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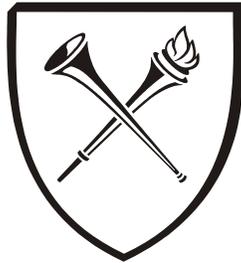
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**THE MYTH OF THE PATENT TROLL:  
AN ALTERNATIVE VIEW OF THE FUNCTION OF  
PATENT DEALERS IN AN IDEA ECONOMY**

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**THE MYTH OF THE PATENT TROLL:  
AN ALTERNATIVE VIEW OF THE FUNCTION OF PATENT  
DEALERS IN AN IDEA ECONOMY<sup>†</sup>**

INTRODUCTION

The evil patent trolls are here, or so the story goes. They have emerged from beneath the patent system's rusty trestles—old, dusty patents in hand. With reckless abandon they have brought some of corporate America's finest specimens humbly to their knees. They have earned the rebuke of the most revered publications—the *New York Times*,<sup>1</sup> the *Wall Street Journal*,<sup>2</sup> and the *Washington Post*,<sup>3</sup> to name a few. These giants are banging on the door of the United States Supreme Court,<sup>4</sup> and they are the new mascot for lobbyists pushing major legal reform.<sup>5</sup> But who are these trolls, and why are they so feared? Are they ghastly monsters suffocating a burgeoning patent system, or are they gentle giants poised to carry the United States patent system beyond the twenty-first century?

A patent troll is a person or entity who acquires ownership of a patent without the intention of actually using it to produce a product.<sup>6</sup> Instead, the patent troll buys the patent and either licenses the technology to a person or entity that will incorporate the patent into a product, or it sues a person believed to already have incorporated the technology in a product without permission.<sup>7</sup> Trolls are being almost universally denounced.<sup>8</sup> Critics argue

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<sup>†</sup> This Comment received the 2006 Mary Laura "Chee" Davis Award for Writing Excellence.

<sup>1</sup> Ian Austen & Lisa Guernsey, *A Payday for Patents 'R' Us*, N.Y. TIMES, May 2, 2005, at C1.

<sup>2</sup> William M. Bulkeley, *Aggressive Patent Litigants Pose Growing Threat to Big Business*, WALL ST. J., Sept. 14, 2005, at A1.

<sup>3</sup> Jonathan Krim, *Patenting Air or Protecting Property?*, WASH. POST, Dec. 11, 2003, at E01; Michael Liedtke, *Microsoft Ruling Overturned*, WASH. POST, Mar. 3, 2005, at E05.

<sup>4</sup> See, e.g., *NTP, Inc. v. Research In Motion, Ltd.*, 418 F.3d 1282 (Fed. Cir. 2005), *cert. denied*, 126 S. Ct. 1174 (2006); *MercExchange, L.L.C. v. eBay, Inc.*, 401 F.3d 1323 (Fed. Cir. 2005), *vacated and remanded*, 126 S. Ct. 1837 (2006); *Eolas Techs., Inc. v. Microsoft Corp.*, 399 F.3d 1325 (Fed. Cir. 2005), *cert. denied* 126 S. Ct. 568 (2005).

<sup>5</sup> Patent Reform Act of 2005, H.R. Res. 2795, 109th Cong. (2005).

<sup>6</sup> See generally 151 CONG. REC. E1160-01 (daily ed. June 8, 2005) (statement of Rep. Howard Berman) [hereinafter *Statement of Rep. Howard Berman*]; Brenda Sandburg, *Trolling for Dollars*, RECORDER (S.F., Cal.), July 30, 2001, at 1.

<sup>7</sup> Joe Beyers, *Perspective: Rise of the Patent Trolls*, CNET NEWS, Oct. 12, 2005, [http://news.com.com/Rise+of+the+patent+trolls/2010-1071\\_3-5892996.html](http://news.com.com/Rise+of+the+patent+trolls/2010-1071_3-5892996.html).

that patent trolls do not promote innovation<sup>9</sup> and are causing excessive, baseless litigation.<sup>10</sup> Accordingly, judicial and legislative action is being undertaken to put a stop to the practices of trolls.

This Comment argues that, contrary to popular belief, patent trolls actually benefit society. These trolls act as a market intermediary in the patent market. Patent trolls provide liquidity, market clearing, and increased efficiency to the patent markets—the same benefits securities dealers supply capital markets. Ultimately, this Comment suggests that the emergence of patent trolls is simply a stage in the natural evolution of the patent market.

Part I begins with a discussion of the new idea economy and the operation of trolls therein. Part II highlights the problems inherent in referring to nonproducing patent holders as trolls and reclassifies them with a more accurate market-contextual label. Part III isolates the activities of patent trolls by decoupling two issues that are erroneously identified with them. Part IV describes how patent trolls make the patent market more efficient by realigning market participant incentives, making patents more liquid, and clearing the patent market. This Part also analyzes the emergence of patent trolls in the context of market evolution. Finally, Part V concludes by rebutting the two major objections to patent trolls: that they stunt innovation and spur unnecessary litigation.

## I. THE IDEA ECONOMY AND THE TROLLS WITHIN

The economic landscape of the United States has changed dramatically in the last thirty-five years.<sup>11</sup> Whereas the value of corporations used to be grounded in land, natural resources, and human capital, the driving force in the U.S. economy today is intellectual property.<sup>12</sup> It should not be surprising, then, to learn of the emergence of companies that specialize in management of

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<sup>8</sup> See *infra* Part I.B.2.a–c.

<sup>9</sup> Letter from Adam Smith, Ellen Tauscher, Ron Kind, Artur Davis, Jay Inslee, Joseph Crowley, Jim Moran, Rick Larsen, Ben Chandler, Jim Davis, Eliot Engel, Gregory Meeks, John Larson, and Melissa Bean, U.S. Representatives, to Lamar Smith, Chairman, and Howard Berman, Ranking Member, Subcomm. on Courts, the Internet and Intellectual Prop. (May 19, 2005), available at <http://www.house.gov/tauscher/ndc/Letters%20on%20Site/Patent%20Letter.pdf> [hereinafter *Letter from New Democrat Coalition*].

<sup>10</sup> Timothy Aepfel, *Patent Dispute Embroils Host of Industries*, WALL ST. J., Oct. 21, 2004, at B1; Beyers, *supra* note 7, at 1; Brad Stone, *Patent Problems*, NEWSWEEK.COM, Oct. 13, 2004, <http://www.newsweek.org/id/6241971/site/newsweek/from/RL.5>.

<sup>11</sup> See *infra* Part I.A.

<sup>12</sup> See *infra* Part I.A.

intellectual property. In response to this emergence, there has been a concerted effort by large corporations and legislators, backed by the media, to put a stop to the practices of these entities pejoratively known as patent trolls.

A. *The New Idea Economy*

To appreciate the magnitude of the patent troll issue, a clear understanding of the importance of intellectual property to the U.S. economy is necessary. “[C]reativity, in the form of ideas, innovations, and inventions, has replaced gold, colonies, and raw materials as the new wealth of nations.”<sup>13</sup> This paradigm shift is illustrated by several key quantitative measures. Over the last twenty years, technology firms have been patenting more, increasing patent scope, licensing more frequently, and revamping their business strategies in an effort to prioritize intellectual property.<sup>14</sup> Between 1970 and 2004, the annual number of patents issued by the U.S. Patent and Trademark Office increased from 67,964 to 181,302.<sup>15</sup>

Intellectual property is equally important to U.S. foreign trade. U.S. trade in intellectual property has consistently produced a trade surplus over the last 20 years.<sup>16</sup> Between 1987 and 2001 (the last year in which such data is available), annual U.S. receipts from intellectual property foreign trade rose from \$9.9 billion to \$38.7 billion, creating a net surplus of \$22.3 billion in 2001.<sup>17</sup>

But, perhaps most convincing is the absolute shift in the economic landscape of the United States. The *Economist* recently observed:

In recent years intellectual property has received a lot more attention because ideas and innovations have become the most important resource, replacing land, energy and raw materials. As much as [75%] of the value of publicly traded companies in America comes from intangible assets, up from around 40% in the early 1980s.<sup>18</sup>

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<sup>13</sup> FRED WARSHOFKY, *THE PATENT WARS: THE BATTLE TO OWN THE WORLD'S TECHNOLOGY* 3 (1994).

<sup>14</sup> See generally *A Market for Ideas*, *ECONOMIST*, Oct. 22, 2005, at 3, 3 (special insert).

<sup>15</sup> See U.S. PATENT AND TRADEMARK OFFICE, U.S. PATENT STATISTICS CHART: CALENDAR YEARS 1963–2004, [http://www.uspto.gov/web/offices/ac/ido/oeip/taf/us\\_stat.htm](http://www.uspto.gov/web/offices/ac/ido/oeip/taf/us_stat.htm).

<sup>16</sup> See Lawrence M. Rausch, *Industry, Technology, and the Global Marketplace*, in 1 *SCIENCE AND ENGINEERING INDICATORS 2004*, at 6–13 (Nat'l Sci. Bd. ed., 2004), available at <http://www.nsf.gov/statistics/seind04/pdf/c06.pdf>.

<sup>17</sup> *Id.*

<sup>18</sup> *A Market for Ideas*, *supra* note 14, at 3.

Alan Greenspan, former Chairman of the Federal Reserve Board, recently proclaimed that “[t]he economic product of the United States . . . has become ‘predominantly conceptual.’”<sup>19</sup> Intellectual property has become the new economic foundation of the United States.<sup>20</sup>

### B. Patent Trolls in the Idea Economy

Given the importance of the patent system,<sup>21</sup> its integrity must be upheld.<sup>22</sup> Consequently, there need to be mechanisms of management for this system. Yet, individuals and investors acting in this capacity are criticized as trolls before a full understanding of their role in the patent economy is understood. This raises the question: are trolls really a threat to the integrity of the patent system? Answering the question demands a closer look at the trolls and the arguments against them.

#### 1. The Anatomy of a Troll

Originally, nonproducing entities that purchased patents were referred to as patent extortionists.<sup>23</sup> By the 1990s, these “unsavory characters who buy up obscure patents to extort money from innovative and law-abiding companies”<sup>24</sup> came to be called “patent trolls.” Peter Detkin, former assistant general counsel for Intel, created the term after Intel was “sued for libel for its use of the term ‘patent extortionist.’”<sup>25</sup> According to Mr. Detkin, “A patent troll is somebody who tries to make a lot of money off a patent that they are not practicing and have no intention of practicing and in most cases never practiced.”<sup>26</sup> Instead of producing products, the troll licenses and enforces patents.<sup>27</sup>

More precisely, the nature of these so-called trolls can be boiled down to three general categories.<sup>28</sup> At one end of the spectrum are individual owners of

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<sup>19</sup> *Id.*

<sup>20</sup> See generally *supra* notes 13–19 and accompanying text.

<sup>21</sup> See *supra* Part I.A.

<sup>22</sup> *The Real Lesson of Blackberry*, ECONOMIST, Dec. 17, 2005, at 13.

<sup>23</sup> Sandburg, *supra* note 6.

<sup>24</sup> Steven Pearlstein, *Big Firms Caught with Their Patents Down*, WASH. POST, Dec. 2, 2005, at D01.

<sup>25</sup> Sandburg, *supra* note 6.

<sup>26</sup> *Id.*; see also *Statement of Rep. Howard Berman*, *supra* note 6, at E1160–61.

<sup>27</sup> See 150 CONG. REC. E1935–03 (Extensions Oct. 11, 2004).

<sup>28</sup> See Brad D. Krueger, *Pulling Trolls Out from Under the Bridge: Proposed Patent Reforms*, GERMESHAUSEN CENTER NEWSL. (Franklin Pierce Law Center, Concord, N.H.), Winter/Spring 2005, at 4, available at <http://www.resources.piercelaw.edu/pubs/Germ05S.pdf>.

patented inventions that do not make a product but are suing a large corporation for infringement.<sup>29</sup> In the middle are companies like Intellectual Ventures, an intellectual property think tank that generates ideas for the purpose of patenting, with an eye towards eventually licensing those patents.<sup>30</sup> On the other end of the spectrum are patent holding companies like Acacia Research Corporation, a company that purchases patents merely for licensing and enforcement purposes.<sup>31</sup> Notably, none of the activities associated with trolls are well-regarded in the corporate community.

## 2. *Battling the Trolls: The Movement to Stop Trolls*

The general attitudes toward trolls are almost uniformly negative.<sup>32</sup> In fact, there are three ways in which efforts are being aggressively undertaken to stop them.<sup>33</sup> In an attempt to curtail the activities of patent trolls, large corporations are seeking the option of having injunctions stayed when the patent holder is not in competition with the infringer.<sup>34</sup> Further, large corporations are pushing for new legislation targeted at stopping trolls.<sup>35</sup> Finally, several commentators have criticized them.<sup>36</sup>

### a. *Legal Action: Trolling at the Supreme Court*

There is substantial activity in the courts relating to patent trolls, and several parties in such cases have petitioned for certiorari to the U.S. Supreme Court.<sup>37</sup> Three cases illustrate the trolls' ubiquitous presence: *NTP, Inc. v. Research In Motion, Ltd.*,<sup>38</sup> *Eolas Technologies, Inc. v. Microsoft Corp.*,<sup>39</sup> and *MercExchange, L.L.C. v. eBay, Inc.*<sup>40</sup> In each case, a small, nonproducing

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<sup>29</sup> See, e.g., Jason Kirby, *Patent Troll or Producer? The Evolution of Intellectual Property*, NAT'L POST (Ont., Can.), Jan. 14, 2006, at FP1.

