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Hearing on: The International Trade Commission and Patent Disputes

Chairman Goodlatte, Ranking Member Watt, and Members of the Subcommittee,

My name is Bernard J. Cassidy, and I am Executive Vice President and General Counsel at Tessera Technologies, Inc., which is headquartered in the heart of Silicon Valley, in San Jose, California. We have facilities in Charlotte, North Carolina, Rochester, New York, and Arcadia, California as well as in Europe and Asia. I deeply appreciate this opportunity to speak before you regarding the importance of the International Trade Commission to my company and our innovation economy.

## The Tessera Story

Tessera Technologies, Inc. is a small publicly-traded holding company that traces its roots to three former IBM technology pioneers who set out on their own in 1990. Tessera, Inc., our oldest subsidiary, pioneered chip-scale packaging solutions for the semiconductor industry. We have become a leader in semiconductor packaging via our inventions which are now widely adopted by the semiconductor industry. This technology enables electronics devices such as cell phones to become as small as they are today.

Today, through subsidiaries, we operate two businesses: Intellectual Property and DigitalOptics. Our Intellectual Property business generates revenue from patented innovations through license agreements with semiconductor companies and outsourced semiconductor assembly and test companies. Our DigitalOptics business offers breakthrough imaging technologies and products will that bring full-featured digital still camera capabilities to the mobile phone camera market through its miniaturized camera module solutions.

None of this would have been possible had we not had a strong patent system to protect our inventions and reward our innovators. Maintaining a strong patent system is essential to our continuing success.

## The Innovation Alliance

Tessera Technologies, Inc. is a co-founder of the Innovation Alliance ("IA"), a coalition of companies seeking to enhance America's innovation environment by improving the quality of patents and protecting the integrity of the U.S. patent system. The Innovation Alliance represents innovators, patent owners and stakeholders from a diverse range of industries that believe in the critical importance of maintaining a strong patent system. Many Innovation Alliance members also manufacture and/or sell products and services that use not only their own patents, but those of third parties as well. The IA's positions on a strong patent system – on the importance of high-quality patents, the pro-innovation and pro-competitive benefits of voluntary standardization efforts and bilateral negotiation of licenses and cross-licenses among standardization participants – are not new.

The Judiciary Committee and its Members appreciate the importance of strong intellectual property law to the U.S. economy. We applaud your leadership in safeguarding our Nation's intellectual property, thereby helping to build a legal system that encourages investment in innovation. The Innovation Alliance welcomes a discussion of the role of the ITC in safeguarding American industries from unfair trade. We believe that the Committee will conclude that the long-term interests of our innovation-based economy outweigh the near-term interests of a few.

Licensing U.S. intellectual property strengthens the economy and improves our trade balance. Section 337, the statute that regulates unfair practices in import trade, is a key element of the nation's trade laws and ensures that American innovators, including licensing companies, will not be harmed by the importation of goods that infringe valid and enforceable U.S. patents. Importers of foreign made products – both U.S. based and foreign companies – have appealed to Congress for several changes to Section 337 that would, in effect, limit access to the ITC and/or weaken the powers of the ITC to deal with cases of unfair trade practices. Weakening the ITC's jurisdiction would benefit foreign economies, foreign competitors, and other foreign manufacturers to the detriment of the U.S. economy. Although one can appreciate the near-term concerns expressed by some U.S.-based technology companies, a discussion of issues affecting the ITC should be undertaken with the long view in mind. Specifically, weakening Section 337 to disadvantage patent holders relative to infringing importers will retard American innovation, weaken the trade position of the United States, and hurt American innovation and manufacturing by protecting infringing products manufactured in other countries.

The International Trade Commission

The U.S. International Trade Commission ("ITC")[1] is a federal administrative body that "administer[s] U.S. trade remedy laws within its mandate in a fair and objective manner."[2] Among those trade laws, the ITC administers Section 337 of the Tariff Act of 1930, as amended ("Section 337"), which makes the ITC responsible for regulating "unfair practices in import trade."[3] To enable the ITC to perform this regulatory duty, Section 337 vests the ITC with authority to issue orders excluding articles from entry into the United States where those articles are imported utilizing (1) unfair methods of competition and unfair acts or (2) infringement of U.S. intellectual property rights.

