Non-practicing Complainants at the ITC: Domestic Industry or Not?

Wei Wang
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Wei Wang†

A imports smartphones and tablet PCs into the United States. B holds intellectual property rights that cover those widgets, but B does not produce any widgets domestically. Should our patent law and international trade regime always, never, or sometimes allow B to stop importation of those widgets by A? This is the question facing the International Trade Commission (“ITC” or “Commission”) more and more often, as non-practicing complainants like B file for investigations by the Commission requesting that very remedy.¹ Moreover, in order to access the ITC forum, an IP owner must satisfy a threshold requirement of demonstrating the existence of a “domestic industry” in the United States.² And non-practicing IP owners now frequently assert “domestic industry” based on the “licensing” activity language in § 337(a)(3)(C) of the Tariff Act of 1930 (19 U.S.C. § 1337).³ In response, the Commission appears to have sought to heighten the requirements for establishing licensing-based domestic industry in its Coaxial Cable⁴ and Multimedia Display⁵ opinions. The Commission made notable refinements to its previous rules regarding (1) the use of prior litigation activity as evidence to establish domestic industry; (2) allocation of portfolio licensing investment to the patents in suit; and (3) treatment of royalty payments.⁶

Current ITC precedent requires that a non-practicing patent owner seeking to access the ITC based on licensing activity demonstrate that (1) it “has made a substantial investment in its licensing program and (2) there is a sufficient nexus between the patent at issue and the alleged domestic

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1. See discussion infra Section I.C.2.
3. See discussion infra Section I.C.
6. See discussion infra Section III.
licensing industry.” The realities of licensing practice in technology-dominated industries, however, mean that meeting these seemingly innocuous requirements is anything but straightforward. For example, if B, in our example above, obtained a licensing agreement through settlement in a prior litigation with C, can the expenses associated with the litigation be used as evidence of a domestic industry when B files a complaint against A?8 Another complication relates to portfolio licensing practice: if the patents in suit belong to a portfolio, can the complainant use the licensing expenses directed towards the entire portfolio as evidence to demonstrate the existence of domestic industry of the asserted patents?9 Yet another issue concerns the Commission’s treatment of royalty payments: should the Commission treat royalty payments as a necessary condition to establish “substantial investment” in licensing?10 As shown in Sections III–IV, infra, in light of the rising number of complaints filed by non-practicing complainants asserting licensing-based domestic industry, the Commission sought to clarify and refine the rules governing these issues with its two latest decisions.

In Coaxial Cable, the Commission held that “patent infringement litigation activities taken alone” do not satisfy the domestic industry requirement and established the “clear link test,” which requires the showing of a “clear link” between prior litigation activity and licensing the patents in suit.11

In Multimedia Display, the Commission held that if a complainant's licensing activity is only partially related to licensing the patents in suit, as in the case of portfolio licensing, the Commission will require the complainant to show a strong nexus between the activity and licensing the asserted patents in the United States (“strong nexus test”).12 As to royalty payments,

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8. See, e.g., Staff Petition for Review at 1, Light Emitting Diodes II, USITC Inv. No 337-TA-640 (May 19, 2009) (granting the complainant’s motion for summary determination that a domestic industry existed based primarily on prior litigation expenses).
9. See, e.g., Certain Semiconductor Chips with Minimized Chip Package Size (Semiconductor Chips II), USITC Inv. No. 337-TA-630, Initial Determination at 7–8 (Sept. 16, 2008) (finding the existence of domestic industry based on licensing expenses of the entire patent portfolio that included the patents in suit).
10. See, e.g., Certain Stringed Musical Instruments (Stringed Musical Instruments), USITC Inv. No. 337-TA-586, Initial Determination on Violation at 19 (Dec. 3, 2007) (holding that complainant failed to establish domestic industry through licensing as the complainant's licensing efforts had not resulted in any license agreement or royalty payment).
the Commission clarified that while “royalties received by a complainant can be circumstantial evidence that an investment was made, they do not constitute the investment itself,” an approach quite contrary to some of the Commission’s own precedents.

Most notably, in Multimedia Display, the Commission distinguished between what it called production-driven licensing activity (activity that “encourages adoption and use of the patented technology to create new products and/or industries”) and revenue-driven licensing activity (activity that “takes advantage of the patent right solely to derive revenue by targeting existing production”). For the first time, the Commission held that “[a]lthough our statute requires us to consider all licensing activities, we give [the complainant’s] revenue-driven licensing activities less weight.”

This Note analyzes how these latest changes to the domestic industry requirement will impact non-practicing complainants at the ITC. Part I gives a brief overview of ITC litigation and recounts the trend of the rising number of ITC complaints filed by non-practicing complainants based on licensing activity under § 337(a)(3)(C). Part II explores the characteristics of five common types of non-practicing complainants at the ITC: (1) research and development entities or “idea shops,” (2) independent inventors, (3) startups, (4) patent assertion entities (“PAEs”), and (5) practicing companies with an offensive patenting strategy. It will focus on these entities’ business practice related to “engineering, research and development, or licensing,” as well as litigation. Part III reviews the evolution and latest developments of the requirements for establishing domestic industry at the ITC based on licensing activity. Part IV then applies these latest developments to the various types of non-practicing complainants, finding that the “clear link” and “strong nexus” tests and the refinement to the treatment of royalty payments will affect different non-practicing complainants with varying degrees of impact. Part V evaluates the likely impact of these latest developments on non-practicing complainants; finds that not all of them are consistent with public policy; and proposes possible alternatives that hopefully are better aligned with public policy considerations. In particular, this Note concludes that the Commission should (1) develop a “pattern of licensing” test instead of requiring a “clear link,” (2) emphasize intrinsic

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13. Id. at 24 (emphasis added).
14. See discussion infra Section III.D.
16. Id.
17. Id. (emphasis added).
technological characteristics of a patent portfolio in determining the existence of “strong nexus” between portfolio licensing expense and the patents in suit, (3) view royalty payments and cross-licenses as telling indicators of “substantial investment,” and (4) evaluate the production/revenue-driven dichotomy by focusing on the overall effect of a complainant’s licensing activities.

I. RISE IN ITC CASES BROUGHT BY NON-PRACTICING COMPLAINANTS

A. BRIEF OVERVIEW OF ITC LITIGATION

The ITC is an independent, quasi-judicial federal agency of the United States with trade expertise.\(^{19}\) It has the authority to issue remedies against certain “unfair trade practices,” such as patent infringement,\(^{20}\) under § 337.\(^{21}\)

Through an ITC investigation, intellectual property (“IP”) owners have an avenue outside of the federal court system to defend their exclusive rights and stop infringing imports from entering the United States.\(^{22}\) Parties involved in a § 337 investigation generally include: complainants, who file complaints at the ITC asking the Commission to initiate an investigation; respondents, who take the place of defendants in the federal courts; administrative law judges (“ALJs”),\(^{23}\) who control the fact-finding trial phase of the investigation and issue an initial determination (“ID”); the Office of Unfair Import Investigations (“OUII”) and its staff attorneys,\(^{24}\) who look out for the public interest as an unbiased third party;\(^{25}\) and the six Commissioners, who upon the parties’ request for review, may vote to “review the ID and affirm, modify, set aside or remand it in whole or in


\(^{21}\) “Section 337” is commonly used to refer to 19 U.S.C. § 1337, which codifies § 337 of the Tariff Act of 1930. Id. at 94 n.8.

\(^{22}\) Id. at 96.

\(^{23}\) See 19 C.F.R. § 210.3 (2012).


