No. 08-964

In The
Supreme Court of the United States

BERNARD L. BILSKI, *et al.*,

Petitioners,

v.

DAVID J. KAPPOS,

Respondent.

On Writ Of Certiorari To The United States Court Of Appeals For The Federal Circuit

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AMICI CURIAE BRIEF OF INTERNET RETAILERS IN SUPPORT OF RESPONDENT

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INTEREST OF *AMICI CURIAE*

Amici Crutchfield Corp., Newegg, Inc., L.L. Bean, Inc., Overstock.com, J.C. Penney Co., Inc., The Talbots, Inc., and Hasbro, Inc. (collectively, the "Internet Retailers") submit this brief in support of the judgment below to explain the practical consequences of a legal regime in which Internet retailers may be sued for alleged infringement of business method patents simply because they sell their goods online.* Each of these retailers came to the Internet by a different route – some started out as a catalog retailer or a single store in the early twentieth century, while others began as online sellers in the early twenty-first century – but they share in common recent experience defending patent infringement claims based not on the tens of thousands of products that they sell, and based not on the fact that some of them sell those products through hundreds of stores or millions of catalogs, but rather based simply on the fact that they sell their products on the Internet.

Crutchfield was founded in 1974 by Bill Crutchfield in his mother's basement in Charlottesville, Virginia, as a catalog company selling electronic

* In accordance with S. Ct. R. 37.3(a), all parties have consented to the filing of this brief. The Petitioners and Respondent have filed consent letters with the Clerk. Pursuant to S. Ct. R. 37.6, counsel for *Amici* state that no counsel for a party authored this brief in whole or in part, and no person or entity other than *Amici* or their counsel made a monetary contribution to the preparation or submission of this brief.

equipment. Beginning in 1996, Crutchfield also began offering its products online, through www.crutchfield.com. Today, Crutchfield has only two small brick-and-mortar stores in Virginia; but, in addition to its catalog sales, it has become one of the country's leading Internet retailers. *See Internet Retailer Top 500 Guide* 202 (2009) (No. 105, $144 million in online sales in 2008). Accompanying its online growth has been its concomitantly increased role as a defendant in patent lawsuits alleging infringement of patents through the operation of its e-commerce site, including, for example, U.S. Patent No. 5,367,627 ("Computer-Assisted Parts Sales Method").

Founded in 2001, Newegg is headquartered in Industry, California, and exclusively sells electronics, software, appliances, and electronic games through its web site, www.newegg.com. Although Newegg offers over 40,000 products online, it has been sued only a handful of times for patent infringement based on the features of any of those products (and has been indemnified by the vendors of the allegedly infringing products in such cases). Instead, as one of the most successful Internet retailers, *see Internet Retailer Top 500 Guide* 100 (2009) (No. 9, $2.1 billion), Newegg frequently must defend itself in patent infringement suits by "non-practicing entities" that claim their patents cover the operation of e-commerce web sites, *e.g.*, a recent suit under U.S. Patent No. 5,715,314 ("Network Sales System").

Leon Leonwood Bean opened his sporting goods store in Freeport, Maine, in 1912, and, on the strength of the Bean Hunting Shoe and other cornerstone products, later expanded to become one of the country's leading catalog merchants. Following the birth of the commercial Internet in 1996, L.L. Bean began to sell outdoor equipment and clothing on its web site, www.llbean.com. As another of the leading online sellers, *see Internet Retailer Top 500 Guide* 119 (2009) (No. 22, $1.0 billion), L.L. Bean is also a recurrent defendant in patent lawsuits claiming some connection to e-commerce, including a recent suit under U.S. Patent No. 5,528,490 ("Electronic Catalog System and Method").

Headquartered in Salt Lake City, Utah, since 1999 Overstock has sold excess inventory of brand-name merchandise at a discount exclusively through its web site, www.overstock.com. Its explosive growth on the Internet, *see Internet Retailer Top 500 Guide* 111 (2009) (No. 29, $834 million), has been accompanied by a similarly explosive growth in patent litigation concerning its method of doing business, *i.e.*, on the Internet.

James Cash Penney launched his dry goods and clothing store ("The Golden Rule") in Kemmerer, Wyoming in 1902. Today, with its headquarters in Plano, Texas, J.C. Penney has become one of the nation's leading retailers with over 1,100 stores located throughout the United States and Puerto Rico, and annual sales of over $18.5 billion. J.C. Penney operates an e-commerce web site, www.jcp.com, and is now one of the nation's leading Internet retailers as well. *See Internet Retailer Top 500 Guide* 111 (2009) (No. 15, $1.5 billion). J.C. Penney similarly faces suits for patent infringement based on the operation of its web site.

Founded in 1947 in Hingham, Massachusetts, Talbots has become a leading specialty retailer and direct marketer of women's classic clothing, shoes, and accessories. In addition to catalog sales and nearly 600 stores in 47 states, Talbots has become one of the country's top Internet retailers. *See Internet Retailer Top 500 Guide* 202 (2009) (No. 106, $142 million). Increasingly, Talbots has become a magnet for patent infringement lawsuits based solely on the method of operation of its web site, www.talbots.com.

Beginning in 1923 from its headquarters in Pawtucket, Rhode Island, Hasbro has become a worldwide leading seller of iconic toys and games, such as Mr. Potato Head and Monopoly. Although its online sales on its retail web site, www.hasbro toyshop.com, are miniscule, nevertheless, Hasbro also has been sued for patent infringement based on the operation of its web sites, including a recent suit under U.S. Patent No. 5,615,342 ("Electronic Proposal Preparation System").

Stated differently, Internet Retailers from Maine to California, with and without stores, with and without catalogs, selling everything from microwave ovens to Easy-Bake ovens, have one thing in common

– they are frequently defendants in patent infringement lawsuits based solely on the method in which they operate their web sites.

SUMMARY OF ARGUMENT

Business method patent claims are the claims most often asserted against companies that sell products online because it is easy for a plaintiff to allege in broad language that its patent can be read onto a retail web site. Faced with the prospect of spending millions of dollars to defend themselves, often in a faraway forum, against patent claims that amount to little more than "we own a patent, you operate a web site," virtually all Internet retailers agree to settle these types of cases before a decision on the merits. Rational retailers settle, not because the allegations of the plaintiff have merit, but because the cost of settlement, although high, is less than the even higher cost of defense.

