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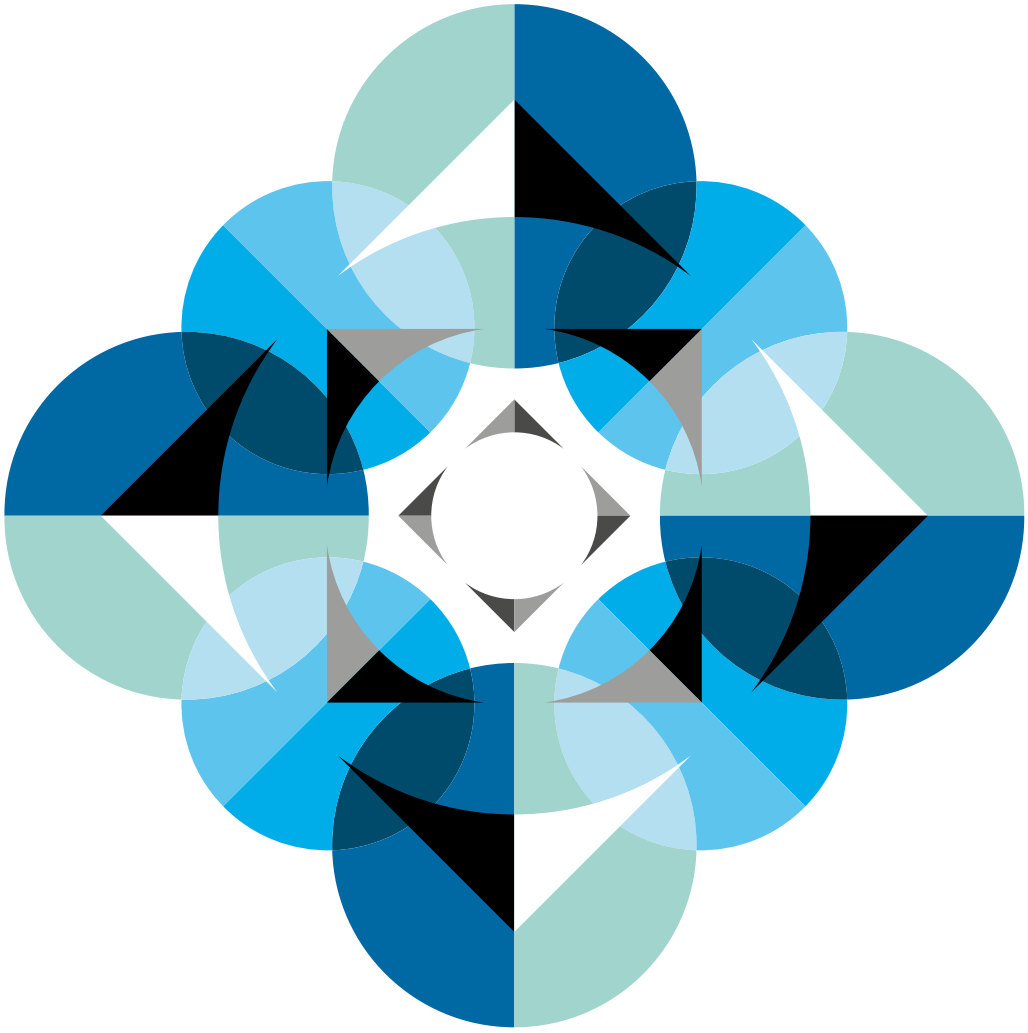
Software apps and patent trolls: Should you be afraid?



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Introduction

For a very long time there has been a debate as to whether software is better protected by copyright or by patents. The State Street Bank case in 1998 (State Street Bank v. Signature Financial Group, 149 F.3d 1368) (Fed. Cir. 1998) opened the floodgates to software patents in the US and it is only recently (due to In re Bilski, 545 F.3d 943, 88 U.S.P.Q.2d 1385 (Fed. Cir. 2008) and some other cases) that the flow has moderated a little. Over the same period, many thousands of software patents have been granted in Europe.

