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Fee Shifting in Patent Litigation

MARK LIANG[†]

BRIAN BERLINER[†]

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[†] Mark Liang is an associate at O'Melveny & Myers LLP in the Intellectual Property and Technology Litigation group. Brian Berliner is a partner at O'Melveny & Myers LLP in the Intellectual Property and Technology Litigation group. The authors would like to thank the librarians at O'Melveny for their help with research, particularly Martha Cocker and Catherine Lam. The authors would also like to thank Lex Machina for providing useful statistics for this Article. The views expressed in this Article are those of the authors alone, and do not represent the views of O'Melveny & Myers LLP.

ABSTRACT

The past decade has seen rapid growth in the number and cost of patent cases litigated in U.S. federal courts. Much of this increase has been caused by plaintiffs that are non-practicing entities (NPEs). To reduce NPE-initiated patent litigation, Congress is now considering proposals that would adopt fee shifting in patent cases as the default rule. This changes the current default rule under 35 U.S.C. § 285 of only shifting fees in “exceptional cases.” This Article concludes that because the merits and outcomes of patent cases are so uncertain, adopting fee shifting as a default rule would lead to undesirable consequences while largely failing to reduce patent litigation. This Article proposes that fee shifting should instead be applied more liberally under § 285 to cases where the merits are clear.

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I. INTRODUCTION

Patent litigation has boomed in the past decade. In 2000, 2296 patent cases were filed across all federal district courts.¹ By 2012, that number had more than doubled to 5422.² Measuring by case count, patent litigation today forms a substantial share of the federal caseload, particularly in a few districts like the Eastern District of Texas and the District of Delaware. Looking at the judicial resources expended compared to other cases, patent litigation takes up an even greater share of federal caseloads given the size and complexity of patent cases. Much of the increase in patent litigation can be attributed to non-practicing entities (NPEs), colloquially known as “patent trolls.”³ In 2012, NPEs filed 62 percent of all patent cases.⁴

¹ *Database on Number of Patent Cases Filed in 2000*, LEX MACHINA, <https://lexmachina.com> (last visited May 15, 2013) (follow “Cases” tab; select “Patent” under “Case Types” category; select “2000-01-01” under “From” and “2000-12-31” under “To,” which is all under the “Filed on” category; then click “Refine Search”).

² *Database on Number of Patent Cases Filed in 2012*, LEX MACHINA <https://lexmachina.com> (last visited May 15, 2013) (follow “Cases” tab; select “Patent” under “Case Types” category; select “2012-01-01” under “From” and “2012-12-31” under “To,” which is all under the “Filed on” category; then click “Refine Search”).

³ *What is an NPE?*, PATENT FREEDOM, <https://www.patentfreedom.com/about-npes/background> (last visited Nov. 14, 2013).

⁴ Colleen Chien, *Patent Trolls by the Numbers*, PATENTLY-O BLOG, (Mar. 14, 2013, 6:31 AM), <http://www.patentlyo.com/patent/2013/03/chien-patent-trolls.html>.

These trends have been noted by practitioners, industry, and policymakers.⁵ Although the boom in patent litigation has made patent lawyers and others in the patent litigation business happy, it has also burdened the judiciary and companies defending against patent suits.

In response, Congress is currently considering four pieces of legislation to reduce patent litigation: (1) H.R. 845, the “SHIELD Act of 2013”; (2) S. 1013, the “Patent Abuse Reduction Act”; (3) H.R. 3309, the “Innovation Act”; and (4) S. 1612, the “Patent Litigation Integrity Act.”⁶ These proposals try to reduce patent litigation by adopting “loser-pays” fee shifting, also known as the “British Rule” because of its use in Britain’s judicial system. But fee shifting is not the current default rule in patent litigation in America. In patent cases today under 35 U.S.C. § 285, attorneys’ fees are only

⁵ Sam Gustin, *Viewpoint: Obama’s ‘Patent Troll’ Reform: Why Everyone Should Care*, TIME (June 8, 2013), available at <http://business.time.com/2013/06/08/viewpoint-obamas-patent-troll-reform-why-everyone-should-care> (“Patent trolls ‘don’t actually produce anything themselves,’ Obama said in February. ‘They’re just trying to essentially leverage and hijack somebody else’s idea and see if they can extort some money out of them.’”).

⁶ See Saving High-Tech Innovators from Egregious Legal Disputes Act of 2013 (“SHIELD Act of 2013”), H.R. 845, 113th Cong. (1st Sess. 2013), available at <http://www.gpo.gov/fdsys/pkg/BILLS-113hr845ih/pdf/BILLS-113hr845ih.pdf>; Patent Abuse Reduction Act of 2013, S. 1013, 113th Cong. (1st Sess. 2013), available at <http://www.gpo.gov/fdsys/pkg/BILLS-113s1013is/pdf/BILLS-113s1013is.pdf>; Innovation Act, H.R. 3309, 113th Cong. (1st Sess. 2013), available at <http://www.gpo.gov/fdsys/pkg/BILLS-113hr3309ih/pdf/BILLS-113hr3309ih.pdf>; Patent Litigation Integrity Act of 2013, S. 1612, 113th Cong. (1st Sess. 2013), available at <http://www.gpo.gov/fdsys/pkg/BILLS-113s1612is/pdf/BILLS-113s1612is.pdf>.

shifted in “exceptional cases,” which are very rare.⁷ Thus, in nearly all cases, courts follow the “American Rule,” where each party bears its own attorneys’ fees, which can be substantial. Parties in a mid-sized patent case can rack up \$2 to 5 million in attorneys’ fees,⁸ while larger cases can cost each side over \$10 million.⁹ By comparison, between 2006 and 2011, the median damages award was \$4 million.¹⁰

The thinking behind Congress’ current efforts is that raising the stakes in patent litigation may incentivize potential plaintiffs to either not sue or settle before trial if they do. Faced with the possibility of being on the hook for defendants’ hefty fees, a party will not initiate or continue pursuing litigation unless its case has sufficient merit. But the literature on fee shifting in other litigation contexts is equivocal as to its effects on the number and cost of cases filed.¹¹ Further, patent litigation has unique characteristics, such as the high uncertainty of outcomes,¹² which affect the fee shifting calculus.

⁷ 35 U.S.C. § 285 (1952).

⁸ Authors’ estimate based on their professional experience.

⁹ C. Erik Hawes & James L. Beebe, *Fee-Shifting Under Rule 11 and 35 USC § 285 – Not Just “Belt and Suspenders”?*, 26 INTELL. PROP. L. NEWSL., 1, 1 (2008).

¹⁰ PRICEWATERHOUSECOOPERS, 2012 PATENT LITIGATION STUDY: LITIGATION CONTINUES TO RISE AMID GROWING AWARENESS OF PATENT VALUE 5 (2012), available at <http://http://www.pwc.com/us/en/forensic-services/publications/2012-patent-litigation-study.jhtml>.

¹¹ See, e.g., Avery W. Katz & Chris W. Sanchirico, *Fee Shifting in Litigation: Survey and Assessment*, 13-16 (Univ. Pa. Law Sch., Inst. for Law & Econ., Research Paper No. 10-30, 2010), available at <http://ssrn.com/abstract=1714089> (citing other studies on fee shifting’s effects).

¹² David L. Schwartz, *The Rise of Contingent Fee Representation in Patent Litigation*, 64 ALA. L. REV 335, 349 (2012).

This Article considers the impact that fee shifting may have on patent cases, and whether it would reduce the volume and cost of patent litigation. Section II considers the goals that a shifting system for patent litigation should achieve. Section III presents an algebraic model to assess the impact of fee shifting on litigation behavior. Section IV evaluates the results of the current default rule, which only awards fees in “exceptional cases.” Section V assesses the likely impact of various alternative fee-shifting rules. The Article concludes that fee shifting might not reduce the number of patent cases and would not drive down the cost of cases that are filed. Given its ambiguous effects and the uncertain outcomes of patent cases, fee shifting should not be adopted as a default rule. Instead, to discourage frivolous patent cases, fee shifting should be used more liberally under § 285 in cases where the merits are clear.

II. GOALS FOR A FEE SHIFTING SYSTEM FOR PATENT LITIGATION

Before discussing whether the British Rule or some other fee shifting system should be adopted, the goals for any fee shifting system should be defined. For any type of litigation generally, a fee shifting system should try to achieve the following goals:¹³

¹³ Other articles have described the same goals for fee shifting. See Jonathan Fischbach & Michael Fischbach, *Rethinking Optimality in Tort Litigation: The Promise of Reverse Cost-Shifting*, 19 *BYU J. PUB. L.* 317, 320-21 (2005); Marie Gryphon, *Assessing the Effects of a “Loser Pays” Rule on the American Legal System: An Economic Analysis and Proposal for Reform*, 8 *RUTGERS J.L. & PUB. POL’Y* 567, 570 (2011); Thomas D.

1. Promote compliance with the law: any fee shifting system should discourage parties from violating legal rules. In the context of patent law, this means individuals and companies should avoid selling, making, or using any product or process that practices the claims of a valid patent. It also means that those acquiring patents should avoid claiming subject matter that is known or obvious based on prior art.
2. “Make whole” the prevailing party: any fee shifting system should restore the prevailing party to its position before the alleged legal violation occurred that caused the plaintiff to file suit. If the plaintiff prevails, it should recover damages and fees expended on litigation, restoring it to its pre-violation and pre-suit position. Conversely, if the defendant prevails, it should recover fees expended on litigation, restoring it to its pre-suit position. This goal favors the British Rule.
3. Minimize transaction costs: any fee shifting system should reduce the frequency and cost of patent litigation. A fee shifting system should discourage patentees from filing lawsuits, and encourage them to use cheaper non-litigation options, such as licensing negotiations, to enforce their patents if they have meritorious claims. If a patentee nevertheless files suit, a fee shifting system should

Rowe, Jr., *The Legal Theory of Attorney Fee Shifting: A Critical Overview*, 1982 DUKE L.J. 651, 653-66 (1982).

then encourage the patentee-plaintiff and defendant to settle early to minimize litigation costs.

4. Filter out frivolous cases: any fee shifting system should discourage low-merit suits, while encouraging high-merit suits. Discouraging low-merit suits in patent litigation means discouraging cases that involve frivolous infringement claims or weak patents that should never have issued.

Goal one, promoting compliance with the law, is difficult to achieve as a practical matter in patent cases because they involve complex technologies and have uncertain merits and outcomes. Because two commercial entities may unintentionally adopt similar technologies while also having imperfect knowledge of each other's patenting activities, avoiding infringement is not feasible in many cases and requires expertise and resources that even some large companies do not have. It is unclear then whether a fee shifting system could materially affect compliance with the patent laws.

Goal two, making the prevailing party "whole," is also less applicable to patent cases. The technical and legal complexity of patent cases makes it difficult to decide who is the prevailing party that should be made whole. Many cases are close calls, and patent laws are relatively volatile as compared to other areas of law.¹⁴ And the unfortunate truth of the matter is that patent cases are often decided wrongly by

¹⁴ See S. Jay Plager, *The Federal Circuit as an Institution: On Uncertainty and Policy Levers*, 43 LOY. L.A. L. REV. 749 (2010); Kelly C. Mullally, *Legal (Un)Certainty, Legal Process, and Patent Law*, 43 LOY. L.A. L. REV. 1109 (2010).

judges and juries who lack sufficient understanding of the technologies and patent laws at issue. In fact, the Federal Circuit reverses about 30-40 percent of the cases appealed to it.¹⁵ The “make whole” argument should not, therefore, be given much weight in deciding among fee shifting systems.

On the other hand, goals three and four above should be top policy priorities. Patent litigation has boomed over the past decade. Figure 1 below shows the increase in patent cases filed by year, with 2296 filed in the year 2000 to 5422 filed in the year 2012.¹⁶ (Some of the increase from 2011 and 2012 can be attributed to the new joinder provisions under the America Invents Act of 2011).¹⁷

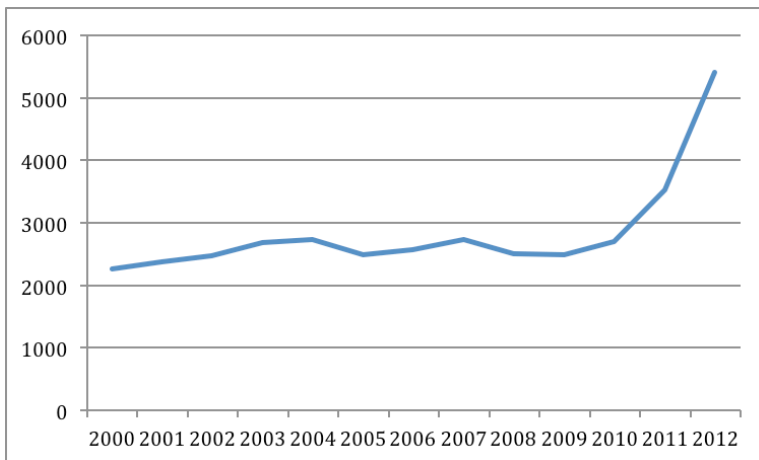


Figure 1: Patent Cases Filed By Year (2000-2012)

¹⁵ Schwartz, *supra* note 12, at 349.