Section 337 was enacted in 1930, the decade that expanded the role of federal administrative agencies. From the onset of this era, a central pillar supporting administrative expansion was the necessity of regulating technical fields that demanded expertise beyond that found in the legislative and judicial branches of government. Stemming from this longstanding policy, Congress and the federal courts have accorded administrative agencies deference and discretion to implement their prescribed regulatory tasks as reflective of their heightened

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[1] The ITC was established in 1916 as the "Tariff Commission." Its name was changed to the International Trade Commission in 1974.

[2] *Mission Statement*, U.S. INT'L TRADE COMM'N, http://www.usitc.gov/press_room/mission_statement.htm (last visited May 3, 2012).

[3] 19 U.S.C. § 1337 (2006).

expertise. In light of this practice, the ITC's interpretation of Section 337 should not be disturbed, unless or until Congress finds fault with the Commission's interpretation of the law.

The 1988 Amendments Recognized the Importance of Licensing to Our Economy

Prior to amendment in 1988, Section 337 treated all unfair import trade practices alike. By the 1980s, however, manufacturing was shifting abroad, and the United States was increasingly becoming a technology-based economy. Therefore, Congress amended Section 337 in 1988[4] to reflect these economic realities. Importantly, the 1988 amendments restructured Section 337 to treat intellectual property infringement separately—and more liberally—from other types of unfair acts.

Particularly noteworthy among these changes, the 1988 amendments eased the domestic industry requirement for Section 337 investigations based on intellectual property rights. First, Congress removed the "injury" requirement, thereby eliminating any test of economic harm to the domestic industry. Second, a new provision, § 1337(a)(3)(C), provided that a domestic industry could be established where there was "substantial investment in [the asserted intellectual property's] exploitation, including engineering, research and development *or* licensing."[5]

Until quite recently, the procedural posture of many Section 337 investigations prevented the ITC from fully defining the boundaries of new § 1337(a)(3)(C).[6] However, in more current Section 337 investigations where parties have attempted to establish domestic industries based exclusively upon licensing, the ITC has been utilizing its administrative expertise to determine, on a case-by-case basis and in a series of balanced and carefully-considered Commission opinions, which entities Congress sought to protect in enacting the 1988 amendments.

Four Key Issues

The remainder of this written submission will briefly address four issues of recent interest to the ITC patent community: domestic industry, public interest factors, the so-called *eBay* principles, and standard-essential patents. I incorporate by reference the attached papers recently published by the Innovation Alliance which deal with the latter two issues in more detail.

The ITC's Ongoing Development of the Domestic Industry Inquiry Under § 1337(a)(3)(C)

The first notable instance where the ITC thoroughly elaborated upon the standard for establishing a domestic industry based upon licensing occurred twenty years after the 1988 amendments, in *Certain Stringed Musical Instruments and Components Thereof* ("*Stringed*

[4] *See* Omnibus Trade and Competitiveness Act of 1988, 102 Stat. 1107, Pub. L. 100-418 (Aug. 23, 1988).
[5] *Id.* (emphasis added). In addition to this new statutory provision, the 1988 amendments retained the ability of a complainant to establish a domestic industry under Section 337 by demonstrating the more traditional manufacturing-based elements.
[6] Indeed, many investigations where the issue had arisen settled prior to the ITC having an opportunity to refine the meaning of this new provision in an authoritative Commission Opinion.

*Instruments"*).[7] In *Stringed Instruments*, the complainant, an individual inventor, invested $8,500 on research and development over multiple years and made numerous unsuccessful attempts to license the asserted patents at trade shows. At issue was whether this investment in licensing and research and development was "substantial" enough to establish a domestic industry under § 1337(a)(3)(C).