<sup>30</sup> See *id.*

<sup>31</sup> *Id.*; see, e.g., Acacia Research Corporation, About Us, [http://www.acaciaresearch.com/aboutus\\_main.htm](http://www.acaciaresearch.com/aboutus_main.htm) (last visited Apr. 17, 2006).

<sup>32</sup> See *infra* Part I.B.2.a-c.

<sup>33</sup> See *infra* Part I.B.2.a-c.

<sup>34</sup> See *infra* Part I.B.2.a

<sup>35</sup> See *infra* Part I.B.2.b

<sup>36</sup> See *infra* Part I.B.2.c

<sup>37</sup> See *NTP, Inc. v. Research In Motion, Ltd.*, 418 F.3d 1282 (Fed. Cir. 2005), *cert. denied*, 126 S. Ct. 1174 (2006); *MercExchange, L.L.C. v. eBay, Inc.*, 401 F.3d 1323 (Fed. Cir. 2005), *vacated and remanded*, 126 S. Ct. 1837 (2006); *Eolas Techs., Inc. v. Microsoft Corp.*, 399 F.3d 1325 (Fed. Cir. 2005), *cert. denied*, 126 S. Ct. 568 (2005).

<sup>38</sup> 418 F.3d 1282.

<sup>39</sup> 399 F.3d 1325.

<sup>40</sup> 401 F.3d 1323.

entity sued a larger company to enforce a patent—the typical patent troll scenario.<sup>41</sup>

The Supreme Court granted certiorari in *MercExchange, L.L.C. v. eBay, Inc.*<sup>42</sup> The main question in the case was whether the district court properly denied MercExchange's motion for injunctive relief against eBay, the alleged infringer.<sup>43</sup> At issue in the case was eBay's fixed-price purchasing feature, which allows customers to purchase items that are listed on eBay's website for static, listed prices.<sup>44</sup> MercExchange owns a patent that broadly covers the creation of an online marketplace where items can be offered under live auction conditions and at fixed prices for immediate purchase.<sup>45</sup> MercExchange claimed that eBay was infringing upon this patent.<sup>46</sup> Although the district court jury verdict favored MercExchange, and found that eBay was infringing the patent, the court did not grant an injunction against eBay because it found that MercExchange's "willingness to license its patents [and] its lack of commercial activity in practicing its patents . . . are sufficient to rebut the presumption that it will suffer irreparable harm if an injunction does not issue."<sup>47</sup> The Federal Circuit did not find the case to be "sufficiently exceptional to justify the denial of a permanent injunction," and it reversed the district court's denial of injunctive relief.<sup>48</sup> The Supreme Court vacated the Federal Circuit decision and remanded after deciding that it is not necessary for a patent owner to actually practice the patent as a prerequisite to getting an injunction.<sup>49</sup> However, in his concurring opinion, Justice Kennedy suggested that trial courts should consider whether the patent holder is a patent troll when considering whether to grant an injunction.<sup>50</sup>

A second prominent patent troll case was *NTP, Inc. v. Research In Motion, Ltd.*,<sup>51</sup> otherwise known as the BlackBerry Case.<sup>52</sup> In that case, an intellectual property holding company called NTP claimed that Research In Motion ("RIM"), the maker of the popular BlackBerry email devices, was infringing

<sup>41</sup> See *NTP*, 418 F.3d 1282; *MercExchange*, 401 F.3d 1323; *Eolas*, 399 F.3d 1325.

<sup>42</sup> 126 S. Ct. 733 (2005).

<sup>43</sup> *MercExchange*, 401 F.3d at 1325.

<sup>44</sup> *Id.*

<sup>45</sup> *Id.* at 1325–26; U.S. Patent No. 5,845,265 (filed Nov. 7, 1995).

<sup>46</sup> *MercExchange*, 401 F.3d at 1325.

<sup>47</sup> *MercExchange, L.L.C. v. eBay, Inc.*, 275 F. Supp. 2d 695, 710–15 (E.D. Va. 2003).

<sup>48</sup> *MercExchange, L.L.C. v. eBay, Inc.*, 401 F.3d 1323, 1339 (Fed. Cir. 2005).

<sup>49</sup> *eBay, Inc. v. MercExchange, L.L.C.*, 126 S. Ct. 1837, 1840–41 (2006).

<sup>50</sup> *Id.* at 1842–43 (Kennedy, J., concurring).

<sup>51</sup> 418 F.3d 1282 (Fed. Cir. 2005).

<sup>52</sup> Krim, *supra* note 3.

on several of its patents.<sup>53</sup> The court found that BlackBerry's email retrieval system infringed upon the NTP patents and awarded damages and a permanent injunction against RIM.<sup>54</sup> Ultimately, RIM's petition for certiorari was rejected,<sup>55</sup> and the case settled for \$612.5 million.<sup>56</sup>

The third high-profile troll case was *Eolas Technologies, Inc. v. Microsoft Corp.*<sup>57</sup> Eolas is a company that "create[s] and develop[s] the inventions that allow information technologies to enhance the quality of life for everyone."<sup>58</sup> Eolas sued Microsoft for infringing on a patent covering embedded website technology,<sup>59</sup> claiming that Microsoft's Internet Explorer incorporated its invention.<sup>60</sup> The Court held that Microsoft was infringing on the patent and granted damages and an injunction pending appeal.<sup>61</sup> A petition for certiorari was rejected by the Supreme Court.<sup>62</sup>

*b. Legislative Action: The Patent Reform Act of 2005*

In addition to challenges to trolls in court, major legislative reform is being pressed.<sup>63</sup> In June of 2005, Congressman Lamar Smith introduced the Patent Reform Act of 2005,<sup>64</sup> the most substantial legislative reform to the patent system since 1952.<sup>65</sup> The Act was largely prompted by disdain for patent trolls and their practices.<sup>66</sup> The proposed bill includes several significant changes to the patent system.<sup>67</sup> For purposes of this Comment, the most significant is the

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<sup>53</sup> 418 F.3d at 1287. There were five patents at issue. U.S. Patent No. 6,317,592 (filed Dec. 6, 1999); U.S. Patent No. 6,067,451 (filed Sept. 28, 1998); U.S. Patent No. 5,819,172 (filed Apr. 23, 1997); U.S. Patent No. 5,625,670 (filed May 18, 1995); U.S. Patent No. 5,436,960 (filed May 20, 1991).

<sup>54</sup> *NTP*, 413 F.3d at 1287 (awarding NTP \$53,704,322.69 in damages).

<sup>55</sup> *Research In Motion, Ltd. v. NTP, Inc.*, 126 S. Ct. 1174 (2006).

<sup>56</sup> Yuki Noguchi, *BlackBerry Patent Dispute Is Settled*, WASH. POST, Mar. 4, 2006, at A01.

<sup>57</sup> 399 F.3d 1325 (Fed. Cir. 2005).

<sup>58</sup> Eolas Technologies Corporate Vision, [http://www.eolas.com/about\\_us.html](http://www.eolas.com/about_us.html) (last visited Apr. 17, 2006).

<sup>59</sup> *Eolas*, 399 F.3d at 1328.

<sup>60</sup> *Id.* at 1329.

<sup>61</sup> *Id.*

<sup>62</sup> *Microsoft Corp. v. Eolas Techs., Inc.*, 126 S. Ct. 568 (2005).

<sup>63</sup> *Opening Statement on the Patent Act of 2005: Hearing on H.R. 2795 Before Subcommittee on Courts, the Internet, and Intellectual Property* (2005) (statement of the Rep. Lamar Smith, Subcommittee on Courts, the Internet, and Intellectual Property) [hereinafter *Opening Statement of Rep. Lamar Smith*].

<sup>64</sup> H.R. 2795, 109th Cong. (2005).

<sup>65</sup> *Id.*

<sup>66</sup> *Letter from New Democrat Coalition*, *supra* note 9; see also *Opening Statement of Rep. Lamar Smith*, *supra* note 63 (stating that the bill will "eliminate legal gamesmanship from the current system that rewards lawsuit abuses over creativity").

<sup>67</sup> H.R. 2795.

proposed injunctive stay provisions, which are aimed directly at trolls.<sup>68</sup> The original bill required a finding of irreparable harm not compensable by damages before an injunction could be granted, and allowed courts to consider how the company owning the allegedly infringed patent actually used the invention when granting an injunction.<sup>69</sup> The sponsors of the bill “encourage[d] the Committee to take aim at those who seek to abuse the patent system for profit.”<sup>70</sup>

*c. Commentary*

Most commentators appear to side with big corporations,<sup>71</sup> and are salivating at the chance to talk about the “troll attack,”<sup>72</sup> portraying patent trolls as “parasites on successful businesses,”<sup>73</sup> and comparing them to the “mold that eventually grows on rotten meat.”<sup>74</sup> Trolls have been described as persons or entities who “secretly [wait] for another inventor to develop the same technology” only to later appear and demand license fees from successful business.<sup>75</sup> They have been called “patent system bottom feeders”<sup>76</sup> that “want[] glittering pots of gold in exchange for doing absolutely nothing.”<sup>77</sup> Commentators criticize the trolls for “manipulat[ing] the patent system for large profits.”<sup>78</sup> Still others say that trolls “are engaging in nothing more than

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<sup>68</sup> § 7.

<sup>69</sup> *Id.*

<sup>70</sup> *Letter from New Democrat Coalition*, *supra* note 9. This subtext refers to the troll problem. The representatives endorsing the letter refer to the “so-called ‘patent trolls’ who accumulate patents not to further innovation and develop new products, but to use patents as litigation tools.” *Id.* This is evidenced by the bill being supported by the New Democrat Coalition (NDC), a coalition of Members of Congress supported by software and hardware industry giants. *Id.*

<sup>71</sup> See, e.g., David G. Barker, Comment, *Troll or No Troll? Policing Patent Usage with an Open Post-Grant Review*, 2005 DUKE L. & TECH. REV. 0009, ¶ 5; Tim Wu, *Weapons of Business Destruction*, SLATE, Feb. 6, 2006, <http://www.slate.com/id/2135559>.

<sup>72</sup> Beyers, *supra* note 7.

<sup>73</sup> Bulkeley, *supra* note 2.

<sup>74</sup> Wu, *supra* note 71.

<sup>75</sup> Barker, *supra* note 71, ¶ 7.

<sup>76</sup> *Patent Quality Improvement: Hearings Before the Subcomm. on Courts, the Internet and Intellectual Property of the House Comm. on the Judiciary*, 108th Cong. 21 (2003) (statement of David M. Simon, Chief Patent Counsel, Intel Corp.).

<sup>77</sup> Sandburg, *supra* note 6.

<sup>78</sup> Roy Mark, *Tech Wants Patent ‘Trolls’ Tamed*, INTERNETNEWS.COM, Apr. 26, 2005, <http://www.internetnews.com/bus-news/article.php/3500546>.

legalized extortion.”<sup>79</sup> Although some commentators recognize the potential value of trolls, their utility is mentioned merely in passing.<sup>80</sup>

### 3. *The Stakes: The Integrity of the U.S. Patent System*

Although the recent Supreme Court activity and the provisions proposed in the Patent Reform Act of 2005 are important, these are only used to illustrate the prominent role trolls occupy in today’s legal landscape. The more pressing issue is the general integrity of the patent system. As the *Economist* recently pronounced, “Defending the patent system is more important than keeping [a company] up and running.”<sup>81</sup> Limiting the patent holder’s ability to stop the infringing activity will severely diminish the value of patents because the only right inherent in a patent is the right to exclude others from its use.<sup>82</sup> Taking this away would weaken the patent—the foundation of the U.S. economy.<sup>83</sup> Before radical changes are enacted at any level, it is imperative to ensure there really is a problem to fix. This Comment suggests that although there are problems with the patent system that need to be addressed, patent trolling is not among them.

## II. A REQUISITE CHANGE IN NOMENCLATURE

In analyzing the criticisms of trolls, and ultimately constructing a broader conception of their role, nondescriptive labels and inaccurate rhetoric need to be set aside. This Comment embarks on an analysis of the function of trolls in the economy. First and foremost, it is important to properly characterize those being labeled as “patent trolls.” This Comment suggests replacing the simplistic, derogatory, and unnecessarily overinclusive troll label with a new, more accurate label.

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<sup>79</sup> Bernard Stamler, *Battles of the Patents, Like David v. Goliath*, N.Y. TIMES, Feb. 21, 2006, at G2.

<sup>80</sup> See Barker, *supra* note 71, ¶ 11 (conceding that some troll behavior is sometimes necessary to protect patent rights); Elizabeth D. Ferrill, Comment, *Patent Investment Trusts: Let’s Build a PIT to Catch the Patent Trolls*, 6 N.C.J.L. & TECH. 367, 378–79 (2005) (noting the benefits of speculators).

<sup>81</sup> *The Real Lesson of Blackberry*, *supra* note 22, at 13.

<sup>82</sup> 35 U.S.C. § 261 (2000). A patentee has an exclusive property right in his patented invention. *James v. Campbell*, 104 U.S. 356, 358 (1881).

<sup>83</sup> See *supra* Part I.A.

### A. *The Inadequacy of the Troll Label*

As Part I explained, under the current understanding “a patent troll is somebody who tries to make a lot of money off a patent that they are not practicing and have no intention of practicing and in most cases never practiced.”<sup>84</sup> This label is clumsy and overinclusive, and is ultimately damaging to the discussion of the American patent system.