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Although the protection granted by a patent is short (20 years) when compared with that of copyright (life of author plus 70 years), the protection a patent affords is far greater, as it is possible to stop a person working your invention even if they have independently created the invention themselves. Copyright law just prevents another person copying what you have created. If they create something substantially similar - but without copying - then there is nothing you can do.

But the software patent situation now seems to have run out of control. We have tech wars raging between the major technology companies, and patent trolls savaging large and small technology firms both in the US and in Europe. But what are patent trolls and what do they do?

What are Patent Trolls?

In simple terms they are companies which aggressively defend their patent portfolio – but who produce no goods of their own. How can that be? Quite simply because they collect royalties on patents they buy up from universities, research institutes and bankrupt firms - they have no other business. This is why they are also known as "non-practising entities" "NPE" for short.

Intellectual Ventures

And being an NPE can be very good for your financial health. Intellectual Ventures ("IV"), which was set up by former Microsoft executive, Nathan Myhrvold, has a portfolio of more than 35,000 patents in more than 50 technology sectors. In the last 11 years or so, this has earned the company some $2 billion, basically through licensing out its portfolio to others.

In early November 2011 LG Electronics became one of a number of other Smartphone manufacturers to sign a licensing deal with them. For LG there is an upside as a few years ago it had to pay Kodak $414m (£257m) for infringing the camera maker's digital imaging rights and that fact probably made the IV deal look pretty attractive. It will now be able to access IV's patents to counter-attack any company planning to sue it for infringing their intellectual property rights.

Jeong Hwan Lee, executive vice president and head of LG's Intellectual Property Centre, said that "LG's patent portfolio is strong and is a critical element to our business strategy," and that, "Our alliance with IV gives us access to patents outside our core and allows us the freedom to focus on what's important in our industry – constant innovation."

IV had a very productive year in 2011, signing patent licensing deals not only with LG Electronics but also with American Express, Samsung, HTC, RIM, Pantech, SAP, Micron, and Wistron. Not only that but they also filed patent suits against Symantec, Trend Micro, Dell, HP and Nikon. In addition, they sued Motorola, which was in the process of being acquired by Google, one of IV's investors. One would expect 2012 to be similarly profitable for IV. It has certainly started well, as on 16th February, Reuters reported that the company has accused AT&T Inc., Sprint Nextel and T-Mobile USA of fifteen counts of infringements of patents related to their wireless network services, in a lawsuit it said it filed in the U.S. District Court of Delaware.

The attack on Independent Developers

The problem is that normal patent litigation is extremely expensive and companies with real businesses are well aware of this and are careful about initiating litigation. Not only that but there's no guarantee of success. In fact, quite the reverse, as a defendant might leverage its own large patent portfolio in a counter-attack. But this strategy doesn't work against patent trolls as they don't make anything, so are immune against such counter-attacks. Not only that but they have money and many are backed by private equity and venture capitalists.

Some NPEs are targeting independent developers - which it can be prohibitively expensive for those developers to defend, even if they are successful.

Take Lodsys as an example. This is a company that does not invent or manufacture anything. The patents it owns have been bought in. Lodsys have been sending out letters to Android and iOS application developers, both large and small, accusing them of infringing its patents. With those letters they enclose another document in which they offer to reach an agreement on licensing those "infringed" patents (and sometimes other related patents) in exchange for a small royalty – or be sued.

This huge growth in US software patent lawsuits has resulted in some independent developers deciding that it might be best for them to avoid the US as a place in which to do business. British and other non-US app developers are withdrawing their products for sale from the US versions of Apple's App Store and Google's Android Market and this is something which must have an effect on innovation - but they have little choice because Lodsys aren't unique. Other companies are also starting to demand payment for such licences, threatening litigation if their "offer" isn't taken up. And what small developer can stand up against these pressures? It would take a seriously well-funded effort to have the patents in question declared invalid and anyway, this is not a short term solution. It could take years to get to that point.

In desperation, many app developers have approached Apple or Google and both companies are trying to do something. Apple has filed a motion with the Eastern District of Texas to intervene as the defendant in a lawsuit from Lodsys that targets seven developers. Apple also used the filing to provide a counterclaim that both it and its developers have the licence rights to use the technology. Google filed a request with the United States Patent and Trademark Office, calling for the organisation to re-examine two patents at the centre of legal disputes between Lodsys and application developers, to determine whether or not the claims within them were valid. But in neither case is the outcome certain and resolution in any case is years down the line.