Upon a thorough analysis of Section 337's legislative history,[8] the ITC stressed that the proper inquiry is highly "fact-dependent," and set forth the following guidelines:

> There is no minimum monetary expenditure that a complainant must demonstrate to qualify as a domestic industry under the 'substantial investment' requirement of [§ 1337(a)(3)(C)] . . . . [S]howing the existence of a domestic industry will depend on the industry in question, and the complainant's relative size. . . . [T]here is no need to define or quantify the industry itself in absolute mathematical terms.[9]

After carefully applying the facts to this standard, the ITC held that that the individual inventor had not made a showing "of substantial investment of the type described in Section 337(a)(3)(c)."[10] However, based upon its earlier statutory analysis, the ITC cautioned that "access to section 337 should not be foreclosed to individual inventors simply because their operations or activities are not on the scale of many corporations or universities."[11]

In 2010, in *Certain Coaxial Cable Connectors and Components Thereof Containing Same* (*"Coaxial Cable"*),[12] the ITC further developed its interpretation of the 1988 statutory provision. At issue was whether expenses incurred in prior patent litigation could be considered investments in licensing and, thus, help establish a domestic industry under § 1337(a)(3)(C). After thoroughly examining Section 337's text and legislative history,[13] the ITC determined that litigation expenses, per se, could not establish a domestic industry under § 1337(a)(3)(C). However, the Commission also held that, if prior litigation expenses exhibited a clear nexus to the complainant's concerted efforts to license the asserted patent, they could be considered as one factor, among others, as to whether there was substantial investment in exploiting the patent via licensing efforts.[14] Thus, *Coaxial Cable*—carefully interpreting Section 337's text and

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[7] 337-TA-586, Comm'n Op. (May 16, 2008).

[8] *See id.* at 14–16 (analyzing House and Senate reports pertaining to Section 337's 1988 amendments).

[9] *Id.* at 25–26.

[10] *Id.* at 26.

[11] *Id.* at 27.

[12] 337-TA-650, Comm. Op., (Apr. 14, 2010), *aff'd*, John Mezzalingua Assocs., Inc. v. Int'l Trade Comm'n (Fed. Cir. 2012).

[13] *Id.* at 44–50.

[14] The Commission provided the following guidance as to whether a sufficient nexus between litigation expenses and licensing efforts may exist:

> Depending on the circumstances, [licensing activities] may include, among other things, drafting and sending cease and desist letters, filing and conducting a patent infringement litigation, conducting settlement negotiations, and negotiating, drafting and executing a license. The mere fact, however, that a license is executed does not mean that a complainant can necessarily capture all expenditures to establish a substantial investment

legislative history—deliberately built upon *Stringed Instruments*, allowing for interpretation of the statute to develop as additional factual nuances arose in future investigations.

The ITC further honed its interpretation of § 1337(a)(3)(C) in *Certain Multimedia Display and Navigation Devices and Systems, Components Thereof, and Products Containing Same* ("*Navigation Devices*").[15] In *Navigation Devices*, the primary issue was whether a complainant could establish a domestic industry based upon its investment in licensing its entire patent portfolio without allocating expenditures to licensing the asserted patents. Despite public comments advocating this broad approach, the ITC determined that Congress did not intend Section 337 to encompass such a liberal interpretation. Instead, the Commission stated that the test is governed by "the strength of the nexus between the licensing activity and the asserted patent."[16] Specifically, the Commission analyzed the complainant's patent portfolio and related activities in three areas to determine whether a "substantial investment" had been made to exploit the patents at issue, namely: (1) "the relative importance or value of the asserted patent within the portfolio"; (2) the extent to which activities are "*solely* related to licensing" versus "serv[ing] multiple purposes,"; and (3) "the extent to which the complainant conducts its licensing operations in the United States, including the employment of U.S. personnel and utilization of U.S. resources in its licensing activities."[17] Consequently, the ITC determined that the burden is on the complainant to "present evidence that *demonstrates the extent of the nexus between the asserted patent and the complainant's licensing activities and investments*."[18]

With respect to the "substantial investment" test, the Commission stated that "[t]he type of efforts that are considered a 'substantial investment' under 337(a)(3)(C) will vary depending on the nature of the industry and the resources of the complainant."[19] The Commission also

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> in the exploitation of the patent. ***A complainant must clearly link each activity to licensing efforts concerning the asserted patent***.