¹⁶ *Database on Number of Patent Cases Filed in 2000*, *supra* note 1; *Database on Number of Patent Cases Filed in 2012*, *supra* note 2.

¹⁷ 35 U.S.C. § 299 (2011).

The cost of patent litigation often runs into the millions of dollars.¹⁸ Both plaintiffs and defendants hire expensive law firms to represent them, and technical experts are typically hired by both sides, which further adds to each side's costs.¹⁹ And then there are discovery costs. Patent cases often result in the production of tens of thousands of dense documents – such as emails, technical specifications, user manuals, source code, and financial spreadsheets – which must be reviewed and produced by one side's attorneys, and then re-reviewed by the other side's attorneys.²⁰ Unlike other forms of litigation, patent litigation is rarely dismissed at the pleading stage.²¹ Even in the simplest cases, a pre-trial resolution is rarely achieved before claim construction or substantial fact and expert discovery has occurred.²²

A 2009 survey done by the American Intellectual Property Law Association puts the median cost of patent cases, by the end of discovery, at \$2.5 million for cases where \$1 to 25 million was at stake.²³ Adding up all costs in patent cases today, even a mid-sized patent case can cost a party \$2 to 5 million in attorneys' fees, while larger cases can cost more than \$10 million.²⁴ As a result, attorneys' fees can exceed the damages ultimately awarded – between 2006 and 2011, the median damages award was \$4 million.²⁵

¹⁸ Hawes & Beebe, *supra* note 9, at 1.

¹⁹ Based on the authors' professional experience.

²⁰ Based on the authors' professional experience.

²¹ Brief for Defendant-Cross Appellant, *Icon Health & Fitness, Inc. v. Octane Fitness, LLC*, 496 Fed. Appx. 57 (Fed. Cir. 2012) (Nos. 2011-1521, 2011-1636), 2012 WL 481412, at *67-68.

²² *Id.* at *68.

²³ *Id.* at *67.

²⁴ Hawes & Beebe, *supra* note 9, at 1.

²⁵ PRICEWATERHOUSECOOPERS, *supra* note 10, at 5.

NPEs are another feature unique to patent litigation that impacts the fee shifting analysis. NPEs are companies that hold patents, but do not exploit them commercially through manufacture or sale of products.²⁶ Instead, NPEs generate revenue from patents through licensing and litigation.²⁷ NPEs are a relatively recent phenomenon, but studies suggest that NPEs now initiate most patent cases in district courts.²⁸ For example, a study by RPX Corp. found that the percentage of cases filed by NPEs grew from 19 percent in 2006 to 62 percent in 2012.²⁹ Another study found that an NPE's share of cases grew from 25 percent in 2007 to 59 percent in 2012.³⁰ That study also suggests that NPEs are now actively applying for patents as the original assignee and then using the patents promptly after issuance for licensing and litigation.³¹ In view of the above, many regard NPEs as a burden on America's patent system.³² Accordingly, any fee shifting system should try to discourage NPE litigation.

²⁶ Mark Liang, "The Aftermath of TS Tech: The End of Forum Shopping in Patent Litigation and Implications for Non-Practicing Entities," 19 TEX. INTELL. PROP. L.J. 29, 32-37 (2010).

²⁷ *Id.*

²⁸ See Chien, *supra* note 4. See Robin Feldman et al., *The AIA 500 Expanded: Effects of Patent Monetization Entities*, 17 UCLA J.L. & TECH. (forthcoming 2013) (manuscript at 7), available at <http://ssrn.com/abstract=2247195>.

²⁹ Chien, *supra* note 4.

³⁰ See Feldman, *supra* note 28, at 7.

³¹ *Id.* at 77-78.

³² See, e.g., The Editorial Board, *Fighting 'Patent Trolls,'* N.Y. TIMES, June 5, 2013, http://www.nytimes.com/2013/06/06/opinion/obamas-promising-reforms-to-fight-patent-trolls.html?_r=0.

A study on NPE characteristics also suggests that NPE-filed patent cases have lower merit but higher damages as compared to cases filed by non-NPEs.³³ PricewaterhouseCoopers's (PwC) 2012 Patent Litigation Study found that in cases reaching a final judgment³⁴ between 1995 and 2011, NPE plaintiffs won 23.3 percent of those cases versus 33.8 percent for non-NPE plaintiffs.³⁵ The lower win rate suggests NPEs bring lower-merit cases. That same study found, however, that when NPEs do prevail on infringement, they tend to win larger damage awards – between 2006 and 2011, the median NPE damages award was \$6.9 million, far higher than the median non-NPE award of \$3.7 million.³⁶

Another unique aspect of NPE plaintiffs is their frequent use of contingent fee arrangements. In its most basic form, a contingent fee arrangement gives the plaintiff's attorney a percentage of any award or settlement that it wins on behalf of the plaintiff. This percentage usually varies from 28-40 percent.³⁷ In exchange, the plaintiff's attorney is not paid on an hourly basis, and in fact, is not paid at all unless the case ends with a monetary gain for the plaintiff. Based on anecdotal experience, contingent fee arrangements are used in a significant percentage of NPE-filed cases, and are becoming more common.

For NPEs, contingent fee arrangements make a great deal of sense. In theory and under the American Rule of no fee

³³ See PRICEWATERHOUSECOOPERS, *supra* note 10, at 12.

³⁴ Based on this Article's research on plaintiffs' win rates, the PwC win rates most likely exclude default and consent judgments for plaintiffs.

³⁵ PRICEWATERHOUSECOOPERS, *supra* note 10, at 12.

³⁶ *Id.* at 7.

³⁷ Schwartz, *supra* note 12, at 360.

shifting, contingent fee arrangements impose no downside costs to filing suit, which aligns with an NPE's main objective to maximize returns on its patent holdings. While any potential award is reduced by the attorney's percentage take, damages awards in patent cases are highly variable and unpredictable, and PwC's findings suggest that NPEs pursue higher-damages cases.³⁸ And an attorney employed on contingency, rather than hourly billing, has a stronger incentive to maximize damages. Thus, a fee shifting system that tries to reduce NPE litigation must account for contingency arrangements.

III. MODELING LITIGATION BEHAVIOR

In the 1970s, a group of University of Chicago academics – John Gould, William Landes, and Richard Posner – developed a mathematical model for analyzing rational litigants' behavior based on their perceptions of the case's merits, costs, and damages at issue under the American Rule with no fee shifting.³⁹ Their model was adapted by others, including Steven Shavell, to analyze behavior under the British Rule with two-way fee shifting.⁴⁰ More recently, academics have developed more complex “multi-phase” models that evaluate litigant behavior over the course of a case.⁴¹ This

³⁸ PRICEWATERHOUSECOOPERS, *supra* note 10, at 7.

³⁹ See generally John P. Gould, *The Economics of Legal Conflicts*, 2 J. LEGAL STUD. 279 (1973); William M. Landes, *An Economic Analysis of the Courts*, 14 J.L. & ECON. 61 (1971); Richard A. Posner, *An Economic Approach to Legal Procedure and Judicial Administration*, 2 J. LEGAL STUD. 399 (1973).

⁴⁰ Steven Shavell, *Suit and Settlement vs. Trial: A Theoretical Analysis Under Alternative Methods for the Allocation of Legal Costs*, 5-6 (Nat'l Bureau of Econ. Research, Working Paper No. 662, 1981), available at <http://www.nber.org/papers/w0662>.

⁴¹ See, e.g., Katz & Sanchirico, *supra* note 11.

Article uses and adapts the basic models developed by Gould, Landes, Posner, and Shavell to evaluate litigant behavior under various fee-shifting systems.

The following variables are defined under the basic models:

- A = The amount at stake in the case, or the amount that plaintiff claims to win;
- C_p = Plaintiff's cost of litigation, including attorneys' fees;
- C_d = Defendant's cost of litigation, including attorneys' fees;
- P_p = Plaintiff's self-perceived chance of winning (percentage);
- P_d = Defendant's perceived chance that plaintiff will win (percentage);
- L = attorney's percentage winnings in contingency arrangements; typically 28-40 percent.

The derivation of all mathematical expressions in this Article is explained in the footnotes associated with each expression. In this section, the derivation is also explained in the main text. In general, the plaintiff will only file suit when its expected award is greater than the cost of litigation.⁴² So,

⁴² Keith N. Hylton, *Fee Shifting and Incentives to Comply with the Law*, 46 VAND. L. REV. 1069, 1078 (1993).

under the American Rule with no fee shifting and traditional hourly billing, a plaintiff will only sue when the following inequality is true:

$$P_p A > C_p \quad (1)^{43}$$

In general, the plaintiff and defendant will only settle when the plaintiff's minimum settlement demand is less than the defendant's maximum settlement offer.⁴⁴ At the start of litigation, the plaintiff's minimum settlement demand is its expected reward, less the cost of litigation.⁴⁵ The defendant's maximum settlement offer is its litigation fees, plus the amount that it expects the plaintiff to win in the case.⁴⁶ So, under the American Rule with no fee shifting and traditional hourly billing, the plaintiff and defendant will only settle when the following inequality is true:

$$P_p A - C_p < C_d + P_d A$$

Manipulating the above expression so that all expected award (or A) terms are on the left side of the inequality and all expected cost (or C) terms are on the right side, the plaintiff and defendant will only settle when the following inequality is true:

$$(P_p - P_d)A < C_p + C_d \quad (2)^{47}$$

⁴³ *Id.* In this derivation, the plaintiff will only sue if its expected award is greater than its cost of litigation.

⁴⁴ *Id.*

⁴⁵ *Id.*

⁴⁶ *Id.*

⁴⁷ *Id.* In this derivation, the basic premise is that settlement only occurs when the plaintiff's minimum settlement demand is less than the

Under the British Rule, the plaintiff's expected winnings are still equal to P_pA , but its expected litigation fees are different. If the plaintiff wins, it incurs no fees; if the plaintiff loses, it incurs both parties' fees, or $C_p + C_d$.⁴⁸ The plaintiff expects to lose with probability $(1 - P_p)$. So, under the British Rule and traditional hourly billing, the plaintiff will only file suit when the following inequality is true:

$$P_pA > (1 - P_p)(C_p + C_d) \quad (3)^{49}$$

The British Rule also affects the parties' settlement demands and offers. The plaintiff's minimum settlement demand is again its expected award, less expected litigation fees, but its expected litigation fees have now changed as shown above in expression (3). Similarly, the defendant's expected litigation fees are affected by fee shifting – it only pays fees if it loses, but it must pay the fees of both parties. So,

defendant's maximum settlement offer. Within this range, settlement is possible.

The plaintiff's minimum demand at the beginning of litigation is its expected award, less its cost of litigation. In other words, when the plaintiff files a lawsuit, it expects to win its expected reward, less costs. Therefore, when settling a case at the start, the plaintiff will demand at least this amount.

The plaintiff's minimum demand is then: $P_pA - C_p$

The defendant's maximum offer at the beginning of litigation is going to be its expected litigation costs, plus the amount that it thinks that the plaintiff is expected to win.

Defendant's maximum offer is then: $C_d + P_dA$

So, for settlement to occur, we require: $P_pA - C_p < C_d + P_dA$ (A)

Manipulating expression (A): $(P_p - P_d)A < C_p + C_d$

⁴⁸ *Id.*

⁴⁹ *Id.* In this derivation, the right side of the equation represents the plaintiff's costs in litigation. The plaintiff only incurs costs if it loses; these costs are equal to its expected probability of losing, $(1 - P_p)$, times the fees of both sides, $(C_p + C_d)$.

under the British Rule and traditional hourly billing, the plaintiff and defendant will only settle when the following inequality is true:

$$P_p A - (1 - P_p)(C_p + C_d) < P_d A + P_d(C_p + C_d)$$

Manipulating the above expression so that all expected award (or A) terms are on the left side of the inequality and all expected cost (or C) terms are on the right side, the plaintiff and defendant will only settle when the following inequality is true:

$$(P_p - P_d)A < (1 + P_d - P_p)(C_p + C_d) \quad (4)^{50}$$

Comparing expressions (1) to (3), with hourly billing, the British Rule, as compared to the American Rule, encourages the plaintiff to file suit in cases where the plaintiff is optimistic because the value of P_p is larger, which decreases the right side of the inequality (3) and increases the left side. But if the plaintiff is not optimistic, the British Rule discourages filing relative to the American Rule. If one assumes that the plaintiff's optimism reflects the merits of its

⁵⁰ *Id.* at 1079. In this derivation, as stated in note 47, settlement only occurs if the plaintiff's minimum settlement demand is less than the defendant's maximum settlement offer. In general, the plaintiff's minimum settlement demand is its expected winnings, less its expected litigation costs. In general, the defendant's maximum settlement offer is its expected litigation costs, plus what it thinks the plaintiff's expected winnings are.