#### 1. “*The King of the Patent Trolls*”<sup>85</sup>

To highlight the problems with the “patent troll” label, a quick look at one of the worst individual trolls in history is illustrative.<sup>86</sup> For decades, this person held the U.S. record for the number of patents held by an individual<sup>87</sup>—an astounding 1,093.<sup>88</sup> This person primarily “described himself as an inventor,”<sup>89</sup> and although many of his inventions were incorporated into products,<sup>90</sup> he made a fortune from many patents that he never practiced.<sup>91</sup> Not only did this man not practice nor have any intention of practicing many of his inventions, but he actually invented items specifically to deter innovation.<sup>92</sup> This king of trolls was none other than Thomas Edison.<sup>93</sup>

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<sup>84</sup> Sandburg, *supra* note 6; *see also* *Statement of Rep. Howard Berman*, *supra* note 6, at E1160–01.

<sup>85</sup> *See* Posting of Gary Odom to The Patent Prospector, [http://www.patenthawk.com/blog/archives/2005/03/patent\\_troll\\_ho\\_1.html](http://www.patenthawk.com/blog/archives/2005/03/patent_troll_ho_1.html) (Mar. 22, 2005, 00:02 EDT) (labeling Edison as the “King of the Patent Trolls”).

<sup>86</sup> *See id.*

<sup>87</sup> ANDRE MILLARD, *EDISON AND THE BUSINESS OF INNOVATION* 43 (1990); *see also* Odom, *supra* note 85.

<sup>88</sup> Kevin Maney, *Search for the Most Prolific Inventors Is a Patent Struggle*, USA TODAY, Dec. 7, 2005, at 3B; Library of Congress, American Memory, *Inventing Entertainment, The Motion Pictures and Sound Recordings of the Edison Companies*, <http://memory.loc.gov/ammem/edhtml/edhome.html> (last visited Apr. 18, 2006).

<sup>89</sup> MILLARD, *supra* note 87, at 43.

<sup>90</sup> *See generally id.* at 43–44 (discussing the inventions that Edison reduced to models).

<sup>91</sup> *See generally id.* (Obviously, Edison did not personally commercialize anywhere near 1,093 patents.).

<sup>92</sup> Thomas Edison invented the electric chair in an attempt to illustrate the dangers of alternating current electricity. *See* RICHARD MORAN, *EXECUTIONER’S CURRENT: THOMAS EDISON, GEORGE WESTINGHOUSE, AND THE INVENTION OF THE ELECTRIC CHAIR* 57–62 (2002) (discussing the battle between George Westinghouse and Edison, and the eventual creation of the electric chair). He also launched a patent war against George Westinghouse and all electric companies. *Id.* at 53.

<sup>93</sup> *See generally* MILLARD, *supra* note 87; *see also* Odom, *supra* note 85.

## 2. *The Trolls of Government and Academia*

In 1980, the Congress passed the Bayh-Dole Act.<sup>94</sup> Under this Act, Congress allowed the fruits of government-funded university research to be commercialized.<sup>95</sup> Prior to the Act, uncertainty about the ownership of federally funded university research and governmental restrictions on technology licensing hampered the commercialization of university research.<sup>96</sup> For instance, “[i]n 1980, the federal government held title to approximately 28,000 patents,”<sup>97</sup> of which, only about five percent were licensed to industry for commercial development.<sup>98</sup> The ultimate effect of the Act is that university research can be patented and sold or licensed to private companies more efficiently.<sup>99</sup> The passing of this Act has been credited as one of the most important contributions to the success of the modern U.S. intellectual property system.<sup>100</sup>

Yet, under Detkin’s definition, the U.S. government and government-funded research universities become trolls by way of the Bayh-Dole Act. The universities, funded by the government, do not intend to use or practice the inventions they patent.<sup>101</sup> Nor do they manufacture goods.<sup>102</sup> Instead, the main goal of university research is to earn revenue by licensing the technology.<sup>103</sup> As a result, government-funded universities make a lot of money off patents that they “are not practicing and have no intention of practicing and in most cases never practiced.”<sup>104</sup>

## 3. *Real Property Trolls*

An analogy to real property illustrates further shortcomings with the troll label. Imagine that Person A discovers a piece of property called Blackacre<sup>105</sup>

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<sup>94</sup> Pub. L. No. 96-517, 94 Stat. 3015 (1980) (codified as amended at 35 U.S.C. §§ 200–12, 301–07 (2000)).

<sup>95</sup> *Id.*

<sup>96</sup> COUNCIL ON GOVERNMENTAL RELATIONS, THE BAYH-DOLE ACT: A GUIDE TO THE LAW AND IMPLEMENTING REGULATIONS 1–2 (1999), available at [http://www.cogr.edu/docs/Bayh\\_Dole.pdf](http://www.cogr.edu/docs/Bayh_Dole.pdf).

<sup>97</sup> *Id.* at 2.

<sup>98</sup> *Id.*

<sup>99</sup> *Id.*

<sup>100</sup> Opinion, *Innovation’s Golden Goose*, ECONOMIST TECH. Q., Dec. 14, 2002, at 3, 3.

<sup>101</sup> Universities often have a clause stating that the university may use the invention as a base upon which to conduct further research. COUNCIL ON GOVERNMENTAL RELATIONS, *supra* note 96, at 9–10.

<sup>102</sup> See Clifton Leaf, *The Law of Unintended Consequences*, FORTUNE, Sept. 19, 2005, at 250, 252.

<sup>103</sup> *Id.*

<sup>104</sup> Sandburg, *supra* note 6.

<sup>105</sup> Clearly rare in modern society, though not impossible, and necessary for the analogy to work.

and registers ownership with the State of Ames.<sup>106</sup> Person A wants to leave the property in its current state and is not sure in exactly what manner he should develop the property, though he is quite willing to sell it or lease it. Corporation X sees Blackacre and decides it is the perfect piece of land upon which to build a shopping center. Corporation X builds the shopping center and opens for business. Person A visits his property one day for maintenance purposes and sees that Corporation X has built the shopping center. Person A immediately notifies Corporation X of his rightful ownership interest in Blackacre. Corporation X denies the ownership of Person A and ignores further demands by Person A to either move the mall or lease the land. Unfortunately, Person A has no money with which to litigate for ejectment.

Unable to proceed with litigation because of financial constraints, Person A sells the property to Corporation Y. Corporation Y has unlimited funds with which to litigate and sends a letter declaring its intent to proceed with litigation against Corporation X. Rather than face the credible threat of litigation, Corporation X settles and buys or leases the land from Corporation Y. A real property troll is born.

In this case, it would be difficult to argue that Corporation Y has anything but full rights to proceed against Corporation X. Corporation Y is seen as merely enforcing its property rights against Corporation X. Under the law of adverse possession in most states, Corporation Y is actually required to act, or it faces losing its interest in the property.<sup>107</sup> However, when it comes to owners of patents, analogous acts are denounced.

#### *B. Patent Dealers: Toward a More Productive Discourse*

The current label for nonpracticing patent-holders is overinclusive.<sup>108</sup> It can be used to describe a broad range of patent users, from the individual inventor to research universities. Further, the term “troll” has obvious negative connotations.<sup>109</sup> To effectuate a more balanced discussion of the phenomena, a change of vocabulary is warranted.

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<sup>106</sup> A hypothetical state in the United States.

<sup>107</sup> See, e.g., *Greenberg v. Sutter*, 684 N.Y.S.2d 571 (N.Y. App. Div. 1999). To prove a prima facie case of adverse possession, the plaintiff must show that possession of subject property was “in an actual, open, notorious, exclusive and hostile manner, under claim of title or ownership.” *Id.* at 1255.

<sup>108</sup> See *supra* Part II.A.

<sup>109</sup> “In Norse Mythology, [trolls were] repulsive dwarfs who lived in caves or other hidden places. They would steal children and property but hated noise.” E.D. HIRSCH, JR. ET AL., *THE NEW DICTIONARY OF CULTURAL LITERACY* 45 (3rd ed. 2002).

A more suitable, market-contextual term for nonpracticing patent owners who license or enforce their patents is “patent dealers.”<sup>110</sup> Patent trolls will be referred to as patent dealers in the remainder of this Comment. This term is more appropriate because, as a market concept, it more accurately identifies the activities at issue.<sup>111</sup> For example, in a securities market the term “dealer” refers to an individual or entity that buys and sells stock and holds an inventory.<sup>112</sup> Patent dealers serve a similar function in the idea economy.<sup>113</sup>

### III. DETANGLING THE DISCOURSE

The first step in promoting a more balanced discussion on this topic was exposing the former derogatory label as deficient and relabeling the individuals or entities as “patent dealers.”<sup>114</sup> This market-contextual label is more accurate.<sup>115</sup> The second step in this analysis is the identification and decoupling of two issues that are being incorrectly conflated with patent dealers: (1) the issuance of poor-quality patents, and (2) the problem of the patent thickets.<sup>116</sup>

A growing collection of literature illustrates the many problems plaguing the U.S. patent system.<sup>117</sup> Long gone are the days when the U.S. patent system’s biggest inefficiency was the fact that the Patent Office had only one

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<sup>110</sup> See DAVID L. SCOTT, WALL STREET WORDS: AN A TO Z GUIDE TO INVESTMENT TERMS FOR TODAY’S INVESTOR 87 (3rd ed. 2003).

[A dealer is an] individual or a firm that buys assets for and sells assets from its own portfolio as opposed to bringing buyers and sellers together. In practice, many firms operate as broker-dealers and perform both services depending on the market conditions and on the size, type, and security involved in a particular transaction.

*Id.*

<sup>111</sup> *Id.*; see also *infra* Part IV.C.

<sup>112</sup> See generally SCOTT, *supra* note 110, at 87. More specifically, the term “dealer” is defined in the Securities Act of 1933 as “any person who engages either for all or part of his time, directly or indirectly . . . in the business of offering, buying, selling, or otherwise dealing or trading in securities issued by another person.” 15 U.S.C. § 77b(a)(12) (2000).

<sup>113</sup> See *infra* Part IV.C.

<sup>114</sup> See *supra* Part II.

<sup>115</sup> See *supra* Part II.B.

<sup>116</sup> See *infra* Part III.A–B.

<sup>117</sup> See, e.g., Michael S. Mireles, Jr., *The United States Patent Reform Quagmire: A Balanced Proposal*, 6 MINN. J. L. SCI. & TECH. 709, 716, 719 (2005) (reviewing ADAM B. JAFFE & JOSH LERNER, INNOVATION AND ITS DISCONTENTS: HOW OUR BROKEN PATENT SYSTEM IS ENDANGERING INNOVATION AND PROGRESS, AND WHAT TO DO ABOUT IT (2004)); John R. Thomas, *Collusion and Collective Action in the Patent System: A Proposal for Patent Bounties*, 2001 U. ILL. L. REV. 305, 316–22.

pony riding across town to secure the President's signature.<sup>118</sup> This Comment strives to separate the two aforementioned issues from the patent dealer discussion. Confusing these two issues with the activities of patent dealers is causing the negative effects of poor-quality patents to be associated with patent dealers. Therefore, a brief review of the poor-quality patent and the patent thickets problems will be undertaken so they may be recognized and isolated from the discussion.

#### A. *The Issuance of Poor-Quality Patents*

The first problem frustrating discussion is the quality of the patents being issued by an understaffed U.S. Patent and Trademark Office.<sup>119</sup> Bad patents are being issued daily: the issuance of patents for the protection of inventions like the crust-free peanut butter and jelly sandwich,<sup>120</sup> a method of exercising a housecat with a laser pointer,<sup>121</sup> and a method for swinging on a swing<sup>122</sup> illustrate the status quo. This is by far the most glaring issue with the patent system.<sup>123</sup>

Regrettably, opponents of patent trolls associate this issue with patent dealers, effectively imputing the problems of poor-quality patents to patent dealers.<sup>124</sup> In reality, anyone wielding a bad patent can abuse the patent system; this problem is not unique to patent dealers. Therefore, it should be addressed separately.<sup>125</sup> Accordingly, when this Comment refers to patents, it refers only to quality patents, meaning patents with well-defined property rights that are neither overinclusive nor underinclusive.

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<sup>118</sup> KENNETH W. DOBYNS, *THE PATENT OFFICE PONY: A HISTORY OF THE EARLY PATENT OFFICE* 4 (1994).

<sup>119</sup> Letter from Michael K. Kirk, Executive Dir., Am. Intellectual Prop. Law Ass'n, to Hon. Jon Dudas, Acting Dir., U.S. Patent and Trademark Office (Feb. 7, 2004), available at <http://www.uspto.gov/web/offices/pac/dapp/opla/comments/oedrep/aipla.html>.

<sup>120</sup> U.S. Patent No. 5,567,454 (filed July 13, 1994).

<sup>121</sup> U.S. Patent No. 6,701,872 (filed Oct. 30, 2002).

<sup>122</sup> U.S. Patent No. 6,368,227 (filed Nov. 17, 2000).

<sup>123</sup> Peter Geier, *Bill in Congress to Overhaul Patent Law Seeks to Quell Suits*, NAT'L L.J., Aug. 15, 2005, at 1. This appears to parallel, coincidentally of course, the creation of the U.S. Court of Appeals for the Federal Circuit on October 1, 1982. Federal Courts Improvement Act of 1982, Pub. L. No. 97-164, 96 Stat. 25.

<sup>124</sup> See, e.g., Krueger, *supra* note 28, at 4; Letter from New Democrat Coalition, *supra* note 9.

<sup>125</sup> Geier, *supra* note 123.