In effect, business method patents amount to a tax on Internet commerce, transferring hundreds of millions of dollars from Internet retailers, the innovative bright spot in a dim economy, to "non-practicing entities," also known as "patent trolls." Although the Federal Circuit properly concluded that the Petitioners' claims were not patentable in its opinion below, this Court should not only affirm that judgment, but also should state unequivocally that business methods are not patentable because they flunk the applicable constitutional test: "To promote the Progress of Science and useful Arts[.]" U.S. Const. Art. I, § 8, cl. 8 (brackets added).

ARGUMENT

INTERNET RETAILERS ARE FREQUENTLY SUED UNDER BUSINESS METHOD PATENTS, AND, AS A PRACTICAL MATTER, CANNOT EFFICIENTLY, EFFECTIVELY, OR ECONOMICALLY DEFEND THEMSELVES.

Although they may operate their web sites in the virtual world of the Internet, online retailers operate their businesses in the very real world of the twenty-first century economy. It is the often grimy reality of contemporary patent litigation that the Internet Retailers find missing from the debate over the patentability of business methods. The Petitioners argue at a high level of abstraction that "[a]ny concerns over potentially vague or trivial patents for business methods should be addressed by other requirements of patentability, such as novelty, nonobviousness, and definite claiming." Petitioners' Brief at 16 (brackets added). In fact, the Internet Retailers know – and have paid dearly for that knowledge – that these doctrines were not designed for, and are not up to, the task of weeding out unpatentable business method claims on the Internet. These patents should be nipped in the bud because they are not the proper subject matter of a patent grant, and not just uprooted only after they have been allowed to flourish. Although not eager to embrace the role, like Dante's Virgil, the Internet Retailers can serve as guides to the fissures in the patent laws created by the endorsement and proliferation of business method patents.

Growth of the Internet. As one of the dissenters below noted, "[t]he innovations of the 'knowledge economy' – of 'digital prosperity' – have been dominant contributors to today's economic growth and societal change." *In re Bilski*, 545 F.3d 943, 976-77 (Fed. Cir. 2008) (Newman, J., dissenting) (brackets added). In recent decades, that economic growth and societal change has occurred most notably on and through the Internet. From its nascent beginnings of fewer than 150 web sites in 1993, the number of web sites grew exponentially to approximately 100,000 in 1996, and over 162 million in 2008. *See* Royal Pingdom, http://royal.pingdom.com/2008/04/04/how-we-got-from-1-to-162-million-websites-on-the-internet/ (last visited Sept. 30, 2009).

Increasingly, companies and individuals sell their products and services on the Internet. Last year, there were approximately $178 billion in Internet sales. Mark Brohan, *Online Retailing Weathered the Storm in 2008 and Finished as the Retail Market's Only Growth Driver*, Internet Retailer 35 (June 2009). As an oasis in an economic desert, web sales actually increased 4.6% last year. *Id*. Perhaps recognizing the "open source" origins of the Internet or the need to foster the unfettered growth of the Internet and e-commerce, Congress has decreed that access to the Internet should not be taxed in the Internet Tax Freedom Act, codified as a Note to 47 U.S.C. § 151. Private parties, however, are imposing a *de facto* tax on the Internet by asserting business method patent claims against Internet retailers in litigation targeting retail web sites.

Growth of Business Method Patents. The exponential growth in Internet usage has been accompanied by an equally enormous growth in business method patents following the Federal Circuit's approval of such patents in *State Street Bank & Trust Co. v. Signature Fin. Group, Inc.*, 149 F.3d 1368 (Fed. Cir. 1998), *cert. denied*, 525 U.S. 1093 (1999). Over 40,000 business method patent applications have been filed since *State Street* opened the floodgates, and over 15,000 such patents have been issued. *See Bilski*, 545 F.3d at 992 (Newman, J., dissenting); *see also eBay Inc. v. MercExchange, L.L.C.*, 547 U.S. 388, 397 (2006) (Kennedy, J., concurring) (noting the "burgeoning number of patents over business methods"). It is currently estimated that approximately 11,000 patents cover various aspects of the Internet, many, if not most, of which, are business method patents, *i.e.*, patents that claim inventions not of specific technologies, but of vaguely worded "methods" for doing something. *See* James Bessen & Michael J. Meurer, *Patent Failure* 8-9 (2008). If the aperture is opened wider to include software patents, it is estimated that there currently are over 200,000 such patents. *Id*. at 22. In other words, literally thousands of people can claim partial invention of the Internet, and thus, potentially can file suit to claim a share of the $178 billion in annual Internet sales.

The increase in the number of business method patents has been accompanied by a corresponding eruption in the number of patent lawsuits filed. As detailed in Figure 1 (Number of Patent Cases Filed by Year: 1994-2008, Appendix ("App.") 1, the number of new-filed patent infringement actions as recorded in the federal courts' Public Access to Court Electronic Records ("PACER") system has nearly doubled in the years following *State Street*.

Moreover, the number of cases filed is not a reliable indicator of the number of defendants accused of infringement since, increasingly, "non-practicing entities" file omnibus infringement actions naming dozens of companies in a single complaint. *See*, *e.g.*, Complaint (Doc. No. 1), *Paul N. Ware*, *et al. v. Abercrombie & Fitch Stores, Inc.*, *et al.*, Civil Action No. 4:07-cv-122 (N.D. Ga. June 19, 2007) (alleging infringement of U.S. Patent No. 4,707,592 ("Personal Universal Identity Card System for Failsafe Interactive Financial Transactions") by 109 separate defendants). Additionally, "[s]oftware patents are more than twice as likely to be litigated as other patents; patents on methods of doing business, which are largely software patents, are nearly *seven* times more likely to be litigated." Bessen & Meurer, *Patent Failure*, *supra,* at 22 (brackets added and emphasis in original). In other words, the chance of being sued for patent infringement has skyrocketed since the Federal Circuit approved business method patents in *State Street*.

Patent Law Purpose. "[T]he primary purpose of our patent laws is not the creation of private fortunes for the owners of patents but is 'to promote the progress of science and useful arts.'" *Motion Picture Patents Co. v. Universal Film Mfg. Co.*, 243 U.S. 502, 511 (1917) (quoting U.S. Const. Art. I, § 8, cl. 8) (brackets added); *see also Aronson v. Quick Point Pencil Co.*, 440 U.S. 257, 262 (1979) ("patent law seeks to foster and reward invention") (citation omitted); *Sanofi-Synthelabo v. Apotex, Inc.,* 470 F.3d 1368, 1383 (Fed. Cir. 2006) ("We have long acknowledged the importance of the patent system in encouraging innovation."). Particularly in "[a]n industry [that] has developed in which firms use patents not as a basis for producing and selling goods but, instead, primarily for obtaining licensing fees[,]" *eBay*, 547 U.S. at 396 (Kennedy, J., concurring) (brackets added), it is apparent that business method patents asserted against Internet retailers are not being used to promote the progress of science and useful arts, but simply to extract hundreds of millions, if not billions, of dollars from the most successfully innovative members of the digital economy through monopoly claims on e-commerce.