\(^{25}\) Czebiniak, supra note 20, at 97.
The Court of Appeals for the Federal Circuit may review the ITC’s final determination.\textsuperscript{27}

The ITC cannot award monetary damages under § 337\textsuperscript{28}, instead, it may issue what is called an “exclusion order” to deny entry of certain goods into the United States.\textsuperscript{29} There are two types of exclusion orders: the limited exclusion order, which applies only to those parties noticed as respondents to a particular complaint, and the general exclusion order, which applies to all goods of a certain description regardless of the importer’s identity.\textsuperscript{30} A limited exclusion order is the default remedy, whereas the general exclusion order requires a higher showing of the scope of the potential harm.\textsuperscript{31} ITC exclusion orders are enforced at the border by U.S. Customs and Borders Protection.\textsuperscript{32}

In an ITC action based on patent infringement, the Commission will issue an exclusion order upon a finding of infringement, unless the Commission finds that the infringing articles should not be excluded from entering the United States after considering the effect of such exclusion on “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.”\textsuperscript{33} Exclusion orders will bar importation of infringing products into the United States, thereby removing the infringing products from the U.S. market. In this sense, an exclusion order has the same effect as injunctive relief obtained by a plaintiff in a district court action.

\section*{B. Expanding § 337’s Protection to Licensing-Based Industry}

\subsection*{1. The Historical Domestic Industry Requirement}

The core task of the ITC is to shield domestic industry from unfair trade practices that may undercut and hurt such industry.\textsuperscript{34} Thus an IP owner seeking an exclusion order from the ITC must satisfy a threshold requirement of demonstrating the existence of a “domestic industry” in the
United States. This is similar to obtaining standing at the federal courts. Prior to 1988, in order for a domestic industry to exist, a “patent must be exploited by production in the United States . . . [and] where unfair methods and acts have resulted in conceivable losses of sales, a tendency to substantially injure such industry has been established.” The type of exploitation activities include “manufacture or production or serving of the patented item . . . .”

Historically, in every investigation the Commission applied a two-prong test to determine whether a § 337 complainant satisfied the domestic industry requirement. The test consisted of a technical prong and an economic prong. The technical prong requires that the complainant’s activities relate to articles that practice the patented invention. The economic prong measures the investment that the complainant has made in the United States for exploiting the patents in suit. But significant changes to the language of § 337 in 1988 required a modification of this test.

2. The Gremlins Case Triggered the 1988 Amendment to § 337

In the Gremlins case, Warner Brothers filed a copyright-based § 337 complaint against unlicensed entities that imported articles depicting characters from the movie “Gremlins.” Warner Brothers had an established division dedicated to the licensing program, and it had successfully licensed its copyrights to domestic producers of similar articles. However, the ITC determined that Warner Brothers had not established a domestic industry in part because licensing activities did not constitute an industry. The Commission further held that Warner Brothers’ licensees’ production of articles that reproduced the copyrighted image could not satisfy domestic

35. Id. at 108.
40. Id.
42. Czebiniak, supra note 20, at 110.
44. Id. at 9.
45. Id. at 7–11.
industry either, because such production was done overseas. The Commission thus determined that no violation of § 337 had occurred.

Congress was disappointed with the Commission’s decision in *Gremlins*, which drove Congress to amend § 337 to extend the statute’s protection to IP owners who engaged in activities such as licensing or research and development, but not actual production of the covered article. In introducing the bill, Representative Kastenmeier explained why § 337 should be reworked to include licensing-based domestic industry: “Such a change will enable universities and small businesses who do not have the capital to actually make the goods in the United States to still have access to the ITC forum for the protection of their rights.”

Subsequently, in 1988 Congress added subsection (C) to the domestic industry requirement under § 337:

>[A]n industry in the United States shall be considered to exist if there is in the United States, with respect to the articles protected by the patent, copyright, trademark, mask work, or design concerned—

(A) significant investment in plant and equipment;

(B) significant employment of labor or capital; or

(C) *substantial investment* in its *exploitation*, including engineering, research and development, or *licensing*.

Thus the amendment opened the ITC forum to both traditional entities that invest in plant and equipment or employ labor and capital in the United States, as well as entities with little or no traditional investment but that engage in commercializing their intellectual property through licensing or research and development.52

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46. *Id.* at 14–15.
47. See, e.g., 132 CONG. REC. 7119 (1986) (statement of Rep. Robert Kastenmeier). Representative Kastenmeier sought to “avoid unfortunate results which have occurred in some recent cases, such as *Gremlins*” through amendments to § 337(a). *Id.*
48. *Id.*
50. *Id.* § 1337(a)(3)(A).
51. *Id.* § 1337(a)(3)(B).
52. *Id.* § 1337(a)(3)(C).
3. Elimination of the Technical Prong Requirement for Licensing-based Domestic Industry

As discussed in Section I.B.1, supra, complainants seeking to access the ITC traditionally needed to satisfy both the economic prong and technical prong of the domestic industry requirement. However, entities asserting domestic industry through licensing under the amended § 337(a)(3)(C) often do not have an article that practices the patented invention, and so the Commission decided that the traditional technical prong of the domestic industry requirement does not apply to those entities. This means that the complainant is not required to show that it or its licensees practice the patent in suit.

Instead, the Commission employs a “simpler test” to determine whether a complainant has established a domestic industry under subsection (C). A complainant asserting § 337(a)(3)(C) needs to satisfy only the economic prong of the domestic industry requirement by demonstrating that (1) it “has made a substantial investment in its licensing program and (2) there is a sufficient nexus between the patent at issue and the alleged domestic licensing industry.” It is this simpler test that comes into play when a non-practicing complainant seeks an ITC investigation of allegedly infringing imports.

C. RELIANCE OF NON-PRACTICING ITC COMPLAINANTS ON LICENSING

In recent years, and particularly following the U.S. Supreme Court’s eBay v. MercExchange57 decision, non-practicing complainants have increasingly turned to the ITC in their efforts to obtain injunctive relief against infringers.58 These complainants often rely on their licensing activities under subsection (C) to satisfy the domestic industry requirement.59 This Section briefly explores the possible driving force behind the trend of increasing non-practicing complainants at the ITC.

55. See Certain Light Emitting Diodes & Prods. Containing Same (Light Emitting Diodes I), USITC Inv. No. 337-TA-512, Initial Determination at 134 (May 10, 2005) (“[T]he domestic industry analysis under criterion (C) subsumes within it a technical-prong aspect.”).
58. See discussion infra Section I.C.2.
59. See discussion infra Section I.C.2.
1. The ITC Does Not Follow eBay

The U.S. Supreme Court’s decision in eBay is widely regarded to have limited the ability of non-practicing entities (“NPEs”) to secure an injunction in a federal district court. In eBay, the Court held that district courts must apply the traditional four-factor test in determining whether to issue injunctive relief in patent infringement suits, upon a finding of infringement and validity. Of the four factors, the requirement that a plaintiff demonstrate “irreparable injury” has proved most detrimental to NPEs’ ability to secure an injunction. This is because an NPE is usually unable to demonstrate a loss of market share for patented goods or services since they do not produce or provide those goods or services—the existence of such a market is often a crucial piece of evidence for showing irreparable injury. However, the Commission refused to adopt the eBay four-factor test in deciding whether to issue an exclusion order—which acts like an injunctive remedy—at the ITC, a position that the Federal Circuit later affirmed in Spansion, Inc. v. International Trade Commission. As shown in Section I.C.2, infra, this effectively makes the ITC a more favorable forum for NPEs who seek injunctive relief.

In Spansion, Tessera Inc. filed a complaint with the ITC against seven respondents who allegedly imported or sold semiconductor chips that infringed Tessera’s patents on chip packaging. After a finding of infringement, respondent Spansion urged the Commission to consider the eBay factors before issuing an exclusion order. Specifically, they urged the Commission to consider that “Tessera is simply a licensor and does not actually practice the invention” and to conclude that there was no irreparable harm and that an injunction was inappropriate under eBay. The

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61. eBay, 547 U.S. at 394.

62. See Paice LLC v. Toyota Motor Corp., No. 2:04-CV-211-DF, 2006 WL 2385139, at *3–5 (E.D. Tex. Aug. 16, 2006) (finding no irreparable harm because Paice LLC failed to demonstrate that Toyota’s infringing activity caused the failure of its licensing practices, since the two did not compete in the same market, with one in the market of technology licensing and the other in the market of automobile manufacturing and sales).

