Strength in numbers

2,500 companies will be sued by NPEs this year. Will yours be one of them? John A. Amster explains how companies can take a proactive approach to the NPE threat.

Patent disputes seem to be an almost everyday story in the business media, but while Apple v Samsung or Google v Microsoft make for riveting reading, the fact is that such company-to-company patent quarrels are relatively rare. This is because almost all companies today maintain large portfolios of broadly-applicable patents, creating a tacit understanding that any infringement litigation would be met with a countersuit. The resulting state of "mutually assured destruction" dissuades companies from starting infringement fights except in highly strategic situations.

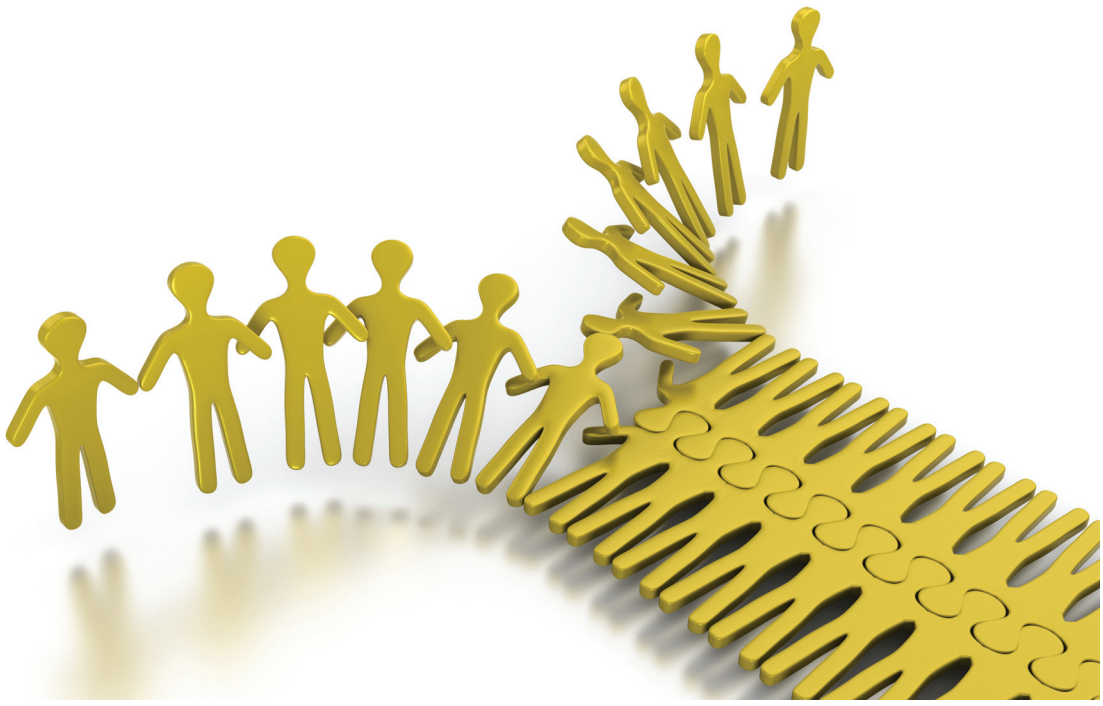
Instead, the vast majority of patent litigation today is being initiated by non-practicing entities (NPE). NPEs, also often referred to as "patent trolls", are companies that do not design or make any products. Their business model is simple: acquire patents, identify operating companies that may be infringing those patents, and bring legal action to generate a settlement and/or license payments. Because they have no products or services of their own, NPEs are not susceptible to being countersued and "mutually assured destruction" is not a deterrent.