In this regard, the true digital divide is between companies that make goods and companies that sell those goods. Because it can take $800 million to $1.7 billion to develop a new drug that can obtain FDA approval, *see* Jay Dratler, Jr., *Alice in Wonderland Meets the U.S. Patent System*, 38 Akron L. Rev. 299, 313-14 & n.57 (2005); *Sanofi-Synthelabo*, 470 F.3d at

1383-84, courts, commentators, and Congress have concluded that patent protection is essential to promote the progress of science and useful arts in the pharmaceutical industry. *Id.*; *see, e.g., Eli Lilly & Co. v. Premo Pharm. Labs., Inc.*, 630 F.2d 120, 137 (3d Cir. 1980) (after noting it took Eli Lilly 20 years and tens of millions of dollars to develop the drug at issue, the court observed "[u]nless this type of an investment of human and capital resources is rewarded by some form of patent protection, companies such as Eli Lilly might well choose not to undertake such large expenditures and instead devote themselves to other endeavors") (brackets added). Accordingly, in extending patent protection for pharmaceuticals in the Hatch-Waxman Act, the House Committee on Energy and Commerce Report explained:

> Patents are designed to promote innovation by providing the right to exclude others from making, using, or selling an invention. They enable innovators to obtain greater profits than could have been obtained if direct competition existed. These profits act as incentives for innovative activities.

H.R. Rep. No. 98-857, at 15, reprinted in U.S. Code Cong. & Admin. News 2647, 2650 (1984) (quoted in *Biotechnology Indus. Org. v. District of Columbia*, 505 F.3d 1343, 1346 (Fed. Cir. 2007) (Gajarsa, J., concurring in the denial of the petition for rehearing *en banc*)).

The same rationale does not apply to a business method that, even taken at face value, simply adds a new feature to a web site. *See* Jay Dratler, Jr., *Does Lord Darcy Yet Live? The Case Against Software and Business-Method Patents*, 43 Santa Clara L. Rev. 823, 848-51 (2003). For business methods, unlike pharmaceuticals, the risk generally is not the loss of an unrecoverable past investment, but rather the future risk that the business method will not succeed in the marketplace. *Id.* Stated differently, the reward for creating a successful business method, say, for example, the Petitioners' method of hedging risk in the field of commodities, *see Bilski*, 545 F.3d at 949, is that the business method actually works and will, for example, hedge risk in the field of commodities more successfully. Whereas a drug company needs assurance that its multi-million dollar pre-market investment in a drug will be repaid, a commodity trader needs no further incentive to improve how he or she hedges risk than the market pressure to outperform rival traders. Because successful business methods are their own just reward, we need not suffer "the embarrassment of an exclusive patent" in order to encourage innovators to develop better web sites. *See* Dratler, 43 Santa Clara L. Rev. at 883 (quoting Letter from Thomas Jefferson to Isaac M'Pherson (Aug. 13, 1813) (reprinted in 5 *The Writings of Thomas Jefferson* 181 (H.A. Washington ed., New York, John C. Riker 1857)); *cf. Graham v. John Deere Co.*, 383 U.S. 1, 7 (1966) (describing Jefferson as the "first administrator of our patent system") (quotation omitted).

Notwithstanding "[t]he potential vagueness and suspect validity of some of these patents," *eBay*, 547

U.S. at 397 (Kennedy, J., concurring) (brackets added), it is highly unlikely that any court will ever evaluate the validity of most such patents because of the nature and inherent cost of patent litigation. Internet retailers sued for patent infringement based on the operation of their web sites face hydraulic pressures to settle such cases. Thus, under the current patent litigation regime, the "[o]ther requirements of patentability, such as novelty and nonobviousness" cited by Petitioners as "better tools for eliminating trivial patents," Petitioners' Brief at 41, are rendered almost wholly ineffective because they are in reality unavailable to a rational Internet retailer with an eye on its short-term bottom line.

Legal Roadblocks to Defending Business Method Claims. An admixture of legal and practical reasons renders patent litigation as presently practiced unsuited to weeding out improvidently issued business method claims. As a threshold matter, issued patent claims are entitled to a presumption of validity, 35 U.S.C. § 282, which can only be overcome by clear and convincing evidence of invalidity. *Kaufman Co. v. Lantech, Inc.*, 807 F.2d 970, 973-74 (Fed. Cir. 1986). The presumption derives from the assumption that the United States Patent and Trademark Office (the "PTO") has approved the claim after reviewing relevant prior art. *See KSR Int'l Co. v. Teleflex, Inc.*, 550 U.S. 398, 425 (2007). Although this Court has recognized that the rationale for the presumption is "much diminished" when a piece of prior art presented to a court was not before the examiner in the PTO, *see id.*, the presumption nonetheless stands between an accused infringer and a judicial determination of invalidity.

Moreover, the invalidity defenses Petitioners cite as "better tools for eliminating trivial patents," *i.e.*, novelty, obviousness, and definite claiming, *see* Petitioners' Brief at 16, 41, are not designed to address the inherent problem with business method patent claims. The trouble with business method claims is not simply that they are trivial – they may be – but that they are abstract, and thus they are not susceptible to ready categorization as innovations in a particular "art," which, in turn, makes them difficult to invalidate once they have issued. *Cf. Gottschalk v. Benson*, 409 U.S. 63, 67 (1972) (abstract intellectual processes not eligible for patent protection).

Indeed, "non-practicing entities," who are not concerned with practicing what they preach, exploit this abstractness to assert that patents which make no mention of the Internet or web site design cover retail web sites based on the logic that a "method for doing X" covers "a method for doing X on a web site." *Cf.* Petitioners' Brief at 7 ("The method of the invention does not necessarily have to be performed on a particular machine or computer, although the practice of the invention will most likely involve both computers and modern telecommunications. The method steps are no less real, however, as they require communicating and negotiating with consumers and suppliers in a particular way to balance risk positions."). Thus, in determining the prior "art" concerning the Petitioners' alleged innovative method of hedging risk in the field of commodities, it is by no means clear whether one should look in the fields of computer science, statistics, game theory, commodities trading, psychology, or someplace else.