63. Spansion Inc. v. Int’l Trade Comm’n, 629 F.3d 1331 (Fed. Cir. 2010).

64. Id. at 1336.

65. Id. at 1357.

66. Id.

67. Id. at 1357–58.
Commission ruled that *eBay* does not apply to ITC remedy determinations.\(^{68}\) Instead, the ITC focuses entirely on the statutorily mandated public interest factors listed in § 337: “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.”\(^{69}\) Finding that none of these were implicated in the investigation, the Commission granted the exclusion order.\(^{70}\)

The Federal Circuit affirmed, recognizing that, unlike district courts’ discretionary power to grant injunctive relief, Congress intended injunctive relief to be the normal remedy for a § 337 violation, and that a showing of irreparable harm is not required to receive such injunctive relief.\(^{71}\) Moreover, “[t]he difference between exclusion orders granted under § 337 and injunctions granted under the Patent Act, 35 U.S.C. § 283, follows ‘the long-standing principle that importation is treated differently than domestic activity.””\(^{72}\)

The *Spansion* decision affirmed the different standards for granting injunctions in a district court and issuing exclusion orders at the ITC.\(^{73}\) Under these different standards, a patent owner may obtain an exclusion order from the ITC even when it may not be entitled to an injunction under *eBay*.\(^{74}\) These differences are particularly significant to non-practicing patent owners seeking injunctive relief, who may have great difficulty proving “irreparable harm” in a district court.\(^{75}\) A 2011 FTC report on the evolving IP marketplace (“FTC Report”) finds that, among post-*eBay* patentees that do not practice their patents, district courts have granted only 50% of

\(^{68}\) *Id.* at 1358.


\(^{70}\) *Spansion*, 629 F.3d at 1358.

\(^{71}\) *Id.* at 1358–59 (“Congress amended Section 337 by passing the Omnibus Trade and Competitiveness Act of 1988 . . . explicitly removing the requirement of proof of injury to the domestic industry and making it unnecessary to show irreparable harm to the patentee in the case of infringement by importation.”).

\(^{72}\) *Id.* at 1359.

\(^{73}\) *See id.* at 1358 (“Congress intended injunctive relief to be the normal remedy for a Section 337 violation and that a showing of irreparable harm is not required to receive such injunctive relief.”); *cf. eBay Inc. v. MereExchange, L.L.C.*, 547 U.S. 388, 391–92 (2006) (holding that the well-established four-factor test for permanent injunctions also applies to disputes arising under the Patent Act, including the requirement that plaintiff has suffered irreparable harm).


requested injunctions where the patentees won,\textsuperscript{76} compared with 100\% in the year prior to eBay.\textsuperscript{77} In contrast, a finding of infringement at the ITC almost always leads to an exclusion order.\textsuperscript{78} At least one study has pointed to this divergence between the ITC and the district court as a reason for the increasing popularity of the ITC among non-practicing patent owners.\textsuperscript{79}

2. Non-practicing Patentees Increasingly Turn to the ITC

After Spansion, although non-practicing patent owners arguably have a better chance of obtaining exclusion orders at the ITC than obtaining injunctive relief at the district court, they must first overcome the threshold hurdle of establishing domestic industry at the ITC, a hurdle which does not exist at the district court. Non-practicing patent owners do not practice the patents in suit and therefore lack any investments in manufacturing, either through investments in plant and equipment\textsuperscript{80} or employment of labor or capital.\textsuperscript{81} In order to satisfy the domestic industry requirement, non-practicing patent owners have frequently relied on “licensing” activity under § 337(a)(3)(C).\textsuperscript{82}

A study of § 337 complaints filed between 2000 and August 2010 shows both an increasing number and increasing percentage of ITC complaints where the complainants asserted domestic industry based on licensing.\textsuperscript{83} Although it is impossible to precisely determine the exact contribution of patentees looking to avoid the eBay analysis to the increase in ITC complaints,\textsuperscript{84} this trend has drawn close attention of academics, practitioners,

\textsuperscript{76} Fed. Trade Comm’n, The Evolving IP Marketplace: Aligning Patent Notice and Remedies with Competition 256 (2011), available at http://www.ftc.gov/os/2011/03/110307patentreport.pdf [hereinafter FTC Report] (“A longer term review of the post-eBay case law reveals that as of March 1, 2010, courts had heard thirteen requests for permanent injunctions where the opinion suggests that the patent owner is one of several types of non-practicing entities, including a university, research institute and independent inventor. Of those thirteen cases, district courts granted an injunction seven times.”).


\textsuperscript{78} FTC Report, supra note 76, at 242 n.131 (finding that “[t]he ITC has used [the public interest] provision to deny an injunction only three times . . . [where all three] cases involved issues of public health or broad public interest”).

\textsuperscript{79} Chien, supra note 74, at 172–73.


\textsuperscript{81} Id. § 1337(a)(3)(B).


\textsuperscript{83} Id. at 910.

\textsuperscript{84} FTC Report, supra note 76, at 240.
and the Federal Trade Commission,\textsuperscript{85} and serves as backdrop for the ITC’s recent opinions that appear to have sought to heighten the domestic industry requirement for licensing activity. But who, exactly, are these non-practicing ITC complainants?

II. NON-PRACTICING COMPLAINANTS AT THE ITC

This Part explores the characteristics of five types of typical non-practicing complainants at the ITC: (1) research and development entities, or “idea shops”;\textsuperscript{86} (2) independent inventors; (3) startups; (4) patent assertion entities;\textsuperscript{87} and (5) practicing companies with an offensive patenting strategy.

To clarify terminology, this Note uses the term “non-practicing complainants” to describe patent owners who file complaints at the ITC based on a patent that they do not practice. By using this term, the focus of the analysis is on the acts of the complainants regarding the specific patents in suit.\textsuperscript{88} Non-practicing complainants may include NPEs, who generally do not practice any of their patents, as well as practicing entities, who assert patents in areas where the company no longer operates or never did.\textsuperscript{89} Although generally “it is not specific entities but rather specific tactics or practices that are most relevant,”\textsuperscript{90} business models of an entity may, in many cases, dictate how entities behave in accordance with new developments of the law. Therefore in order to accurately predict how the change in the domestic industry requirement will shape the behaviors of non-practicing complainants, it is helpful to understand their various business practices, particularly those relevant to “engineering, research and development, or licensing,”\textsuperscript{91} as well as litigation activities, through which a patentee compels royalty payments from accused infringers.

\textsuperscript{85} See FTC REPORT, supra note 76, at 2, 186.


\textsuperscript{87} Colleen V. Chien, From Arms Race to Marketplace: The Complex Patent Ecosystem and Its Implications for the Patent System, 62 HASTINGS L.J. 297, 328 (2010) (“Patent-assertion entities are focused on the enforcement, rather than the active development or commercialization of their patents.”).

\textsuperscript{88} Mark A. Lemley, Are Universities Patent Trolls, 18 FORDHAM INTELL. PROP. MEDIA & ENT. L.J. 611, 630 (2008) (“Instead of singling out bad actors [trolls], we should focus on bad acts and the laws that make them possible.”).

\textsuperscript{89} See Chien, supra note 87, at 322–23 (giving examples of practicing entities who implement offensive patent strategies).

\textsuperscript{90} Merges, supra note 86, at 1610.

A. Patent Assertion Entities

Patent assertion entities are entities that focus on the enforcement, and not the active development or commercialization of their patents. They can be further divided into two categories: small portfolio companies and mass patent aggregators. Although Professor Chien also included independent inventors in the category of patent assertion entities, this Note treats independent inventors as a separate category due to the different characteristics that independent inventors exhibit with respect to their licensing activities and the complex policy considerations specifically afforded to independent inventors.

1. Small Portfolio Companies

Small portfolio companies focus their investment at identifying, acquiring, and enforcing valuable patents against existing, successful products. These entities usually selectively purchase small portfolios of patents. However, these specially-selected patents account for a substantial percentage of the most litigated patents and are arguably the most valuable patents available.

