

EXPERT ANALYSIS

'Reverse' Patent Trolling: Nontraditional Participants in the Inter Partes Review Process

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So-called patent trolls are popular villains in the intellectual property world. Likened to the fairytale monsters that hide under bridges, only to jump out and demand a toll from those who wish to cross, trolls have ignited a seldom-seen public fascination with the patent system.¹

Generally speaking, patent trolls — also called “non-practicing entities” or “patent assertion entities” — are firms that do not make or sell products of their own but instead acquire and enforce patent rights against those who do.

Legal scholars have described the troll dilemma as a matter of economic holdup: An industry participant makes a substantial, fixed investment in developing a product and bringing it to market, only to be surprised after the fact with a demand for licensing fees from a patent holder it did not know existed.²

The resulting payments have been called a “tax on innovation.”³

Congress had trolls in mind when drafting the Leahy-Smith America Invents Act, the 2011 legislative overhaul of the U.S. patent system.

In addition to other sweeping changes, the act replaced a struggling “inter partes re-examination” system with the new “inter partes review” system — an adversarial, trial-like procedure for challenging a patent’s validity before the Patent and Trademark Office, or PTO.

Many hoped IPRs — envisioned as a faster and cheaper alternative to district court litigation — would provide an efficient way for innovative companies to fight back against trolls.

By statute, anyone “who is not the owner of a patent” can file a petition seeking to invalidate it with the Patent Trial and Appeal Board under 35 U.S.C.A. § 311(a).

Regulations impose some additional limitations, such as the rule, codified in 37 C.F.R. § 42.101, that bars a defendant facing infringement claims in court from initiating an IPR on the same patent more than a year after being served with the complaint.

But IPR filers do not face any threshold barriers nearly as high as the “case or controversy requirement” of Article III of the U.S. Constitution, which governs who has standing to sue in court.

UNEXPECTED CONSEQUENCES

The lack of a standing requirement, combined with the relatively high rate at which the PTO invalidates patents, has spawned a new, unanticipated phenomenon that turns the patent troll model on its head.

Rather than acquiring and asserting their patents on products they did not develop, legal entities are now regularly threatening to challenge, and then challenging, the validity of patents held by major corporations, including those in the pharmaceutical industry.

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This recent trend has been called reverse patent trolling — “reverse” because the non-practicing entity, instead of asserting its own idle patents, is threatening to file IPR petitions *against* patent owners.

Knowing that patent rights are often critical to a company’s value, so-called reverse trolls operate in one of two general ways.

One approach is to contact their targets with draft petitions before filing, hoping to extract quick, quiet payments in exchange for keeping an IPR petition off the docket, especially if a patent holder has a recent infringement or settlement award to protect.

A second approach takes short positions in the stock of potential targets before filing a petition, hoping a serious patent challenge will cause the company’s stock value to plummet.

Even though only a small percentage of IPRs filed to date concern the pharmaceutical industry, the importance of patent protection to the value of branded drug companies has made them an attractive target for reverse trolling behavior.

REVERSE TROLLING FOR A PAYOFF

In some cases, reverse trolls represent themselves in demand letters as part of the generic pharmaceutical market.

In January 2016, for example, a company called Frontier Therapeutics sent Medac Pharma a letter enclosing a draft IPR petition for Medac’s U.S. Patent No. 8,664,231. The patent is listed in the FDA’s “Orange Book” of pharmaceutical patents as protecting Rasuvo (methotrexate), Medac’s injectable psoriasis treatment.

Frontier’s letter stated the company would “approach its development partners to prepare and file an abbreviated new drug application, or ANDA, for Rasuvo” as soon as the patent board acted on an enclosed petition, which it would file unless Medac agreed to a settlement.⁴

Medac declined to negotiate, and Frontier filed the petition.

In preliminary filings, Medac pointed out several facts suggesting that Frontier was, in truth, unlikely to seek FDA approval.⁵

Frontier was “a limited liability company established about two months before it filed th[e] IPR,” Medac said, whose place of business is a private residence in Washington state.