So, our starting expression for settlement is:

$$P_p A - (1 - P_p)(C_p + C_d) < P_d A + P_d(C_p + C_d) \quad (B)$$

Manipulating expression (B): $(P_p - P_d)A < (1 + P_d - P_p)(C_p + C_d)$

case, then the British Rule discourages low-merit cases while encouraging high-merit cases.⁵¹

Comparing expressions (2) to (4), the effect of the British Rule on settlements is more ambiguous. In cases where the plaintiff's perception of its likelihood of victory is higher than the defendant's (*i.e.*, $P_p > P_d$), the British Rule actually discourages settlements because the right side of the inequality representing litigation costs is weighed down while the left side of the inequality increases. Intuitively, the British Rule also raises the stakes of the case, which makes the plaintiff less likely to want to settle when it is more optimistic about its chances than the defendant. The effect on settlement is the opposite when the defendant is more optimistic about the plaintiff's chances than the plaintiff – in this scenario, a settlement is more likely under the British Rule than the American Rule. In most cases, however, the plaintiff filing suit is more optimistic than the defendant about the likelihood that the case will end favorably for the plaintiff, or $P_p > P_d$. Therefore, the *British Rule usually discourages settlement as compared to the American Rule*.⁵²

The litigation model used when the plaintiff uses a contingent fee arrangement is presented below. This model assumes that if the defendant loses, it must pay the plaintiff's fees, P_p , under a lodestar calculation, even though the plaintiff is not being billed by the hour. This model also assumes that the plaintiff's contingency arrangement gives the attorney a straight percentage take, L , of any award to the plaintiff. As a result, under the American Rule with no fee shifting, the plaintiff's expected award is reduced by a factor of L without

⁵¹ *Id.* at 1078.

⁵² *Id.* at 1079.

incurring any litigation fees by filing suit. Under the American Rule then, with no fee shifting and contingent fee billing, the plaintiff will only file suit when the following inequality is true:

$$P_p A(I - L) > 0 \quad (5)^{53}$$

Because the plaintiff incurs no litigation fees under a contingent fee arrangement and the American Rule, its minimum settlement demand will simply be its expected award, $P_p A(I - L)$. Contingency does not affect the defendant's litigation fees or its perception of the plaintiff's likelihood of success. Thus, the defendant's maximum settlement offer is the same as with hourly billing and the American Rule. Under the American Rule with no fee shifting and contingent fee billing, the plaintiff and defendant will only settle when the following inequality is true:

$$P_p A(I - L) < C_d + P_d A$$

Manipulating the above expression so that all expected award (or A) terms are on the left side of the inequality and all expected cost (or C) terms are on the right side, the plaintiff and defendant will only settle when the following inequality is true:

$$[P_p(I - L) - P_d]A < C_d \quad (6)^{54}$$

⁵³ In this derivation, the plaintiff's winnings under the American Rule will be lowered by a factor of $(I - L)$, given that L percent of its winnings go to its attorneys.

⁵⁴ In this derivation, the starting expression is:

$$P_p A(I - L) < C_d + P_d A \quad (C)$$

With the contingent fee arrangement and the British Rule, the plaintiff potentially has to pay the defendant's attorneys' fees, C_d , if the plaintiff loses. So, under the British Rule with no fee shifting and contingent fee billing, the plaintiff will only file suit when the following inequality is true:

$$P_p A(1 - L) > (1 - P_p)C_d \quad (7)^{55}$$

The plaintiff's minimum settlement demand is reduced by the right side of expression (7) above, which corresponds to how much the plaintiff expects to pay in litigation fees. Contingency does not affect the defendant's litigation fees or its perception of the plaintiff's likelihood of success. Thus, the defendant's maximum settlement offer is the same as with hourly billing and the British Rule. So, under the British Rule with no fee shifting and contingent fee billing, the plaintiff and defendant will only settle when the following inequality is true:

$$P_p A(1 - L) - (1 - P_p)C_d < P_d A + P_d(C_p + C_d)$$

For the plaintiff side of the equation (left side), there are no costs to deduct from the expected winnings. Thus, the plaintiff will demand at least its expected winnings, less the attorneys' percentage take.

For the defendant side of the equation (right side), the costs of litigation are the same as under the American Rule, since in theory the plaintiff's contingency arrangement does not affect the defendant's costs of litigation or the defendant's perception of the plaintiff's odds of victory.

Manipulating expression (C): $[P_p(1 - L) - P_d]A < C_d$

⁵⁵ In this derivation, the plaintiff's expected winnings under the British Rule are the same as under the American Rule, so the left side of the equation is the same. But there is now an expected potential downside cost to litigation that comes from fee shifting. The plaintiff who loses would have to pay the defendant's attorneys' fees; the probability of loss is $(1 - P_p)$, and the defendant's fees are C_d .

Manipulating the above expression so that all expected award (or A) terms are on the left side of the inequality and all expected costs (or C) terms are on the right side, the plaintiff and defendant will only settle when the following inequality is true:

$$[(P_p(1-L)-P_d]A < (1+P_d-P_p)C_d+P_dC_p \quad (8)^{56}$$

From a consideration of expression (5), it is apparent why contingent fees are favored by patent plaintiffs. In theory, there is no downside cost to filing suit under the American Rule; contingency simply lowers any potential payoff by a factor of L , the attorney's percentage take. Hence, a rational plaintiff will always file suit. In reality, there may be indirect or non-financial costs – reputation, commitment of plaintiff's resources, or threat of a countersuit – that may discourage a plaintiff from filing suit in certain cases. By contrast, expression (7) shows that the British Rule can prevent contingency plaintiffs from filing suit because there is the potential downside cost of paying defendant's fees if the

⁵⁶ In this derivation, the starting expression is:

$$P_pA(1-L) - (1-P_p)C_d < P_dA + P_d(C_p + C_d) \quad (D)$$

The left side of the expression is the plaintiff's minimum demand, which is its expected award, minus its expected cost – these two terms follow from note 54.

The defendant's maximum offer is its expectation of the plaintiff's award, P_dA , plus its expected fees in litigation, $P_d(C_p + C_d)$. If the defendant loses, which has probability P_d , it will have to pay its own attorneys' fees, C_d , and the plaintiff's, C_p , which is calculated under the lodestar method. If the plaintiff wins, which has probability P_p , it pays no fees.

Manipulating expression (D) gives us:

$$A[P_p(1-L) - P_d] < C_d - P_pC_d + P_dC_p + P_dC_d$$

plaintiff loses. The British Rule is therefore better at discouraging contingency plaintiffs from filing suit.

Comparing expression (8) to (6), with contingency, the British Rule is more likely than the American Rule to encourage settlement because the plaintiff's "fees," calculated under the lodestar method, could be shifted even though the plaintiff is not actually paying its attorney any fees. Mathematically, the right side of inequality (8) is greater in most cases than the right side of inequality (6):

$$(1 + P_d - P_p)C_d + P_d C_p > C_d$$

(Contingency, British Rule vs. American Rule)

Only in cases where the plaintiff's expectation of its victory, P_p , is much greater than the defendant's expectation of the plaintiff's victory, P_d , is the above inequality not true.

Some practical points about using the above models are worth noting:

- First, these models are single-phase, meaning that the models assume values at a single point in time just before the plaintiff files suit. A multi-phase model is more realistic (and complex) and considers changes to the parties' perceived probabilities, amount at stake, and costs as the case progresses.⁵⁷ For example, the plaintiff's optimism, claimed damages, and remaining litigation costs will change after significant case events, such as claim construction rulings and discovery.

⁵⁷ See generally Katz & Sanchirico, *supra* note 11.

- Second, P_p and P_d reflect the parties' subjective view of the merits of the case, rather than the objective merits of the case. Behavioral studies suggest that humans are overoptimistic.⁵⁸ This may be especially true for plaintiffs. In fact, under any model except contingency with the America Rule, plaintiffs would not have filed suit in the first place without sufficient optimism, P_p . Behavioral studies also suggest that humans are averse to losses.⁵⁹ For example, most people would not trade a 10 percent chance of winning \$10,000 for a 9 percent chance of losing \$10,000 of their existing savings. This suggests that the downside costs of litigation, C_p and C_d , may discourage litigation more than the above models indicate.
- Third, the two cost numbers, C_p and C_d , are high in patent cases, sometimes exceeding damages, A . This should discourage litigation and encourage settlement.
- Fourth, the two cost numbers, C_p and C_d , are also causally correlated. One party incurring costs by filing a motion, serving discovery requests, or producing documents, will cause the other party to incur costs in responding to those requests.

⁵⁸ Christine Jolls & Cass R. Sunstein, *Debiasing through Law*, 35 J. LEGAL STUD. 199, 204 (2006).

⁵⁹ Cass R. Sunstein, *Behavioral Analysis of Law*, 5-8, (Chi. Working Paper in Law & Econ. No. 046, 1997), available at http://www.law.uchicago.edu/files/files/46.CRS_.Behavioral.pdf; Cass R. Sunstein, *People Hate Losses and That Affects U.S. Budget Talks*, BLOOMBERG (Dec. 24, 2012, 6:30 PM), <http://www.bloomberg.com/news/2012-12-24/people-hate-losses-and-that-affects-u-s-budget-talks.html>.

IV. EVALUATING THE AMERICAN RULE AND § 285

A. Section 285: No Fee Shifting by Default

The default rule in litigation in U.S. federal courts is the American Rule under which both sides, win or lose, must bear their own attorneys' fees. The American Rule is codified in Fed. R. Civ. P. 54(d), which provides that "costs – *other than attorney's fees* – should be allowed to the prevailing party."⁶⁰ Thus, Rule 54(d) provides for "cost" shifting, but the costs are limited mainly to court fees and do not include attorneys' fees or other expensive fees, such as expert witness fees.⁶¹ Such "costs" are usually insignificant relative to attorneys' fees.

There are exceptions to the American Rule. In patent cases, attorneys' fees are usually pursued and shifted under 35 U.S.C. § 285, which provides: "The court in *exceptional cases* may award reasonable attorney fees to the prevailing party."⁶² Federal courts can also shift attorneys' fees using 28 U.S.C. § 1927, Fed. R. Civ. P. 11 and 37, or the court's "inherent power."⁶³ But these fee shifting provisions only apply to litigation misconduct, and the amount of fees shifted is usually tied to the misconduct, so not all of the winning party's fees are shifted onto the losing party.

⁶⁰ FED. R. CIV. P. 54(d) (emphasis added).

⁶¹ James R. Maxeiner, *Cost and Fee Allocation in Civil Procedure*, 58 AM. J. COMP. L. 195, 197 (2010).

⁶² 35 U.S.C. § 285 (2011) (emphasis added).

⁶³ Hawes & Beebe, *supra* note 9, at 16.

There is a high standard for awarding attorneys' fees under § 285. A court only awards fees if: (1) the case is exceptional; and (2) attorneys' fees are appropriate.⁶⁴ In nearly all cases found to be exceptional, thereby satisfying the first prong, a court will award fees. The "exceptional" case inquiry varies depending on whether fees are being awarded against the plaintiff or defendant. In either case, however, the party moving for fees must show that the case is exceptional with clear and convincing evidence.⁶⁵

Defendants are typically awarded attorneys' fees if they can show: (1) inequitable conduct by the plaintiff during prosecution of the asserted patent; (2) litigation misconduct by the plaintiff, such as discovery violations; or (3) the case is objectively baseless and brought in subjective bad faith.⁶⁶ Prong (3) provides an opportunity to shift fees when the plaintiff's infringement case is frivolous. But courts rarely find a case to be "frivolous"; such cases are usually limited to when the plaintiff pursued an infringement position that was absurd in light of a claim construction ruling or its own claim construction position, or was clearly contradicted by the evidence or statements by its own expert.⁶⁷

Plaintiffs are typically awarded attorneys' fees in the following circumstances: (1) default judgment against the

⁶⁴ *E.g.*, *Eon-Net LP v. Flagstar Bancorp*, 653 F.3d 1314, 1323-24 (Fed. Cir. 2011).

⁶⁵ *E.g.*, *Checkpoint Sys., Inc. v. All-Tag Sec. S.A.*, 711 F.3d 1341, 1346 (Fed. Cir. 2013).

⁶⁶ *E.g.*, *MarcTec, LLC v. Johnson & Johnson*, 664 F.3d 907, 915-16 (Fed. Cir. 2012); *Wedgetail Ltd. v. Huddleston Deluxe, Inc.*, 576 F.3d 1302, 1304-05 (Fed. Cir. 2009).

