel one or more claims in a patent within 12 months of issuance. The counterpart U.K. opposition law provides for an opposition proceeding within 24 months after the date of grant,¹⁴ but the European Patent Convention opposition period is only 9 months.¹⁵ We respectfully suggest the creation of a reasonably moderate time frame of 12 months.

With respect to a second window, we recommend allowing anyone who is threatened with a patent infringement action to file a request for an opposition proceeding within six months after receiving notice of the patent infringement action. Without the six-month window for initiation of an opposition proceeding upon a threat of patent infringement, the opposition proceeding would not achieve its goal of significantly improving patent quality by having suspect patents reviewed. In the United States, financial institutions currently have no infrastructure in place to monitor patents in time for parties to fully take advantage of the first window. As many products and services today integrate multiple technologies it will be difficult, if not impossible, to monitor all the categories necessary in the time allotted for the first window. Further, the public often does not truly know what the patentee intends the scope of the claims to be until that patent is enforced. We respectfully submit that it is not reasonable to expect businesses to review all patents issued within a year of their issue date, determine every possible interpretation an inventor may ascribe to the claims, identify those of suspect validity, and undergo the expense of attacking all of those that may be applicable and suspect during a first window.

For both windows, launching an opposition would foster a more detailed scrutiny of patents than ordinarily occurs during the typical 25 hours or less of examination at the PTO. A first window could be subject to a preponderance of evidence standard for a showing of invalidity, the second window could be generally subject to a clear and convincing standard for proof of invalidity, consistent with current treatment in trial court to foster efficient use of dispute resolution resources.

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Improving Quality of District Court Patent Decisions and Interlocutory Appeal

One of the most, if not the most, important determinations in a patent litigation is the determination of the meaning of the claims. This determination takes place early in the suit during the Markman hearing and will essentially define the scope of the patent. This determination is crucial to questions of both validity and infringement. It is difficult to overstate the importance to the parties of obtaining claim construction they can rely on. The quality of Markman decisions in district courts can be improved by allowing interlocutory appeal of Markman decisions. District court patent claim interpretations frequently are overturned by the Federal Circuit. For instance, in the period from 1996 to 2003, 35% of district court claim interpretations were overturned by the Federal Circuit.³ The inconsistent claim interpretations between the district court and the Federal Circuit are representative of how the current system has a deleterious impact on the patent system and how the current procedures create uncertainty and imbalance between the parties.

An interlocutory appeal to the Federal Circuit should be permitted after a Markman hearing. This procedure would help to mitigate the judicial inefficiency that occurs when a full trial is conducted based on an incorrect interpretation of the patent at the district court proceeding and the Federal Circuit then modifies or reverses that interpretation and orders a new trial based on that modified interpretation or reversal. In addition to attorney fees and other incurred costs, litigants pay heavy business costs due to this uncertainty. For example, litigants may experience escalated business costs because of delayed product launches and decreased productivity, which arise from distracted key employees who must focus on litigation instead of their business.

Interlocutory appeal will bring more certainty to claim construction to help each party

more accurately evaluate its settlement position which in turn will lead to earlier settlements and fewer suits in the legal system. Moreover, interlocutory appeal removes the undue advantage that a party who benefits from the erroneous claim construction has not only on the opposing party, but to others in the industry who fear they will be subject to the same faulty interpretation.

Improving Disclosure

The application process must be reformed to ensure that relevant art is disclosed in a meaningful way for Examiners that are pressed for time. Any examination of the PTO is only as reliable as the information that the Examiner is readily able to apply to the claims under review.

In furtherance of this goal, we are quite pleased that H. R. 2795 has a third party submission procedure, which will allow for more effective disclosure of relevant prior art to the Examiners at the PTO.

3 Kimberly Moore, Markman Eight Years Later: Is Claim Construction More Predictable?, 9 Lewis & Clark L. Rev. 231 (2005).

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Other Litigation related Issues

On the litigation side, improvements must be made in the way in which cases are tried, the types of courts involved in adjudicating cases, and remedies that are imposed if patents are found to be valid and infringed.