*Id.* at 43–44 (emphasis added). Ultimately, the Commission remanded the investigation to the ALJ for determination of whether the complainant's litigation expenses exhibited a sufficient nexus to licensing efforts. A portion of the prior litigation expenses satisfied the nexus test. However, they were not sufficiently "substantial" under 1337(a)(3)(C).

[15] Inv. No. 337-TA-694, Comm'n Op. (Aug. 8, 2011).

[16] *Id.* at 9.

[17] *Id*. at 9-15. The nexus between the licensing activity and the asserted patent, as well as the nexus between the activity and the U.S., is "fact-focused and case-specific." *Id.* at 9, 14.

[18] *Id.* (emphasis added). In so holding, the ITC provided a list of non-exhaustive considerations to better guide future litigants:

> In determining whether there is a strong enough nexus between an asserted patent and a larger patent portfolio as a whole, the ITC identified the following non-exhaustive factors: "(1) the number of patents in the portfolio, (2) the relative value contributed by the asserted patent to the portfolio, (3) the prominence of the asserted patent in licensing discussions, negotiations and any resulting license agreement, and (4) the scope of technology covered by the portfolio compared to the scope of the asserted patent.

*Id.* at 10.

[19] *Id.* at 15. The ITC also provided a list of several additional factors to take into consideration:

> Other factors that might be relevant in determining whether a complainant's investment is substantial are (1) the existence of other types of 'exploitation' of the asserted patent such

emphasized that investment in licensing "must be domestic, i.e., it must occur in the United States."[20] Ultimately, the Commission found that the complainant had not made a substantial U.S. investment in exploitation of the specifically asserted patents through its licensing activities. By carefully analyzing and applying the statutory language, the Commission determined that the complainant's activities did not create the type of domestic industry envisioned by Congress.

The Commission's most recent comments on the economic prong of the domestic industry analysis came in *Certain Liquid Crystal Display Devices, Including Monitors, Televisions, Modules, and Components Thereof* (*"Liquid Crystal Display Devices"*)[21] and demonstrate that the ITC's balanced interpretation of § 1337(a)(3)(C) continues. In *Liquid Crystal Display Devices*, the complainant purchased a substantial patent portfolio covering a broad array of technology and subsequently filed parallel suits at the district court and the ITC against a number of respondents. The Commission was tasked with determining which of the complainant's activities and investments related to its efforts to license the patents at issue in the suit and ultimately determined that only the "activities relating to [complainant's] LCD licensing program, including employee time, facility use, travel, and product acquisition," qualified as "substantial investment" under Section 337(a)(3)(C).[22] The Commission began its analysis by reiterating the guidance laid out in *Navigation Devices*, that "the complainant must demonstrate that a particular activity: (1) relates to the asserted patent; (2) relates to licensing; and (3) occurred in the United States."[23] Importantly, the Commission determined that expenses and activities related to the purchase of patent portfolios, litigation of underlying 337 investigations and parallel district court actions, and reexamination of the patents at issue did not qualify as exploitation through licensing.[24]

Specifically, the Commission reasoned that the act of purchasing a patent portfolio "is solely related to ownership, not licensing," and noted that "Congress clearly stated that it did not intend mere patent ownership to constitute a domestic industry."[25] Similarly, the Commission rejected complainant's argument that expenses relating to reexamination of the patents in the context of licensing negotiations initiated by one of the respondents during the course of the investigation should qualify as exploitation through licensing. The Commission thus held that, like the act of purchasing a portfolio, "reexaminations are simply a continuation of prosecution that reaffirm or modify the boundaries of the patentee's ownership."[26]

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> as research, development, or engineering, (2) the existence of license-related ancillary activities such as ensuring compliance with license agreements and providing training or technical support to its licensees, (3) whether complainant's licensing activities are continuing, and (4) whether complainant's licensing activities are those that are referenced favorably in the legislative history of Section 337(a)(3)(C). The complainant's return on its licensing investment (or lack thereof) may also be circumstantial evidence of the complainant's investment.