⁶⁷ *E.g.*, *MarcTec, LLC*, 664 F.3d at 915; *Phonometrics, Inc. v. Westin Hotel Co.*, 350 F.3d 1242, 1248 (Fed. Cir. 2003).

defendant; (2) litigation misconduct by the defendant; (3) willful infringement by the defendant; or (4) vexatious or bad faith litigation.⁶⁸ Section 285's use to punish willful infringement is perhaps redundant given that 35 U.S.C. § 284 already permits trebling of damages in cases of willful infringement.⁶⁹ Further, the Federal Circuit has explained that the willfulness inquiry under § 284 and the "objective baselessness" inquiry under § 285 is actually the same "objective recklessness" standard and that enhanced damages under both provisions are usually awarded hand-in-hand.⁷⁰

B. Statistical Results Under § 285

In the vast majority of patent cases, attorneys' fees are not shifted under § 285. One article states that only 1 percent of all cases that ended by pre-trial motion or trial were found to be "exceptional" under § 285.⁷¹

An investigation conducted by the authors suggests this 1 percent figure understates § 285's use, but is nevertheless correct in that fee awards are rarely awarded.⁷² Fees are only

⁶⁸ *E.g.*, *MarcTec, LLC*, 664 F.3d at 915-16; *iLOR, LLC v. Google, Inc.*, 631 F.3d 1372, 1376-77 (Fed. Cir. 2011).

⁶⁹ 35 U.S.C. § 284 (2011). *See* *Knorr-Bremse Systeme Fuer Nutzfahrzeuge GmbH v. Dana Corp.*, 383 F.3d 1337, 1342 (Fed. Cir. 2004).

⁷⁰ *iLOR, LLC*, 631 F.3d at 1377.

⁷¹ Anna Mayergoyz, Note, *Lessons from Europe on How to Tame U.S. Patent Trolls*, 42 CORNELL INT'L L.J. 241, 266 (2009).

⁷² *Database for Number of Patent Cases Where Fees Were Shifted Under § 285*, LEX MACHINA, <https://lexmachina.com> (last visited May 15, 2013) (Methodology: For district court cases, Lex Machina was used to search for all docket entries or court orders with the following search terms: (1) "285" AND "exceptional"; or (2) "285" AND "attorney's fees." These docket entries and court orders were all reviewed and sorted by whether fees were awarded to plaintiffs versus defendants. The results were filtered to be

awarded when the case ends with a judgment; they are not awarded in cases that end in settlement or voluntary dismissal. Between the year 2003 and May 15, 2013, about 3400 cases ended in a judgment.⁷³ In this time period, fees were shifted in only 208 cases under § 285.⁷⁴ Thus, fees were awarded in about 6 percent of all patent cases ending in judgment (208 of 3400 cases), or 0.6 percent of all patent cases (208 of 32,570 cases).

A review of *when* fees are awarded suggests that plaintiffs are far more likely than defendants to be awarded attorneys' fees under § 285. Plaintiffs' motions for fees under

limited to cases that reached judgment and to orders issued between 2003 and May 15, 2013 inclusive. Orders granting fees in part (e.g., partial fees) were counted as "grants." Declaratory judgment cases were not distinguished in the results and comprised less than 5 percent of the results. Cases where fees were sought or granted on the basis of attorney/litigation misconduct were not excluded. Regarding misconduct, it is assumed that misconduct is roughly equal between the plaintiffs and defendants and that the courts are not biased in favor of granting fees for/against either, so its effect would not skew the results for purposes of comparing the frequency of fee-shifting for defendants versus plaintiffs.).

⁷³ The 3400 figure is an approximation. *Database for the Number of Judgments in Patent Cases from 2003 to May 2013*, LEX MACHINA, <https://lexmachina.com> (last visited May 15, 2013) (Lex Machina collects statistics from the year 2000 to the present. Between the year 2000 and May 15, 2013, 39,712 total federal cases were filed. 32,570 cases were filed between the year 2003 and May 15, 2013. Thus, 82 percent of the cases filed between the year 2000 and May 15, 2013 were filed between the year 2003 and May 15, 2013 inclusive. The total number of judgments between the year 2000 and May 15, 2013 was 4211. Assuming that the share of cases reaching judgment from the year 2003 to May 15, 2013 is the same as from the year 2000 to May 15, 2013, then between the year 2003 and May 15, 2013, about 3400 cases reached judgment (or 82% of 4,211)).

⁷⁴ See *Database for Number of Patent Cases Where Fees Were Shifted Under § 285*, *supra* note 72.

§ 285 were granted 57 percent of the time (142 of 248 motions).⁷⁵ Defendants' motions for fees under § 285 were granted only 26 percent of the time (66 of 252 motions).⁷⁶ Assuming litigation misconduct is equally prevalent on both sides, plaintiffs' higher success rate is most likely because they often win attorneys' fees after default judgment or based on a finding of willful infringement.⁷⁷ Defendants, on the other hand, must prove specific facts showing inequitable conduct or that the plaintiff's infringement case is frivolous. Federal Circuit decisions only widen the disparity between the plaintiffs' and defendants' success rates in seeking attorneys' fees under § 285. The Federal Circuit reversed attorney fee awards to plaintiffs in 25 percent (2 of 8) cases, but reversed attorney fee awards to defendants in 46 percent (11 of 24) cases, a much higher reversal rate.⁷⁸

The imbalance of fee awards in favor of plaintiffs is all the more noteworthy when one considers that between 2000 and 2013, defendants won 59 percent of cases that reached judgment, excluding consent judgments for which attorneys'

⁷⁵ *See id.*

⁷⁶ *See id.*

⁷⁷ A review of orders found that attorneys' fees under § 285 were usually awarded to plaintiffs after they won on default judgment.

⁷⁸ *Westlaw Database of Federal Circuit Decisions (CTAF)*, WESTLAW, <http://www.westlaw.com> (last visited May 15, 2013) (Methodology: The following search term was used to find Federal Circuit decisions: ("exceptional" OR "attorney's fees") AND "285". For Federal Circuit cases, decisions on fees that were simply based on the underlying merits were excluded. For example, if an award of fees was reversed because the Federal Circuit disagreed with a finding of inequitable conduct, this was not included in the results. The results were limited to decisions between the year 2003 and May 15, 2013.).

fees are not awarded.⁷⁹ Further excluding default judgments, defendants won 71 percent of cases that reached judgment.⁸⁰ Defendants are, therefore, the “prevailing party” in the majority of cases where there is a prevailing party. One would expect then that defendants win a proportionally larger share of fee awards under § 285. But the evidence described above shows the opposite: plaintiffs won more than twice the number of fee awards as defendants.

V. ALTERNATIVES TO THE AMERICAN RULE AND § 285

This section evaluates alternatives to the current fee shifting system under § 285. Alternatives include: (1) adopting the British Rule, or two-way fee shifting; (2) one-way fee shifting in favor of defendants; (3) one-way fee shifting in favor of plaintiffs; (4) fee-shifting rules advanced by past and present legislative proposals; and (5) loosening the “exceptional case” standard under § 285.

⁷⁹ *Database of the Winning Percentage of Defendants of Patent Cases that Reach Judgment*, LEX MACHINA, <https://lexmachina.com> (last visited May 15, 2013) (Lex Machina’s database provides outcome statistics from 2000 to the present for each district court. The outcomes include number of judgments segmented by the number of judgments won by plaintiff or defendant. Judgments are further segmented into consent judgments and default judgments. For each district, the authors compiled statistics on the number of plaintiff and defendant wins among: (1) all judgments; (2) all judgments excluding consent judgments; and (3) all judgments excluding consent and default judgments. The authors then added the figures for all 91 U.S. judicial districts to calculate the final figures and percentages. Data was collected on May 15, 2013.).

⁸⁰ *Id.*

A. British Rule – Two-Way Fee Shifting

As current legislative proposals indicate, many perceive the British Rule, or two-way fee shifting, as more effective than the American Rule at reducing the number and cost of cases filed. The litigation model developed in Section III and the empirical evidence, however, suggests that the British Rule is not the panacea that its proponents claim.

i. Litigation Model Comparison – British Rule Versus American Rule

Consider again the litigation models under the British Rule, which were introduced in Section III and repeated here with the same expression number designations. With traditional hourly billing, the plaintiff will only file suit when the following inequality is true:

$$P_p A > (1 - P_p)(C_p + C_d) \quad (3)$$

With traditional hourly billing, the plaintiff and defendant will only settle when the following inequality is true:

$$(P_p - P_d)A < (1 + P_d - P_p)(C_p + C_d) \quad (4)$$

With contingent fee billing, the plaintiff will only file suit when the following inequality is true:

$$P_p A(1 - L) > (1 - P_p)C_d \quad (7)$$

With contingent fee billing, the plaintiff and defendant will only settle when the following inequality is true:

$$[(P_p(1 - L) - P_d)A < (1 + P_d - P_p)C_d + P_d C_p \quad (8)$$

A comparison of these expressions (3), (4), (7), and (8) to their counterparts under the American Rule was already described in Section III. The key points in brief are that, as compared to the American Rule, the British Rule: (a) discourages low-merit cases while encouraging high-merit cases; (b) reduces filings by plaintiffs using contingency arrangements because they face a downside cost to filing suit; (c) with hourly billing, discourages settlement in most cases because plaintiffs who just filed suit tend to be more optimistic than defendants about the odds of the plaintiff prevailing; and (d) with contingent fee billing, encourages settlement in most cases because the plaintiff's "fees," calculated under a lodestar method, can be shifted even though the plaintiff is not technically paying any fees to its attorney.

ii. Empirical Evidence

The above conclusions based on the litigation models are partially confirmed by empirical evidence. There is a general consensus that the British Rule, as used in Britain, encourages high-merit, low-damage cases, while discouraging low-merit, high-damage cases.⁸¹ In other words, plaintiffs with surefire small claims cases are more likely to file in Britain. The American Rule, by comparison, encourages plaintiffs with questionable claims, but large claimed damages, to file suit.⁸² There is less consensus though on whether the British Rule

⁸¹ Gryphon, *supra* note 13, at 572-73; Katz & Sanchirico, *supra* note 11, at 10.

⁸² Gryphon, *supra* note 13, at 572-73; Katz & Sanchirico, *supra* note 11, at 9-12; Walter Olson & David Bernstein, *Loser-Pays: Where Next?*, 55 MD. L. REV. 1161, 1161-63 (1996).

encourages settlement and reduces litigation costs.⁸³ Empirical evidence in Britain is not convincing in either direction, and commentators have mixed opinions. Some argue that the British Rule scares parties away from spending more on litigation,⁸⁴ while others contend that with higher stakes, parties are willing to spend even more to win.⁸⁵

Empirical studies have also considered the effect of fee shifting in state courts in the United States. One study of fee shifting's impact in California state courts found that it caused wealthier defendants to drive up their litigation spending to scare poorer plaintiffs into dismissing their cases or settling for low amounts.⁸⁶ Another study focused on Florida's use of fee shifting from 1980 to 1985 for medical malpractice cases.⁸⁷ During that five-year period, plaintiffs dismissed cases at a slightly higher frequency than before, 54 percent versus 44 percent, and fewer cases went to trial, down to 6 percent from 11 percent.⁸⁸ Median settlement awards went up to \$94,000 from \$74,000, and trial award values also went up to \$69,000 from \$25,000.⁸⁹ These numbers suggest that plaintiffs were dismissing low-merit cases with greater frequency, settling

⁸³ Katz & Sanchirico, *supra* note 11, at 13-16 (discussing the uncertain effect of the British Rule versus the American Rule on settlement and litigation costs).

⁸⁴ Gryphon, *supra* note 13, at 589; Olson & Bernstein, *supra* note 82, at 1161-63.

⁸⁵ Jay P. Kesan, *Carrots and Sticks to Create a Better Patent System*, 17 BERKELEY TECH. L.J. 763, 792 (2002).

⁸⁶ John F. Vargo, *The American Rule on Attorney Fee Allocation: The Injured Person's Access to Justice*, 42 AM. U. L. REV. 1567, 1619-20 (1993).

⁸⁷ Gryphon, *supra* note 13, at 598-603.

⁸⁸ *Id.* at 599.

⁸⁹ *Id.* at 600-01.

more often, and only going to trial on claims of higher merit. But Florida's results could also be explained by small sample size or other factors.

iii. Applying the British Rule to U.S. Patent Litigation

The above discussion suggests that fee shifting's effects are more nuanced than many think. Still, the pros and cons of the British Rule discussed above suggest that its use would improve U.S. patent litigation and address some of the policy goals identified in Section II. Some of the cons of the British Rule – such as discouraging poor, risk-averse plaintiffs from pursuing litigation – are not as applicable to patent cases. Most patent plaintiffs are not poor or risk-averse, and are unlikely to be intimidated by large defendants. Further, many patent plaintiffs also use contingent fee arrangements, further mitigating plaintiff's risk aversion or litigation funding concerns.

The British Rule has advantages that address problems with U.S. patent litigation. First, as discussed, while suing is costless under the American Rule for plaintiffs using contingent fee arrangements, contingent fee plaintiffs under the British Rule face a potential loss. The British Rule therefore discourages contingent fee plaintiffs from filing suit and encourages those who do file to settle. Given that many plaintiffs, particularly NPEs, use contingent fee arrangements, the British Rule has the potential to reduce NPE litigation. Second, the British Rule discourages low-merit, high-damage cases. Such "lottery suits" are commonly filed by NPEs, as confirmed by PwC's study, which shows that NPEs have lower

win rates, but obtain larger damages.⁹⁰ NPEs often sue based on patents with broad and vaguely defined claims that cover wide-ranging technologies, increasing potential damages.⁹¹ But broad and vague claims often make a patent's validity questionable and can lead to dubious infringement arguments.