In the context of patent litigation, and in the face of the presumption of the validity of issued patent claims, an Internet retailer cannot necessarily address the abstractness problem by finding a single anticipatory piece of prior art that disproves the novelty of the invention. *See* 35 U.S.C. § 102; *Verdegaal Bros., Inc. v. Union Oil Co. of Cal.*, 814 F.2d 628, 631 (Fed. Cir. 1987) (patent claim anticipated if each element of the claim is found in a single piece of prior art). Indeed, the more abstract the concept, the less likely there is to be such a piece of prior art. Nor can an Internet retailer necessarily prove "that there existed at the time of invention a known problem for which there was an obvious solution encompassed by the patent's claims" through one or more pieces of prior art. *KSR*, 550 U.S. at 420. Nor still by demonstrating that the claims are not "amenable to construction" or are "insolubly ambiguous," and therefore indefinite. *Datamize, LLC v. Plumtree Software, Inc.*, 417 F.3d 1342, 1348 (Fed. Cir. 2005) (quotation omitted).

An idea may be new, innovative, and commercially successful, yet not patentable. *See Lowe's Drive-In Theatres v. Park-In Theatres*, 174 F.2d 547, 552 (1st Cir. 1949) ("For we are not here called upon to deal with the novelty, usefulness, or commercial success of the outdoor drive-in theatre as an idea, or as a system for transacting business, but with the mechanical means or instrumentalities by which it may be made practically useful.") (quotations omitted). That is the core problem with business method patent claims, not that they are always or necessarily anticipated, obvious, or indefinite, but that they are ethereal, and thus, do not fit neatly into the usual categories in which the validity of patents are ordinarily tested.

Practical Roadblocks to Defending Business Method Claims. Even setting aside doctrinal difficulties, the practical realities of contemporary patent litigation make invalidity defenses a distant mirage for most defendants. First and foremost, patent litigation is notoriously expensive. According to the American Intellectual Property Law Association, in 2007, when over $1 million was at stake, the average cost of defending a patent lawsuit was over $2.5 million. *See* Christopher A. Harkins, *Tesla, Marconi, and the Great Radio Controversy: Awarding Patent Damages Without Chilling a Defendant's Incentive to Innovate*, 73 Mo. L. Rev. 745, 766-67 (2008). When over $25 million is at stake, the average cost of defending a patent lawsuit through trial climbs to $5 million. *Id.*

> Defending a patent suit can easily cost millions of dollars, with no guarantee of success. The patent troll offers a license for under $100,000. The end user makes a business decision – millions of dollars to

> defend a suit that might be lost, or $100,000 or less for certainty? The end user takes a license.

Darren Cahr & Ira Kalina, *Of PACs and Trolls: How the Patent Wars May Be Coming to a Hospital Near You*, 19 Health Lawyer 15, 16 (Oct. 2006).

Because business method patents concerning the operation of a web site, by definition, do not affect an Internet retailer's core products, but simply a marketing and sales channel, it almost always will be more cost effective to settle the case to get back to the business of selling computer equipment, or hunting shoes, or whatever. This is particularly true when the company confronts the presently existing roadblocks to defending successfully such vague and suspect claims.

The initial complaint in a patent case usually alleges no more than "we own a patent, you operate a web site." Notwithstanding the promise of *Bell Atlantic Corp. v. Twombly*, 550 U.S. 544 (2007), and *Ashcroft v. Iqbal*, 129 S. Ct. 1937 (2009), that plaintiffs must allege a plausible claim against a specific defendant, in patent cases a different *de facto* rule governs – the plaintiff need only allege that it owns a patent and that the defendant infringes. *See McZeal v. Sprint Nextel Corp.*, 501 F.3d 1354 (Fed. Cir. 2007); *cf.* Fed. R. Civ. P. Form 18 (sample patent complaint requiring only allegations of jurisdiction, ownership, infringement "by making, selling, and using" a device "embodying the patented invention," notice of infringement, and demand for relief). Thus, an Internet retailer cannot short-circuit nebulous claims against its retail web site by filing an early and relatively inexpensive motion to dismiss that would require the plaintiff to identify, for example, what claims of the patent are infringed by what features of the web site. *See, e.g., Edge Capture, L.L.C. v. Lehman Bros. Holdings, Inc.*, 2008 WL 4083146, *1 (N.D. Ill. Aug. 28, 2008); *see also* R. David Donoghue, *The Uneven Application of* Twombly *in Patent Cases: An Argument for Leveling the Playing Field*, 8 J. Marshall Rev. Intell. Prop. L. 1, 2-3 (2008) (in patent cases, "the uneven application of *Twombly* by lower courts has tilted that playing field decidedly in favor of plaintiffs").

Furthermore, patent lawsuits can be filed anywhere the alleged infringement occurs. 28 U.S.C. § 1400; *see Trintec Indus., Inc. v. Pedre Promotional Prods., Inc.*, 395 F.3d 1275 (Fed. Cir. 2005). For claims allegedly relating to the Internet, this has been interpreted to mean that anywhere a customer can access an interactive web site, the court has personal jurisdiction over the defendant and venue is proper. *See, e.g., Gorman v. Ameritrade Holding Corp.*, 293 F.3d 506 (D.C. Cir. 2002) (non-patent case); *Autobytel, Inc. v. Insweb Corp.*, 2009 WL 901482 (E.D. Tex. Mar. 31, 2009) (patent case); *see* 28 U.S.C. § 1391 (venue proper where court has personal jurisdiction).

Because anyone who operates a web site can be sued in any district in the country, the leading district for filing patent lawsuits is not the district that covers Silicon Valley, the Northern District of California. Nor is it the district in which the most companies are incorporated, the District of Delaware. Nor is it a district in one of the country's largest urban business centers, such as the Southern District of New York, the Northern District of Illinois, or the Central District of California. Rather, as shown on Figure 2 (Number of Patent Cases Filed by Jurisdiction: 1994-2008), App. 2, the most popular judicial district for new patent infringement lawsuits over the last two years – as measured by the number of new lawsuits designated as raising patent infringement claims on PACER – has been the Eastern District of Texas, which is not a major commercial center, but rather a district which has, rightly or wrongly, developed a reputation as a plaintiff-friendly forum.