*Id.* at 16.

[20] *Id.* at 8.

[21] *Liquid Crystal Display Devices*, Inv. Nos. 337-TA-741, 337-TA-749, Comm'n Op. (Jul. 6, 2012).

[22] *Id.* at 110.

[23] *Id.* at 109 (citing *Navigation Devices* at 7-8).

[24] *Id.*

[25] *Id*. at 111.

[26] *Id.* at 115.

Finally, the Commission reaffirmed ITC precedent that, generally, only activities occurring before the filing of the complaint are eligible to qualify as part of the "substantial investment" analysis.[27] Consequently, the Commission rejected complainant's argument that its litigation expenses for an underlying 337 investigation and parallel district court action should count towards the establishment of a domestic industry. This, the Commission noted, "would essentially eliminate the domestic industry requirement."[28] The Commission added that "[p]ermitting complainants to rely on these activities and investments to establish a domestic industry, would be inconsistent with the statute and legislative history,"[29] again demonstrating the ITC's abiding commitment to careful and well-reasoned statutory interpretation.

The preceding discussion illustrates that the ITC has interpreted Section 337 in a balanced manner. Harnessing its administrative expertise, it has consistently remained mindful of the 1988 amendments' intent to liberalize Section 337 but also remained equally vigilant in not allowing an expansion of the domestic industry test beyond the intent of Congress. As illustrated in Commission opinions analyzing § 1337(a)(3)(C), the ITC continues to interpret Section 337 in a balanced, case-by-case manner, carefully considering the statutory language and intent of Congress. As the ITC continues to harness its expertise, further Congressional action should be reserved for a time when there is disagreement with the interpretive efforts of the ITC.

<u>Public Interest Factors in Fashioning ITC Remedies</u>

The ITC has no authority to award damages based upon past infringement; it can only issue prospective relief by issuing limited or general exclusion orders that block infringing goods at the border, as well as and cease and desist orders that forbid the domestic sale of already-imported infringing goods. Section 337 states that the Commission "shall" exclude goods it has found to be infringing from entry into the United States, "unless" it finds that relief is not appropriate in light of its consideration of four public interest factors set out in the statute:

- the public health and welfare,
- competitive conditions in the United States economy,
- the production of like or directly competitive articles in the United States,
- and United States consumers.

Importantly, even if the ITC decides that a remedy is appropriate, the President has the power to prevent the remedy from going into effect if he or she determines that a remedy is not appropriate for what the statute refers to as "policy reasons," an open-ended term not defined in the statute.

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[27] *Id.* at 113. "The Commission agrees with the ALJ that, as a general matter, 'only activities that occurred before the filing of a complaint with the Commission are relevant to whether a domestic industry exists or is in the process of being established,'" (quoting *Certain Coaxial Cable Connectors, Components Thereof and Prods. Containing Same*, Inv. No. 337-TA-650, Comm'n Op., at 51 n.17 (Apr. 14, 2010)).
[28] *Id.*
[29] *Id*. at 114. Section 337 "imposes an affirmative requirement of demonstrating the domestic industry, one which cannot be automatically fulfilled by the filing of a Section 337 complaint."

In short, the statute provides a remedy along with robust built-in safeguards against misuse.

Moreover, following the 2007 investigation titled *Baseband Processor Chips*, the ITC plunged itself into an internal and public comment review of how the public interest factors would best be treated within the investigation process. The result was a pilot program which in turn was followed by the issuance of new rules in November 2011. Under this recently enacted regime, the complainant must file a statement on the public interest concurrently with the complaint, and include certain information relevant to the public interest factors. The respondents and the general public have an opportunity to respond and the complainant may reply. These filings help the ITC Administrative Law Judge to develop a full record about public interest factors early in the case, and supplement the multiple opportunities interested parties have to comment during full Commission review at the end of the case.