Despite these positive aspects of the British Rule, this Article does not recommend adopting two-way fee shifting as the default rule for patent cases. The British Rule's efficacy relies on finding clear "winners" and "losers." But in many patent cases, the merits are not so clear, and "winners" and "losers" cannot be easily discerned. Patent cases present highly complex technical and legal issues, and are often decided by judges and juries with little to no technical background and understanding of patent law.⁹² Patent litigators presenting arguments to juries will often avoid discussing the merits of the technology and patents – *i.e.*, the actual substance of the case – and instead, present simplified arguments that would most likely not pass muster with experts in the relevant technical field.⁹³ Patent laws may also be too

⁹⁰ PRICEWATERHOUSECOOPERS, *supra* note 10, at 12.

⁹¹ Anthony Biller, *A cure for the common troll*, OPENSOURCE.COM (Feb. 20, 2012) ("Their club of choice is the broad, complex, and vague patent claim."), <http://opensource.com/law/12/2/cure-common-troll>; James Bessen et. al, *The Private and Social Costs of Patent Trolls*, 34 REG., Winter 2011-2012, at 26, 26 ("The critics call NPEs 'patent trolls,' claiming that they buy up vaguely worded patents that can be construed to cover established technologies and use them opportunistically to extract licensing fees from the real innovators. Indeed, there has been a general and dramatic rise in patent litigation that some analysts attribute to rapid growth in the number of patents with unclear or unpredictable boundaries."), available at <http://object.cato.org/sites/cato.org/files/serials/files/regulation/2012/5/v34n4-1.pdf>.

⁹² Brief of Defendant-Cross Appellant, *supra* note 21, at *68.

⁹³ Based on the authors' professional experience.

slow to adapt to new technologies that present new fact patterns, which adds further uncertainty as to the merits of a patent case. Unsurprisingly, district court decisions are reversed on appeal by the Federal Circuit at a rate of 30-40 percent,⁹⁴ and Federal Circuit decisions are routinely criticized by academics and practitioners.⁹⁵ This sad state of affairs implies that awarding fees in all cases is unjust because in many cases, the merits were wrongly decided and fees will be shifted onto the wrong party. Because plaintiffs and NPEs are well aware of this uncertainty, fee shifting may not discourage them from rolling the dice with low-merit cases. To the contrary, by putting more at stake, fee shifting may actually encourage more lawsuits and more spending on litigation.

B. One-Way Fee Shifting in Favor of Defendants

If the only goal of a fee shifting system was to drive down the frequency and cost of litigation, then one would expect one-way fee shifting in favor of defendants to be the most effective. With pro-defendant one-way fee shifting, only the prevailing defendant can recover attorneys' fees. The litigation model for pro-defendant fee shifting, presented below, largely confirms these expectations.

i. Litigation Model Comparison – One-Way Fee Shifting in Favor of Defendants Versus the British Rule and the American Rule

The litigation model for one-way fee shifting in favor of defendants is presented below in expressions (9) to (12).

⁹⁴ Schwartz, *supra* note 12, at 349.

⁹⁵ See Plager, *supra* note 14, at 754; Mullally, *supra* note 14, at 1114.

The derivation of these expressions is not shown here in the main text, but is described in the footnotes. With traditional hourly billing, the plaintiff will only file suit when the following inequality is true:

$$P_p A > C_p + C_d - P_p C_d \quad (9)^{96}$$

With traditional hourly billing, the plaintiff and defendant will only settle when the following inequality is true:

$$(P_p - P_d)A < C_p + (1 + P_d - P_p)C_d \quad (10)^{97}$$

With contingent fee billing, the plaintiff will only file suit when the following inequality is true:

$$P_p A(1 - L) > (1 - P_p)C_d \quad (11)^{98}$$

⁹⁶ In this derivation, the plaintiff's expected winnings are $P_p A$. With one-way fee shifting against the plaintiff, it will incur its own fees, C_p , if it wins, with probability P_p . The plaintiff will incur fees of both sides, $(C_p + C_d)$, if it loses, with probability $(1 - P_p)$. Thus, the plaintiff will file suit if:

$$P_p A > P_p C_p + (1 - P_p)(C_p + C_d) \quad (E)$$

Manipulating expression (E): $P_p A > C_p + C_d - P_p C_d$

⁹⁷ In this derivation, the starting expression is:

$$P_p A - [P_p C_p + (1 - P_p)(C_p + C_d)] < P_d C_d + P_d A \quad (F)$$

The left side of the expression is the plaintiff's expected winnings, minus the plaintiff's expected fees in litigation. The right side is the sum of the defendant's expectation of plaintiff's winnings and the defendant's expected fees in litigation. Note that the defendant's expected fees are less under the British Rule than under the American Rule, since there is a chance that it will incur no fees if it prevails; the defendant will only incur costs of the amount, C_d , if it loses with probability P_d .

Manipulating expression (F): $(P_p - P_d)A < C_p + (1 + P_d - P_p)C_d$

⁹⁸ In this derivation, in contingency arrangements, the plaintiff's expected winnings are reduced by L percent. Thus, the left side of the inequality is

With contingent fee billing, the plaintiff and defendant will only settle when the following inequality is true:

$$[P_p(1 - L) - P_d]A < (1 + P_d - P_p)C_d \quad (12)^{99}$$

These expressions demonstrate mathematically that pro-defendant, one-way fee shifting discourages the filing of litigation versus the American and British Rules. Comparing expression (9) to expressions (1) and (3), with hourly billing, pro-defendant, one-way fee shifting discourages plaintiffs from filing suit relative to the American and British Rules because:

$$C_p + C_d - P_p C_d > C_p$$

(Hourly, pro-D fee shifting vs. American Rule)

$$C_p + C_d - P_p C_d > (1 - P_p)(C_p + C_d)$$

(Hourly, pro-D fee shifting vs. British Rule)

$P_p A(1 - L)$. The plaintiff only incurs attorneys' fees if it loses, in which case it has to pay the defendant's fees. The plaintiff never has to pay its own attorneys' fees because of the contingency arrangement. Thus, the right side of the inequality is $(1 - P_p)C_d$.

⁹⁹ In this derivation, the starting expression is:

$$P_p A(1 - L) - (1 - P_p)C_d < P_d C_d + P_d A \quad (G)$$

The left side of the expression is the plaintiff's expected winnings, minus its expected litigation costs, which follows from the expression describing the plaintiff's likelihood of filing suit. The right side is the sum of the defendant's expectation of the plaintiff's winnings and the defendant's expected fees in litigation. This is the same as under the hourly arrangement discussed in note 97, because the defendant's costs and perception of the plaintiff's case are not changed in theory by the plaintiff's use of contingency versus hourly billing.

Manipulating expression (G): $[P_p(1 - L) - P_d]A < (1 + P_d - P_p)C_d$

Comparing expression (11) to expressions (5) and (7), with contingent fee billing, pro-defendant, one-way fee shifting discourages plaintiffs from filing suit relative to the American Rule and is equal to the odds of filing suit under the British Rule:

$$(1 - P_p)C_d > 0$$

(Contingency, pro-D fee shifting vs. American Rule)

$$(1 - P_p)C_d = (1 - P_p)C_d$$

(Contingency, pro-D fee shifting vs. British Rule)

The effect of one-way fee shifting on settlement with hourly billing is more ambiguous and depends on the parties' relative perception of the merits. Comparing expression (10) with (2), with hourly billing, there are three scenarios for comparing the relative impacts of pro-defendant fee shifting to the American Rule:

- If $P_d > P_p$, then $C_p + (1 + P_d - P_p)C_d > C_p + C_d$

(Settlement more likely with pro-D fee shifting)

- If $P_d = P_p$, then $C_p + (1 + P_d - P_p)C_d = C_p + C_d$

(Settlement equally likely with pro-D fee shifting)

- If $P_d < P_p$, then $C_p + (1 + P_d - P_p)C_d < C_p + C_d$

(Settlement less likely with pro-D fee shifting)

Comparing expression (10) to (4), with hourly billing, there are three scenarios for comparing the relative impacts of pro-defendant fee shifting to the British Rule:

- If $P_d > P_p$, then $C_p + (I + P_d - P_p)C_d < (I + P_d - P_p)(C_p + C_d)$

(Settlement less likely with pro-D fee shifting)

- If $P_d = P_p$, then $C_p + (I + P_d - P_p)C_d = (I + P_d - P_p)(C_p + C_d)$

(Settlement equally likely with pro-D fee shifting)

- If $P_d < P_p$, then $C_p + (I + P_d - P_p)C_d > (I + P_d - P_p)(C_p + C_d)$

(Settlement more likely with pro-D fee shifting)

Under all three fee shifting systems, settlement is more likely if the plaintiff is less optimistic about its case than the defendant is, or $P_d > P_p$. The effect of this difference in optimism on settlement is most pronounced under the British Rule, because it raises the stakes in all cases, while the American Rule never does. Given that one-way fee shifting raises the stakes in certain cases, settlement odds in those cases will be more sensitive to differences in optimism.

With contingent fee billing, comparing pro-defendant fee shifting to the American Rule again presents the same three scenarios as in hourly billing. But the British Rule will encourage settlement more often than pro-defendant, one-way fee shifting will because in comparing expression (12) to (8):

$$(I + P_d - P_p)C_d < (I + P_d - P_p)C_d + P_d C_p$$

The above result makes intuitive sense because with contingency and pro-defendant fee shifting (the left side of the above inequality), there is never a situation in which either party must pay the plaintiff's attorneys' fees, C_p . With the British Rule and contingency (the right side of the above inequality), however, there is the extra $P_d C_p$ term, meaning that there is some chance that the plaintiff's attorneys' fees must be covered. Because total expected fees for recovery are less with pro-defendant, fee shifting and contingency, settlement is less likely under that system than under the British Rule.

ii. Policy Concerns with One-Way Fee Shifting in Favor of Defendants

Although pro-defendant, one-way fee shifting reduces litigation filings and costs, it provides defendants with an unfair advantage. If pro-defendant, one-way fee shifting was implemented, defendants can run up their fees, C_d , to intimidate plaintiffs, knowing that only their fees could be recovered. The asymmetry in fee shifting may also cause plaintiffs to become less optimistic, meaning P_p would decline. Although this would promote settlement, more settlements are not desirable if they discourage plaintiffs with meritorious claims from filing suit and if the settlement terms fail to adequately compensate plaintiff for its loss and punish the defendant for infringement.

iii. Kesan Proposal: One-Way Fee Shifting in Favor of Defendants if the Plaintiff Does Not Perform a "Reasonable Search" for Invalidating Prior Art

In an article published in 2002, Jay Kesan proposed using pro-defendant fee shifting in the narrow circumstance

where the defendant prevailed by proving patent invalidity with prior art that was “reasonably discoverable” by the plaintiff.¹⁰⁰ Kesan argued that this fee-shifting rule would encourage plaintiffs to search for prior art before filing an infringement suit.¹⁰¹ Kesan contended that the plaintiff, who has an interest in the asserted patent, would be in the lowest-cost position to find prior art, given its knowledge of the patent, the prosecution history, and the relevant technical field.¹⁰²

Kesan’s proposal was later criticized in a paper by Matthew Sag and Kurt Rohde on the grounds that it would harm smaller plaintiffs who have fewer resources to find prior art.¹⁰³ Another more practical objection to Kesan’s proposal is defining “reasonably discoverable,” as it is unclear when a particular prior art reference should have been found by the plaintiff.

Despite the above shortcomings, Kesan’s proposal has appeal in view of the increase in NPE-initiated litigation, which took off in the years after his proposal was published in 2002.¹⁰⁴ As mentioned above, NPEs often file infringement cases based on patents with broad and vague claims that are vulnerable to invalidity challenges. Incentivizing all NPEs, which now comprise the majority of plaintiffs, to conduct prior art due diligence on their patents’ validity before suing may significantly reduce such litigation. And Sag and Rohde’s concern over smaller plaintiffs is not applicable to NPEs. While some NPEs are “small,” NPEs are in the business of

¹⁰⁰ Kesan, *supra* note 85, at 787-88, 795-97.

¹⁰¹ *Id.* at 795.

¹⁰² *Id.*

¹⁰³ Matthew Sag & Kurt Rohde, *Patent Reform and Differential Impact*, 8 MINN. J.L. SCI. & TECH. 1, 69 (2007).

¹⁰⁴ Chien, *supra* note 4.

monetizing patents, and many do conduct due diligence investigations before acquiring a patent or using it offensively.¹⁰⁵ Further, the “reasonably discoverable” issue can be overcome using procedural requirements. If plaintiffs took sufficient steps to find prior art before filing suit, then fee shifting would not apply against them. For example, courts can consider the number of hours or the amount of money that the plaintiff spent on prior art searches before filing suit and require the plaintiff to produce a listing of prior art reviewed as part of its pre-suit investigation.