For defendants sued in a distant forum, attempts to transfer such cases to more convenient venues where parties or witnesses are located are usually unsuccessful. Despite a flurry of recent mandamus petitions following denials of motions to transfer in patent cases, *see In re Genentech, Inc.*, 566 F.3d 1338 (Fed. Cir. 2009); *In re Volkswagen of America, Inc.*, 566 F.3d 1349 (Fed. Cir. 2009); *In re TS Tech USA Corp.*, 551 F.3d 1315 (Fed. Cir. 2008), motions to transfer patent cases still are routinely denied. *See, e.g., Aloft Media, L.L.C. v. Yahoo!, Inc.*, 2009 WL 1650480 (E.D. Tex. June 10, 2009). In multi-defendant cases, the fact that the plaintiff has chosen to sue multiple defendants from across the country in a single lawsuit has been deemed to render any forum equally convenient or inconvenient to the defendants, tipping the balance in favor of the plaintiff's chosen forum. *See*, *e.g.*, *MHL Tek, LLC v. Nissan Motor Co.*, 2009 WL 440627, *4 (E.D. Tex. Feb. 23, 2009). Thus, Internet retailers sued under broadly worded and undeveloped patent infringement claims often must defend those claims in distant districts, which further increases the pressure to settle.

If Internet retailers do choose to litigate these lawsuits, they then often confront the impact of Local Patent Rules promulgated first by the Northern District of California, and now adopted by many districts, including the Southern District of California, Northern District of Georgia, Eastern District of Missouri, Eastern District of North Carolina, District of New Jersey, Western District of Pennsylvania, Eastern District of Texas, Southern District of Texas, and Western District of Washington. (Many other districts and individual judges have adopted partial patent rules or issued patent-specific standing orders.) As the Federal Judicial Center explains, Local Patent Rules "were developed to facilitate efficient discovery by requiring patent litigants to promptly disclose the bases underlying their claims." Peter S. Menell, *et al.*, *Patent Case Management Judicial Guide* 2-9 (2009). In practice, however, mandatory disclosures under the Local Patent Rules and the accompanying wide-ranging discovery, like injunctions, "can be employed as a bargaining tool to charge exorbitant fees to companies that seek to buy licenses to practice the patent." *eBay*, 547 U.S. at 396 (Kennedy, J., concurring).

It is not uncommon for parties in patent litigation to exchange hundreds of thousands, if not millions, of pages of documents. *See, e.g., Network Appliance Inc. v. Sun Microsystems Inc.*, 2008 WL 4821318, *1 (N.D. Cal. Nov. 3, 2008) (3 million pages of documents); *Hynix Semiconductor Inc. v. Rambus Inc.*, 591 F. Supp. 2d 1038, 1067 (N.D. Cal. 2006) (1.2 million pages of documents). In patent cases in which the right to a billion-dollar blockbuster drug is at stake, it may make economic sense to spend the money necessary to produce 3.3 million pages of documents, *see Astrazeneca AB v. Ranbaxy Pharms., Inc.*, 2008 WL 5272018, *5 (D.N.J. Dec. 16, 2008), but that is rarely going to be the case when a "non-practicing entity" is challenging only a minor feature of an Internet retailer's web site, but nevertheless is demanding all of a company's source code and documentation relating to the web site for the claimed purpose of fleshing out its infringement claim.

In patent cases in which a company's web site allegedly infringes the plaintiff's business method patent, plaintiffs often provide only a handful of screen shots in purported satisfaction of their obligation to provide detailed infringement contentions, *see, e.g.,* N.D. Cal. L. Pat. R. 3-1, claiming, successfully, that they cannot provide additional information until they obtain all documentation concerning the design and operation of the web site, including the highly confidential source code. *See, e.g., Am. Video Graphics, L.P. v. Elec. Arts, Inc.*, 359 F. Supp. 2d 558, 560-61 (E.D. Tex. 2005). Thus, neither the allegations in the complaint nor the infringement contentions mark the metes and bounds of vague business method patents in a way that makes it clear to a defendant what it has specifically been accused of doing.

> Although not all software patents suffer from abstract or overly broad claims, software technology is especially prone to these problems. Indeed, software patents are much more likely than other patents to have their claim construction reviewed on appeal – an implicit indication that parties to lawsuits have fundamental uncertainty over the boundaries of these patents. This uncertainty leads to more frequent litigation and substantially higher litigation costs.

Bessen & Meurer, *Patent Failure*, *supra,* at 23. Faced with abstract and all-encompassing claims, and the resulting increase in uncertain and costly litigation, Internet retailers usually succumb to the siren song of settlement and licensing.

Adding insult to injury, because the language of the patent claims themselves is so ill-defined, *everything* relating to the design and operation of the web site is considered relevant to such claims, and thus subject to the plaintiff's demand that *all* documents relating to the web site be produced so that the plaintiff can discover where and how the alleged infringement occurs. *Cf. Soverain Software LLC v. Amazon.com, Inc*., 356 F. Supp. 2d 660, 663 (E.D. Tex. 2005) (parties "produced hundreds of thousands of pages of documents and millions of lines of source code"). For a retailer with a highly successful retail web site, this is being asked to hand over the keys to the kingdom.

Meanwhile, defendants shortly thereafter must provide their invalidity contentions, including all prior art, together with source code, schemata, flow charts, and detailed claim charts explaining exactly how the prior art invalidates the patent. *See, e.g.,* N.D. Cal. L. Pat. R. 3-3; *see also O2 Micro Int'l Ltd. v. Monolithic Power Sys., Inc.*, 467 F.3d 1355, 1365-66 (Fed. Cir. 2006) (Local patent rules require "both the plaintiff and *the defendant* in patent cases to *provide early notice* of their infringement and *invalidity contentions*, and to proceed with diligence in amending those contentions when new information comes to light in the course of discovery.") (emphasis added and quotation omitted); *Nova Measuring Instruments Ltd. v. Nanometrics, Inc.*, 417 F. Supp. 2d 1121, 1123 (N.D. Cal. 2006) (Local Patent Rules "are designed to require parties to *crystallize their theories of the case early in the litigation* and to adhere to those theories once they have been disclosed.") (emphasis added). Indeed, defendants are frequently prohibited from raising certain invalidity defenses because they did not raise them or identify the relevant prior art sufficiently early in the case in accordance with the Local Patent Rules. *See, e.g., Network Appliance Inc. v. Sun Microsystems, Inc*., 2009 WL 2761924, *4-5 (N.D. Cal. Aug. 31, 2009) (partial denial of motion to amend invalidity contentions); *Funai Elec. Co. v. Daewoo Elec. Corp*., 593 F. Supp. 2d 1088, 1102 (N.D.

Cal. 2009) (waiver by failure to include specific legal theory in invalidity contentions).