A growing problem

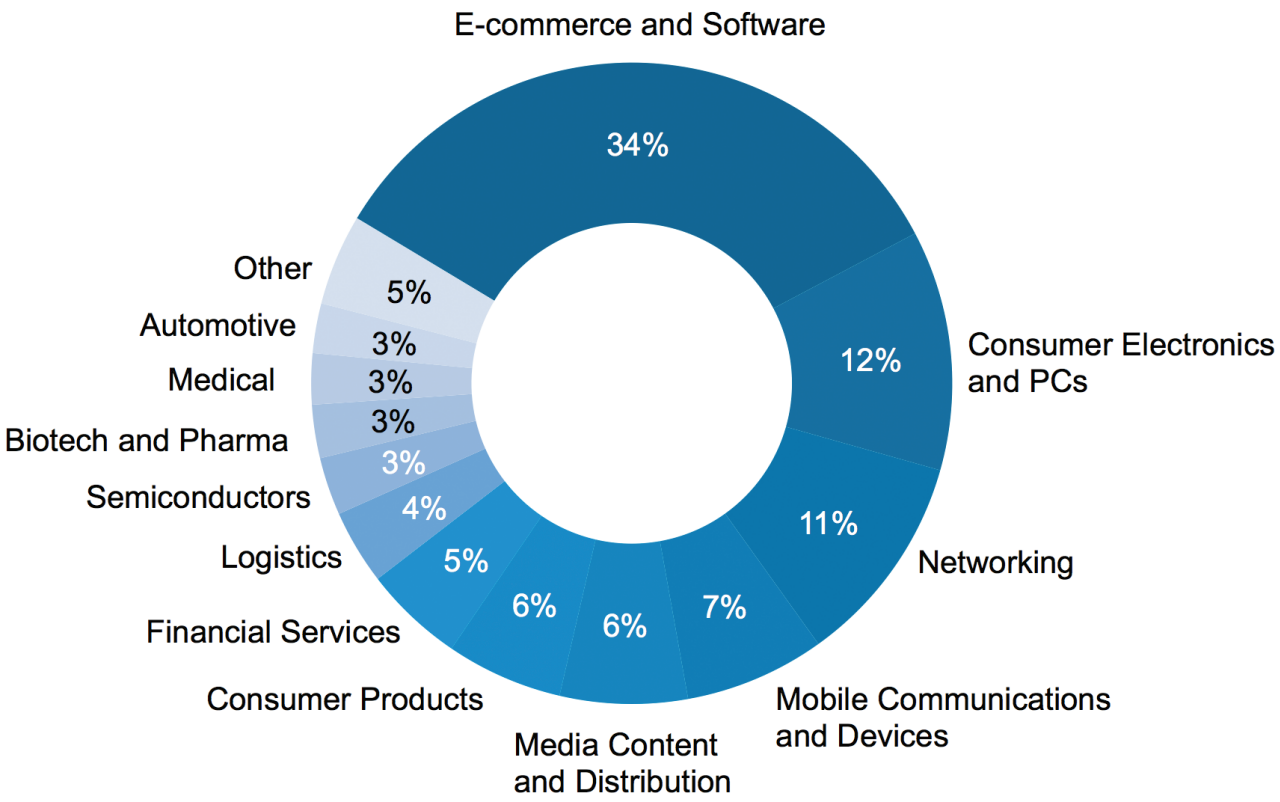
NPE-based litigation has rapidly become a large and expensive problem for operating companies. The number of NPE lawsuits has risen from 450 filed in 2005 to more than 3,000 filed last year, and a recent study by two Boston University academics calculated that operating companies incur aggregate costs (legal expenses, settlements and redirecting of internal resources) of roughly US $30 billion a year dealing with NPEs. Today, there are more than 900 active NPEs with an estimated $8 billion in patent-buying power. In 2013, it is expected that more than 2,500 operating companies will be sued in NPE-initiated infringement actions, and the number is rising.

Clearly, NPE risk is growing, but not all risk is created equal. Certain sectors and certain kinds of companies are more frequently targeted by NPEs. The reason is simple: NPEs are smart and opportunistic. They are experienced with particular kinds of technologies and how to build legal arguments for infringement in those areas. As a result, certain sectors carry a higher degree of patent risk, including consumer electronics and PCs, mobile

John A. Amster
CEO and
Co-Founder,
RPX Corporation



Total Defendants Added by Sector



- RPX definition of NPEs include patent assertion entities, universities, individual Inventors, and non-competing entities.
- "Total defendants added" is the total number of case/defendant pairings.
- RPX manually categorizes each case filed into a market sector based on a review of the accused products, defendants, and asserted patents.

Source: RPX Research

communications and devices, E-commerce and networking (see chart above for details). Companies making or using these technologies are squarely in the cross-hairs of NPEs.

It is important to note, however, that while these sectors are currently the most perilous, other sectors cannot rest easy. The expanding adoption of advanced technologies is also escalating the likelihood of being targeted by an NPE. Technology migrates, converges, and evolves into new applications and, as it does, new markets and new companies draw NPE attention.

Financial services and automotive companies, for example, do not design or sell proprietary digital technologies, but they are increasingly incorporating such technology into their products (think mobile banking applications or on-board satellite-enabled entertainment and GPS navigation systems). It should be no surprise that NPE litigation is on the rise in both sectors.

Dealing with the threat

So NPE risk is growing deeper and broader. What are your options to deal with this emerging threat to your company?

Until recently, the traditional approach has been reactive: wait for the worst and hope for the best. If a company did receive an assertion letter or was named in an infringement complaint, the response was to hire outside counsel and devote hundreds of hours of its own management and senior staff time to preparing a legal response. The cost of being reactive can easily run into the millions of dollars each time an NPE brings suit.