C. One-Way Fee Shifting in Favor of Plaintiffs

Another fee shifting option is one-way fee shifting in favor of plaintiffs. Intuitively, pro-plaintiff fee shifting empowers the plaintiff, which should generate more litigation and reduce the odds of settlement. The litigation model for pro-plaintiff, one-way fee shifting, presented below, confirms most of these expectations.

i. Litigation Model – One-Way Fee Shifting in Favor of Plaintiffs Versus the British Rule and the American Rule

The litigation model for one-way fee shifting in favor of plaintiffs is presented below in expressions (13) to (16). The derivation of these expressions is not shown here in the main text, but is described in the footnotes. With traditional hourly billing, the plaintiff will only file suit when the following inequality is true:

¹⁰⁵ Based on the authors’ professional experience.

$$P_p A > (I - P_p) C_p \quad (13)^{106}$$

With traditional hourly billing, the plaintiff and defendant will only settle when the following inequality is true:

$$(P_p - P_d) A < C_d + (I + P_d - P_p) C_p \quad (14)^{107}$$

With contingent fee billing, the plaintiff will only file suit when the following inequality is true:

$$P_p A (I - L) > 0 \quad (15)^{108}$$

With contingent fee billing, the plaintiff and defendant will only settle when the following inequality is true:

$$(P_p (I - L) - P_d) A < C_d + P_d C_p \quad (16)^{109}$$

¹⁰⁶ In this derivation, the left side of the expression is the plaintiff's expected winnings. The right side is the plaintiff's costs. With fee shifting in plaintiff's favor, the plaintiff will only incur attorneys' fees in the event that it loses, in which case it must pay its own fees, C_p . The plaintiff's perceived probability of losing is $I - P_p$.

¹⁰⁷ In this derivation, the starting expression is:

$$P_p A - (I - P_p) C_p < P_d A + P_d (C_d + C_p) + (I - P_d) C_d \quad (G)$$

The left side of the expression is the plaintiff's expected winnings, minus its expected litigation costs, which follows from the expression describing the plaintiff's likelihood of filing suit. The right side is the sum of the defendant's expectation of the plaintiff's winnings and the defendant's expected fees in litigation. The defendant's fees are different depending on whether it wins or loses. If the defendant wins, then it still must bear its own fees; this accounts for the term $(I - P_d) C_d$. If the defendant loses, then it must pay its own fees and the plaintiff's fees, which accounts for the term $P_d (C_d + C_p)$.

Manipulating expression (G): $(P_p - P_d) A < C_d + (I + P_d - P_p) C_p$

¹⁰⁸ In this derivation, with fee shifting in the plaintiff's favor, the plaintiff does not incur fees if it loses. The plaintiff also does not incur fees if it wins because the plaintiff's attorney is working under contingency.

These expressions prove mathematically that pro-plaintiff, one-way fee shifting encourages filing suit versus the American and British Rules. Comparing expression (13) to expressions (1) and (3), with hourly billing, pro-plaintiff fee shifting increases the likelihood of filing suit as compared to both the American and British Rules because:

$$(1 - P_p)C_p < C_p$$

(Hourly, pro-P fee shifting vs. the American Rule)

$$(1 - P_p)C_p < (1 - P_p)(C_p + C_d)$$

(Hourly, pro-P fee shifting vs. the British Rule)

Comparing expression (15) to expressions (5) and (7), with contingent fee billing, the likelihood of filing suit under pro-plaintiff fee shifting is equal to the likelihood under the American Rule (in both cases, there is no cost to filing) and greater than under the British Rule:

$$0 = 0$$

¹⁰⁹ In this derivation, the starting expression is:

$$P_p A(1 - L) < P_d A + P_d(C_d + C_p) + (1 - P_d)C_d \quad (\text{H})$$

The left side of the expression is the plaintiff's expected winnings, minus its expected litigation costs, which follows from the expression describing the plaintiff's likelihood of filing suit. The right side is the sum of the defendant's expectation of the plaintiff's winnings and the defendant's expected fees in litigation. The defendant's fees are different depending on whether the defendant wins or loses. If the defendant wins, then it still must bear its own fees; this accounts for the term $(1 - P_d)C_d$. If the defendant loses, then it must pay its own fees and the plaintiff's fees, which accounts for the term $P_d(C_d + C_p)$.

Manipulating expression (H): $[P_p(1 - L) - P_d]A < C_d + P_d C_p$

(Contingency, pro-P fee shifting vs. the American Rule)

$$0 < (1 - P_p)C_d$$

(Contingency, pro-P fee shifting vs. the British Rule)

With hourly billing, the effect of pro-plaintiff fee shifting depends on the relative optimism, P_p and P_d of the parties. Comparing expression (14) to expression (2), which corresponds to the American Rule:

- If $P_d > P_p$, then $C_d + (1 + P_d - P_p)C_p > C_p + C_d$

(Settlement more likely with pro-P fee shifting)

- If $P_d = P_p$, then $C_d + (1 + P_d - P_p)C_p = C_p + C_d$

(Settlement equally likely with pro-P fee shifting)

- If $P_d < P_p$, then $C_d + (1 + P_d - P_p)C_p < C_p + C_d$

(Settlement less likely with pro-P fee shifting)

Comparing expression (14) to expression (4), which corresponds to the British Rule:

- If $P_d > P_p$, then $C_p + (1 + P_d - P_p)C_d < (1 + P_d - P_p)(C_p + C_d)$

(Settlement less likely with pro-P fee shifting)

- If $P_d = P_p$, then $C_p + (1 + P_d - P_p)C_d = (1 + P_d - P_p)(C_p + C_d)$

(Settlement equally likely with pro-P fee shifting)

- If $P_d < P_p$, then $C_p + (1 + P_d - P_p)C_d > (1 + P_d - P_p)(C_p + C_d)$

(Settlement more likely with pro-P fee shifting)

The above results make intuitive sense. Again, the British Rule raises the stakes in all cases, the American Rule never raises the stakes, and one-way fee shifting raises the stakes in some cases. With higher stakes, parties' willingness to continue litigating becomes more sensitive to their relative optimism about the case, with settlement being more likely if $P_d > P_p$.

With contingent fee billing, comparing pro-plaintiff, one-way fee shifting to the British Rule again presents the same three scenarios as with hourly billing. But one-way fee shifting for plaintiffs will always encourage settlement more often than the American Rule does, as shown by comparing expression (16) to expression (6):

$$C_d + P_d C_p > C_d$$

This result makes intuitive sense because with contingent fee billing and pro-plaintiff, one-way fee shifting, plaintiffs could recover their attorneys' fees (calculated under a lodestar method), whereas they could not under the American Rule. This accounts for the extra $P_d C_p$ term on the left side of the inequality, where the left side represents total expected litigation costs for both parties with pro-plaintiff fee shifting. With expected total fees for recovery being greater with contingent fee billing and pro-plaintiff fee shifting, settlement is more likely under that system than under the American Rule.

ii. Less Litigation with Pro-Plaintiff Fee Shifting?

Although the above model and intuition suggest that pro-plaintiff fee shifting increases patent litigation, some commentators contend that pro-plaintiff fee shifting actually reduces litigation. Their argument considers the impact that pro-plaintiff fee shifting has on behavior outside of litigation. They contend that would-be defendants will take more precautions to avoid infringement given the threat of asymmetrical fee shifting in favor of plaintiffs.¹¹⁰ As applied to patent litigation, for example, before designing or manufacturing any product, a potential defendant may spend extra resources searching for patents that may be infringed by its product and incur greater costs, if necessary, on design-around. Because of these extra measures, fewer defendants would, in theory, be infringing. As a result, patentees would file fewer infringement actions. And even if patentees filed an infringement action, their awareness that defendants likely took extra measures to avoid infringement would lower their optimism, P_p , thereby encouraging settlement and reducing litigation costs.

But the above argument is less applicable to patent litigation because of the uncertain merits and outcomes of patent cases. Technology products are complex and claim language is often difficult to parse. It is costly and difficult for a company to determine when it is infringing a patent. And in many fields, particularly electronics and software, there are “patent thickets.” For example, a mobile phone manufacturer

¹¹⁰ See Hylton, *supra* note 42, at 1072; Kesan, *supra* note 85, at 791; Thomas D. Rowe, Jr., *Indemnity or Compensation? The Contract with America, Loser-Pays Attorney Fee Shifting, and a One-Way Alternative*, 37 WASHBURN L.J. 317, 339 (1998).

could easily find hundreds of patents, each of which poses some small non-infringement risk.¹¹¹ Even if a company concluded that the infringement risk for certain patents was high, a design-around may not be technically or commercially feasible.

Given these considerations, the minute risk of pro-plaintiff fee shifting in some future litigation is unlikely to change the behavior of would-be defendants. In fact, encouraging companies to take all these precautions, and over-comply with patent laws, may chill innovation. Ironically, by taking extra precautions, the defendant is more likely to have pre-suit awareness of a later-asserted patent, which increases the likelihood that the defendant will be liable for willful infringement and thus, attorneys' fees under § 285, should it decide to continue developing its product without designing around existing patents. And regardless of what precautions the defendant takes, the plaintiff may still decide that the outcome of its own infringement case is still sufficiently uncertain that filing suit is worth the gamble. For these reasons, one-way fee shifting in favor of plaintiffs would not result in less patent litigation and should not be adopted.

D. Past and Present Legislative Proposals

i. Patent Reform Act of 2006

¹¹¹ See Iain M. Cockburn & Megan J. MacGarvie, *Patents, Thickets, and the Financing of Early-Stage Firms: Evidence from the Software Industry*, 18 J. ECON. & MGMT. STRATEGY 729 (2009). See Mark A. Lemley, *Software Patents and the Return of Functional Claiming*, (Stanford Pub. Law Working Paper No. 2117302, 2012), available at <http://ssrn.com/abstract=2117302>.

As part of the Patent Reform Act of 2006, Congress considered adopting the British Rule as the default, by amending § 285 as follows:

(b) ATTORNEY'S FEES.—
Section 285 is amended to read:

“(a) The court shall award, to a prevailing party, fees and other expenses incurred by that party in connection with that proceeding, unless the court finds that the position of the nonprevailing party or parties was substantially justified or that special circumstances make an award unjust.”¹¹²

The proposed legislation did not pass. For the reasons discussed previously in Section V.A., adopting the British Rule as the default is not recommended.

ii. SHIELD Act of 2012

In 2012, Congress considered fee shifting against patentees in cases involving “computer hardware and software” patents where the patentee “did not have a reasonable likelihood of succeeding.”¹¹³ The legislation, titled the “Saving High-Tech Innovators from Egregious Legal Disputes

¹¹² Patent Reform Act of 2006, S. 3818, 109th Cong. § 5 (2d Sess. 2006).

¹¹³ Saving High-Tech Innovators from Egregious Legal Disputes Act of 2012 (“SHIELD Act of 2012”), H.R. 6245, 112th Cong. § 2(a) (2d Sess. 2012).

Act of 2012,” or “SHIELD Act of 2012,” would have added § 285A, quoted below.

§ 285A. Recovery of litigation costs for computer hardware and software patent

“(a) IN GENERAL. – Notwithstanding section 285, in an action disputing the validity or alleging the infringement of a computer hardware or software patent, upon making a determination that the party alleging the infringement of the patent did not have a reasonable likelihood of succeeding, the court may award the recovery of full costs to the prevailing party, including reasonable attorney’s fees, other than the United States.

“(b) DEFINITIONS. – In this section:

“(1) COMPUTER. – The term ‘computer’ means an electronic, magnetic, optical, electrochemical, or other high-speed data processing device performing logical, arithmetic, or storage functions, and includes –

“(A) any data storage facility or communications facility directly related to or operating in conjunction with such device; and

“(B) any processor or peripheral, such as a monitor or input device, directly related to or operating in conjunction with such device.

“(2) COMPUTER HARDWARE PATENT. – The term ‘computer hardware patent’ means a patent that covers computer hardware, including a device or component of such device.

“(3) SOFTWARE PATENT. – The term ‘software patent’ means a patent that covers –

“(A) any process that could be implemented in a computer regardless of whether a computer is specifically mentioned in the patent; or

“(B) any computer system that is programmed to perform a

process described in subparagraph (A).”¹¹⁴

The SHIELD Act of 2012 did not pass, but was reworked entirely and reintroduced the next year as the SHIELD Act of 2013, which is discussed below in Section V.D.iii. A primary defect of the SHIELD Act of 2012 was its attempt to define terms such as “computer,” “computer hardware patent,” and “software patent.” Any definitions of such terms are likely to be both under- and over-inclusive, inevitably leading to litigation over whether those terms cover the subject matter of the litigation. Another problem was that the legislation covers “software patents,” which suggests that all software is patentable subject matter. The legislation was, therefore, in conflict with current case law that suggests that software is only patentable subject matter in limited circumstances.¹¹⁵

iii. SHIELD Act of 2013

The SHIELD Act of 2013, quoted below, targets NPEs. It shifts fees against any party that is not: (1) the original inventor or assignee; (2) exploiting the patent commercially through sale or production of items practicing the patent; or (3) a university or technology transfer organization.¹¹⁶

¹¹⁴ *Id.*

¹¹⁵ See, e.g., *CLS Bank Int’l v. Alice Corp. Pty. Ltd.*, 717 F.3d 1269 (Fed. Cir. 2013) (en banc) (finding that the software patent at issue was not directed to eligible subject matter under 35 U.S.C. § 101) (five different concurrences and dissents were filed). See also Dennis Crouch, *Ongoing Debate: Is Software Patentable?*, PATENTLY-O BLOG (July 27, 2012, 3:53 PM), <http://www.patentlyo.com/patent/2012/07/ongoing-debate-is-software-patentable.html>.