It would seem be premature for Congress to legislate on the public interest factors process until the ITC has had an opportunity to determine whether its new process sufficiently and fairly addresses the concerns voiced about these factors.

*eBay*: Should an Interpretation of the Patent Act Be Imported Into the Tariff Act?

It has also been suggested that the ITC be required to apply the so-called *eBay* standards for injunctions used in U.S. district courts. This argument ignores the fact that the ITC and U.S. District Courts are markedly different venues with different jurisdiction and powers necessitating the differing standards. Given that the only remedy available to the ITC is exclusion orders, mandating application of *eBay* would substantially weaken the power of the ITC to deal with unfair trade practices. Furthermore, the Federal Circuit Court of Appeals expressly rejected homogenization of injunction and exclusion standards in the case of *Spansion, Inc. v. ITC*, 629 F.3d 1331 (Fed. Cir. 2010).

Standard-Essential Patents

Finally, a few important comments about standard-essential patents ("SEPs"). The Innovation Alliance hopes the Congress will seriously consider the adverse and unintended consequences of a blunt response to dealing with disputes involving SEPs. The IA would be very concerned if the ITC or the courts established a bright line rule or presumption that prohibited a patent holder from seeking or obtaining an exclusion order/ injunction due to the "possibility" of patent hold-up or because the patent(s) at issue is a SEP. A rule prohibiting or limiting the availability of exclusion orders or injunctions to SEP holders would tip the balance in favor of infringers to the detriment of innovation and ultimately consumers.

There is no evidence to suggest that such sweeping changes to the current law, remedies or processes are necessary or in the public interest. Rather than presume hold-up exists in every instance, it should be noted that a patent holder and a standards implementer both have strong incentives to negotiate in good faith. The implementer does not wish to risk an injunction that could prevent or disrupt its manufacturing, and the patent holder wants a return on its investment and funding for continued R&D. These incentives encourage negotiation, which has been the preferred mechanism under most standard setting organization ("SSO") policies for establishing license terms. Under a no-exclusion-order/no-injunction policy, however, the implementer has little incentive to bargain in good faith because by litigating it can avoid paying royalties until at least the litigation is over, if not longer. Moreover, a patent holder's good faith offer becomes a ceiling that caps the implementer's litigation risk. The result would be more and longer litigation, with the inefficiency that litigation entails, and an unjustified shift in bargaining power from patent holders to implementers that would destroy the balance which currently exists.

A no-injunction rule would also create a perverse incentive: innovators who participate in SSOs (and give FRAND commitments) would have fewer rights than innovators that do not participate. The predictable result would be that fewer innovators would participate in SSOs with such IPR rules (or make FRAND commitments if they do participate) or engage in R&D for technologies that may be standardized. Reduced participation in SSOs or reduced funding of R&D would likely result in delay, technologically inferior standards, and reduced information about patents implicated by standards. Refusals to make FRAND commitments would similarly lead to delay and technologically inferior standards as SSOs would attempt to "design out" the technologies of companies that refuse to make FRAND commitments.

Conclusion

The ITC has the capability, resources, and track record to permit it to resolve the difficult issues being examined by this Committee and apply the law. If there are specific examples of where the ITC has erred that warrant attention, we will work with the Congress to develop consensus solutions. Nevertheless, we are generally of the view that the long term interests of our innovation economy and the public will be served if the ITC is permitted to fulfill its obligations pursuant to existing law.

At a time when policymakers rightly argue that other countries need to do more to clamp down on IP infringement overseas, it is unwise to impose new hurdles on U.S. IP owners trying to protect their IP rights against foreign infringers.

Tessera and the Innovation Alliance thank the Subcommittee for affording us the opportunity to provide our views. We stand ready to work with the Congress on consensus proposals to enhance the rights of patent owners and improve the operation of our courts and the ITC.