

# Patent Trolls: Do The Benefits Outweigh the Costs?

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CS 305

12/08/17

Word Count: 1,594

Patent trolls are companies that obtain patents with the intent to profit off of them through litigation rather than producing some form of service. These companies are capable of putting quite the strain on even large corporate entities. However, smaller startups are the ones who are the most affected by these types of litigation, as they do not have the monetary capabilities of larger companies. The issue of patent trolls is, however, not as black and white as it is portrayed to be. Some argue that the term patent troll is not only clumsy and overly intrusive, but that these so called patent trolls are a necessity in evolving the market as well as making it more efficient. With the role of patent trolls being so unclear the question is asked, are patent trolls a threat to innovation or a necessity to evolving the market?

If small companies are the backbone of the american economy, startups are the backbone of the tech business. Startups, specifically ones that focus on research and development, are at the most risk of facing litigation from patent trolls, as they suffer more than other companies after dealing with patent trolls (Bessen, 2014). Stunting companies that focus on R&D will inevitably stunt the overall innovation of the tech industry, as it will only be the larger companies who will be able to keep moving forward. The harm patent trolls cause when targeting smaller companies, overshadows the benefits they bring about when they are: buying patents, helping smaller companies defend patents, and strengthening the overall patent market.

This paper will focus on two sides of this argument. Firstly the importance of patent trolls in the market. This portion will focus on the existence of the patent market and how patent trolling entities are improving it. The positive effects patent trolls can have on startups will also be discussed. The second side will be based on the affects patent trolls have on smaller companies, with a focus on startups that specialize in research and development. After both arguments are clearly stated they will be compared and contrasted to show the benefits of patent trolling entities as well as the potential harm they can cause.

Patent trolls are becoming more relevant in today's society, as the amount of tech startups grow the number of attempted litigations by patent trolls grows with it. Litigation by patent trolls more than quadrupled between 2003 and 2013, and in 2014 a majority of patent lawsuits were filed by patent trolls (Bessen, 2014). However these entities are not a new issue to be brought about by the tech boom, patent trolls have been around - and been an issue for quite some time. The king of patent trolls is none other than Thomas Edison. He may have quite a few inventions under his belt, but he also made a fortune from the patents

he owned that he never used in his products. For multiple decades Edison held the record for individual with the most number of patents, at 1,093. Another surprising patent troll entity is the federal government, who hold a vast number of academic patents. This is due to the Bayh-Dole act, which was passed in 1980 and allowed government funded research by universities to be commercialized. In 1980 roughly 5% of the 28,000 patents created by the government were licensed out to industry (McDonough, 2007). By our current understanding of the term, both Thomas Edison and the federal government are patent trolls. However, not all cases of patent trolling are bad. The Bayh-Dole act has been credited as one of the most important contributions to the success of the modern U.S. intellectual property system (McDonough, 2007). Patent trolling entities may be framed in a very poor light, but they do offer up some surprising benefits.

The term patent troll itself is kind of derogatory, and can be overinclusive. To properly discuss the issues around this topic a more proper term should be used, such as patent assertion entities, or PAE's. There are a lot of issues with the current patent system that should not be blamed on PAE's. Mainly, the poor quality of many patents, specifically in software. Bad patents are being issued daily, and almost anyone can abuse the system with a bad patent (McDonough, 2007). Larger companies that are not known to be PAE's have been known to take advantage of the system. Many companies keep patent portfolios (which are lists of patents) to use as a threat to counter sue when being threatened with patent litigation (McDonough, 2007). Patents are more than just a way to protect some sort of intellectual property. If a credible threat of litigation exists a patent becomes commodity, and if a patent can be exchanged between a buyer and a seller, than a legitimate patent market exists (McDonough, 2007). This market can become more efficient with time as long as there are more transactions. There are many people who could benefit from a patent market. When patents are sold they are taxed, as new wealth is created and thus a capital gains tax is paid, creating new revenues (Benjamin, 2013). Smaller companies can also be benefited by PAE's. They can monetize their patents by selling them to PAE's, who can also offer insurance (Clinton, 2015). One of the key motives for patent holders to sell their patents is the huge gap in financial resources between inventors and manufacturers (Clinton, 2015). Large companies don't need to worry about whether they are violating the rights of a patent owner as there is nothing that they can do about it (Benjamin, 2013). Without the intermediary role between inventors and large manufacturers played by PAE's, there would be no credible threat of

litigation, devaluing the patent market. Inventors would also be more limited, stunting the innovation the tech market thrives on (Clinton, 2015).

The patent market has improved over the last few decades as more patent intensive products are produced (Clinton, 2015). New technologies can contain hundreds of patented parts, many of which are not owned by the creator of the new product. These parts must be negotiated to use and this robust innovation has brought a dramatic decline in prices for patent-intensive products (Clinton, 2015). With these improvements being made by the patent market, it is important to defend not only PAE's but patents themselves. The patent system is more important than keeping a single company afloat, limiting a holder's ability to use litigation to stop someone from infringing on their patent would weaken the overall value of patents, which in a way are the backbone of innovation (McDonough, 2007).

PAE's can help smaller companies, but they can also devastate them. Over 60 percent of small companies that faced litigation from PAE's experienced a financial impact and over 85 percent say that their company was extremely distracted from core business, which can be very damaging for startups as "no one wants to invest in a company where founder time and investor money is going to be "bled to patent trolls" (Chien, 2012). Startups that have to deal with PAE's face many issues, not all of which are financial. 41 percent of software startups that faced patent litigation reported "significant operational impacts" causing them to exit business lines, change products, or change strategy (Bessen, 2014). On top of that small companies that chose to fight this litigation in court spent an average of 24 percent of their annual revenue, which is a huge gamble (Chien, 2012). This is a huge problem that unfortunately seems to be getting worse. In 2013 there were six times as many patent lawsuits last year than in the 1980's (Bessen, 2014). PAE's cost defendant firms roughly 29 billion dollars and destroy 60 billion in firm wealth each year and these costs end up being disproportionately spread to companies that focus on R&D (Bessen, 2014). These companies that focus on R&D are incredibly important to innovation. Blocking them creating new products and patents can potentially harm the entire market and stunt growth in the tech industry. R&D firms that face patent litigation reduced their R&D spending by \$211 million and reduced their patenting significantly (a 48% decline) in subsequent years (Bessen, 2014). Larger companies are capable of handling PAE's, its smaller companies that sometimes can't recover after facing this kind of lawsuit. Unfortunately, most patent trolls target firms selling less than \$100 million a year (Bessen, 2014).

PAE's entities are usually seen as bad guys when looking at the tech industry. They may bring a lot of harm to companies, but they also have some surprising benefits. The harm patent trolls cause when targeting smaller companies, overshadows the benefits they bring about when they are: buying patents, helping smaller companies defend patents, and strengthening the overall patent market. PAE's can offer insurance and monetization to small companies for their patents, which can end up helping them when defending their patents against larger manufacturers. The patent market itself helps to strengthen patents and allows for innovation in patent intensive products. However, the benefits brought about by PAE's are overshadowed by the harm they can bring to startups. If PAE's focused on helping these smaller companies by strengthening the patent market, they'd be great. But, as a majority of PAE's choose to target small companies for financial gain, they bring an overall negative affect to the current innovative market. Fixing this problem will be difficult as the patent and patent market are still very useful to the economy and need to be protected.

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