On the one hand, the plaintiff may have had years to investigate and develop its infringement theories, and yet, as a practical matter, need not disclose much more than screen shots of the defendants' web sites and the statement that the infringement can be found somewhere in the defendants' source code. On the other hand, defendants must immediately determine the likely reach of the plaintiff's claims, and then identify all of the prior art that anticipates each and every element of each claim, or otherwise invalidates the patent. *Cf. Impax Labs., Inc. v. Aventis Pharm. Inc.*, 468 F.3d 1366, 1381 (Fed. Cir. 2006) ("A patent claim is invalid as anticipated if every limitation in a claim is found in a single prior art reference, either explicitly or inherently.") (citation omitted). Thus, the Local Patent Rules effectively may require an Internet retailer to produce – and to produce in short order – hundreds of thousands, if not millions, of pages of internal documents containing proprietary information relating to its web sites, business plans, and operations in order to force the plaintiff to comply with its obligation to provide meaningful infringement contentions, and to search the world to locate prior art to comply with the Internet retailer's obligation to provide meaningful invalidity contentions.

Meanwhile, the plaintiff, especially if it is an entity created solely to acquire and litigate patents, has few, if any, documents to produce because its only business is litigation and it does not practice the invention it is litigating. "At this task, they must labour in the face of the majestic equality of the laws, which forbid the rich and poor alike to sleep under the bridges, to beg in the streets, and to steal their bread." Anatole France, *The Red Lily* 95 (Frederic Chapman ed. 1910). Faced with enormous discovery costs and the disclosure of the intimate details of their e-commerce strategy and operations, most companies settle even meritless patent claims rather than bear the expense or take the competitive risk of gathering and producing this sensitive information.

Likewise, claim construction, the process by which the court decides on the proper definition of disputed terms in the patent, provides little succor to many defendants. Claim construction orders, because they are interlocutory, are not immediately appealable. *Nystrom v. TREX Co., Inc.*, 339 F.3d 1347 (Fed. Cir. 2003). As a practical matter, the defendant who loses a claim construction battle generally cannot remedy an erroneous claim construction until after trial. Suffice it to say, summary judgment is rarely a viable alternative after vague claim terms have been construed. *See, e.g., Transamerica Life Ins. Co. v. Lincoln Nat'l Life Ins. Co.*, 550 F. Supp. 2d 865 (N.D. Iowa 2008) (construing claims for a "method and apparatus for providing retirement income benefits"); *Transamerica Life Ins. Co. v. Lincoln Nat'l Life Ins. Co.*, 2008 WL 4787173 (N.D. Iowa Oct. 27, 2008) (denying motion for summary judgment of non-infringement).

Estimates of the rate of reversal of claim construction orders has been measured from 33 to 71 percent, making it exceedingly difficult, if not impossible, for litigants to make informed decisions about their prospects on appeal. *See* Donna M. Gitter, *Should the United States Designate Specialist Patent Trial Judges? An Empirical Analysis of H.R. 628 in Light of the English Experience and the Work of Professor Moore*, 10 Colum. Sci. & Tech. L. Rev. 169, 171 n.5 (2009); *see also Cybor Corp. v. FAS Techs., Inc.*, 138 F.3d 1448, 1476 & n.4 (Fed. Cir. 1998) (Rader, J., dissenting) ("[O]ne study shows that the plenary standard of review has produced reversal, in whole or in part, of almost 40% of all claim constructions since *Markman* [*v. Westview Instruments, Inc.*, 52 F.3d 967 (Fed. Cir. 1995) (*en banc*)]) (brackets added). In circumstances in which the central issue in the case – the construction of the vague terms of a business method patent that may, or may not, read on the operation of a company's web site – cannot be finally determined until after a trial and an appeal, and the chance that the district court correctly construed the claims is the equivalent of a coin-flip, rational Internet retailers will find the offer of a license for hundreds of thousands, and perhaps even millions, of dollars, a preferable alternative to the uncertainty and cost of continued litigation.

Furthermore, if an Internet retailer perseveres in the face of the obstacles outlined above – choosing to spend on average $2.5 million to litigate in a far-off forum an amorphous claim that may, or may not, be construed properly – it faces a trial in which the plaintiff claims it is entitled to a "reasonable royalty" (because it has no lost profit damages as a "non-practicing entity"). Hijacking the reasonable royalty analysis for apparatus claims, *see Minco, Inc. v. Combustion Eng'g, Inc.*, 95 F.3d 1109, 1119 (Fed. Cir. 2003) (in patent infringement case involving an infringing product, "reasonable royalty" is calculated using "the percentage of sales or profit likely to have induced the hypothetical negotiators to license use of the invention"), the plaintiff often seeks a percentage of all Internet sales for the past six years and for the future life of the patent. *Cf. Lucent Tech., Inc. v. Gateway, Inc.*, 2009 WL 2902044, *16-17 (Fed. Cir. Sept. 11, 2009) (plaintiff sought 8% of sales revenue of accused software products, *i.e.,* $561.9 million, and was awarded $357.7 million by jury). Even seemingly miniscule percentages claimed by a plaintiff's expert as a "reasonable royalty" result in claimed damages of tens or hundreds of millions of dollars – once again, leading the clear-eyed Internet retailer to settle a patent suit concerning its web site even when it developed its web site entirely on its own, is convinced that such web site does not infringe the patent, and is equally convinced that the patent is invalid as obvious or anticipated by numerous other similar web sites.

In *Lucent*, the Federal Circuit vacated the damages award because "[w]e find it inconceivable to conclude, based on the present record, that the use of one small feature, the date-picker, constitutes a substantial portion of the value of Outlook." *Id*. at *25 (brackets added). In other words, although Lucent sought a percentage of the entire value of Microsoft's popular Outlook email program, the court concluded there was not sufficient evidence to anchor the jury award. *Id*. at *16-33.

Although some Internet retailers may be encouraged by the result in this case, it is more likely that they will draw less comforting conclusions from this litigation. The Federal Circuit did *not* reject the concept of awarding a percentage of all revenue based on alleged infringement by a minor feature in a software program, and the Federal Circuit *did* emphasize that "[c]reating a licensing agreement for patented technology is, at best, an inexact science," and that "[m]ost jury damages awards reviewed on appeal have been held to be supported by substantial evidence." *Id*. at *29 (brackets added). In other words, it was only "based on the present record" that the specific jury award in this specific case was vacated on appeal. *Id*. at *25. Thus, this decision leaves open the possibility on remand that Lucent will introduce sufficient evidence to support its claim of $561.9 million in damages, or that future plaintiffs will seek – and recover – a percentage of all online revenues because an Internet retailer's web site infringes their patent.