After acquiring a portfolio of valuable patents, small portfolio companies usually operate based on a litigation-first model, rather than a licensing-first model. This means that instead of engaging in genuine efforts to negotiate licensing agreements with potential licensees that may adopt the patented technology, small portfolio companies will strategically time the filing of their

92. Chien, supra note 87, at 328.
93. Id.; Robin Feldman & Tom Ewing, The Giants Among Us, 1 STAN. TECH. L. REV. (forthcoming 2012) (manuscript at 2–3) (stating that the mass patent aggregator is “an entirely different beast” than small patent assertion entities).
94. Chien, supra note 87, at 328.
95. Id. at 330; Feldman, supra note 93, at 2–3. The idea of acquiring valuable patents is based on the assumption that patents have an objective value that can be estimated from intrinsic qualities of the patent. See John R. Allison et al., Extreme Value or Trolls on Top? The Characteristics of the Most Litigated Patents, 158 U. PA. L. REV. 102, 112 (2009) (showing that “the most litigated patents differ fundamentally in virtually every respect from even the once-litigated patents,” including number of continuation applications, number of self-citations, etc.).
96. Chien, supra note 87, at 330 (“For example . . . , Las Vegas-based Synchrome Technologies has sued Samsung, Panasonic and other electronics device makers based on a portfolio of fewer than ten patents.”).
97. Allison et al., supra note 95, at 124.
98. Id. at 103 (stating that “most valuable” refers to private value, or value to the owner); see also Chien, supra note 87, at 318 (explaining that small portfolio companies’ patent portfolios “tend to have a higher proportion of ‘crown jewels’ ”).
lawsuits to occur after some companies are already committed to the
technology in their products. 100 By doing so, small portfolio companies
advantageously position themselves in court and optimize their chances of
winning the infringement claim while having little to lose. 101 For their
opponents, on the other hand, the stakes can be extremely high: a district
court judge may order them to pay a large amount of damages, or they may
risk losing access to the U.S. market once the ITC issues an exclusion order.
Over the years, small portfolio companies have been able to employ these
tactics to extract sizable royalties from unwilling licensees, either through
court-imposed royalty payments or through settlement negotiations and
agreements. 102 Saxon Innovations, LLC is an example of a small portfolio
company that has successfully brought suits at the ITC. 103


Mass patent aggregators operate similarly to small portfolio companies,
but on a much more sophisticated scale. 104 The largest mass patent
aggregators are Acacia and Intellectual Ventures ("IV"). 105 These entities
usually have deep-pocket investors, such as big technology companies and
investment banks, enabling them to purchase a large number of patents from
virtually all types of patentees. 106 For example, as recently as May 2011, IV is
estimated to have a portfolio of 30,000 to 60,000 patents and patent
applications worldwide. 107

Perhaps the most prominent characteristic of mass patent aggregators is
that they engage in a wide range of different activities. For example, IV
acquires IP rights, licenses patents for fees and equity investments, 108 and

100. Chien, supra note 87, at 319.
101. See id. at 318 ("[Patentees] that do not make products . . . are not burdened by the
need to manage investor expectations or minimize disruption to the company’s core
business.").
102. See, e.g., Rob Kelley, *BlackBerry Maker, NTP Ink $612 Million Settlement*, CNN
rimm_ntp/ (describing a patent-assertion entity that obtained $612 million in a settlement
arising from a patent infringement suit against BlackBerry).
103. See Chien, supra note 87, at 343 (stating that Saxon owns a patent portfolio of about
200 patents); see, e.g., Complaint at 1, Certain Electronic Devices, Including Handheld,
Saxon brought the suit to the ITC).
104. Feldman et al., supra note 93, at 3–4.
105. Chien, supra note 87, at 328.
107. Id. at 11.
enforces patents by litigation. In recent years, IV also opened up its own research and development division. Similarly, Acacia’s strategy is to generate revenue through licensing or litigating patents. It generally splits the revenues it receives, giving half to the inventor and retaining half for itself.

B. PRACTICING COMPANIES WITH AN OFFENSIVE PATENTING STRATEGY

Historically, practicing companies that generate revenue from product sales have implemented a defensive patenting strategy, typically by developing a large trove of patents (often through their own research and development) for cross-licensing. This strategy has the dual benefits of avoiding licensing fees and preventing competitors from blocking their products. A defensive patenting strategy affords practicing companies freedom to operate in a particular market, which furthers technological adoption. Empirical observations show that companies with a defensive IP strategy usually do not initiate lawsuits.

However, throughout the lifetime of an issued patent, practicing companies may shift their patenting strategy and use a once-defensive patent to selectively monetize and enforce their IP right in areas where they no longer or never did operate, employing the same tactics as patent-assertion entities. For instance, licensing a technology may be the most efficient way

110. See Allen W. Wang, Note, Rise of the Patent Intermediaries, 25 BERKELEY TECH. L. J. 159, 181 (2010) (explaining that some of IV’s intellectual property is developed internally, instead of being acquired from outside sources); see also Feldman & Ewing, supra note 93, at 40 (noting that IV set up an internal lab).
111. Chien, supra note 87, at 320.
113. Chien, supra note 87, at 321 (citing Cisco as an example of a high-tech company that implements a defensive patenting strategy).
114. Id.
115. Id.
116. Id. at 322.
117. See id. at 324–25. There is disagreement among scholars about the likelihood that a practicing entity with a large patent portfolio may transition from defensive accumulation to offensive patent monetization and enforcement. Compare Wang, supra note 110, at 175 (“A successful defensive aggregator with a massive portfolio would possibly have only the conscience of its leadership to prevent it from becoming an aggressive and litigious licensor and NPE [non-practicing entity] in its own right.”) with Chien, supra note 87, at 326 (“[M]aking the transition from defensive accumulation to patent monetization is neither easy nor automatic.”).
for a company to recoup its R&D expenses. Similarly, an early-stage technology may have been patented without much further development. With respect to such patents, the companies are non-practicing. When they assert such patents at the ITC, they effectively become non-practicing complainants, notwithstanding their investments in practicing other technologies unrelated to the patents in suit. As an example, Motorola Inc. recently brought a suit at the ITC asserting domestic industry based on licensing activity for a patent that it did not practice.

Practicing entities transitioning from a defensive to an offensive patenting strategy usually possess a large portfolio of patents, historically accumulated for defensive purposes. Such patent portfolios are typically of high volume, low cost, and uneven quality with respect to individual patents. In addition, such patent portfolios are often associated with a trail of cross-licensing negotiations and agreements. During cross-licensing negotiations, because of both parties’ obsession with the number of patents in the patent portfolios rather than the content of the patents, companies might sample a few typical patents in each of the portfolios, but they very rarely scrutinize each patent individually.

C. RESEARCH AND DEVELOPMENT ENTITIES

Research and development entities, or “idea shops,” are entities that develop their own technologies and then sell the innovations in “disembodied form,” rather than embedding innovation in manufactured products. This category includes universities who develop technologies in their labs and earn licensing revenues through technology-transfer offices. This category also includes companies like Rambus, which invests heavily in

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118. Chien, supra note 87, at 322.
119. Id. at 322.
120. Id. at 322 (“When they assert such patents, companies have been accused of being corporate ‘trolls.’”).
122. Chien, supra note 87, at 325 (showing stages of a company’s patent strategy which include a transition from defensive accumulation to offensive patent monetization).
123. Id. at 338 (showing that defensive patenting emphasizes “the quantity of patents, rather than the quality of any individual patent”).
124. Id. at 308 (“As general counsel of TI famously put it, ‘for [TI] to know what’s in [its patent] portfolio, we think, is just a mind-boggling, budget-busting exercise to try to figure . . . out with any degree of accuracy at all.’”).
125. Merges, supra note 86, at 1599.
126. Lemley, supra note 88, at 614 (“Patents are now a significant contributor to some university bottom lines.”).
research and development and has a revenue stream based primarily on royalty payments. The 2011 FTC Report identified technology transfer from specialized research and development entities to larger manufacturing firms as an “increasingly important pathway of open innovation.”