### B. *The Patent Thickets*

The patent thickets problem, a form of “tragedy of the anticommons,”<sup>126</sup> is a phenomenon by which people underuse scarce resources because of overlapping ownership.<sup>127</sup> In the patent thickets, a technology is prone to underuse because of the high costs of licensing resulting from multiple ownership stakes in the same technology.<sup>128</sup> The patent thicket problem is at the forefront in corporate settings, as evidenced by the defensive use of patent portfolios.<sup>129</sup> Patent portfolios are being used defensively in efforts to alleviate the patent thicket problem, encourage cross-licensing, and create leverage in infringement lawsuits.<sup>130</sup> Essentially, if a company is threatened with a suit, it can threaten to countersue with patents from their own patent portfolio, thereby encouraging a more favorable settlement.<sup>131</sup> Commentators deem the defensive use of patent portfolios necessary to balance competition in this patent-rich environment.<sup>132</sup>

Patent dealers are generally immune from the effects of defensive patenting because they do not manufacture products,<sup>133</sup> and therefore there is no basis for a potential countersuit. Consequently, a company’s extensive patent portfolio creates no countersuit threat, and the patent dealer does not have to factor in the cost of a countersuit when deciding whether to bring a lawsuit.<sup>134</sup> As a result of this immunity to the use of defensive patent portfolios, the patent thickets problem is more evident when patent dealers are involved in a suit. Consequently, the patent thickets problem and patent dealers are often discussed together, creating confusion.<sup>135</sup> Again this problem is distinct from the existence of patent dealers and their practices, so this Comment will not address the problem directly.<sup>136</sup> The patent thicket problem is broad and

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<sup>126</sup> See Michael A. Heller & Rebecca S. Eisenberg, *Can Patents Deter Innovation? The Anticommons in Biomedical Research*, 280 *SCIENCE* 698, 698 (1998).

<sup>127</sup> FED. TRADE COMM’N, *TO PROMOTE INNOVATION: THE PROPER BALANCE OF COMPETITION AND PATENT LAW AND POLICY* 25 box2-3a (2003), available at <http://www.ftc.gov/os/2003/10/innovationrpt.pdf>.

<sup>128</sup> *Id.* at 34.

<sup>129</sup> Krueger, *supra* note 28, at 4.

<sup>130</sup> See FEDERAL TRADE COMMISSION, *supra* note 127, at 31.

<sup>131</sup> Krueger, *supra* note 28, at 4–5.

<sup>132</sup> See Carl Shapiro, *Navigating the Patent Thicket: Cross Licenses, Patent Pools, and Standard Setting*, 11 *INNOVATION POL’Y & ECON.* 119, 125 (2001).

<sup>133</sup> Krueger, *supra* note 28, at 5; see also FEDERAL TRADE COMMISSION, *supra* note 127, at 31.

<sup>134</sup> Krueger, *supra* note 28, at 4.

<sup>135</sup> *Statement of Rep. Howard Berman*, *supra* note 6.

<sup>136</sup> FEDERAL TRADE COMMISSION, *supra* note 127, at 31.

applicable to the entire patent system.<sup>137</sup> Therefore, its resultant problems should be addressed separately.

Keeping the issues of poor-quality patents and patent thickets on a separate footing will promote a clear understanding of the function of patent dealers. As it stands, most discussions about patent dealers concurrently refer to these two issues. As a result, the true function patent dealers play in the new economy is being obscured.

#### IV. MARKET MAKERS: AN ALTERNATIVE STORY OF PATENT DEALERS

The remainder of this Comment argues that *the activities of patent dealers in their pure form benefit society*.<sup>138</sup> The first step leading to this hypothesis was to relabel the individuals or entities as patent dealers.<sup>139</sup> The second step was to identify and conceptually decouple two independent issues—poor-quality patents and patent thickets—that are often improperly associated with patent dealers.<sup>140</sup>

The third step will be to analyze the activities of patent dealers from an economic perspective. Section A argues the premise that the patent system is a market unto itself, that patents have been commodified within this market, and that there is a need for a credible threat of litigation to ensure market success. Section B analyzes the market state without patent dealers and then explains the change in market dynamics that would occur if a patent dealer entered the market. Section C then explains how these changes make the patent market more efficient by creating a credible threat of litigation, making patents more liquid, and clearing the patent market. Finally, Section D contextualizes patent dealers within the patent market through a market evolution framework.

##### A. *The Market for Ideas*

“[J]ust as the banking system created a market for capital and the insurance industry created a market for risk, the growth of the patent system may be creating a market for innovation.”<sup>141</sup> This proposition can be easily accepted

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<sup>137</sup> See generally Shapiro, *supra* note 132, at 119–26.

<sup>138</sup> The term “pure form” refers to the activities of patent dealers without conflating the issues surrounding poor patents and the patent thickets.

<sup>139</sup> See *supra* Part II.B.

<sup>140</sup> See *supra* Part III.

<sup>141</sup> *A Market for Ideas*, *supra* note 14, at 6.

under the following conditions: (1) the evolution of markets is understood, (2) the nonrival nature of patents is accounted for, and (3) patents are accepted as a commodity.

### 1. *The Evolution of a Marketplace*

At its most basic level, a market is an institution that exists to facilitate exchange; it exists to reduce the costs of carrying out exchange transactions.<sup>142</sup> A historical backdrop is appropriate:

In the medieval period in England, fairs and markets were organized by individuals under a franchise from the King. They not only provided the physical facilities for the fair or market but were also responsible for security . . . and administered a court for settling disputes. . . . Fairs and markets have continued to be provided in modern times, including exhibition halls and the like, and have often . . . been a municipal function. . . . With the government providing security and with a more developed legal system, proprietors of the old markets no longer had to assume a responsibility for providing security or to undertake legal functions . . . .<sup>143</sup>

Markets have continued to evolve.<sup>144</sup> In modern times, a more conceptual marketplace, an amalgam of social institutions that “construct, channel, and shape the commercial exchange interaction . . . has replaced physical facilities.”<sup>145</sup> Similarly, those operating in markets no longer provide their own security but depend on the legal system of the state.<sup>146</sup> To ensure the continued viability of a modern market, the state must provide (and enforce) law.<sup>147</sup>

### 2. *The Nonrival Nature of Patents*

The legal system<sup>148</sup> assumes particular importance where patents are concerned. Patents by their nature differ significantly from tangible goods

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<sup>142</sup> R.H. COASE, *THE FIRM, THE MARKET, AND THE LAW* 7 (1988).

<sup>143</sup> *Id.* at 8.

<sup>144</sup> Oren Bracha, *How Patents Became Rights and Why We Should Care*, 38 *LOY. L.A. L. REV.* 177, 179 (2004).

<sup>145</sup> *Id.*

<sup>146</sup> COASE, *supra* note 142, at 10.

<sup>147</sup> *See generally id.*

<sup>148</sup> In the case of the United States, the federal government controls the patent law, as it arises under the Constitution. U.S. CONST. art. I, § 8, cl. 8; 35 U.S.C. §§ 102–03 (2000).

because ideas are intangible and nonrival.<sup>149</sup> While tangible property can only be in one place at one time, ideas can be used in multiple places at one time without depleting the original.<sup>150</sup> This fact makes expropriation of the patent easy because another person can easily use an invention without the patent holder knowing.<sup>151</sup> The patent system specifically attempts to ameliorate this problem by granting property entitlements in the innovation through excludability.<sup>152</sup>

However, unlike in criminal law, where trespass or theft is prosecuted by the state,<sup>153</sup> the only mechanism by which a patent owner may enforce his entitlement is a civil lawsuit.<sup>154</sup> But such a mechanism only works if the patent owner has the financial means to litigate.<sup>155</sup> At a minimum, there must be a credible threat of litigation to incentivize potential infringers to license the patent.

### 3. Patent Commodification

If a credible threat of litigation exists, a patent becomes a commodity. The term commodity derives from the Latin word *commodus*, meaning “useful.”<sup>156</sup> As an economic good, commodities became associated with abundant, mass-produced goods, such as cotton, cocoa, minerals, or pork bellies traded on exchanges in Chicago or London.<sup>157</sup> The understanding of commodification has since been extended to “the action of turning something into, or treating something as, a (mere) commodity; commercialization of an activity, etc., that is not by nature commercial.”<sup>158</sup>

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<sup>149</sup> Thomas, *supra* note 117, at 305, 308. Nonrival goods are those goods that can be used by more than one person at the same time without reducing the marginal value of the good to concurrent users. *Id.* at 308.

<sup>150</sup> See generally Eli Noam, *Two Cheers for the Commodification of Information*, in *THE COMMODIFICATION OF INFORMATION* 43 (Niva Elking-Koren & Neil Weinstock Netanel eds., 2002).

<sup>151</sup> See, e.g., Joshua S. Gans & Scott Stern, *The Product Market and the Market for Ideas: Commercialization Strategies for Technology Entrepreneurs*, 32 RES. POL'Y 333, 338 (2003).

<sup>152</sup> See generally Noam, *supra* note 150.

<sup>153</sup> See, e.g., MODEL PENAL CODE § 221.2 (Proposed Official Draft 1962) (explaining criminal trespass); § 223.2 (explaining theft by unlawful taking or disposition).

<sup>154</sup> 35 U.S.C. § 154 (2000).

<sup>155</sup> See generally Jeff A. Ronspies, Comment, *Does David Need a New Sling? Small Entities Face a Costly Barrier to Patent Protection*, 4 J. MARSHALL REV. INTELL. PROP. L. 184, 195–96 (2004).

<sup>156</sup> THE AMERICAN HERITAGE DICTIONARY OF THE ENGLISH LANGUAGE 367 (4th ed. 2000).

<sup>157</sup> See Noam, *supra* note 150, at 43, 45.

<sup>158</sup> 3 OXFORD ENGLISH DICTIONARY 563 (2d ed. 1989).

Under capitalism, almost everything becomes a commodity because almost anything can be bought and sold.<sup>159</sup> Commodification entails becoming the potential object of a commercial transaction in the market or being transferable.<sup>160</sup> By statutory definition, patents are transferable in commercial exchange; they are fully “assignable in law by an instrument in writing.”<sup>161</sup> The United States is a capitalist country, and patents are fully transferable; therefore, patents are a commodity and can be treated as such.<sup>162</sup>

The establishment of the previous three premises validates the claim that there exists a legitimate patent market.<sup>163</sup> Patent dealers operate within this market by buying and licensing patents.<sup>164</sup> This capability, as will be demonstrated, makes the patent market more efficient.<sup>165</sup>

### B. Patent Market Mechanics Without Patent Dealers

The most basic market exchange is a two-party transaction consisting of a buyer and a seller.<sup>166</sup> In the patent market, this transaction involves an exchange between an inventor and the patent buyer or licensee, often a large corporation with the means to exploit the product.<sup>167</sup> Before building the case for the utility of patent dealers, an understanding of the incentives driving each market participant is desirable.

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<sup>159</sup> 1 KARL MARX, CAPITAL 178–87 (Ben Fowkes trans., Vintage Books 1977) (1867). In a capitalist system, production is not determined by intrinsic merit of the work, but by exchange value. *Id.* at 126–28.

<sup>160</sup> Bracha, *supra* note 144, at 177–78.

<sup>161</sup> 35 U.S.C. § 261 (2000).

<sup>162</sup> This idea is nothing new; entitlements in information have been subject to commercial exchange under the law for centuries. Sixteenth century English stationers regularly sold and mortgaged their copyrights. *See* LYMAN RAY PATTERSON, COPYRIGHT IN HISTORICAL PERSPECTIVE 54–59, 71–73 (1968). Additionally, royal patent grants of the seventeenth century routinely confirmed that the entitlements they created applied to assignees. *See* BRUCE W. BUGBEE, GENESIS OF AMERICAN PATENT AND COPYRIGHT LAW 31–33 (1967) (discussing English patent policy).

<sup>163</sup> *See supra* Part IV.A.

<sup>164</sup> *See supra* Part I.B.

<sup>165</sup> *See infra* Part IV.B.

<sup>166</sup> ROBIN PAUL MALLOY, LAW IN A MARKET CONTEXT 115 (2004). More specifically, rationality means that every person goes through a cost-benefit analysis before each decision at some level. *Id.* A person then only engages in activities where the expected benefits from that activity exceed the expected costs, or if the decision positively benefits the decision maker. *Id.*

<sup>167</sup> *See generally id.*

### 1. *Market Participant Incentives*

A general assumption can be made that people will act rationally.<sup>168</sup> This rationality assumption means that a person will choose and make decisions in the pursuit of self-interest.<sup>169</sup> “Every individual is continually exerting himself to find out the most advantageous employment for whatever capital he can command. It is his own advantage . . . which he has in view.”<sup>170</sup>

If an individual is an inventor, more specific claims can be made about his incentives. The individual as inventor often has dual incentives in pursuing self-interest: altruism in the advancement of humanity<sup>171</sup> and monetization of the patent.<sup>172</sup> Publication of the patent is a realization of the incentive to advance civilization and provides intrinsic benefit to the inventor.<sup>173</sup> Monetization of the patent is a realization of the extrinsic economic benefit to the inventor.<sup>174</sup> Consequently, once the patent is granted, the inventor has realized part of the incentive, but has yet to realize the economic benefit. Thus, there still remains an incentive to monetize the patent.

While an inventor pursues his self-interest,<sup>175</sup> the overriding motive of a for-profit firm is to maximize profits.<sup>176</sup> One way in which a firm in a competitive market maximizes profits is by minimizing costs, a goal often realized by providing something for itself that it otherwise would seek through exchange on the market.<sup>177</sup> Ultimately, whether a firm will transact in the market or create an internal solution is dictated by cost.<sup>178</sup> If the cost of market

<sup>168</sup> In fact, this assumption is fundamental to elementary economic analysis. *Id.* at 144–45.

<sup>169</sup> At a fundamental level, each human being pursues ends “valued and chosen by himself.” G. F. Thirlby, *Economists’ Cost Rules and Equilibrium Theory*, in 11 L.S.E. ESSAYS ON COST 273, 275–76 (J. M. Buchanan & G. F. Thirlby eds., Inst. for Humane Studies 1981) (1973).