More ominously, the *Lucent* case was filed seven years ago, and not only was the case tried to a jury, but the district court rejected virtually all of Microsoft's post-trial motions, the appeals court rejected

Microsoft's invalidity and infringement challenges on appeal, and even though the damages award was overturned for insufficient evidence, the case has been remanded for yet another trial on damages. *Id*. at *1-16, 34; *see also Lucent Tech., Inc. v. Gateway, Inc*., 580 F. Supp. 2d 1016 (S.D. Cal. 2008) (denying post-trial motions), *affirmed in part, vacated in part, remanded by* 2009 WL 2902044 (Fed. Cir. Sept. 11, 2009). Although Microsoft may be prepared to spend $100 million a year defending itself in patent litigation, Q&A: Microsoft Calls for Reforms to the U.S. Patent System, www.microsoft.com/presspass/features/2005/mar05/03-10PatentReform.mspx (last visited Sept. 30, 2009), and to litigate the *Lucent* case for up to 10 years (including the trial on remand and any possible further appeals), that is not a realistic choice for most Internet retailers. Faced with the prospect of years of uncertain, but certainly expensive, litigation, most Internet retailers will never be able to take advantage of the theoretical defenses identified by the Petitioners as bulwarks against "vague or trivial patents for business methods," namely, the "other requirements of patentability, such as novelty, nonobviousness, and definite claiming." Petitioners' Brief at 16.

Moreover, even the defendants that draw a line in the sand against amorphous and suspect business method patents cannot prevent the same plaintiff which litigated and lost from suing other Internet retailers on the same, rejected, infringement theory. In *Furnace Brook LLC v. Overstock.com, Inc*., 2006

WL 2792692 (S.D.N.Y. Sept. 27, 2006), the district court had no difficulty construing the claims of U.S. Patent No. 5,721,832 (the "'832 Patent") ("Method and Apparatus for an Interactive Catalog System"), and after concluding that the patent had absolutely nothing to do with the Internet or Overstock's web site, the court granted summary judgment on the grounds of non-infringement. *See Furnace Brook LLC v. Overstock.com, Inc.*, 2006 WL 3078905 (S.D.N.Y. Oct. 26, 2006). The Federal Circuit summarily affirmed. *See Furnace Brook LLC v. Overstock.com, Inc.*, 230 Fed. Appx. 984 (Fed. Cir. 2007).

That, however, is not the end of the story. Although Overstock demonstrated a willingness to defend itself rather than simply knuckling under and taking a license on the grounds that it cost less than the litigation, that has not prevented other "non-practicing entities" from suing Overstock for alleged infringement based on other aspects of the operation of its web site, including a recent suit concerning U.S. Patent No. 6,330,592 B1 ("Method, Memory, Product, and Code for Displaying Pre-Customized Content Associated with Visitor Data"). Likewise, although the district court and the Federal Circuit readily concluded in 2006-2007 that Furnace Brook's patent had nothing to do with the Internet, that has not prevented Furnace Brook from suing – and settling with – other Internet retailers in 2008-2009 for allegedly infringing the '832 Patent. *See* Complaint (Doc. No. 1), *Furnace Brook LLC v. Orbitz, LLC*, Case No. 08-cv-1851 (N.D. Ill. Apr. 1, 2008); Complaint

(Doc. No. 1) *Furnace Brook LLC v. Anna's Linen Co.*, Case No. 08-cv-2121 (N.D. Ill. Apr. 14, 2008); Complaint (Doc. No. 1), *Furnace Brook LLC v. Playboy Enters., Inc.*, Case No. 08-cv-4656 (N.D. Ill. Aug. 15, 2008); Complaint (Doc. No. 1), *Furnace Brook LLC v. Walgreen Co., et al.*, Case No. 09-cv-862 (N.D. Ill. Feb. 11, 2009); Complaint (Doc. No. 1), *Furnace Brook LLC v. Aeropostale, Inc., et al.*, Case No. 09-cv-4310 (N.D. Ill. July 17, 2009). With the cost of settlement substantially less than the cost of winning, few companies are willing to obtain the Pyrrhic victory achieved by Overstock. Thus, rather than drawing lines in the sand, companies are building sand castles to keep out the sea if they choose to contest lawsuits asserting business method patents instead of settling and taking a license.

Even settlement does not bring certainty because another (or even the same) plaintiff can bring suit under one of the other 11,000 similar or overlapping patents allegedly covering the Internet, asserting that they own the rights to some slightly different method of operating a web site. Unlike inventors who practice what they invent, and license their technology for others to use, "non-practicing entities" do not provide the same kind of indemnification to those who take licenses from them because their business model is not developing and selling technology, but rather, buying up and litigating patents. *Cf. Taurus IP, LLC v. DaimlerChrysler Corp.,* 559 F. Supp. 2d 947, 958 (W.D. Wis. 2008) (describing pattern of "non-practicing entities" owned by same principal filing repeated lawsuits against the same defendants, recovering approximately $72.3 million in license fees in 100 separate settlements). To a "non-practicing entity," the willingness of an Internet retailer to settle early is not the end of litigation, but an invitation to the next suit.

In this environment, it is scarcely surprising, according to PACER, that Amazon.com has been sued for patent infringement 131 times, and that other companies with large Internet sales of products one does not ordinarily associate with patent infringement have been repeatedly sued for patent infringement, such as Victoria's Secret (lingerie, 29 patent suits) and Saks Fifth Avenue (men's and women's fashion, 27 patent suits). Virtually every one of these lawsuits has settled. Indeed, since business method patents almost never concern a company's core business, and thus are not worth millions of dollars to contest as a drug patent might be for a drug manufacturer whose signature drug is targeted by a competitor, virtually all such lawsuits settle so long as the license fee is less than the multimillion dollar cost of litigation. Accordingly, Internet retailers collectively spend hundreds of millions of dollars on patent settlements that would be much better spent on innovation, job creation, and job retention, and some or all of this cost gets passed on to the consumer in the form of higher prices – a tax on e-commerce that benefits the few at the expense of the many. A result further removed from the goals of the United States patent laws is hard to imagine.