One type of R&D entity is the university. Universities tend to patent “on the very earliest stages of technology.” Their licensing efforts are generally directed towards technology transfer for commercialization, rather than rent-seeking.

Unlike universities, research and development companies have a more 
hybrid practice regarding their licensing activities. For example, Rambus has a well-established licensing program seeking to bring its innovations to the marketplace through technology transfer. At the same time, it enforces its patents very actively, filing strings of lawsuits at both district courts and the ITC when accused infringers refuse to take a license. Another notable characteristic of R&D companies is that they usually license a portfolio of patents covering a specific field of technology, rather than licensing individual patents. Unlike defensive patent portfolios accumulated by practicing entities that focus on quantity rather than quality of patents, the patent portfolios of R&D companies bear the primary function of enabling its licensees to practice a particular technology without worrying about

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128. FTC REPORT, supra note 76, at 37.
129. Lemley, supra note 88, at 615 (“Universities, which account for 1% of patents on average across all fields, account for 12% of all patents in nanotechnology, and more than two-thirds of . . . the basic building block patents in nanotechnology.”).
130. Chien, supra note 87, at 327 (“The standard paradigm of university technology transfer is to license patents ex ante . . . rather than to wait until a company has independently developed and commercialized an infringing product.”). But see Lemley, supra note 88, at 618 (“[U]niversities are increasingly enforcing their patents. Recent years have seen high-profile cases litigated to judgment by [universities].”).
133. See, e.g., Certain Semiconductor Chips (Semiconductor Chips III), USITC Inv. No. 337-TA-661, Order No. 21, Initial Determination at 7 (Oct. 7, 2009) (noting that Rambus licensed the Concurrent Interface Technology license portfolio and XDR Technology license portfolio, each covering a specific technology field).
further investments in new licenses. Thus an R&D company usually carefully chooses closely-related patents for its portfolio to ensure sufficient coverage of a technology field. R&D companies are also more likely than practicing entities to invest in high-quality patent prosecution in order to preserve the validity of their patents that in many cases constitute the company’s primary asset. Over the years, R&D companies such as Rambus have successfully brought multiple suits to the ITC.

D. INDEPENDENT INVENTORS

Independent inventors present a curious case at the ITC. On one hand, independent inventors seem to fall well within the group that the 1988 Amendment sought to benefit. On the other hand, independent inventors are among the most avid litigants in the patent system, often working together with contingency-fee lawyers. One scholar actually characterizes independent inventors as “trolls” when they “turn[] their focus away from the active development or practice of their patents and [move] towards patent enforcement.”

One study offers a viable explanation why independent inventors are actively engaged in patent litigation: these investors typically have developed the patents that they are asserting and are therefore more personally involved in enforcing the patents. There is, however, another explanation: independent inventors may have a difficult time convincing manufacturers to take a license and commercialize the patented technology. As a result,

137. See 132 CONG. REC. 7119 (statement of Rep. Kastenmeier) (“Such a change will enable universities and small businesses who do not have the capital to actually make the goods in the United States to still have access to the ITC forum for the protection of their rights.”) (emphasis added).
138. Allison et al., supra note 95, at 126 (showing that individual inventors or individual-inventor-started companies “account for 74.4% of the most litigated patent lawsuits”).
139. Chien, supra note 87, at 331.
140. Id. at 330.
141. Id. at 331.
142. See Peter Whalley, The Social Practice of Independent Inventing, 16 SCI. TECH. & HUM. VALUES 208, 225 (1991) (describing the mistrust between manufacturers and independent
litigation may, at times, be the only recourse for independent inventors to obtain a license and exploit the patented technology, as is likely the situation with the independent inventor in *Stringed Musical Instruments*.  

E. **Startups**

Startups are young companies that have yet to establish their operating history. Like independent inventors, startups usually have a small patent portfolio, as they are short on both time and funding for patent accumulation. However, unlike independent inventors who lack the capital to commercialize their technologies, start-ups are typically formed to pursue commercialization opportunities, usually through venture capital financing.

According to the 2008 Berkeley Patent Survey, a startup secures patents primarily to prevent others from copying the technology and to protect its first-mover advantage in the marketplace. Monetizing patents through licensing revenue is among the lowest priorities for startups.

Historically, startups have not been active patent litigants at either district courts or the ITC. However, in a recent ITC investigation, a startup company Motiva tried to gain access to the ITC and obtain an exclusion order against foreign competitors, in an effort “to be the exclusive entity with the rights to use the technology embodied by the asserted patents.”

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143. *See Stringed Musical Instruments*, USITC Inv. No. 337-TA-586, Initial Determination on Violation at 2–3, 19, 23 (Dec. 3, 2007) (stating that independent inventor failed to obtain any licensing agreements over a period of nearly 20 years despite continuous efforts to obtain licensees, whereas he secured two settlements after filing a complaint at the ITC).


145. *Id.*


147. *Id.* at 1300–01.

148. Allison et al., *supra* note 95, at 123 tbl.7 (showing startups have no part in either the “most litigated patents” or the “once-litigated patents” category).

149. *See Certain Video Game Sys. & Controllers (Video Game Systems)*, USITC Inv. No. 337-TA-743, Commission Opinion at 10 (Apr. 14, 2011) (relating that startup Motiva sued Nintendo because “Nintendo’s Wii caused all the interest in [Motiva’s] technology to fade and that litigation against Nintendo was a necessary step to establish its claim to the technology . . . in order to bring its technology to market”).
III. ESTABLISHING DOMESTIC INDUSTRY BASED ON LICENSING ACTIVITY

As mentioned in Section I.B.3, supra, a non-practicing complainant seeking to access the ITC needs to satisfy only the economic prong, and not the technical prong, of the domestic industry requirement by demonstrating (1) a substantial investment in “engineering, research and development, or licensing” and (2) that there is a “nexus” between the activities upon which it relies and the asserted patent. A complainant does not need to show that it, or one of its licensees, is practicing the patent in suit under § 337(a)(3)(C).\(^{150}\)

This Part reviews the history and the latest development of the requirements for establishing domestic industry at the ITC based on licensing activity.\(^ {151}\)

Controversies as to what kind of licensing activity is sufficient to establish domestic industry have focused on: (1) pure licensing activity; (2) enforcement/litigation activity with which a patent owner compels royalty payments from accused infringers; (3) portfolio licensing activity; (4) royalty payments; and (5) a licensee’s production-type activity.\(^ {152}\) In its two recent decisions \textit{Coaxial Cable}\(^ {153}\) and \textit{Multimedia Display},\(^ {154}\) the Commission sought to heighten the requirement for asserting domestic industry based on licensing activities. The two opinions reaffirmed that pure licensing activities alone can constitute substantial investment, whereas they made notable changes regarding the treatment of enforcement/litigation activity, portfolio licensing activity, and royalty payments.\(^ {155}\) The Commission also, for the first time, made a point of distinguishing so-called revenue-driven licensing activity from production-driven licensing activity, even though the statute does not make such a distinction.\(^ {156}\) Finally, the so-called potential “backdoor” opened by a licensee’s activity is largely left intact by the Commission’s latest movement.\(^ {157}\)

\(^{150}\) See supra Section I.B.3.

\(^{151}\) This Section includes both cases where complainants alleged satisfaction of the domestic industry requirement solely through licensing activities and cases where complainants alleged both licensing and R&D activities.

\(^{152}\) See discussion \textit{infra} Sections III.A–D, F.


\(^{156}\) \textit{Multimedia Display}, USITC Inv. No. 337-TA-694, Commission Opinion at 25.