As a result, more and more companies have begun taking a proactive approach to mitigating NPE risk. Rather than wait passively while NPEs acquire dangerous patent portfolios, these companies are preemptively buying the patents to keep them out of NPE hands. Few companies do this unilaterally because 1) it is extraordinarily expensive and 2) it is fundamentally unfair – a single company clearing a dangerous portfolio is bearing the entire cost of relieving every other company threatened by those patents (the so-called "free rider" dilemma).

Instead of acting unilaterally, more companies are joining together to clear patent risk. RPX now has a network of 140 subscription fee-paying clients on whose behalf we identify and buy high threat patents. We represent our clients' collective interests in the marketplace and, by leveraging the capital provided by annual subscription fees, we are able to make acquisitions at a scale that has a significant positive impact.

These kinds of risk mitigation services – which include an innovative patent litigation insurance product – are based on our unique ability to analyze, quantify, and fairly price the risk faced by a particular company in its particular circumstances. And that capability is based on data. The precise actual costs of NPE litigation and the factors affecting those costs have traditionally not been disclosed by plaintiffs

or defendants. But because of our central role in the patent market, RPX has been the first to compile a comprehensive and highly accurate database of this information.

We administered the recent large-scale NPE Cost Study that was performed at the behest of the US General Accounting Office. More than 80 participating companies shared information including external and internal legal costs, length of litigation, relative costs for companies of different sizes/ages/industry sectors, frequency and size of settlements, factors affecting settlement terms, and more. RPX is also continuously adding detailed – and anonymized – legal cost and settlement information to its overall database.

This in-depth data set has allowed RPX to create the first accurate actuarial model to predict NPE risk. For companies that provide us with historical litigation information, we can conduct an actuarial analysis that predicts how often that company would be sued by an NPE and how much that litigation would cost in legal expenses and settlement payments. It is a breakthrough in how operating companies can assess, anticipate and quantify patent risk.

A better understanding

Ten years ago, companies had little recognition of and no visibility on NPE risk. The NPE business model was too new, there was only minimal public disclosure of case details, and operating companies had no way to share resources or data on patent and litigation costs. NPEs had a significant information advantage over operating companies and could leverage that advantage in court proceedings and settlement negotiations.

Today, the threat is far larger, but also far better understood. Companies now have a clearer understanding of the NPE model, and through third-party solutions like RPX, they are able to collaborate to remove risk and share data to better predict and quantify it. For operating companies that face a growing threat from NPEs, this is a huge advantage. Legal and finance departments can now coordinate to anticipate patent risk and plan for it as they would for any other kind of operating risk.

NPE risk used to be a matter of educated guess work. It is rapidly becoming a predictable budget line item. In less than five years, RPX and its growing network of member companies have pioneered a practical and highly efficient way to share resources, transfer risk, and monetize patent assets. Good news, indeed, for the thousands of companies that are just now beginning to deal with the inevitable and growing challenge of NPE litigation.

RPX
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John A. Amster, Chief Executive Officer and Co-Founder

John is the CEO and co-founder of RPX Corp. Prior to co-founding RPX, Mr. Amster was the General Manager of Strategic Acquisitions and Vice-President of Licensing at Intellectual Ventures, responsible for strategic acquisitions of patent portfolios as well as developing the software and e-commerce licensing programs.

Prior to joining IV, Mr. Amster was Managing Director and founded the M&A Advisory practice for Ocean Tomo, completing several important transactions in the early patent market, including the sale of Commerce One. Prior to joining Ocean Tomo, Mr. Amster was Vice President and Secretary at InterTrust Technologies, where he worked on intellectual property transactions, merger and acquisition activities, and late-stage financing activities, including the sale of InterTrust to a Philips-Sony joint venture for $453 million.

Mr. Amster started his career as an associate at Weil Gotshal & Manges, where his practice included mergers and acquisitions, equity investments, venture capital financings, intellectual property licensing, and patent litigation.

Mr. Amster received his JD from Benjamin N. Cardozo School of Law and his BA from Middlebury College.

Mr. Amster frequently speaks on patent litigation matters at various industry conferences and in the media. He has been recognized in The American Lawyer's 2010 review of "The 25 Most Influential People in IP" and in Managing Intellectual Property magazine's "The 50 Most Influential People in IP."

Mr. Amster is active in non-profit volunteer work as President of the Board for Lone Mountain Children's Center, and serves on the Board of Trustees of Town School for Boys.

Contact:

Address: One Market Plaza, Steuart Tower, Suite 800
San Francisco, CA 94105
Tel: +1 866 779 7641
Website: www.rpxcorp.com