Patent Law Specialization in District Courts

Many district court judges have no special technical expertise, patent law experience, and very few have been admitted to practice before the U.S. Patent and Trademark Office. At law firms, patent attorneys specialize in patent matters and often hold technical degrees. The lack of expertise in the district court encourages a rush to the Federal Circuit where there is more patent expertise. Other industrialized foreign countries, such as the U.K., Germany, and Japan, have sought to remedy the problem of patent expertise with specialized patent trial courts, to much success.

As an intermediate or alternative step to a single specialized district patent court, which may require additional funding and a lengthy approval process, our proposed venue language (set forth below) encourages preferential venue in the ten district courts that currently handle the most patent matters.⁴ These ten district courts could be further reduced gradually over time to a single specialized district court to ease the transition and prevent disruptions in the flow of litigation. If venue does not lie where a defendant resides under the new definition or in the preferential district courts, proper venue is determined consistent with general venue provision under 28 USC § 1391 (e.g., venue applied to foreign corporations with only personal jurisdiction in the U.S.). The proposed venue language allows broad unrestricted venue for federally funded universities to encourage their ability to enforce patent rights resulting from federally funded research. Accordingly, the status quo is preserved with the ability of federally funded universities to bring patent infringement suits in their choice of jurisdiction where there is personal jurisdiction.

⁴ See, e.g., Kimberly A. Moore, Forum Shopping in Patent Cases: Does Geographic Choice Affect Innovation, 79 N.C.L. Rev. 934 (2001)(for information on selection of the ten district courts that handle the most patent matters).

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We recommend replacing the current language of 28 U.S.C. §1400(b) with the following venue language to promote specialization in patent matters in 10 district courts, where 65% of patent matters are presently heard:⁵

"Civil actions, suits, or proceedings arising under any Act of Congress relating to patents may be brought (1) in the judicial district where the defendant resides, or (2) in any of the following federal district courts where the defendant is subject to personal jurisdiction at the time the action is commenced to foster judicial expertise in patent matters: Northern District of California, Central District of California, Southern District of New York, Northern District of Illinois, District

of Massachusetts, District of Delaware, Southern District of Florida, Eastern District of Virginia, District of New Jersey, and the District of Minnesota. Notwithstanding the definition of resides under 28 U.S.C. §1391(c) "resides" under this section shall mean the judicial district where the defendant is registered as a business entity, incorporated or where its principal business office is located. If the plaintiff cannot bring a proceeding against a defendant under any of the patent venue provisions of this section in a patent matter or if the plaintiff is a university or college that has received federal funding within the last calendar year, or a non- for-profit organization controlled by such university, then the general venue provisions of 28 U.S.C. § 1391 shall apply to that patent matter."

Notice and Remedies

One of the main motivations behind our support of patent law reform is to ensure that 1) patentees provide sufficient notice of the patent claims infringed 2) courts penalize only for actual willfulness, and 3) damages match the harm done by any infringement determined.

Specific notice of patent infringement is essential to a fair and efficient proceeding. Presently, by sending a vague letter with merely a charge of infringement and a reference to a patent number, a patentee can create the false assertion that the defendant has been notified of the details of which products and services infringe which claims. Currently, such vague and unspecified notice can also set the stage for a finding of willful infringement, which incurs treble damages. Willfulness in patent law should not be divorced from the concept of willfulness in other areas of the law, such as copyright. Therefore we propose a standard that requires a finding of notice only if the defendant received written notice from the plaintiff of a charge of infringement that identifies the specific patent, claims, and alleged infringing products or services at issue and that is sufficient to give the defendant an objectively reasonable apprehension of suit on the patent.

5 Kimberly A. Moore, Forum Shopping in Patent Cases: Does Geographic Choice Affect Innovation, 79 N.C.L. Rev. 934 (2001).

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At the same time, the Patent Act should make clear that enhanced damages should not be available with respect to any period during which the infringer had an informed good faith belief that the patent was invalid or unenforceable, or would not be infringed by the conduct later shown to constitute infringement. This informed good faith belief could be established by advice of counsel. Further, a patentee should not be able to plead willful infringement before a court has determined that the patent is valid and infringed by the defendant.