\(^{157}\) See discussion \textit{infra} Section III.F.
A. **PURE LICENSING ACTIVITY**

Entities that engage in pure licensing activity without practicing the patented technology may satisfy the requirement for domestic industry.\(^{158}\) After the 1988 Amendment to § 337, the Commission held in *Semiconductor Chips I* that licensing activity alone could constitute “substantial investment” for purpose of establishing domestic industry under § 337(a)(3)(C).\(^{159}\) In that case, the ALJ granted complainant Tessera’s motion for summary determination on domestic industry even though Tessera’s only claim regarding domestic industry was its licensing activity and it had never practiced the technology in suit.\(^{160}\) The exact number of licenses and employees involved and the amount of the royalty payments made were redacted in the public version of the order. However, the order did state that Tessera licensed the patents in suit to several companies, employed internal licensing and contract attorneys to negotiate and draft licenses related to the technology at issue, incurred cost of licensing, and negotiated with most of the semiconductor manufacturers in the world.\(^{161}\) The Commission found that all of these activities were relevant evidence for satisfying the domestic industry requirement.\(^{162}\) Nothing in *Coaxial Cable* and *Multimedia Display* indicates that the Commission intends to change this rule regarding pure licensing activity.

B. **LITIGATION EXPENSES**

Prior to *Coaxial Cable* the Commission never explicitly excluded litigation expenses through which an entity compels royalty payments, from the consideration of “substantial investment” under § 337(a)(3)(C). For example, in *Light Emitting Diodes II*, the ALJ granted the complainant’s motion for summary determination that a domestic industry existed based primarily on the complainant’s enforcement/litigation activity.\(^{163}\) In reaching its conclusion, the ALJ gave great weight to the multiple licenses that the complainant had managed to obtain through a series of prior district court


\(^{159}\) See *id.* at 12–13.

\(^{160}\) *Id.* at 5, 15.

\(^{161}\) *Id.* at 7–9, 14.

\(^{162}\) *Id.* at 14–15.

\(^{163}\) Staff Petition for Review at 1, *Light Emitting Diodes II*, USITC Inv. No. 337-TA-640 (May 19, 2009) (“Complainant’s legal expenses . . . primarily consist of fees paid to outside counsel to bring infringement suits, coupled with royalty income received as a result of such litigation.”).
litigations. Although the Commission issued a notice of review for the ALJ's initial determination, the investigation was terminated as a result of settlement before the Commission could issue its opinion.

*Coaxial Cable* specifically addressed the extent to which a complainant could satisfy the domestic industry requirement by relying on its prior litigation activity for enforcing the patent in suit. In *Coaxial Cable*, the complainant PPC had been involved in multiple district court lawsuits and had only obtained one license at the conclusion of one of its litigations. PPC contended that the money it had spent during the years of litigation leading up to the eventual license should be treated as an investment in licensing.

The Commission disagreed. It held that “patent infringement litigation activities *taken alone*” do not satisfy the domestic industry requirement, and “[a]llowing patent infringement litigation activities alone to constitute a domestic industry would place the bar for establishing a domestic industry so low as to effectively render it meaningless.” However, instead of establishing a categorical rule excluding litigation expenses as evidence to meet the domestic industry requirement, the Commission set forth a test that requires a “clear link” between each litigation activity and the licensing efforts regarding a particular patent in suit (“clear link” test). Such activities may include “drafting and sending cease and desist letters, filing and conducting a patent infringement litigation, conducting settlement negotiations, and negotiating, drafting, and executing a license.” And only activities that occur before filing of an ITC complaint are relevant to whether a domestic industry exists under §337(a)(3).

The Federal Circuit affirmed. “[R]ecogniz[ing] that the Commission is fundamentally a trade forum, not an intellectual property forum,” the Federal

164. *Id.* at 10.
167. *Id.*
169. *Id.* at 45–46 (emphasis added).
170. *Id.* at 50–51 (“A complainant must clearly link each activity to licensing efforts concerning the asserted patent.”).
171. *Id.* at 50.
172. *Id.* at 51 n.17 (emphasis added).
Circuit concluded that only intellectual property owners who actively engage in exploitation of the intellectual property should have access to the ITC. As such, the majority agreed with the Commission that patent litigation expenditures “do not automatically constitute evidence of the existence of [domestic industry] . . . .”175 Even if a lawsuit eventually leads up to a license agreement between the litigation adversaries, not all litigation expenses may be attributed to licensing effort.176 The complainant must also establish that its litigation activities are “directed toward” licensing the specific patent in suit.177

Applying the rule to the facts of the investigation, the Federal Circuit held that the complainant PPC in *Coaxial Cable* failed to satisfy the economic prong of the domestic industry requirement.178 With respect to one of the litigations eventually leading up to the license agreement, which PPC relied on principally, the Federal Circuit emphasized the ALJ’s finding “that there was no evidence that PPC had offered to license the patent . . . before commencing litigation, no evidence that PPC had sent a cease and desist letter mentioning the possibility of a settlement, and no evidence that PPC had conducted either settlement or licensing negotiations during the lawsuit itself.”179 The two-year delay from the date PPC obtained a favorable jury verdict until the date PPC licensed the patent in suit to its litigation opponent suggested that PPC’s purpose in litigation was not to obtain a license, but to stop its opponent from manufacturing the infringing products.180 PPC’s lack of a formal licensing program also cut against finding “substantial investment” in licensing.181 Furthermore, the court found that the ALJ was correct in disregarding PPC’s statement that industry members were “generally reluctant to accept a license” until the patentee obtained a favorable jury verdict, as it merely reflected “the state of mind of competitors.”182

174. *Id.* at 1328 (citing H.R. REP. NO. 100-40, at 157 (1987)).
175. *Id.*
176. *Id.* at 1329.
177. *Id.* (“The administrative law judge . . . examined PPC’s legal bills in all three cases and credited entries that had a work description related to ‘licensing’ or ‘settlement’ toward PPC’s investment in licensing.”).
178. *See id.* at 1331.
179. *Id.* at 1325, 1328.
180. *Id.* at 1329.
181. *Id.* at 1330.
182. *Id.* at 1328.
C. PORTFOLIO LICENSING

Historically, when a complainant directed its licensing efforts toward a patent portfolio instead of specific patents in suit, the Commission took into consideration the entire amount of portfolio licensing expenses so long as the portfolio included the patents in suit. For example, in *Semiconductor Chips II*, the ALJ granted complainant Tessera’s motion for summary determination that it had satisfied the domestic industry requirement based on licensing.183 There, the three patents in suit were part of Tessera’s TCC technology license portfolio.184 In response to the respondents’ conclusion “that Tessera has failed to show that the licensing revenues generated from TCC technology licensing portfolio . . . [were] specifically related to the patents in suit,”185 the ALJ held that a “nexus” existed between Tessera’s portfolio licensing activities and the patents in suit, when the patents in suit were “part of the TCC technology license portfolio.”186 Accordingly, the ALJ rejected respondents’ argument that Tessera must segregate the amount of licensing revenues attributable to the asserted patents.187

In contrast, the Commission made it clear in *Multimedia Display* that the mere fact that a patent portfolio includes the patents in suit is not enough to justify taking into consideration the entire portfolio licensing expense.188 In *Multimedia Display*, the complainant, Pioneer Corporation (“Pioneer”), filed a complaint against Honeywell International Inc. and Garmin, asserting three patents based on licensing activity that were part of a large patent portfolio.189

The Commission reversed the ALJ’s finding that the economic prong of the domestic industry requirement was satisfied for the asserted patents,190 holding that “if a complaintant’s activity is only partially related to licensing the asserted patent,” as in the case of portfolio licensing, the complainant must show a strong nexus between the activity and licensing the asserted patents in the United States (“strong nexus test”).191 A complainant may be

184. Id. at 7.
185. Id. at 6.
186. Id. at 8.
187. Id. at 7.
189. Id. at 5.
190. Id. at 1.
191. Id. at 8, 25.
able to establish a strong nexus between licensing the portfolio and licensing the asserted patents by showing that its portfolio licensing activities are “particularly focused on the asserted patent among the group of patents in the portfolio or through other evidence that demonstrates the relative importance or value of the asserted patent within the portfolio.”