<sup>170</sup> ADAM SMITH, AN INQUIRY INTO THE NATURE AND CAUSES OF THE WEALTH OF NATIONS 216 (1776), reprinted in 36 GREAT BOOKS OF THE WESTERN WORLD (Mortimer J. Adler ed., 2d ed. Univ. of Chicago Press 1990) (1952).

<sup>171</sup> The inventor’s desire to invent evidences this idea, although in some cases this may be merely a by-product of the patent systems’ disclosure requirements, and their self-interest is realized when the person feels good and gets a benefit from the act of helping that exceeds the costs.

<sup>172</sup> This inference is based on the fact that the inventor did not merely publicly disclose the invention, but sought to exclude others from nonconsensual use by means of a patent.

<sup>173</sup> This intrinsic benefit could be realized as the personal satisfaction in solving a problem.

<sup>174</sup> The profit motive drives the entrepreneur. See LUDWIG VON MISES, HUMAN ACTION: A TREATISE ON ECONOMICS 286–97 (1949) (discussing at length profit, loss, and the entrepreneur in a capitalist society).

<sup>175</sup> See *supra* notes 168–74 and accompanying text.

<sup>176</sup> R.H. Coase, *The Nature of the Firm*, 4 *ECONOMICA* 386, 390–92 (1937).

<sup>177</sup> *Id.* at 394–95.

<sup>178</sup> *Id.*

exchange is cheaper, the firm will enter the market; if internal production is more cost-effective, the firm will rely on itself.<sup>179</sup>

If a credible threat of litigation exists,<sup>180</sup> an inventor's incentive to realize an economic return on the patent and the firm's incentive to realize savings in its operations are complementary.<sup>181</sup> Suppose Dr. Bob invents a process that makes the production of Liquid X more efficient. Drink Inc. produces Liquid X. Dr. Bob files for a patent on the process and is thereafter granted Patent X. Subsequently, Dr. Bob approaches Drink Inc. with an offer to license or sell Patent X. If Dr. Bob offers Patent X to Drink Inc. for less than the marginal value of Patent X's effect on Liquid X's production, Drink Inc. will purchase the patent. The incentives correspond, and there is no problem. Each market participant has an incentive to exchange.<sup>182</sup> By exchanging goods, the inventor monetizes the patent and the firm saves money, thereby increasing profits. The market facilitates a mutually beneficial exchange.<sup>183</sup> However, this assumption requires that the inventor, in this case Dr. Bob, poses a credible threat of litigation, which is not always the case.<sup>184</sup>

## 2. Market Failure: Empty Pockets, Empty Threats

Because of the nonrival nature of a patent, the licensing of a patent lends itself to problems in the form of market failure.<sup>185</sup> If a potential licensee of the technology reads the patent documentation or is presented with the technology by an inventor with ambitions of licensing the technology,<sup>186</sup> the corporation can simply use the patented technology without permission.<sup>187</sup> As mentioned earlier,<sup>188</sup> the threat of litigation encourages the exchange in the patent market.<sup>189</sup> Regrettably, this threat is missing in most transactions between

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<sup>179</sup> *Id.*

<sup>180</sup> See *infra* Part IV.C.1.

<sup>181</sup> See Gans & Stern, *supra* note 151, at 339.

<sup>182</sup> See *supra* Part IV.B.1.

<sup>183</sup> In reality, patents are nonrival goods. See Thomas, *supra* note 117, at 308.

<sup>184</sup> See, e.g., Ronspies, *supra* note 155, at 185–86.

<sup>185</sup> For a discussion of market failure generally, see ROBERT A. SCHWARTZ & RETO FRANCONI, EQUITY MARKETS IN ACTION 292–99 (2004).

<sup>186</sup> All patents are filed with the U.S. Patent and Trademark Office and are available for lookup by searching the USPTO database, available to the public at <http://www.uspto.gov/patft/index.html>.

<sup>187</sup> See Ronspies, *supra* note 155, at 185.

<sup>188</sup> See *supra* Part IV.A.2.

<sup>189</sup> See generally Kimberly A. Moore, *Xenophobia in American Courts*, 97 NW. U. L. REV. 1497, 1532 (2003).

large firms and individual inventors or small entities.<sup>190</sup> Because the state does not initiate the lawsuits, the plaintiff must instigate the suit, which of course, requires money.

Individual inventors and small entities rarely have the financial resources to commence and sustain a lawsuit.<sup>191</sup> The average cost of patent litigation is \$2 million,<sup>192</sup> and to get and maintain a patent for the full twenty years costs an average of \$24,285.<sup>193</sup> This relatively high cost has the effect of inhibiting the abilities of individual inventors and small entities to enforce their patents against large corporations.<sup>194</sup> Consequently, the inventor often poses no credible threat of litigation.<sup>195</sup> When no credible threat exists, the incentives of market participants become inconsistent, which ultimately causes market failure.<sup>196</sup>

Altering the previous hypothetical to reflect the nonrival nature of patents exposes the problem.<sup>197</sup> Assume the same facts as earlier: Dr. Bob owns Patent X on the process that makes Liquid X's production more efficient.<sup>198</sup> However, this time when Dr. Bob shows Drink Inc. the Patent X process, Drink Inc. realizes that it can duplicate this process internally.<sup>199</sup> Although Dr. Bob still has the economic incentive to monetize the patent, Drink Inc.'s incentives change.<sup>200</sup> Drink Inc. is tempted to expropriate the technology revealed to them.<sup>201</sup> Drink Inc. can either pay Dr. Bob for the marginal value of the patent or internalize the process by providing it itself.<sup>202</sup> Of these two choices, the latter is more consistent with the motive of the firm because it will

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<sup>190</sup> See Ronspies, *supra* note 155, at 185–86; see also Posting of Gary Odom to The Patent Prospector, [http://www.patenthawk.com/blog/archives/2005/10/patent\\_liquidit.html](http://www.patenthawk.com/blog/archives/2005/10/patent_liquidit.html) (Oct. 3, 2005, 20:23 EST) (discussing the unwillingness of some companies to negotiate with small inventors).

<sup>191</sup> Ronspies, *supra* note 155, at 201.

<sup>192</sup> *Id.* at 197.

<sup>193</sup> *Id.* at 185.

<sup>194</sup> *See id.* at 195.

<sup>195</sup> *Id.* at 185–86.

<sup>196</sup> Granted, this is not always the case because some companies pride themselves on treating individual inventors fairly. See, e.g., Gans & Stern, *supra* note 151, at 344.

<sup>197</sup> *See supra* Part IV.B.1.

<sup>198</sup> *See supra* Part IV.B.1.

<sup>199</sup> This happens frequently. See, e.g., John Seabrook, *The Flash of Genius*, NEW YORKER, Jan. 11, 1993, at 38, 44–45.

<sup>200</sup> *See, e.g.*, Gans & Stern, *supra* note 151, at 338.

<sup>201</sup> *Id.* at 344; see also Ronald J. Riley, *Pressure on the American Patent System: Part 1, The Japanese Influence*, ABOUT.COM, <http://inventors.about.com/library/weekly/aa072797.htm>. “My personal experience has been that large corporate interests often commit fraud to avoid compensating inventors.” *Id.*

<sup>202</sup> *See, e.g.*, Gans & Stern, *supra* note 151, at 338.

increase profits more effectively.<sup>203</sup> The choice to expropriate the technology, of course, denies the inventor his economic reward,<sup>204</sup> and has the downstream effect of discouraging innovation.<sup>205</sup> Ultimately, potential inventors have less confidence in their ability to monetize their patents.<sup>206</sup>

### C. Patent Dealers Alter Patent Market Dynamics

As the *Economist* recently noted, “A new breed of companies has appeared on the periphery of today’s tech firms, acting as intellectual-property intermediaries and creating a market for ideas.”<sup>207</sup> The aggregate effect of this entry is a more efficient market.<sup>208</sup> Patent dealers provide the patent market with many of the same benefits that securities dealers provide in over-the-counter capital markets.<sup>209</sup> Unlike a national securities exchange that has a physical trading floor and is based on an auction paradigm, an over-the-counter market is not a centralized organization.<sup>210</sup> To maintain a market for securities without a physical central exchange, designated dealers operate as market makers by buying and selling stocks on their own account.<sup>211</sup> In doing this, securities dealers make the capital market more efficient by providing liquidity and serving a market clearing function.<sup>212</sup>

Similarly, patent dealers make the patent market more efficient through buying and licensing patents.<sup>213</sup> Patent dealers create a credible threat of litigation, which encourages exchange, makes patents more liquid, and facilitates market clearing through price equalization. As a result, the patent market becomes more efficient.<sup>214</sup>

<sup>203</sup> A firm maximizes profits and minimizes costs when it provides something for itself that it otherwise would seek through exchange on the market. The choice is dictated by cost. Although the firm in this case is minimizing cost through expropriation, the situation is analogous to Coase’s theorem regarding cost internalization and outsourcing. *C.f. supra* Part IV.B.1 (applying Coase’s ideas concerning the firm).

<sup>204</sup> See Gans & Stern, *supra* note 151, at 344.

<sup>205</sup> See *id.*

<sup>206</sup> See *id.*

<sup>207</sup> *A Market for Ideas*, *supra* note 14, at 3.

<sup>208</sup> See *infra* Part IV.D.

<sup>209</sup> See The Motley Fool, Investing Basics: Stocks, <http://www.fool.com/school/basics/basics03.htm> (last visited Apr. 18, 2006).

<sup>210</sup> See THOMAS LEE HAZEN, THE LAW OF SECURITIES REGULATION § 14.10[2] (5th ed. 2005).

<sup>211</sup> *Id.*

<sup>212</sup> See SCHWARTZ & FRANCIONI, *supra* note 185, at 15–16, 198–99 (generally discussing the function of market makers or dealers in the market). They also provide services that are not pertinent to this discussion. *Id.*

<sup>213</sup> See *infra* Part IV.C.1–3.

<sup>214</sup> See *infra* Part IV.D.

### 1. Patent Dealers Create a Credible Threat of Litigation

Once a patent dealer enters the market, the incentives become more like those existing in the market for rival commodities. The threat of litigation becomes credible, and the incentives of the market participants realign.<sup>215</sup> Unlike the individual inventor who poses no real litigation threat,<sup>216</sup> the patent dealer has ample funds with which to litigate.<sup>217</sup> Armed with the capital to launch litigation, the patent dealer can buy the patent from the inventor and pursue an infringement claim.<sup>218</sup>

A return to the previous hypothetical is informative. Again, assume the same facts: Dr. Bob owns Patent X on the process that makes Liquid X's production more efficient.<sup>219</sup> But this time, Dr. Bob sells Patent X to Patent Dealer Bill. Patent Dealer Bill shows the Patent X process to Drink Inc. Drink Inc. realizes that it can duplicate this process internally and is tempted to expropriate the technology.<sup>220</sup> However, Drink Inc. also realizes that Patent Dealer Bill has substantial capital<sup>221</sup> and is willing to litigate if necessary. Drink Inc.'s potential costs now change. Drink Inc. still has the same choices of either paying Patent Dealer Bill for the marginal value of the patent or internalizing the process by providing it itself.<sup>222</sup> However, the cost of the second option has risen. If it chooses option two, Drink Inc. could end up paying \$2,000,000 in litigation fees in addition to Patent Dealer Bill's license fee, plus more if willful infringement is found.<sup>223</sup> Of these two choices, the first choice is reestablished as the more attractive option.<sup>224</sup>

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<sup>215</sup> See generally Jean O. Lanjouw & Mark Schankerman, *Protecting Intellectual Property Rights: Are Small Firms Handicapped?*, 47 J.L. & ECON. 45, 49–50 (2004).

<sup>216</sup> *Id.*

<sup>217</sup> See Tomas Kellner, *Perot Backs \$200 Million Bet on Patents*, FORBES.COM, Aug. 9, 2005, [http://www.forbes.com/2005/08/09/perot-patents-fund-cz\\_tk\\_0809patents.html](http://www.forbes.com/2005/08/09/perot-patents-fund-cz_tk_0809patents.html).

<sup>218</sup> See, e.g., Acacia Research Corporation, Acacia Technologies Group Fact Sheet, <http://www.acaciaresearch.com/pr/AcaciaFactSheet.pdf> (last visited Apr. 18, 2006).

<sup>219</sup> See *supra* Part IV.B.1.

<sup>220</sup> See *supra* note 199.

<sup>221</sup> See, e.g., Acacia Research Corporation, *supra* note 31 (“Acacia controls 46 patent portfolios, which include over 160 U.S. patents . . .”).

<sup>222</sup> See, e.g., Gans & Stern, *supra* note 151, at 338.

<sup>223</sup> See, e.g., Ronspies, *supra* note 155, at 197.

<sup>224</sup> See *supra* Part IV.B.1.

## 2. *Patents Become More Liquid*

Patent dealers also make patents more liquid by coordinating exchange.<sup>225</sup> Patents are nominally illiquid commodities<sup>226</sup> because they are not “readily convertible into cash.”<sup>227</sup> Without the presence of patent dealers in the market, the patent market is a simple decentralized or “search” market.<sup>228</sup> In the patent “search” market, the patent holder (the seller) has to search for a company to which it can license a particular patent (the buyer).<sup>229</sup> Conversely, the company (the buyer) seeks new beneficial and promising technology from an inventor (the seller).<sup>230</sup> The inventor and the company both incur the costs of travel, learning about prices, and comparing products and prices.<sup>231</sup> Because there is no centralized market, the patent can not be liquidated in a timely manner without the price being negatively affected.<sup>232</sup>

When a patent dealer joins the market, the market dynamics change. The market moves toward a more centralized or “dealer” market in which the patent dealer becomes a focal point for transactions.<sup>233</sup> For instance, NASDAQ operates as an over-the-counter dealer market; the dealers “act as market makers, posting their bid-ask quotations based on their inventories of

<sup>225</sup> See SCHWARTZ & FRANCONI, *supra* note 185, at 198.