¹¹⁶ SHIELD Act of 2013, *supra* note 6, § 2(a).

“§ 285A. Recovery of litigation costs

“(a) IN GENERAL. – In an action involving the validity or infringement of a patent –

“(1) a party asserting invalidity or noninfringement may move for judgment that the adverse party does not meet at least one of the conditions described in subsection (d);

“(2) not later than 90 days after a party has moved for the judgment described in paragraph (1), the adverse party shall be provided an opportunity to prove such party meets at least one of the conditions described in subsection (d);

“(3) as soon as practicable after the adverse party has been provided an opportunity to respond under paragraph (2), but not later than 120 days after a party has moved for the judgment described in paragraph (1), the court shall make a determination

whether the adverse party meets at least one of the conditions described in subsection (d); and

“(4) notwithstanding section 285, the Court shall award the recovery of full costs to any prevailing party asserting invalidity or noninfringement, including reasonable attorney’s fees, other than the United States, upon the entry of a final judgment if the court determines that the adverse party did not meet at least one of the conditions described in subsection (d), unless the court finds that exceptional circumstances make an award unjust.

“(b) BOND REQUIRED. – Any party that fails to meet a condition under subsection (a)(3) shall be required to post a bond in an amount determined by the court to cover the recovery of full costs described in subsection (a)(4).

...

“(d) **CONDITION DEFINED.** – For purposes of this section, a ‘condition’ means, with respect to the party alleging infringement, any of the following:

“(1) **ORIGINAL INVENTOR.**
– Such party is the inventor, a joint inventor, or in the case of a patent filed by and awarded to an assignee of the original inventor or joint inventor, the original assignee of the patent.

“(2) **EXPLOITATION OF THE PATENT.** – Such party can provide documentation to the court of substantial investment made by such party in the exploitation of the patent through production or sale of an item covered by the patent.

“(3) **UNIVERSITY OR TECHNOLOGY TRANSFER ORGANIZATION.** – Such party is –

“(A) an institution of higher education (as that

term is defined in section 101 of the Higher Education Act of 1965 (20 U.S.C. 1001); or

“(B) a technology transfer organization whose primary purpose is to facilitate the commercialization of technology developed by one or more institutions of higher education.”¹¹⁷

This proposal adopts one-way fee shifting against NPEs, who are usually plaintiffs. This Article recommends against pro-defendant fee shifting in Section V.B, because (1) it would cause defendants to run up their litigation fees; (2) it would place defendants in a superior litigation and bargaining position, leading to settlements that are unfair to plaintiffs; and (3) its effect on settlement is ambiguous. An article authored by Michael Risch identified other problems with this proposal, relating mainly to its attempt to define an NPE by excluding three types of non-NPE entities:¹¹⁸

- The fee shifting provision is not limited to cases where the NPE is the plaintiff asserting infringement; it can also apply to declaratory judgment actions. This may cause more litigation, because non-NPEs will file more

¹¹⁷ *Id.*

¹¹⁸ Michael Risch, *Scratching my Head Over the SHIELD Act*, MADISONIAN.NET (Mar. 10, 2013), <http://madisonian.net/2013/03/10/scratching-my-head>.

declaratory judgment actions against NPEs knowing that only their fees are recoverable.

- Category (d)(2) tries to capture parties who practice their patents (non-NPEs), but it defines such parties based on “substantial investment” in production or sale of products practicing the patents. An NPE, however, could simply buy and resell products that it claims are infringing, thus satisfying the “substantial investment” requirement.
- Category (d)(2) uses “exploitation of the patent” to determine whether a party is or is not an NPE. This inquiry into “exploitation” is akin to the technical prong of domestic industry in ITC cases,¹¹⁹ and litigation of the issue will add significantly to litigation costs. Consider also a situation where a company sues for infringement of its patent and that company manufactures and sells a product that it reasonably believes practices the asserted patent. But during litigation, a claim construction ruling determines that the claims are narrower in scope, such that the plaintiff’s product no longer practices the patent. That company is now an NPE with respect to the asserted patent because it is no longer exploiting it.
- Category (d)(2)’s “exploitation of the patent” does not define the time period of exploitation. Thus, if a company once made a product that practiced the patent

¹¹⁹ Certain Elec. Imaging Devices, Inv. No. 337-TA-850, 2013 WL 5956227, at *98 (Sept. 30, 2013) (“To meet the technical prong, the complainant must establish that it practices at least one claim of the asserted patent.”).

but stopped manufacturing it before filing suit, that company is an NPE with respect to the asserted patent under the proposed statute.

- Category (d)(1) excludes original inventors and assignees from the definition of NPE. But as discussed in Section II, NPEs are increasingly filing and obtaining patents, making them the original assignees of these patents.
- Because of category (d)(1)'s exclusion of original inventors and assignees, many large technology companies now spin off NPE subsidiaries that hold the company's patents and enforce them. But these spin-off entities might not be considered NPEs under the proposed statute because they are subsidiaries or affiliates of the "original assignee."

In sum, SHIELD Act of 2013 contains too many escape hatches through which an NPE could still bring infringement actions and avoid fee shifting. It could also potentially sanction many entities that are not NPEs. Further, the proposal would raise litigation costs: subsections (a) and (c) require motion practice to determine whether a party qualifies as an NPE. One can expect parties to bicker extensively about whether the party asserting infringement is an NPE, particularly in view of the above substantive flaws with the way in which the legislation carves out non-NPEs. Both sides would likely also seek and produce voluminous discovery on the issue. At the time of this writing, the SHIELD Act of 2013 has not passed, and this Article does not recommend its passage for the reasons described above.

iv. Patent Abuse Reduction Act of 2013

The Patent Abuse Reduction Act of 2013 is an ambitious attempt to reduce the frequency and cost of patent litigation. It includes two fee-shifting provisions. The first fee-shifting provision, § 300(b), would shift certain attorneys' fees relating to discovery.¹²⁰ The provision defines two categories of evidence: (1) "core documentary evidence," which in turn has eight enumerated subcategories, but by default excludes all email, text messages, and "computer code"; and (2) "additional discovery," which is anything beyond "core documentary evidence."¹²¹ A party that requests "additional discovery," must bear the cost of that additional discovery, including attorney's fees.¹²² Section 300(b) is quoted below:

[Sec. 300](b) SEQUENCE
AND SCOPE; COST-
SHIFTING. –

“(1) DEFINITIONS. – In this
subsection –

“(A) the term ‘additional
discovery’ means discovery
of evidence other than core
documentary evidence; and

“(B) the term ‘core
documentary evidence’, with
respect to a civil action

¹²⁰ Patent Abuse Reduction Act of 2013, *supra* note 6, § 4(a).

¹²¹ *Id.*

¹²² *Id.*

arising under any Act of Congress relating to patents –

“(i) subject to clause (ii), includes only documents that –

“(I) relate to the conception, reduction to practice, and application for the asserted patent;

“(II) are sufficient to show the technical operation of the instrumentality identified in the complaint as infringing the asserted patent;

“(III) relate to potentially invalidating prior art;

“(IV) relate to previous licensing or conveyances of the asserted patent;

“(V) are sufficient to show revenue attributable to any claimed invention;

“(VI) are sufficient to show the organizational ownership and structure of each party, including identification of any person that has a financial interest in the asserted patent;

“(VII) relate to awareness of the asserted patent or claim, or the infringement, before the action was filed; and

“(VIII) sufficient to show any marking, lack of marking, or notice of the asserted patent provided to the accused infringer; and

“(ii) does not include computer code or electronic communication, such as e-mail, text messages, instant messaging, and other forms of electronic communication, unless the court finds good cause

for including such computer code or electronic communication as core documentary evidence of a particular party under clause (i).

...

“(3) DISCOVERY COST-SHIFTING. –

“(A) IN GENERAL. – In a civil action arising under any Act of Congress relating to patents, each party shall be responsible for the costs of producing core documentary evidence within the possession, custody, or control of that party.

“(B) ADDITIONAL DISCOVERY. –

“(i) IN GENERAL. – A party to a civil action arising under any Act of Congress relating to patents may seek additional discovery if the party bears the costs of the additional discovery,

including reasonable
attorney's fees."¹²³

This proposal, like the SHIELD Act of 2013, suffers from definitional problems because it tries to define the types of evidence and claims that are acceptable in discovery. First, the proposal defines “core documentary evidence” to exclude computer code and emails. But in many patent infringement cases, these forms of evidence are critical. For example, in cases relating to electronics and computers, the underlying functionality of the accused products often cannot be determined without examination of computer code. And proving facts relating to pre-suit awareness of asserted patents or offers to license patents often requires discovery of emails. Second, the definition of “core documentary evidence” in § 300(b)(1)(B)(i) omits categories of evidence that are important in many patent cases. Some patent cases, for example, turn on enforceability defenses relating to the plaintiff's activities before standards-setting organizations. Cases may also involve patent misuse and antitrust defenses, or include joint or indirect infringement claims that depend not only on the “technical operation of the instrumentality identified,” but also the actions of third parties such as customers. Finally, it is not clear whether and how fees are shifted for any third-party discovery.

The proposed legislation's second fee-shifting provision, excerpted below, would amend § 285 to make the British Rule the default.¹²⁴ The proposal's language is similar to the previous 2006 proposal discussed in Section V.D.i. For the reasons discussed above in Section V.A, this proposal should be rejected.

¹²³ *Id.*

¹²⁴ *Id.* § 5.

“§ 285. Costs and expenses

“(a) IN GENERAL. – The court shall award to the prevailing party reasonable costs and expenses, including attorney’s fees, unless –

“(1) the position and conduct of the non-prevailing party were objectively reasonable and substantially justified; or

“(2) exceptional circumstances make such an award unjust.”¹²⁵

v. Innovation Act

Like the Patent Abuse Reduction Act of 2013, the Innovation Act includes several provisions that seek to reduce the cost and frequency of patent litigation.¹²⁶ One of its provisions, excerpted below, amends § 285 to shift fees onto the losing party by default.¹²⁷

“§ 285. Fees and other expenses

(a) AWARD.—The court shall award, to a prevailing party,

¹²⁵ *Id.*

¹²⁶ Innovation Act, *supra* note 6.

¹²⁷ *Id.* § 3(b).

reasonable fees and other expenses incurred by that party in connection with a civil action in which any party asserts a claim for relief arising under any Act of Congress relating to patents, unless the court finds that the position of the nonprevailing party or parties was substantially justified or that special circumstances make an award unjust.”¹²⁸

For the reasons described in Section V.A, this Article disfavors two-way fee shifting. The above proposal is also problematic because of its vague carve-out from fee shifting of cases when the losing party’s position was “substantially justified.” (This carve-out was also in the Patent Reform Act of 2006 discussed in Section V.D.i and is in the pending Patent Abuse Reduction Act of 2013 discussed in Section V.D.iv.) Arguably, the majority of patent plaintiffs have substantial justification for bringing their case, given the complexity of technologies in many patent cases and given that infringement often cannot be determined without discovery of confidential information concerning the accused products or services. Disputes over whether a case was “substantially justified” will likely increase litigation costs.

vi. Patent Litigation Integrity Act of 2013

¹²⁸ *Id.*

The Patent Litigation Integrity Act of 2013 also amends § 285 to shift fees onto the losing party by default, except where the losing party's conduct was "substantially justified."¹²⁹ This amendment, excerpted below, is nearly identical to the Innovation Act's amendment of § 285 and should not be adopted for the same reasons discussed in Section V.D.v.

“§ 285. Fees and other expenses

The court shall award to a prevailing party reasonable fees and other expenses, including attorney fees, incurred by that party in connection with a civil action in which any party asserts a claim for relief arising under any Act of Congress relating to patents, unless the court finds that the position and conduct of the nonprevailing party or parties were substantially justified or that special circumstances make an award unjust.”¹³⁰

E. Award Fees Under § 285 in “Unreasonable” Cases, Not Just “Baseless” Cases

In *Icon Health & Fitness, Inc. v. Octane Fitness, LLC*, defendant Octane moved unsuccessfully for attorneys' fees

¹²⁹ Patent Litigation Integrity Act of 2013, *supra* note 6.