“Neither [the homeowner] nor any of his companies has apparently ever brought a drug to the market or licensed a third party to do so,” the drugmaker wrote.⁶

Medac also noted that Frontier had not bothered to write its own petition, instead submitting a virtual facsimile of a petition filed by an earlier challenger. The company accused Frontier of being “a reverse patent troll looking for a payoff.”⁷

Unfazed, the patent board nevertheless instituted trial.⁸

Allergan Inc. received a similar letter from Ferrum Ferro Capital in March 2015, claiming Ferrum was prepared to seek FDA approval for a generic version of Allergan’s glaucoma drug Combigan (brimonidine tartrate/timolol maleate).

The letter proposed the generic name Combivious, a clear play on Combigan and “obvious.” Ferrum enclosed a copy of an IPR petition it had filed that same day.

In later proceedings Allergan would claim Ferrum “ha[d] no principal place of business” beyond a “mail drop box” and had not hired any personnel or financed any research into developing a generic version of Combigan.⁹

The patent board declined to institute trial, but not because it found that Ferrum was a troll.¹⁰

HEDGE FUNDS GET IN THE GAME

Other reverse patent trolls show no interest in holding themselves out as generics.

Hedge funds, for instance, have jumped head-first into the IPR game. The best-known player is Kyle Bass, a fund manager who challenges pharmaceutical patents through his Coalition for Affordable Drugs.

Bass claims to have the altruistic goal of driving down prescription drug prices by invalidating “spurious” patents. But he has also candidly acknowledged his strategy for turning a profit while embarking on this “crusade.”

Before filing an IPR, Bass shorts the stock of the drug company that owns the patent he plans to challenge. He also may take positive positions in companies that would benefit if the patent were invalidated.¹¹

The results so far have been mixed, both legally and financially.

As of press time, PTO records show his Coalition has filed for 33 IPRs, including 18 that ultimately went to Patent Board trials and 15 petitions the board denied outright.

Of those 18 instituted trials, seven have yielded a final written decision, and six invalidated all the challenged patent claims.

One IPR target, Acorda Therapeutics, suffered a drop in value that appears to have been the result of a successful short. Other targets underwent changes in valuation that are difficult to attribute to Bass’ action alone.¹²

UNSUCCESSFUL RESPONSES

How can companies targeted by reverse trolls fight back?

They have made little headway in the courts or through the PTO. One of Kyle Bass’ targets filed a motion with the patent board alleging an abuse of the IPR process and seeking sanctions.

The board denied the motion, pointedly noting that “[p]rofit is at the heart of nearly every patent and nearly every *inter partes* review.”¹³

Allergan sued Ferrum Ferro in the U.S. District Court for the Central District of California, alleging extortion and unfair business practices. The court dismissed the complaint for lack of subject matter jurisdiction.¹⁴

And finally, Chinook Licensing, itself a non-practicing entity in the high-tech industry, filed a complaint for tortious interference and racketeering in response to a reverse troll’s IPR threat. Chinook’s complaint was likewise dismissed.¹⁵

With courts refusing to jump into the fray, targets of reverse trolling ultimately must look to legislatures for potential fixes.

In the interim, what are some of the considerations patent holders should take into account if they find themselves on the wrong side of a reverse-trolling shakedown?

TROLLS HAVE THE LEVERAGE

Where a valuable patent is threatened, it may be tempting to pay some amount of money to prevent an IPR challenge since the amounts involved are often far smaller than what the patent owner stands to lose.

While that reaction is understandable, there is considerable downside to giving in to the demands of reverse patent trolls.

To begin with, since there is no standing requirement to file an IPR, there is a potentially unlimited universe of possible petitioners. Any one of them is eligible to file an IPR on the very same patent, and feeding the trolls may only encourage more of them to come forward.

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The same troll, emboldened by the payoff, could even return to challenge other patents held by the same company, restarting the whole process from scratch.

Patent owners considering preemptive settlements should have their eyes wide open to the fact that they are unlikely to bring eternal peace.

Another piece of leverage reverse trolls can bring to bear stems from the patent board's expansive joinder rules if it institutes an IPR trial.

For instance, the board can, under 35 U.S.C.A. § 315 and 37 C.F.R. § 42.122(b), join any party that files an IPR petition within a month of its decision to institute trial.