Applying the “strong nexus” test to the facts of the case, the Commission found only “an attenuated nexus between Pioneer’s in-house activities and the asserted patents” because, although the licenses covered the patents in suit and therefore had some link to the patents, Pioneer’s in-house activities were largely directed toward the entire navigation technology portfolio, without expressly identifying the asserted patents. Furthermore, Pioneer presented no evidence of “how the asserted patents fit together congruently with the other patents in the portfolio,” when the technological scope of its navigation portfolio was broad compared to the narrow focus of the asserted patents.

The Commission found a “relatively strong” nexus between Pioneer’s outside counsel activities and the asserted patents, because the outside counsel activities, as shown in Pioneer’s invoices, appeared to be related to products incorporating the patented technology. However, the Commission found that Pioneer’s expenses in licensing the asserted patents through outside counsel was “significantly less” than its total outside counsel expenses, as some outside counsel activities were directed towards litigation. In conclusion, the Commission decided that Pioneer failed to satisfy the “strong nexus” requirement and therefore could not assert the entire amount of portfolio licensing expenses as evidence of “substantial investment,” even though the portfolio included the patents in suit.

192. Id. at 9. Several factors are relevant in assessing the strength of the nexus between a complainant’s portfolio licensing activities and licensing asserted patents: (1) “Whether the licensee’s efforts relate to an article protected by the asserted patent under section 337(a)(2)–(3);” (2) “The number of patents in the portfolio” (“All things being equal, the nexus between licensing activities and an asserted patent may be stronger when the asserted patent is among a relatively small group of licensed patents”); (3) “The relative value contributed by the asserted patent to the portfolio;” (4) “The prominence of the asserted patent in licensing discussions, negotiations and any resulting license agreement;” (5) “The scope of technology covered by the portfolio compared to the scope of the asserted patent.” Id. at 10, 11.

193. Id. at 19.
194. Id. at 20.
195. Id. at 19–20.
196. Id. at 22.
197. Id. at 23.
198. Id. at 23.
D. Royalty Payments

As royalty payments are almost always associated with a successful licensing effort, the Commission would traditionally give great weight to the evidence of existing royalty payments. In some cases, royalty payments were deemed part of the complainant’s licensing investment. On the other hand, lack of a successful license that brings in royalty payments could prevent a finding of substantial investment, regardless of the amount of unsuccessful efforts the patent owner put in. For example, in Stringed Musical Instruments, the ALJ found, and the Commission affirmed, that an independent inventor failed to demonstrate “substantial investment” in licensing. Over a period of nearly twenty years, the complainant actively engaged in licensing negotiations for a patent he had obtained, but he had not been able to obtain any licenses prior to filing the complaint. He had also spent nearly $10,000 developing various prototypes, attended trade shows to promote the technology, and collaborated with various companies and manufacturers. The ALJ nevertheless deemed the complainant’s failure to demonstrate substantial licensing revenue, or royalty payments, as crucial evidence in ultimately denying a finding of domestic industry.

In Multimedia Display, however, the Commission clarified that “[a]lthough royalties received by a complainant can be circumstantial evidence that an investment was made, they do not constitute the investment itself.” Accordingly, although the complainant Pioneer did receive royalties of “arguably considerable” value from a “worldwide license covering over 1,600 patent documents” and a cross-license for one of the respondents’ patents, the Commission determined that the royalty received by Pioneer and the cross-license were “relatively minimal in significance” considering “the context of the broad geographical [‘worldwide’] and technological scope of the license.”

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202. Id. at 13–19.
203. Id. at 24.
205. Id. at 25.
E. **PRODUCTION-DRIVEN VERSUS REVENUE-DRIVEN LICENSING DICHOTOMY**

Perhaps the most notable change in the legal standard of establishing licensing-based domestic industry is the Commission’s dichotomy of so-called production-driven licensing activity and revenue-driven licensing activity. In *Multimedia Display*, the Commission examined the complainant Pioneer’s activities as a whole to determine whether they represent a “substantial investment” under the statute. 206 There, for the first time, the Commission stated that

Pioneer’s activities, on the whole, reflect a revenue-driven licensing model targeting existing production rather than the industry-creating, production-driven licensing activity that Congress meant to encourage. . . . Although our statute requires us to consider all “licensing” activities, we give Pioneer’s revenue-driven licensing activities less weight. 207

The Commission defined production-driven licensing activity as activity “which encourages adoption and use of the patented technology to create new products and/or industries,” 208 and revenue-driven licensing activity as activity “which takes advantage of the patent right solely to derive revenue by targeting existing production.” 209 This is the “production/revenue dichotomy.” However, the Commission did not identify any relevant factors or contours for distinguishing production-driven from revenue-driven licensing activities, leaving the application of the dichotomy ambiguous.

Applying this dichotomy, the Commission found that Pioneer’s activities, taken as a whole, related “only minimally” to licensing the “asserted patents” in the United States. 210 Based on the above finding, the Commission held that Pioneer’s activities were too limited in light of its resources and the relevant market to be considered “substantial” under § 337(a)(3)(C). 211 Therefore the Commission reversed the ALJ’s finding that a domestic industry existed. 212

F. **LICENSEE’S ACTIVITIES**

As an alternative to establishing domestic industry based on the complainant’s own licensing activities under § 337(a)(3)(C), the Commission

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206. *Id.*
207. *Id.*
208. *Id.* at 25 n.20.
209. *Id.*
210. *Id.* at 25.
211. *Id.*
212. *Id.*
also allows a non-practicing complainant to rely on its licensee’s domestic activities to satisfy the economic prong of the domestic industry requirement.\textsuperscript{213} This is the so-called “backdoor” opened by licensees’ activities.\textsuperscript{214} However, non-practicing complainants seeking to gain access to the ITC through their licensees’ production-type activity must meet both the economic prong and the technical prong of the domestic industry requirement.\textsuperscript{215}

The recent \textit{Electronic Devices} investigation illustrates this use. The complainant, Saxon Innovations, LLC (“Saxon”), a small portfolio company, sought to prove its domestic industry based on the activities of its licensees AMD and Motorola.\textsuperscript{216} The ALJ granted Saxon’s “summary determination that it [had] met the economic prong of the domestic industry requirement based on its licensee Motorola’s production-type activities.”\textsuperscript{217} The ALJ also noted that as a separate matter, Saxon needed to meet the technical prong of the domestic industry requirement by proving that Motorola actually practiced the technology in suit.\textsuperscript{218}

\section{IV. IMPACT OF THE NEW DEVELOPMENTS ON VARIOUS NON-PRACTICING COMPLAINANTS}

As discussed in Part III, \textit{supra}, the latest developments at the ITC reaffirmed that pure licensing activities alone can constitute substantial investment and also left intact the potential “backdoor” opened by licensees’ activities, however, the Commission made notable changes regarding the treatment of litigation activity, portfolio licensing activity, and royalty payments.\textsuperscript{219} The Commission also, for the first time, made a point of distinguishing so-called revenue-driven licensing activity from production-driven licensing activity.\textsuperscript{220} One might interpret these developments as the Commission’s efforts to keep trolling out of the ITC. To evaluate how

\textsuperscript{214}. Fram, \textit{supra} note 82, at 25.
\textsuperscript{215}. \textit{See Electronic Devices}, USITC Inv. Nos. 337-TA-673, 337-TA-667 (consolidated), Initial Determination at 12, 12 n.5; \textit{see also} Fram, \textit{supra} note 82, at 27.
\textsuperscript{218}. \textit{Id.} at 12 n.5.
\textsuperscript{219}. \textit{See supra} Sections III.A–D, F.
\textsuperscript{220}. \textit{See supra} Section III.E.
effective these efforts may be, this Part explores the impact of the changes on various types of non-practicing complainants and predicts how their business practices may shift in response. For example, the “clear link” requirement for litigation expenses will most likely limit the ability of patent assertion entities, as well as that of independent inventors, to establish domestic industry. And the “strong nexus” requirement for portfolio expenses will most likely be an obstacle for practicing entities with an offensive patenting strategy and for mass patent aggregators, given the high-volume, low-quality patent portfolios that they often possess. The “strong nexus” rule may also disadvantage some R&D entities whose businesses involve portfolio licensing as standard practice. This Note argues that while the latest developments likely work more or less effectively against trolling, they may unexpectedly exclude truly innovative entities from the ITC and thus negatively impact socially desirable technology innovations.