<sup>226</sup> See Odom, *supra* note 190 (discussing patents as nominally illiquid assets). See generally CAROLINE WOODWARD, PRICEWATERHOUSECOOPERS LLP, ACCOUNTING FOR INTELLECTUAL PROPERTY 1–2 (2003) (discussing accounting treatment of intellectual property as part of overall goodwill value).

<sup>227</sup> See SCHWARTZ & FRANCONI, *supra* note 185, at 60.

<sup>228</sup> See generally DANIEL F. SPULBER, THE MARKET MAKERS: HOW LEADING COMPANIES CREATE AND WIN MARKETS 79–80 (1998) (“Search markets do not involve centralized price setting; individual buyers and seller meet through search . . .”).

<sup>229</sup> See, e.g., Gans & Stern, *supra* note 151, at 334 (discussing how an inventor sought to shop his patent to potential buyers).

<sup>230</sup> *Id.* at 336. “Amazon used emerging technology to shift the basis of competitive advantage in the bookseller market, posing a threat to dominant market players such as Barnes and Noble.” *Id.*

<sup>231</sup> See DANIEL F. SPULBER, MARKET MICROSTRUCTURE xxi–xxii (1999).

<sup>232</sup> See generally SCOTT, *supra* note 110, at 169. An illiquid asset is one that

pertains to an asset that is difficult to buy or sell in a short period of time without its price being affected. For example, a large block of stock or a small amount of an infrequently traded stock is likely to be difficult to sell without a reduced price being offered to potential buyers.

*Id.*

<sup>233</sup> Cf. SPULBER, *supra* note 231, at 80 (this argument is equally applicable to the patent market).

securities in which they choose to make markets.”<sup>234</sup> Dealers “enter orders for their own account against this inventory.”<sup>235</sup>

Just as dealers on the NASDAQ match investors with companies seeking owners and vice versa,<sup>236</sup> patent dealers match patent owners with companies seeking to commercialize a patent. The patent dealer manages transactions and provides a “central place of exchange.”<sup>237</sup> They do this by advertising themselves publicly as dealers and by purchasing patents from the original inventors.<sup>238</sup> Patent dealers then hold a patent inventory and attempt to license to companies seeking a specific technology.<sup>239</sup>

The central place of exchange greatly reduces the search costs of buyers and sellers who must only find the dealer, and not each other. The management of transactions by the dealer reduces the costs of buying and selling and helps the market to operate smoothly. By buying when suppliers are ready to sell and selling when customers are ready to buy, the dealer provides immediacy to the marketplace.<sup>240</sup>

Thus, the patents become more liquid commodities.<sup>241</sup>

### 3. Patent Dealers Clear the Market

In addition to providing market liquidity, patent dealers clear the market<sup>242</sup> by equalizing prices and undertaking risk.<sup>243</sup> In many markets, including the patent market, market participants are “asymmetrically informed.”<sup>244</sup> This causes market friction induced by search costs, which consist of the “time, money, and effort spent learning what is available where for how much,” and

<sup>234</sup> Lawrence E. Mitchell, *Structure as an Independent Variable in Assessing Stock Market Failures*, 72 GEO. WASH. L. REV. 547, 578 (2004); see also NAT’L ASS’N OF SEC. DEALERS, NASDAQ HANDBOOK: THE STOCK MARKET FOR THE NEXT 100 YEARS 350–51 (1992).

<sup>235</sup> See Mitchell, *supra* note 234, at 578.

<sup>236</sup> Cf. SPULBER, *supra* note 231, at 80 (this argument is equally applicable to the patent market).

<sup>237</sup> Cf. *id.* (this argument is equally applicable to the patent market).

<sup>238</sup> See, e.g., Acacia Research Corporation, *supra* note 31.

<sup>239</sup> *Id.*

<sup>240</sup> Cf. SPULBER, *supra* note 231, at 80 (this argument is equally applicable to the patent market).

<sup>241</sup> The patent dealer of course is not the ultimate source of liquidity. Buyers and sellers must be available. Cf. SCHWARTZ & FRANCONI, *supra* note 185, at 198 (this argument is equally applicable to the patent market); see also Odom, *supra* note 190 (concluding that trolls make patents more liquid).

<sup>242</sup> “Clearing is a widely used expression for offsetting or netting obligations across a community. Clearing in an equity market also concentrates the risks to all participants within a single organization.” SCHWARTZ & FRANCONI, *supra* note 185, at 267.

<sup>243</sup> Cf. SPULBER, *supra* note 231, at 86–87 (this argument is equally applicable to the patent market).

<sup>244</sup> *Id.* at xxiii.

evaluation costs, which arise from difficulties in “assessing quality.”<sup>245</sup> Such market frictions often result in inconsistent pricing, the occurrence of transactions “between the wrong people,” and ultimately, market failure.<sup>246</sup>

A successful market has mechanisms that limit market frictions.<sup>247</sup> In asymmetrically informed markets, dealers act as buyer and seller in the market, thereby pooling risk and equalizing prices.<sup>248</sup> For instance, in capital markets securities dealers undertake the risk normally shouldered by buyer and seller, leaving the risk concentrated in the dealer.<sup>249</sup> The dealer can better manage this risk because it has better access to information; it collects information through specialization and by transacting with multiple buyers and sellers.<sup>250</sup> By better managing risk, the dealer can set a market clearing price for the security.<sup>251</sup>

The emergence of patent dealers solves similar risk and asymmetric information problems in the patent market.<sup>252</sup> The patent dealer buys the patent from an inventor and keeps it in inventory.<sup>253</sup> When it finds a potential licensee, the patent dealer licenses the product.<sup>254</sup> In doing so, the patent dealer reduces the risk of the inventor and licensee, instead managing the risk itself.<sup>255</sup> Patent dealers collect and supply information; they evaluate the risk of patent invalidation, the breadth of the patent scope, the prior art, and the attractiveness of the industry.<sup>256</sup> Also, they gain specialization through knowledge of the state of technology and by partnering with technology buyers.<sup>257</sup> Consequently, through risk pooling and equalized pricing, the patent dealer can better set a market clearing price for the patent.

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<sup>245</sup> JOHN MCMILLAN, *REINVENTING THE BAZAAR: A NATURAL HISTORY OF MARKETS* 44 (2002).

<sup>246</sup> *Id.*

<sup>247</sup> *Id.* at 45.

<sup>248</sup> See SCHWARTZ & FRANCONI, *supra* note 185, at 266–67.

<sup>249</sup> *Id.*

<sup>250</sup> SPULBER, *supra* note 231, at 3–4, 175.

<sup>251</sup> See NATIONAL ASSOCIATION OF SECURITIES DEALERS, *supra* note 234, at 264–66.

<sup>252</sup> Cf. SCHWARTZ & FRANCONI, *supra* note 185, at 266–67.

<sup>253</sup> See, e.g., Intellectual Ventures, Who We Are, <http://www.intellectualventures.com/about.aspx> (last visited May 13, 2006).

<sup>254</sup> See, e.g., *id.*

<sup>255</sup> Cf. SCHWARTZ & FRANCONI, *supra* note 185, at 267.

<sup>256</sup> See, e.g., Ocean Tomo, <http://www.patentratings.com> (last visited May 13, 2006).

<sup>257</sup> See, e.g., Intellectual Ventures, *supra* note 253.

#### D. Patent Dealers Make the Patent Market More Efficient

By creating a credible threat of litigation, making patents more liquid, and setting market clearing prices,<sup>258</sup> the patent market becomes more efficient. When economists and legal scholars speak of efficiency, they generally speak of Kaldor-Hicks efficiency.<sup>259</sup> The Kaldor-Hicks test states that “a move is efficient whenever the winners win more than the losers lose, [and] if the winners compensated the losers to their satisfaction, the winners would still be better off than they were before the [transaction].”<sup>260</sup> Thus, “One state of affairs (E’) is Kaldor-Hicks efficient to another (E) if and only if those whose welfare increases in the move from E to E’ could fully compensate those whose welfare diminishes with a net gain in welfare.”<sup>261</sup>

Do patent dealers facilitate Kaldor-Hicks efficient transactions? To address the question, three preliminary propositions must be established. First, there are four parties to this transaction, three direct—the inventor, licensor or transferee, and patent dealer, and one indirect—the public.<sup>262</sup> Each party gains or loses as a result of the transaction.<sup>263</sup> Second, the general assumptions must be made that the goal of efficiency is wealth maximization<sup>264</sup> and that one unit of that wealth is of equal worth to all players.<sup>265</sup> Third, for the purposes of this discussion, E is the state of affairs without patent dealers, and E’ is the state of affairs with patent dealers.<sup>266</sup>

The first logical step in the analysis is identification of the losers and what they lose under allocation E’.<sup>267</sup> The losers are the large corporations,<sup>268</sup>

<sup>258</sup> See *supra* Part IV.B.1.

<sup>259</sup> RICHARD A. POSNER, *ECONOMIC ANALYSIS OF LAW* 14 (4th ed. 1992) (“When an economist says that free trade or competition or the control of pollution or some other policy or state of the world is efficient, nine times out of ten he means Kaldor-Hicks efficient . . .”)

<sup>260</sup> Guido Calabresi, *The Pointlessness of Pareto: Carrying Coase Further*, 100 *YALE L.J.* 1211, 1221 (1991) (describing Kaldor-Hicks or Potential Pareto Superiority).

<sup>261</sup> JULES L. COLEMAN, *MARKETS, MORALS, AND THE LAW* 98 (1988) (emphasis added). Under Kaldor-Hicks, compensation to the losers need not be paid. RICHARD O. ZERBE, JR., *ECONOMIC EFFICIENCY IN LAW AND ECONOMICS* 4–5 (2001).

<sup>262</sup> See generally *supra* Part IV.B.2.

<sup>263</sup> See generally *supra* Part IV.B.2.

<sup>264</sup> Richard A. Posner, *The Value of Wealth: A Comment on Dworkin and Kronman*, 9 *J. LEGAL STUD.* 243, 243 (1980) (supporting the claim that the law should maximize wealth).

<sup>265</sup> These are necessary for our analysis, although the author acknowledges the implausibility of this from a sociological perspective. Philosophical discussion regarding this single claim could be a full article in itself, and is, therefore, better left to Judge Posner or Judge Calabresi. See generally Calabresi, *supra* note 260, at 1211–12 (discussing the problems inherent in such assumptions).

<sup>266</sup> See *supra* note 233 and accompanying text.

<sup>267</sup> See M.W. JONES-LEE, *THE VALUE OF LIFE: AN ECONOMIC ANALYSIS* 4–6 (1976).

which lose the ability to use technology they may have otherwise obtained through expropriation in allocation E.<sup>269</sup> This loss is roughly equal to the price the patentor charges for use of the patent in E', plus the value of the risk that the patent dealer undertook in purchasing the patent in E'.<sup>270</sup> However, this loss is at least partially offset by the likelihood that there will be more inventions brought to the attention of the company in E'. Subsequently, there is a higher probability that the company will find better technology for use in its operations, thereby increasing efficiency.

The second logical step in the analysis is identifying the winners and what they gain under allocation E'.<sup>271</sup> The winners are the individual inventors, the patent dealers, and the public. The individual inventors gain the value of their patent. The patent dealer gains the value of facilitating the transaction, the liquidated value of the risk it undertook in purchasing the patent, and the aggregate value of information it collects in the transaction.<sup>272</sup>

The public benefits indirectly. Although under allocation E the public similarly would have gained from the particular invention being incorporated in a product, in E' the public also gains from the increase in incentives that inventors have to invent.<sup>273</sup> Because inventors in E' have a means to easily liquidate their patents, they are more likely to invent than they would be in E. More inventions lead to an improvement in general welfare, which benefits the public.<sup>274</sup>

The last step in the analysis is an inquiry into whether the transaction increases overall aggregate wealth.<sup>275</sup> Although the costs and benefits cannot be precisely measured, they can be considered in comparative terms. The benefits to the individual inventor and patent dealer are roughly canceled out by the detriment to the large corporations.<sup>276</sup> However, there may be a surplus cost from the price premium that the dealer will charge to incur the risk of buying the patent. Similarly, there are surplus benefits in the form of an

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<sup>268</sup> See generally *supra* Part IV.B.2.

<sup>269</sup> See generally *supra* Part IV.B.2.

<sup>270</sup> The patent dealer is going to charge a price premium that is roughly equal to the risk undertaken in purchasing the patent.

<sup>271</sup> See JONES-LEE, *supra* note 267, at 4–6.

<sup>272</sup> See *supra* Part IV.C.1–3.

<sup>273</sup> See *supra* Part IV.B.1.

<sup>274</sup> See Ted Baker, *Pioneers in Technology: A Proposed System for Classifying and Rewarding Extraordinary Inventions*, 45 ARIZ. L. REV. 445, 458 (2003) (discussing ways patents benefit society).

<sup>275</sup> See JONES-LEE, *supra* note 267, at 4–6.