That rule gives companies facing patent infringement claims in court an end run around the one-year time bar for filing an IPR petition concerning the same patent: If another party files a petition upon which the patent board institutes trial, the time-barred can file an IPR seeking to join the first proceeding no matter how long it was filed after the lawsuit.

Drug companies facing threats from a reverse troll should bear in mind that a newly filed petition could open the door to otherwise time-barred parties who may have greater incentives and resources to litigate than the initial troll, many of whom may be actual competitors of the patent owner.

Smart reverse trolls know their IPR petitions could give traditional drug companies another bite at the apple, and they may use that potential scenario as leverage.

CONCLUSION

At the end of the day, reverse trolls are an unanticipated and undesirable consequence of the new IPR regime, but any move to limit their activities will likely require legislation.

In the meantime, any company on the receiving end of a demand letter from a reverse troll must carefully assess the value of the property at stake and the strength of the challenger at hand.

It will often be a close call whether a reverse troll's targets are better off fighting the merits before the PTO or trying to avoid an IPR in the first place.

NOTES

¹ Mark A. Lemley, *Are Universities Patent Trolls?* 18 FORDHAM INTELL. PROP. MEDIA & ENT. L.J. 611, 613 n.2 (2008); This American Life: When Patents Attack! (originally aired July 22, 2011), transcript available at <http://bit.ly/2m8pJGE>.

² Tun-Jen Chiang, *Trolls & Orphans*, 96 B.U. L. REV. 691, 694–702 (2016).

³ James Bessen & Michael J. Meurer, *The Direct Costs from NPE Disputes*, 99 CORNELL L. REV. 387, 417 (2014).

⁴ *Frontier Therapeutics LLC v. Medac Gesellschaft Für Klinische Spezialpräparate MBH*, No. IPR2016-649 (PTAB Feb. 22, 2016) (Ex. No. 2001).

⁵ *Frontier Therapeutics LLC v. Medac Gesellschaft Für Klinische Spezialpräparate MBH*, No. IPR2016-649 (PTAB June 2, 2016) (Paper 9).

⁶ *Id.*

⁷ *Id.*

⁸ *Frontier Therapeutics LLC v. Medac Gesellschaft Für Klinische Spezialpräparate MBH*, No. IPR2016-649 (PTAB Sept. 1, 2016) (Paper 10).

⁹ *Allergan Inc. v. Ferrum Ferro Capital LLC*, No. 15-cv-992, complaint filed (C.D. Cal. June 19, 2016).

¹⁰ *Ferrum Ferro Capital LLC v. Allergan Sales LLC*, No. IPR2015-858 (PTAB Sept. 21, 2015) (Paper 10), 2015 WL 5608290 at *7.

¹¹ Joseph Walker & Rob Copeland, *New Hedge Fund Strategy: Dispute the Patent, Short the Stock*, WALL ST. J., Apr. 7, 2015, available at <http://on.wsj.com/1GJSjDE>; CNBC Exclusive: CNBC Transcript: Hayman Capital Management Founder Kyle Bass Speaks with CNBC's David Faber on "Squawk on the Street" Today, CNBC, Sept. 15, 2015, available at <http://cnb.cx/2lrnu1v>.

¹² Christopher Edward Neill, Note, *The Drug Short: A New Mechanism for Creating Financial Incentives for the Discovery of Invalid Pharmaceutical Patents*, 23 J. INTELL. PROP. L. 329, 343–44 (2016).

¹³ *Coal. for Affordable Drugs VI v. Celgene Corp.*, IPR Nos. 2015-1092, 2015-1096, 2015-1102, 2015-1103 and 2015-1169 (PTAB Sept. 25, 2015) (Paper 19).

¹⁴ *Allergan Inc. v. Ferrum Ferro Capital LLC et al.*, No. 15-cv-992, 2015 WL 12670417 (C.D. Cal. Dec. 28, 2015).

¹⁵ *Chinook Licensing DE v. RozMed LLC*, No. 14-cv-598, order issued (D. Del. June 13, 2014); *Chinook Licensing DE v. RozMed LLC*, No. 14-cv-598, order issued (D. Del. Dec. 18, 2014).



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