*   *   *

"[S]ometimes *too much* patent protection can impede rather than 'promote the Progress of Science and useful Arts[.]' " *Labs. Corp. of Am. Holdings v. Metabolite Lab., Inc.*, 548 U.S. 124, 126 (2006) (Breyer, J., dissenting from dismissal of certiorari as improvidently granted) (brackets added, emphasis in original, and quoting Patent Clause). The confluence of the expanding Internet and burgeoning business method patents following *State Street* confirms the correctness of that observation. Far from promoting the progress of science or the useful arts, such patents impede innovation "by forcing researchers to avoid the use of potentially patented ideas, by leading them to conduct costly and time-consuming searches of existing or pending patents, by requiring complex licensing arrangements, and by raising the costs of using the patented information, sometimes prohibitively so." *Id.* at 127. Ultimately, consumers pay the price through increased costs of products sold on the Internet and through decreased capital available to innovate and improve Internet web sites.

The Federal Circuit properly concluded that the Petitioners' purported invention was not patentable. As a practical matter, however, the Federal Circuit's articulation of the limits on business method patents – requiring a process to be tied to a particular machine or apparatus or to transform a particular article into a different state or being, *see Bilski*, 545 F.3d at 961 – will provide only cold comfort to most Internet retailers sued by "non-practicing entities" who are interested in litigation, not innovation. To restore the "careful balance" between innovation and competition that "the federal patent laws . . . embod[y]," *Bonito Boats, Inc. v. Thunder Craft Boats, Inc.*, 489 U.S. 141, 146 (1989) (ellipsis and brackets added), the Court should not only affirm the judgment below, but do so through a rule that cuts off business method patents at the source, making plain that such methods are not patentable.

CONCLUSION

Based upon the foregoing, the Court should affirm the judgment.

Respectfully submitted,

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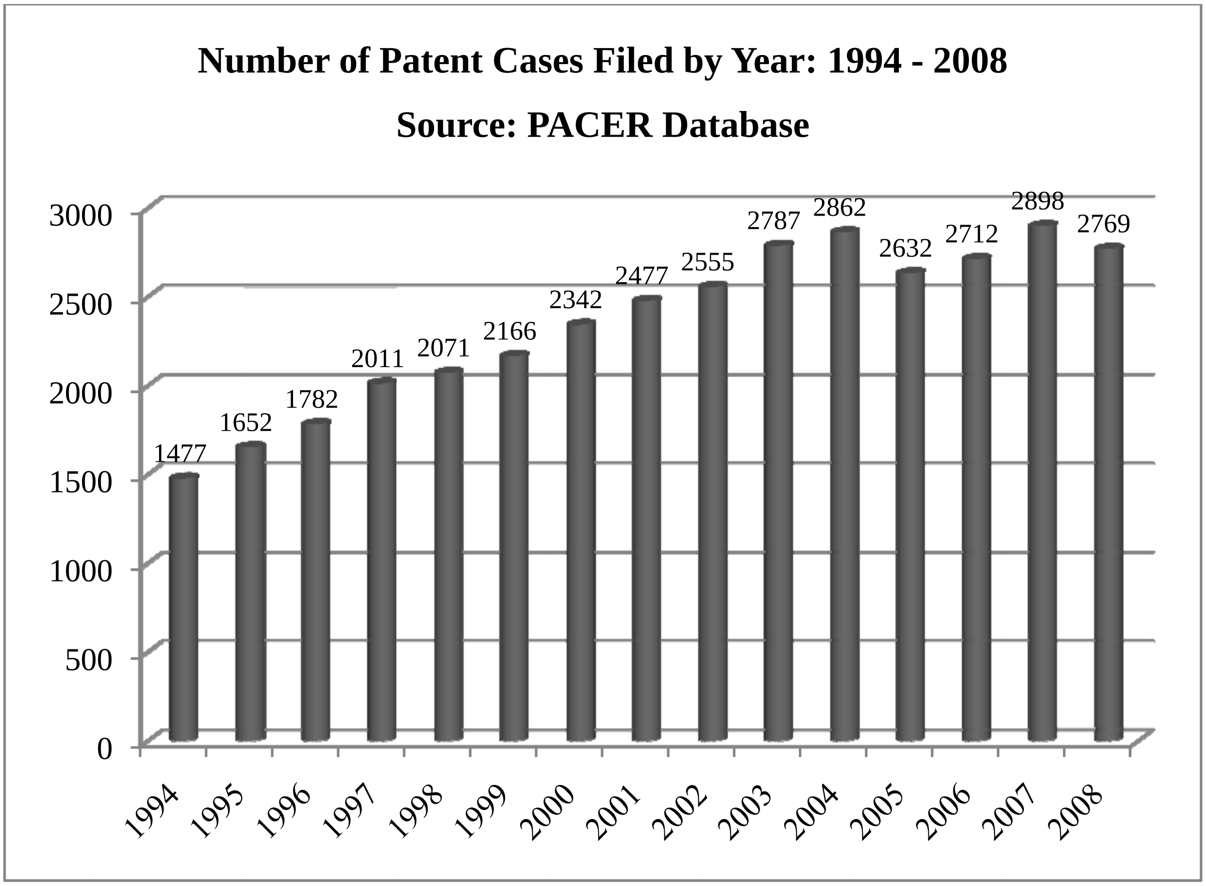
Number of Patent Cases Filed by Year: 1994 - 2008
Source: PACER Database
3000
2500
2000
1500
1000
500
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1477
1652
1782
2011
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2342
2477
2555
2787
2862
2632
2712
2898
2769
1994
1995
1996
1997
1998
1999
2000
2001
2002
2003
2004
2005
2006
2007
2008

Figure 1

Number of Patent Cases Filed by Jurisdiction: 1994 - 2008

Source: PACER Database

Year	E.D. Tex.	S.D.N.Y.	N.D. Cal.	C.D. Cal.	D. Del.	N.D. Ill.	W.D. Wis.
1994	6	60	83	147	33	86	17
1995	5	65	108	130	59	92	19
1996	9	80	115	162	49	126	20
1997	10	76	153	166	62	115	27
1998	19	67	158	193	89	113	21
1999	13	87	153	227	84	136	17
2000	20	102	156	268	98	148	16
2001	30	142	145	267	139	134	19
2002	32	105	197	247	117	186	16
2003	56	128	171	404	137	144	26
2004	106	149	176	292	147	168	33
2005	157	133	184	248	126	144	19
2006	259	119	148	272	146	131	23
2007	368	106	135	334	164	143	50
2008	316	117	166	214	173	150	43
Total	**1,406**	**1,536**	**2,248**	**3,571**	**1,623**	**2,016**	**366**
Average	**94**	**102**	**150**	**238**	**108**	**134**	**24**
Post - 2002 Average	**210**	**125**	**163**	**294**	**149**	**147**	**32**

Figure 2