<sup>276</sup> See *supra* notes 272–74 and accompanying text.

increase in information, increased liquidity, and creation of a market clearing price via risk pooling.<sup>277</sup> Even if these canceled each other out, there remains an additional surplus benefit—the increased incentive for individuals to invent. This surplus benefit is quite significant, so much so that the Framers thought that it was necessary to address it in the Constitution.<sup>278</sup>

Overall, the emergence of pure form patent dealing represents a Kaldor-Hicks efficiency improvement because the benefits of pure patent dealing outweigh the costs. At worst, if the price premium that dealers charge equals the added benefit in creating more liquid patents and setting a market clearing price,<sup>279</sup> there remains the benefit of effectuating the Constitution through the presence of a credible litigation threat.<sup>280</sup>

#### *E. Emergence of Patent Dealers: A Necessary Step in Market Evolution*

The patent dealer phenomena can be further appreciated within the framework of market evolution. In this context, it becomes clear that the emergence of patent dealers evinces a natural progression of the patent market. Markets do not simply appear; rather “they are responses to latent or overt demand.”<sup>281</sup> For a developing market to successfully evolve, “specific legal and institutional infrastructures” must be developed.<sup>282</sup> This developmental evolution can be viewed as a seven-stage process.<sup>283</sup>

In the first stage, “[A] structural economic change . . . creates the demand for capital.”<sup>284</sup> As discussed earlier, a structural economic change has most certainly occurred.<sup>285</sup> This change is evidenced in the movement from a land and natural resource-based economy to one based on intangible assets.<sup>286</sup> In turn, demand for patents has intensified.<sup>287</sup> In the second stage, uniform asset

<sup>277</sup> See *supra* Part IV.C.1–3.

<sup>278</sup> U.S. CONST. art. I, § 8, cl. 8.

<sup>279</sup> See *supra* Part IV.C.2–3.

<sup>280</sup> See *supra* Part IV.C.1.

<sup>281</sup> Richard L. Sandor, *The Convergence of the Insurance and Capital Markets*, in *SECURITIZED INSURANCE RISK: STRATEGIC OPPORTUNITIES FOR INSURERS AND INVESTORS* 1, 2 (Michael Himick & Sylvie Bouriaux eds., 1998). These stages need not evolve sequentially. *Id.* at 3.

<sup>282</sup> *Id.* at 2.

<sup>283</sup> *Id.*

<sup>284</sup> *Id.*

<sup>285</sup> See *supra* Part I.A.

<sup>286</sup> *A Market for Ideas*, *supra* note 14, at 3.

<sup>287</sup> See *supra* notes 14–17 and accompanying text.

standards arise.<sup>288</sup> In the patent market, these specifications have been established.<sup>289</sup> Congress has used the power conferred in Article I of the Constitution to give the inventor exclusive rights over an invention as long as it is useful, novel, and nonobvious.<sup>290</sup> Additionally, Congress created the United States Court of Appeals for the Federal Circuit to enforce and specialize in understanding those standards.<sup>291</sup>

In the third stage of market evolution, legal instruments providing evidence of ownership develop.<sup>292</sup> Patents are legal instruments in themselves.<sup>293</sup> The U.S. Patent and Trademark Office issues them to signify ownership and the right to exclude.<sup>294</sup> Therefore, the patent market is beyond this stage. The fourth stage is characterized by “the development of informal spot markets . . . where ‘receipts’ of ownership are traded.”<sup>295</sup> Up until now, spot markets have been the only means of licensing and transferring patents. Cash is paid at the market price for a patent owner to forgo his right to exclude, or alternatively, the patent right is transferred outright with immediate delivery.<sup>296</sup>

The fifth stage is reached upon “the emergence of securities and commodities exchanges.”<sup>297</sup> The emergence of patent dealers evinces the first manifestations of this stage. As discussed earlier, the patent dealer becomes a focal point for the patent market, making patents more liquid, setting market clearing prices, and generally making the market more efficient.<sup>298</sup> Yet, there are still no existing formal trading markets for patents. So, it appears that the patent market is in the midst of the fifth stage of evolution. The formation of futures markets and development of over-the-counter markets generally signal entry into the last two stages.<sup>299</sup> As of today, the patent market has not yet reached these stages. However, if the patent market follows the evolutionary patterns of capital markets, agricultural commodities, or mortgage-backed

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<sup>288</sup> See Sandor, *supra* note 281, at 2.

<sup>289</sup> U.S. CONST. art. I, § 8, cl. 8; 35 U.S.C. §§ 102–03 (2000); *Sinclair & Carroll Co. v. Interchemical Corp.*, 325 U.S. 327, 330 (1945); *Marconi Wireless Tel. Co. of Am. v. United States*, 320 U.S. 1, 32 (1943).

<sup>290</sup> 35 U.S.C. § 103.

<sup>291</sup> See *supra* note 123.

<sup>292</sup> See Sandor, *supra* note 281, at 2.

<sup>293</sup> See U.S. CONST. art. I, § 8, cl. 8; 35 U.S.C. §§ 102–03 (2000).

<sup>294</sup> See §§ 102–03.

<sup>295</sup> See Sandor, *supra* note 281, at 2.

<sup>296</sup> See *infra* Part V.A.1–2.

<sup>297</sup> See Sandor, *supra* note 281, at 2.

<sup>298</sup> See *supra* Part IV.C–D.

<sup>299</sup> See Sandor, *supra* note 281, at 2–3.

securities, the patent dealer phenomena is merely the beginning of this fifth stage, a precursor to formal trading markets for patents.<sup>300</sup>

#### V. REBUTTAL: OBJECTIONS TO PATENT DEALERS.

Thus far, this Comment has advanced the idea that the activities of patent dealers in their pure form are beneficial to society. This Comment began by briefly surveying the current movement against patent dealers.<sup>301</sup> It then relabeled the subject of this Comment as patent dealers, a more functionally accurate label.<sup>302</sup> Next, this Comment isolated from discussion two problems often improperly conflated with patent dealers.<sup>303</sup> Finally, an economic analysis of patent dealers, with an eye towards securities dealers as a reference point, demonstrated that patent dealers make the patent market more efficient.<sup>304</sup> The Comment now looks through this new lens and revisits the two main criticisms of patent dealers.

Although the practices of patent dealers have been criticized on several grounds, there are two worthy of consideration.<sup>305</sup> Detractors argue that patent dealers (1) abuse the patent system because they do not promote the progress of useful arts,<sup>306</sup> and (2) spur vexatious litigation through overly aggressive and unfair patent enforcement.<sup>307</sup> Although each argument has appeal, further exploration reveals their collective shortcomings. In reality, patent dealers “promote the Progress of . . . useful Arts”<sup>308</sup> and are merely litigating to protect their exclusive rights.

##### A. *Patent Dealers Do Not Undermine Constitutional Objectives*

Patent dealers are most often criticized for “accumulat[ing] patents not to further innovation and develop new products, but to use the patents as

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<sup>300</sup> See, e.g., *id.* at 3–4.

<sup>301</sup> See *supra* Part I.B.2.

<sup>302</sup> See *supra* Part II.

<sup>303</sup> See *supra* Part III.

<sup>304</sup> See *supra* Part IV.D.

<sup>305</sup> Other problems are those caused by the issuance of bad patents and the patent thickets, which have been conflated with the effects of patent trolls. Therefore, addressing them here is outside the scope of this Comment. See *supra* Part III.

<sup>306</sup> This complaint is not explicitly framed in legal jargon, but the criticism is that the “trolls” do not promote innovation. In legal terms, this is taken to mean that they do not “promote the Progress of . . . useful Arts.” See *Letter from New Democrat Coalition, supra* note 9.

<sup>307</sup> *Id.*; e.g., Beyers, *supra* note 7; Aepfel, *supra* note 10, at B1.

<sup>308</sup> U.S. CONST. art. I, § 8, cl. 8.

litigation tools.”<sup>309</sup> In other words, patent dealers do not meet the required constitutional quid pro quo—they do not “promote the Progress of . . . useful Arts.”<sup>310</sup> However, a close look at the function of patent dealers makes this argument less compelling, for patent dealers do indeed promote constitutional objectives.<sup>311</sup>

### *1. No Commercialization Requirement for the Patent Holder*

Although the argument sounds appealing, the Constitution does not require the patent holder to actually commercialize the patent themselves.<sup>312</sup> The U.S. Constitution grants Congress the power to “promote the Progress of . . . useful Arts, by securing for limited Times to . . . Inventors the exclusive Right to their respective . . . Discoveries.”<sup>313</sup> Congress has used this power to give the inventor exclusive rights over their invention as long as it is useful, novel, and displays “more ingenuity . . . than the work of a mechanic skilled in the art.”<sup>314</sup> If the invention meets this congressional standard, the inventor is granted, as a reward, the right to exclude others in exchange for the public disclosure of the invention in sufficient detail such that one of ordinary skill in the art could reproduce the invention.<sup>315</sup>

There is not, and has never been, a requirement that the inventor actually use the invention in the marketplace.<sup>316</sup> The monopoly granted to the inventor is in the form of property, which is recognized by the grant of a “right to exclude.”<sup>317</sup> Accordingly, the inventor may choose to forgo the enforcement of that right for a license fee.<sup>318</sup> By couching the rights of the patent holder in monopolistic terms, Congress and the Framers of the Constitution ultimately

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<sup>309</sup> *Letter from New Democrat Coalition*, *supra* note 9; Krim, *supra* note 3 (quoting Andrew S. Grove, Chairman of Intel Corp., who derided “trolls” for “showing little interest in producing goods with their inventions in favor of demanding licensing fees from others”).

<sup>310</sup> U.S. CONST. art. I, § 8, cl. 8.

<sup>311</sup> *See infra* Part V.A.

<sup>312</sup> U.S. CONST. art. I, § 8, cl. 8; *see also* 35 U.S.C. §§ 102–03 (2000).

<sup>313</sup> U.S. CONST. art. I, § 8, cl. 8.

<sup>314</sup> *Sinclair Co. v. Interchemical Corp.*, 325 U.S. 327, 330 (1945) (citing *Hicks v. Kelsey*, 85 U.S. 670 (1873)); *see Marconi Wireless Tel. Co. v. United States*, 320 U.S. 1 (1943); 35 U.S.C. §§ 102–03 (2000).

<sup>315</sup> 35 U.S.C. § 261. A patentee has an exclusive property right in his patented invention. *James v. Campbell*, 104 U.S. 356 (1882).

<sup>316</sup> To obtain a patent one need only create a work that is novel, useful, and nonobvious. 35 U.S.C. §§ 102–03 (2000).

<sup>317</sup> § 261. A patentee has an exclusive property right in his patented invention. *Campbell*, 104 U.S. at 356.

<sup>318</sup> In strict technical sense, a “license” is a “mere contractual immunity from suit for infringement.” *United States v. Radio Corp. of Am.*, 117 F. Supp. 449, 454 (D. Del. 1954).

left to the inventor the choice of dissemination.<sup>319</sup> As much as it may seem like an inventor should make use of the discovery, the public has no positive right in the invention until the end of the patent term.<sup>320</sup> Accordingly, as long as the invention details are disclosed and the invention is useful, novel, and nonobvious, the patent dealers are operating completely within the law, even when they do nothing but litigate to protect their exclusive right.<sup>321</sup>

## 2. Patent Dealers Promote the Progress of Useful Arts

Not only do patent dealers operate completely within the boundaries of the Constitution,<sup>322</sup> but they “promote the Progress of . . . useful Arts” within any meaningful interpretation of the word “Progress” in the Constitution. Surprisingly, the Supreme Court has never directly defined the word “Progress” in the Progress Clause.<sup>323</sup> However, patent dealers “promote the Progress” under any intelligible interpretation of the word. Two recent articles have analyzed the possible meanings of the terms “Progress” in the Constitution.<sup>324</sup> Each article has concluded with a different definition of progress. These two potential definitions are: (1) spread or distribution to the population,<sup>325</sup> and (2) advancement or movement forward.<sup>326</sup>

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<sup>319</sup> A valid patent gives to its holder the right to grant or not to grant licenses for use thereof by others; therefore, there is no violation of any law caused by holder's refusal to grant licenses or rights under patent. *United States v. L. D. Caulk Co.*, 126 F. Supp. 693, 708 (D. Del. 1954).

<sup>320</sup> A patent conveys no property right of the government, but merely creates a property right in the inventor. *Marsh v. Nichols, Shepard & Co.*, 128 U.S. 605, 611–12 (1888).

<sup>321</sup> Litigating to protect a patent right is the corollary to licensing that right, and, therefore, the invention is actually being commercialized as a result.

<sup>322</sup> See *supra* Part V.A.

<sup>323</sup> See THURSTON GREENE, *THE LANGUAGE OF THE CONSTITUTION: A SOURCEBOOK AND GUIDE TO THE IDEAS, TERMS, AND VOCABULARY OF THE UNITED STATES CONSTITUTION* xv, xviii (1991). There are no cases, advisory committee notes, or other legal authorities cited for explaining the word “Progress.” *Id.*; see also Lawrence B. Solum, *Congress's Power to Promote the Progress of Science: Eldred v. Ashcroft*, 36 LOY. L.A. L. REV. 1, 44–47 (2002) (attempting to define the term without judicial guidance). The Court has only gone so far as to state that the “Progress” limitation relates to: (1) Congress's inability to remove *res* from the public domain, (2) the nonobviousness requirement, and (3) the requirement that the *res* be a “Discovery” by an “inventor.” See *Graham v. John Deere Co.*, 383 U.S. 1, 6 (1966).

<sup>324</sup> Malla Pollack, *What Is Congress Supposed to Promote?: Defining “Progress” in Article I, Section 8, Clause 8 of the United States Constitution, or Introducing the Progress Clause*, 80 NEB. L. REV. 754 (2001); Solum, *supra* note 324, at 44–47.

<sup>325</sup> See Pollack, *supra* note 324, at 755. Professor Pollack notes that of these, “quantity” is the least supportable, “quality” has low support and creates problems in context, and “spread” has the highest support. *Id.* at 757.