Options for Independent Developers

For the small app developer, there is not much it can do unless it can easily design around the NPE patent. There, the balance is between the cost of the re-design and the cost of paying the NPE a licence fee. (Which, of course, means that the limit that the NPE can charge any developer is a licence fee equating to the cost of the design around.)

Colleen Chien, Assistant Professor of Law at Santa Clara University, advocates that companies sued by trolls should use the same techniques trolls use to gain the upper hand against them. Patent trolls have captured the economies of scale in the courtroom. They use the same patents over and over again, they sue multiple defendants at the same time and they use the same counsel (on a contingency basis) in case after case – so the costs are kept right down. So she suggests, for example, that defence payments to lawyers be linked to the successful and low-cost resolution of cases. However, she may be on a hiding to nothing on that one as what private practice lawyer will want to risk taking these costs on board with little or no prospect of being paid. Far better for them to concentrate on their other remunerative work, which really leaves these companies on their own with the NPEs in an even stronger position.

The benefits of collaborative action

She has a point on collective defence however and also in using lawyers with a track record in this area. This enables joint funding and efficient defence tactics. Mike Lee, Mac and iOS developer and founder of Appsterdam, an organisation that brings together application developers, has formed the "Appsterdam Legal Defense Team", meant to defend independent developers against the patent claims recently made by the likes of Lodsys.

Such collaborative actions may allow the validity of a patent to be challenged in opposition proceedings, for example because the claimed invention is not new or not inventive or that the patent does not describe in sufficient detail how the claimed invention can be carried out and/or that the granted patent contains new matter that has been added since filing. The problem with such "opposition" challenges is that they can only be filed within nine months of grant and that it takes two or three years (or even more in complex cases) to get to a decision.

Another course of action could be to try to have the patent revoked on the grounds that it should not have been granted in the first place. The problem here is not if you win, when the patent can be revoked but if you lose, as the loser usually has to pay both sides' costs. Thus a careful cost-benefit analysis needs to be taken before commencing such an action. However, the deeper pockets of a collaborative action may allow such a course and, with the whole existence of a patent at stake, the NPE may back down and seek an easier target.

There are other less obvious tactics that can be used. For example, in Europe, Articles 101 and 102 of the Treaty on the Functioning of the European Union ("TFEU") require patents, essential to ICT standards, to be licensed on fair, reasonable and non-discriminatory ("FRAND") terms. This can be used, amongst other things, to curtail excessive royalty rates demanded by trolls. (Apple used the FRAND defence to prevent Samsung from banning sales of its iPhone in the Netherlands.).

Intellectual Property Insurance aside, if these options aren't available, an early settlement is probably the most cost-effective solution to take.

Reform of Patent Law

But really, the only certain way forward seems to lie in a reform of current patent law, both in Europe and in the United States. Many commentators consider that if the US Patent Office set higher standards, patent trolls would be less able to bring suits based on vague patents with little merit. Others think that patent renewal rates should be raised considerably on the basis that this might deter trolls from simply accumulating patents they use for nothing but litigation. More radically, but with a strong following, is the proposition that patents should be abolished in certain areas of innovation, notably for software and for business methods. After all, it can be argued that patents should

not have been granted for these things in the first place. Article 52 of the European Patent Convention states that computer programs and business methods shall not be regarded as inventions and therefore not patentable "as such". So the intention was that they should not be patentable - but the "as such" exception has allowed patentability by the back door, as (say) software isn't software "as such" if it is combined with "hardware". Further, in the US, some jurisdictions have a record of favouring claimants, so a prohibition on jurisdiction shopping might also help, by levelling the playing field.

So there are significant difficulties to be faced by legislators in adopting such reforms, as challenge is to find a reasonable balance between adequately protecting innovation and limiting or curtailing the remedies of patent owners holding technology patents, especially where those patents protect just one small element in a complex brew of technology.

No easy task.

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