Also, damages in patent suits should in some way correspond to the amount of harm done by the infringement. Under the current precedent, potential for abuse exists when a patent claim or the true invention only covers a small component of a larger product. In such cases, damages should be apportioned in accordance with the inventive contribution of the patent claim at issue as distinguished from other features of the product, the manufacturing process, business risk, or improvements added by the infringer. For example, if an invention relates to an intermittent windshield wiper, a reasonable royalty should be based on the intermittent windshield wiper and not the entire automobile. We are pleased that H.R. 2795 has appropriate language concerning apportionment.

Venue Reform to Curb Forum Shopping

In addition we further recommend limiting patent venue to curb the abuses of forum shopping in patent disputes. In general, with appropriate exceptions, patent cases should only be brought in the venue where the defendant is incorporated or in a limited group of district courts that specialize in patent matters, as opposed to anywhere there is personal jurisdiction against the defendant. Such a venue provision would prevent forum shopping and discourage frivolous litigation in patent disputes.

Under current law, plaintiffs can sue corporate business defendants for patent infringement anywhere the defendant is subject to personal jurisdiction because of the broad judicial interpretation of "resides" in 28 U.S.C. 1400.6 In VE Holding Corp.,

the Federal Circuit applied the broad definition of "resides" under the general venue statute of 28 U.S.C. 1391 to the patent venue statute of 28 U.S.C. §1400, which effectively makes the patent venue limitations of 28 U.S.C. 1400 meaningless for corporate defendants. Instead, to give effect to 28 U.S.C. §1400, its patent venue language should control over the general venue language of 28 U.S.C. § 1391, with respect to patent matters.

6 VE Holding Corp. v. Johnson Gas Appliance Co., 917 F.2d 1574 (Fed. Cir. 1990).

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Our proposed venue language limits venue to correct the broad definition of "resides" that currently allows corporate defendants to be sued in virtually any district court within the U.S. for patent infringement. The redefinition of "resides" is generally consistent with the pre-1988 standard for patent venue in which patent venue was favored in the state of incorporation or location of principle place of business. It is our understanding that such a limitation would discourage frivolous litigation. Professor Heller proposed similar venue language for H.R. 2795, which is equally acceptable to our proposal. However, any restriction of venue to reduce forum shopping should be supplemented with a move toward a specialized court for patent matters. To summarize, there are two benefits that can be gained from redefining venue: (1) limiting the applicable jurisdiction to a location that is convenient to the defending organization to discourage frivolous litigation and, (2) developing specialization and expertise in handling patent matters at the district court level, much like the Federal Circuit does at the appellate level.

The Prior User Rights Defense

The prior user rights defense under 35 U.S.C. 273 is an important protection for financial institutions especially due to the recent growth in patent litigation. However, in its current form, the prior user rights defense is merely limited to "business methods." Business methods have proved difficult to define in practice and are not defined anywhere in the Patent Act. Accordingly, a patent owner of a business method patent may characterize its business method as a system or apparatus to circumvent the application of the prior user defense. For this reason, the prior user defense should be modified to apply equally to methods and systems covered by a patent.

Another problem with the prior use defense is the high level of proof required to successfully assert the prior user defense. Currently, the prior user defense requires "clear and convincing evidence." Although "clear and convincing evidence" is generally appropriate where patent invalidity is invoked as a defense,⁷ it is not appropriate for the prior user defense, where validity is not at issue. "Preponderance of the evidence" is a better standard for a personal defense based largely on factual matters. Therefore we support amending to the degree of proof required in former Section 273(b)(4) from "clear and convincing" to "preponderance of the evidence."

Finally, the prior user right should be available to any entity that controls, is controlled by, or is under common control with the prior user. This is particularly important in the financial services industry, where companies tend to establish separate subsidiaries for the provision of new services because of the applicable regulatory framework.

7 Bausch & Lomb, Inc. v. Barnes-Hind/Hydrocurve, Inc., 796 F.2d 433 (Fed. Cir. 1986).

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CONCLUSION

The Financial Services Roundtable membership believes a properly functioning patent process is fundamental to a healthy U.S. economy and robust free enterprise system. With increases in pending patent applications and claims of infringement, we believe that the time has come for Congress to consider fundamental reforms to the patent process, with the participation of members of the financial services industry and the patent community at large.

It is in all parties' best interests to have matters adjudicated in the fairest and most efficient manner, and we believe our suggestions for litigation reform achieve this end. We look forward to participating further as you develop and move legislation to improve the patent laws.