<sup>326</sup> Solum, *supra* note 323, at 44.

Patent dealers more effectively distribute knowledge throughout the population. Under this definition of “Progress,” Congress is required to “prioritize public access to works over the mere existence of works.”<sup>327</sup> Because of the biased media attention surrounding patent dealers,<sup>328</sup> the claim that patent dealers promote public access to works over the mere existence of works may seem counterintuitive. However, patent dealers promote public access in several ways.

First, by increasing patent liquidity and decreasing risk,<sup>329</sup> patent dealers incentivize individual inventors and small entities to invent, making more technology available to the public.<sup>330</sup> Second, patent dealers serve as a focal point for the patent market. By acting as a market intermediary for patents, collecting information regarding patents and their associated industries, and forming relationships with corporations, a patent dealer becomes a focal point for those who create and seek technology.<sup>331</sup> This results in easier and broader access to inventions. Third, patent dealers encourage people to invent around patents.<sup>332</sup> With knowledge that patents will be enforced by patent dealers, potential infringers are forced to either license technology, or increase research and development to invent around these patents.<sup>333</sup> Regardless of the choice, the end result for the public is broader access to works.

Patent dealers also promote the advancement of innovation for the same reasons.<sup>334</sup> The presence of patent dealers in the market allows individual inventors and small entities to gain easy access to the patent market.<sup>335</sup> Increased patent liquidity and reduced risk gives inventors more incentive to invent, which results in advancement within that particular industry.<sup>336</sup>

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<sup>327</sup> See Pollack, *supra* note 324, at 760.

<sup>328</sup> See *supra* Part I.B.2.c.

<sup>329</sup> See *supra* Part IV.C.

<sup>330</sup> See *supra* Part IV.C.2 (discussing liquidity).

<sup>331</sup> See, e.g., Intellectual Ventures, *supra* note 253.

<sup>332</sup> See generally Jonathan M. Barnett, *Private Protection of Patentable Goods*, 25 CARDOZO L. REV. 1251, 1279 (2004) (discussing how the concept of “inventing around patents” changes as technology becomes more complex); Michael A. Carrier, *Cabining Intellectual Property Through a Property Paradigm*, 54 DUKE L.J. 1, 122–23 (2004) (discussing the use of the experimental use exception in connection with the concept of inventing around patents).

<sup>333</sup> Barnett, *supra* note 332, at 1278–79; Carrier, *supra* note 332, at 122–23.

<sup>334</sup> Solum, *supra* note 323, at 44.

<sup>335</sup> See *supra* Part IV.C.2–3.

<sup>336</sup> See *supra* Part IV.C.2–3.

The strongest counterargument here is that the collection of patents and the subsequent need to invent around patents can stifle innovation. This argument has merit. However, this problem implicates the patent thicket problem.<sup>337</sup> And as discussed earlier, that issue is completely separate and should be addressed as such.<sup>338</sup>

### *B. Patent Dealers Do Not Spur Vexatious Litigation*

Another commonplace criticism of patent dealers is that they spur vexatious litigation.<sup>339</sup> When looking to the law for remedies concerning the creation of unnecessary litigation, the state-law doctrine of champerty avails itself at first glance.<sup>340</sup>

#### *1. Patent Dealing Is Not Champertous*

Champerty at English common law was a bargain between a stranger and a litigant to fund the lawsuit whereupon if the party undertaking the suit prevailed, the stranger would receive part of the disputed res.<sup>341</sup> This practice was prohibited under the English common law.<sup>342</sup> The doctrine of champerty arose under American common law “to prevent officious intermeddlers from stirring up strife and contention by vexatious and speculative litigation which would disturb the peace of society, lead to corrupt practices, and prevent remedial process of law.”<sup>343</sup> Generally, the interference in the litigation must have been “clearly officious and for the purpose of stirring up strife and continuing litigation.”<sup>344</sup>

In modern times, the doctrine is not recognized to the same degree as it was acknowledged in England.<sup>345</sup> As an example, a chose in action is generally

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<sup>337</sup> See *supra* Part III.B.

<sup>338</sup> See *supra* Part III.B.

<sup>339</sup> Stone, *supra* note 10.

<sup>340</sup> Champerty is a form of maintenance. “Maintenance” is the officious intermeddling in a lawsuit, in which the meddler has no interest or stake, by assisting an interested party financially or otherwise. As with any state law doctrine, the actual requirements vary by state. See, e.g., *Hall v. State*, 655 A.2d 827 (Del. Super. Ct. 1994); *Macke Laundry Serv. L.P. v. Jetz Serv. Co.*, 931 S.W.2d 166 (Mo. Ct. App. 1996); *McKellips v. Mackintosh*, 475 N.W.2d 926 (S.D. 1991).

<sup>341</sup> 4 WILLIAM BLACKSTONE, COMMENTARIES ON THE LAWS OF ENGLAND 135 (1765).

<sup>342</sup> *Id.*

<sup>343</sup> 14 AM. JUR. 2D *Champerty, Maintenance, and Barratry* § 1 (2005).

<sup>344</sup> *Am. Hotel Mgmt. Assocs. v. Jones*, 768 F.2d 562, 571 (4th Cir. 1985) (quoting *Smith v. Hartsell*, 63 S.E. 172, 174 (N.C. 1908)).

<sup>345</sup> *Schnabel v. Taft Broad. Co.*, 525 S.W.2d 819, 823 (Mo. App. 1975). The court in *Schnabel* recognized that the common law actions of maintenance of litigation and champerty are rare in modern times,

regarded as assignable under modern law,<sup>346</sup> while it was “within the scope of champerty” under English common law.<sup>347</sup> Additionally, certain assignments of rights of action have been altogether removed from the domain of champerty. These include attorney-client contingency fees,<sup>348</sup> assignments of debts to collectors, assignments to maintain will contests, and assignments of judgments.<sup>349</sup> Further still, the doctrine of champerty was never recognized, or is no longer recognized, in some American jurisdictions.<sup>350</sup> The general relaxation of the doctrine is rooted in two societal developments: a fundamental change in society’s view of litigation from a social ill that should be minimized to a useful means of resolving disputes,<sup>351</sup> and the development of effective control by other devices over the wrongs the doctrine was aimed at suppressing.<sup>352</sup>

Where champerty remains law, it has evolved differently from state to state. The laws in New York and Ohio are illustrative of this divergence in evolution. For a transaction to be considered champertous in New York, a person must directly or indirectly take assignment of a chose in action “with the intent and for the purpose of bringing an action or proceeding thereon.”<sup>353</sup> Further, the primary purpose of the purchase must be to bring suit or proceed with action upon the claim they received.<sup>354</sup> Alternatively, in Ohio a champertous transaction is one in which a “nonparty undertakes to further another’s interest in a suit in exchange for a part of the litigated matter if a favorable result ensues.”<sup>355</sup> Unlike in New York,<sup>356</sup> in Ohio the mere “assignment of rights to a lawsuit . . . [is] void as champerty.”<sup>357</sup>

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having been replaced by the causes of action of abuse of process, wrongful initiation of litigation and malicious prosecution. *Id.* at 824.

<sup>346</sup> *Saladini v. Righellis*, 687 N.E.2d 1224, 1226 n.4 (Mass. 1997); 6 AM. JUR. 2D *Assignments* § 51 (2005).

<sup>347</sup> *Saladini*, 687 N.E.2d at 1226 n.4.

<sup>348</sup> 14 C.J.S. *Champerty and Maintenance* § 12 (2005).

<sup>349</sup> *Id.* § 6.

<sup>350</sup> *Saladini*, 687 N.E.2d at 1224; *A v. D*, 482 A.2d 531 (N.J. Super. Ct. 1984).

<sup>351</sup> *Saladini*, 687 N.E.2d at 1226.

<sup>352</sup> *Id.* The court specifically identified rules governing contingent fees, public policy against the recovery of excessive fees, sanctions for misconduct, regulation of frivolous lawsuits, and the doctrines of unconscionability, duress, and good faith. *Id.* at 1225–27.

<sup>353</sup> *Echeverria v. Estate of Lindner*, 2005 WL 1083704, at \*4 (N.Y. Sup. Ct. Mar. 2, 2005) (quoting N.Y. JUD. LAW §§ 478, 479 (2005)).

<sup>354</sup> *Knobel v. Estate of Eugene A. Hoffman*, 432 N.Y.S.2d 66, 68 (N.Y. Sup. Ct. 1980).

<sup>355</sup> *Rancman v. Interim Settlement Funding Corp.*, 789 N.E.2d 217, 219 (Ohio 2003).

<sup>356</sup> See *supra* notes 353–54 and accompanying text.

<sup>357</sup> *Rancman*, 789 N.E.2d at 220.

*a. Patent Dealers in a New York-Type Jurisdiction*

In a New York-type jurisdiction,<sup>358</sup> the patent dealer operates within the law. The transfer of a patent is significantly different from the transfer of an ordinary cause of action. Although the patent confers the right of action with it, patents are a form of property and therefore have use beyond the exclusive rights they confer.<sup>359</sup> So, the transfer of a patent under which a cause of action for infringement has accrued does not merely confer that specific cause of action. Like property that has been possessed by a trespasser, the patent is useful in itself. Therefore, by definition a patent is excluded from the umbrella of the New York-style champerty law because it cannot be said that the primary purpose of the purchase is to bring suit or proceed with action upon the claim.<sup>360</sup>

*b. Patent Dealers in an Ohio-Type Jurisdiction*

In Ohio-type jurisdictions,<sup>361</sup> the case for patent dealers as champertors is more compelling, but it still falls short. If a patent dealer merely funded the patent holder, there is a very strong chance that the transaction would be found to be champertous under Ohio law. However, patent dealers generally purchase the patent outright. In *Rancman v. Interim Settlement Funding Corp.*, the court deemed a transaction in which a company loaned the plaintiff money based on a pending lawsuit to be champertous.<sup>362</sup> The discussion in that case focused on the fact that the loan and the interest thereupon limited the plaintiff's freedom in settling the case.<sup>363</sup> The court was also bothered by the severity of the loan's interest rate.<sup>364</sup>

The enforcement of patent rights implicates no such concerns relating to funding of lawsuits. By fully assigning the patent rights, the original owner or inventor is not placed in a position where the ability to settle is hindered, nor are there interest rate concerns because the original owner sets the sale price himself.

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<sup>358</sup> See *supra* notes 353–54 and accompanying text.

<sup>359</sup> 35 U.S.C. § 261 (2000). A patentee has an exclusive property right in his patented invention. *James v. Campbell*, 104 U.S. 356 (1882).

<sup>360</sup> See *supra* notes 353–54 and accompanying text.

<sup>361</sup> See *supra* notes 355, 357 and accompanying text.

<sup>362</sup> 789 N.E.2d 217, 221 (Ohio 2003).

<sup>363</sup> *Id.* at 220–21.

<sup>364</sup> *Id.* at 221.

The patent dealer is somewhat affected. Although patent dealers with clear title have no lien upon which interest accrues, the dealers would probably not settle for less than what they paid for the patent. However, dealers presumably decide to purchase the patent with an idea of its value, and should have paid less than that value. Before purchasing a patent or patent portfolio, patent dealers would thoroughly value the patent, taking into consideration the amount they would pay for the patent, the amount litigation could cost, and the time that would be expended. A strong argument can be made that an owner of a property right should not be forced into settling a case for less than what the property right is worth.

In examining the legal status of patent dealers within this context, it becomes clear that when the owner of a valid patent undertakes enforcement of their exclusive right, they do not violate the law. The law provides the owner of a patent, whether it was invented by that person or has been acquired by transfer,<sup>365</sup> the right to sue a person who violates the exclusive right that the patent grants.<sup>366</sup> This is an absolute right. Therefore, if a patent was properly granted by the Patent and Trademark Office, not only are the owners allowed to ensure nobody infringes the exclusive right, they are actually required to do so by law.<sup>367</sup>

#### CONCLUSION

Just as markets for intangibles like capital, debt, and risk have evolved over the past one hundred years,<sup>368</sup> a market for patents has also taken form. The recent emergence of patent dealers within this market is no cause for concern; rather, it signals progression, efficiency, and market evolution. Patent dealers

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<sup>365</sup> Patents and patent applications are fully "assignable in law by an instrument in writing." 35 U.S.C. § 261 (2000).

<sup>366</sup> Section 154(a)(1) provides that "Every patent shall contain . . . a grant . . . of the right to exclude others from making, using, offering for sale, or selling the invention throughout the United States or importing the invention into the United States." § 154. Section 271(a) then defines infringement by providing that "whoever, without authority makes, uses, offers to sell, or sells any patented invention within the United States or imports into the United States any patented invention during the term of the patent therefore, infringes the patent." § 271(a).

<sup>367</sup> In the interest of fairness and equity, those granted a monopoly under the patent system must enforce their rights in a timely manner, and where a defendant has suffered a detriment, a court of equity will bar a plaintiff whose institution of the action was inexcusably delayed. *See Advanced Hydraulics, Inc. v. Eaton Corp.*, 415 F. Supp. 283, 286 (N.D. Ill. 1976).

<sup>368</sup> *See Sandor, supra* note 281, at 2–4.

function as market intermediaries, and by doing so, they increase patent liquidity, set market clearing prices, and foster efficiency in the idea economy. The use of derogatory labels and alarmist dialogue has no place in an area of law so vital to the U.S. economy. As a rule, understanding should precede action, lest uninformed haste cause a gentle giant to be mistaken for a ghastly troll.

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## **The Myth of the Patent Troll: An Alternative View of the Function of Patent Dealers in an Idea Economy**

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