¹³⁰ *Id.* § 101.

under § 285, contending that the case was exceptional after winning summary judgment of non-infringement.¹³¹

Octane appealed the district court's decision to the Federal Circuit. In its appellate brief, Octane argued that the current standard for "exceptional case" under § 285 is too stringent in situations where the defendant moves for attorneys' fees based on the weakness of the plaintiff's infringement case, as it requires the defendant to prove that the plaintiff's case was "objectively baseless" and brought in "subjective bad faith."¹³² Octane proposed that the standard be relaxed to "objectively unreasonable."¹³³ With this modification, Octane argued, weaker infringement cases would be discouraged.¹³⁴

Octane proposed seven factors for assessing whether an infringement case is "objectively unreasonable":

- (1) more than one claim element was missing in the accused device,
- (2) the case was resolved on summary judgment,
- (3) the patentee was not practicing the claimed invention,

¹³¹ *Icon Health & Fitness, Inc. v. Octane Fitness, LLC*, No. 09-319, 2011 WL 3900975, at *4 (D. Minn. Sept. 6, 2011).

¹³² Brief for Defendant-Cross Appellant, *supra* note 21, at *67-68.

¹³³ *Id.* at *69.

¹³⁴ *Id.* at *74.

(4) the patentee's claim of infringement was based on a claim construction position that:

(a) contradicted the prosecution history, or

(b) read a limitation out of the claim entirely, or

(c) was not rationally related to what was actually invented,

(5) the patentee ignored or reargued the court's claims construction,

(6) the accused device incorporated technology that predated the asserted patent, in lieu of the technology disclosed in the patent-in-suit, and

(7) the accused infringer communicated to the patentee near the start of the case an alleged design around or element(s) not present in the accused product; the patentee proceeds forward unreasonably;

and the defendant ultimately prevails on that issue.¹³⁵

The Federal Circuit affirmed the district court's denial of fees on appeal and rejected Octane's "objectively unreasonable" standard.¹³⁶

The U.S. Supreme Court has granted Octane's petition for writ of certiorari to review the Federal Circuit's decision.¹³⁷ In its petition to the U.S. Supreme Court, Octane contended that the "exceptional case" standard used by the Federal Circuit makes it nearly impossible for accused infringers to recover fees, thereby doing little to discourage low-merit actions from being filed.¹³⁸ Octane argued that a case with an "objectively low likelihood of success" is an "exceptional case."¹³⁹ This Article recommends adopting Octane's proposal to relax § 285's "exceptional case" standard, and to allow fee shifting in a higher percentage of cases, particularly in favor of prevailing accused infringers.

As discussed throughout this Article, fee shifting does present certain advantages as compared to the American Rule. The British Rule discourages low-merit cases and imposes costs on plaintiffs who use contingent fee arrangements. Pro-defendant, one-way fee shifting, meanwhile, discourages all plaintiffs from filing suit. Applying fee shifting against

¹³⁵ *Id.* at *73.

¹³⁶ *Icon Health & Fitness, Inc. v. Octane Fitness, LLC*, 496 F. App'x 57, 65 (Fed. Cir. 2012).

¹³⁷ *Octane Fitness, LLC v. Icon Health & Fitness, Inc.*, 496 F. App'x 57 (Fed. Cir. 2012), *cert. granted*, 134 S.Ct. 49 (2013).

¹³⁸ Petition for Writ of Certiorari, *Octane Fitness*, 2013 WL 1309080, at *19-20 (2013) (No. 12-1184).

¹³⁹ *Id.* at *33.

plaintiffs then, should reduce the number of patent cases filed and weed out weaker cases. But applying these rules rigidly in all patent cases is not recommended because, as discussed in Section V.A.iii, a significant share of patent cases are wrongly decided by district courts and many cases are close calls. As a result, if fee shifting was applied in nearly all cases, patentees may actually pursue more litigation, because outcomes are uncertain and the potential rewards of a favorable outcome are greater.

Fee shifting should instead be applied selectively to cases where the merits are clearly in favor of one party. Exactly how often fee shifting should apply is a more difficult question. But the patent litigation boom of the past decade and the recent surge of NPE-litigation suggest that § 285's current usage rate of about 6 percent of all cases reaching judgment is too low.¹⁴⁰ The 6 percent figure actually overstates § 285's usage against plaintiffs who file low-merit cases given that the fees under § 285 are awarded to plaintiffs at least twice as often as defendants, and a significant share of defendant awards are based on litigation misconduct, not on the weak merits of the plaintiff's case.¹⁴¹ In its petition for writ of certiorari, Octane identified the asymmetry in plaintiffs' favor as a reason to modify the "exceptional case" standard.¹⁴² Fee shifting should be used in about 20-30 percent of all patent cases that reach judgment, with greater use against plaintiffs bringing weak infringement cases.

To achieve this increase and improve § 285's usage to combat weak infringement cases, the "exceptional case"

¹⁴⁰ See *supra* Section IV.B.

¹⁴¹ *Id.*

¹⁴² Petition for Writ of Certiorari, *supra* note 138, at *26-32.

standard under § 285 should be modified in three ways. First, Octane’s proposal to the Federal Circuit of seven factors to guide the relaxed “exceptional case” inquiry should be adopted. Other factors that courts can consider include:

- Patentee’s complaint was dismissed with prejudice for failure to state a claim under Federal Rule of Civil Procedure 12(b)(6);
- Patentee’s asserted patents were invalidated based on prior art that was “reasonably discoverable,” as discussed in Section V.B.iii;
- Patentee’s infringement positions were contradicted by stipulated facts or facts judicially noticed, or the opinion of plaintiff’s own expert.

Other factors can be used to apply fee shifting against defendants who take frivolous positions, such as presenting non-infringement or invalidity positions that contradict the court’s claim construction order, raising many questionable § 112 arguments, losing infringement on summary judgment, or identifying hundreds of prior art references per patent that, when combined under § 103, are still missing more than one element of the patent’s claims.

Second, if § 285 relies on “objective unreasonableness,” then “subjective bad faith” can be eliminated.¹⁴³ A party that takes unreasonable positions, such as an infringement position that was precluded by a claim

¹⁴³ Brief for Defendant-Cross Appellant, *supra* note 21, at *77-79.

construction ruling, should be sanctioned regardless of whether it took its position in good faith.

Third, to correct the current pro-plaintiff bias in how § 285 is applied, attorneys' fees should not be awarded as a matter of course to plaintiffs based on default judgment or a finding of willful infringement. A default judgment says little in most cases about the merits of the plaintiff's infringement case. As for willful infringement, § 284 already imposes punitive treble damages to punish the infringer for willfulness; tacking on attorneys' fees is redundant and probably excessive in terms of achieving any deterrent or retributive goals.

F. Other Proposals

Other adjustments can be made to the patent litigation system to dissuade weak cases from being filed and to encourage settlement. Two adjustments discussed in this section are using offers of judgment to shift attorney's fees and requiring patentee-plaintiffs to post a bond.

i. Offer of Judgment

Fed. R. Civ. P. 68 provides for cost shifting based on an unaccepted "offer of judgment."¹⁴⁴ An offer of judgment¹⁴⁵ means that if during litigation, the defendant makes a settlement offer to the plaintiff – or "an offer to allow judgment on specified terms" – and the plaintiff does not accept that offer, then the plaintiff must pay costs incurred after that offer was made if the judgment is ultimately less favorable than that

¹⁴⁴ FED. R. CIV. P. 68.

¹⁴⁵ *Id.* 68(a) (stating that offers of judgment must be made 14 days before trial).

past offer.¹⁴⁶ For example, suppose that just after the close of fact discovery, the defendant offered the plaintiff \$1 million to settle the case, and the plaintiff refused. If the plaintiff ultimately loses the case, or wins less than \$1 million, then the plaintiff must pay the defendant all “costs” incurred after the close of fact discovery when the defendant’s offer of settlement was made.

Rule 68’s offer of judgment procedure only shifts “costs,” which do not include attorneys’ fees.¹⁴⁷ Section 285 should be amended to shift attorneys’ fees to defendants if their offers of judgment are not accepted. Giving offers of judgment more teeth would strongly encourage settlement, thereby reducing litigation costs. Plaintiffs will be incentivized to take settlement offers more seriously, knowing that failing to prove liability and damages above the offer amount would mean paying substantial sums in attorneys’ fees. Defendants, in turn, will also be encouraged to make more settlement offers to end the case. The amount shifted may also be capped by the difference between the offer of judgment amount and the ultimate damages award to account for cases where the plaintiff’s award is slightly below the settlement offer.

In their paper discussing use of offers of judgment to shift attorneys’ fees in litigation generally, Avery Katz and Chris Sanchirico found that if the offer of judgment is not accepted, it may lead to higher litigation costs because both sides would spend more resources to litigate damages.¹⁴⁸ Katz

¹⁴⁶ *Id.* 68(d).

¹⁴⁷ Robert G. Bone, “To Encourage Settlement”: Rule 68, Offers of Judgment, and the History of the Federal Rules of Civil Procedure, 102 NW. U. L. REV. 1561, 1566–67 (2008).

¹⁴⁸ Katz & Sanchirico, *supra* note 11, at 22.

and Sanchirico argued that the plaintiff would spend higher fees than it otherwise would in trying to prove that its damages exceeded defendant's offer amount, while the defendant would spend higher fees in trying to prove that plaintiff's damages were less than the offered amount.¹⁴⁹

Katz and Sanchirico's finding is less applicable to patent cases. Damages in patent cases are notoriously wide-ranging. Plaintiffs and defendants usually identify damages amounts that differ by orders of magnitude.¹⁵⁰ Court decisions on damages are unpredictable, with differences in accounting and measurement theories creating potential swings of hundreds of millions of dollars in large cases.¹⁵¹ And damages awards are often reversed on appeal.¹⁵² Further, the law on calculating damages in patent cases has been, and is now, in a state of flux. Recognizing this uncertainty, parties already invest significant resources on proving the correctness of their widely disparate damages theories and figures. A past offer of judgment is unlikely to create a demarcation line that affects the parties' strategies on damages, or cause the parties to commit even greater resources to proving damages.

ii. Bond Requirement

¹⁴⁹ *Id.*

¹⁵⁰ Based on the authors' professional experience.

¹⁵¹ Based on the authors' professional experience.

¹⁵² In cases from 2000–2007 where the patentee won at the district court, the Federal Circuit reversed lost profit and reasonable royalty awards in 21 percent and 15 percent of cases, respectively. In cases from 2000–2007 where the accused infringer won at the district court, the Federal Circuit reversed lost profit and reasonable royalty awards in 25 percent and 50 percent of cases, respectively. Ted Sichelman, *Myths of (Un)Certainty at the Federal Circuit*, 43 LOY. L.A. L. REV. 1161, 1177 (2010).

Although this Article disapproved the fee-shifting provisions of the SHIELD Act of 2013 and the Patent Litigation Integrity Act of 2013, a positive aspect of both is the inclusion of a plaintiff bond requirement. Under § 285A(b) of the SHIELD Act of 2013, a party that cannot prove that it is one of the three types of non-NPE entities listed in subsection (d) must post a bond of an amount intended to cover all of the adverse party's anticipated litigation costs, including attorneys' fees.¹⁵³ Similarly, proposed § 285A of the Patent Litigation Integrity Act, provides a list of factors to consider for imposing a bond that covers the accused infringer's anticipated litigation costs, including attorneys' fees.¹⁵⁴ Most of these factors implicitly take aim at NPEs by disfavoring imposing bond on non-NPE entities such as universities, research institutions, manufacturers or sellers of products relating to the asserted patent, and original inventors and assignees.

The bond requirement should be applied to all patent cases. The bond could be refunded with interest if the case did not result in judgment against the plaintiff or if the court decided against shifting fees under § 285. Requiring the plaintiff to post a bond early in the case would impose a significant upfront cost on filing suit. This may discourage plaintiffs from filing weaker suits because they are not optimistic that the bond will be recovered. A bond requirement may also encourage plaintiffs to settle in order to guarantee recovery of their bond. This upfront cost also addresses the concern that the plaintiff using a contingent fee arrangement under the American Rule has no financial disincentive to filing suit. And if attorneys' fees under § 285 are awarded in 20-30

¹⁵³ SHIELD Act of 2013, *supra* note 6, § 2(a).

¹⁵⁴ Patent Litigation Integrity Act of 2013, *supra* note 6, § 201.

percent of patent cases that reach judgment as this Article recommends, the plaintiff faces a significant risk that its bond payment will not be recovered.

VI. CONCLUSION

Patent cases are difficult for courts to resolve correctly. The technology is complex, defining the scope of claimed inventions is difficult, and patent laws are constantly trying to keep pace with new fact patterns. Because of this, patent cases have grown in number and cost over the past decade, to the point where some companies (*i.e.*, NPEs) can make patent litigation their main business.

Policymakers should be lauded for trying to take on NPEs and reducing the number and cost of patent cases through fee shifting. But as this Article concludes, fee shifting's effects are more nuanced and complex than its proponents realized when applied to patent cases. The main reason why is because patent cases are tough to get right. Adopting fee shifting in patent cases is unlikely then to discourage plaintiffs from filing and continuing litigation, and may in fact have the opposite effect.

But using fee shifting selectively to sanction parties who bring objectively weak cases may effectively weed out the weak cases while maintaining a fair playing field for parties who bring meritorious cases. Combining selective fee shifting with other measures, such as offers of judgment and bond requirements, better achieves the policy goals of current legislative proposals.