A. PATENT ASSERTION ENTITIES

1. The “Clear Link” Requirement Will Limit Small Portfolio Companies’ Access to the ITC

Patent assertion entities focus on patent enforcement and litigation rather than the active development or commercialization of their patents.221 As such, the “clear link” requirement for litigation expense222 will likely limit the ability of both small portfolio companies and mass patent aggregators to establish domestic industry, but limit that ability to a different extent for each.

Small portfolio companies may have a more difficult time than mass patent aggregators to establish a “clear link” between their litigation activities and licensing. Like the complainant in Mezzalingua, who “had no formal licensing program” and did not offer “to license the patent to any party” before litigation,223 small portfolio companies, which generally rely heavily on litigation, are also unlikely to follow the licensing-first model in their rent-seeking business.224 In this case, small portfolio companies’ litigation expenses, which understandably constitute a significant portion of the companies’ overall expenses, may be cast aside in the “substantial investment” determination for failing to satisfy the “clear link” requirement, as the requirement looks much more favorably on the practices of a

221. See supra Section II.A.
222. See supra Section III.B.
224. See supra Section II.A.1.
licensing-first approach. This reduces the amount of investment small portfolio companies may rely on to establish domestic industry and undercuts their ability to gain access to the ITC, so long as they continue eschewing the licensing-first approach.

The effect of the “clear link” requirement on mass patent aggregators is less certain because most mass patent aggregators do have a formal licensing program despite being active litigants at the court. Thus they may take a licensing-first approach for some patents and a litigation-first approach for others. The decision about whether their litigation expenses are clearly linked to licensing would have to be made on a case-by-case basis. Nevertheless, the “clear link” requirement may prompt mass patent aggregators to shift their practice from a litigation-first model towards a licensing-first model, resulting in less litigations overall.

However, both the Commission’s opinion in Coaxial Cable and the subsequent Federal Circuit opinion in Mezzalingua left open the question of what exactly must be proved to establish a “clear link” between litigation expenses and licensing. For instance, the Commission stated that “drafting and sending cease and desist letters” and offering to license before initiating a lawsuit could be valid evidence for establishing the “clear link.”\(^\text{225}\) But investment in such efforts may be “nothing more than approaching another party to ask if they would like to take a license.”\(^\text{226}\) This might provide an opportunity for PAEs to game the system: a small portfolio company may spend minimum efforts “sending cease and desist letters”\(^\text{227}\) and offering licenses to just one potential licensee prior to bringing the lawsuit. It would then rely on such efforts to establish the “clear link” between litigation activity and licensing its IP, since the Commission does not look at the parties to an investigation but rather to efforts made in respect of an IP right being asserted. Thus a more specific and heightened standard for the “clear link” test is called for; Section V.A, infra, offers and analyzes one such possible test.


In addition to the threat posed by the “clear link” test, the “strong nexus” requirement for portfolio licensing expenses\(^\text{228}\) may, at times, threaten
mass patent aggregators’ ability to establish domestic industry through licensing. Because mass patent aggregators acquire patents from various sources, some of their patent portfolios may have come from practicing companies that previously accumulated them for defensive purposes. Such patent portfolios are often of high volume, low quality, and poor coherency.229 Thus it may be difficult to establish a “strong nexus” between licensing activity directed towards such patent portfolios and a handful of specific patents in suit, thereby reducing the likelihood that the Commission will find such activity to constitute “substantial investment.” On the other hand, small portfolio companies are less likely to be negatively influenced by the “strong nexus” requirement because they generally focus on a small group of high-quality and coherent patents.

3. The Production/Revenue Dichotomy Will Negatively Impact Both Small Portfolio Companies and Mass Patent Aggregators

The PAE business model suggests that the entity will typically assert patents against existing industry and products. This is especially so at the ITC, given that the Commission cannot award monetary damages directly. At the ITC, PAEs’ best chance to recoup their investment in the lawsuit would be to target mature products with which the respondents have the most to lose, and then extract settlement payment with the imminent threat of an exclusion order. The Commission’s production/revenue dichotomy will have a deterrent effect on such rent-seeking activities; however, the effect is uncertain due to the ambiguities related to the mechanism of the dichotomy.230

B. Practicing Companies with an Offensive Patenting Strategy

The “strong-nexus” requirement for portfolio licensing expenses will likely impact practicing companies employing an offensive patenting strategy even more than it will impact mass patent aggregators. As their standard business practice, practicing companies accumulate a large number of high-volume, low-quality patent portfolios, used primarily for defensive cross-licensing.231 When they assert one or two patents out of hundreds or even thousands of patents in a portfolio and attempt to rely on the entire portfolio licensing expense to demonstrate “substantial investment,” they will find themselves in a situation similar to that of the Multimedia Display complainant,

229. See supra Section II.B.
230. See supra Section III.E.
231. See supra Section II.B.
facing a judge unsympathetic to their arguments in favor of establishing domestic industry through licensing.\textsuperscript{232}

Further, the Commission’s latest treatment of royalty payments as mere “circumstantial evidence,” and not “the investment itself,”\textsuperscript{233} may also negatively influence practicing entities with an offensive patenting strategy. As well illustrated in \textit{Multimedia Display}, the mere fact that a patentee received considerable royalty payments for its large patent portfolio may no longer be deemed strong evidence for establishing domestic industry.\textsuperscript{234} The Commission may even find this type of evidence to be “minimal” in light “of the broad geographical and technological scope of the license.”\textsuperscript{235}

However, unlike mass patent aggregators, whose practice focuses on patent enforcement, practicing companies do invest considerable sums of money in research and development.\textsuperscript{236} It is often impossible for practicing entities to practice \textit{every} technology resulting from R\&D, given the limitation of their manufacturing resources. Their “patent enforcement programs, by providing a return on R\&D expenses, can underwrite and . . . encourage socially desirable innovation.”\textsuperscript{237} A legal rule that overly restrains practicing entities’ patent-enforcement ability might introduce new uncertainties into corporate officials’ decision-making processes regarding research and development and indirectly chill at least some innovation.

C. \textsc{Research And Development Entities}

Until recently, the Commission has consistently found R\&D entities, like Rambus, who employ a formal licensing program for commercializing their innovating ideas, to “satisf[y] the domestic industry requirement based on

\begin{itemize}
\item \textsuperscript{232} \textit{Multimedia Display}, USITC Inv. No. 337-TA-694, Commission Opinion at 25 (Aug. 8, 2011); \textit{see, e.g.,} \textit{Certain Wireless Commun’n Devices, Portable Music & Data Processing Devices, Computers & Components Thereof}, USITC Inv. No. 337-TA-745, \textit{Commission Notice to Review, Vacate, and Remand} (July 22, 2011) (reviewing and vacating the ALJ’s initial determination granting Motorola’s motion for summary determination that it satisfied the domestic industry requirement based on licensing industry). The case was remanded to the ALJ in keeping with \textit{Multimedia Display}. \textit{Id.}
\item \textsuperscript{233} \textit{Multimedia Display}, USITC Inv. No. 337-TA-694, Commission Opinion at 24.
\item \textsuperscript{234} \textit{Id.}
\item \textsuperscript{235} \textit{Id.} at 24–25.
\item \textsuperscript{236} \textsc{FTC Report}, supra note 76, at 34 n.8 (“Cisco invests more than $5 billion annually in R\&D . . . Sun reinvests between 15 and 20 percent of its annual revenues back into R\&D annually.”).
\item \textsuperscript{237} Chien, supra note 87, at 325.
\end{itemize}
their licensing activities.” However, some of the new rules, in practice, may be interpreted in such a way that disadvantages such R&D entities.

For example, portfolio licensing is a standard practice of R&D entities, and a single R&D entity may have multiple technology-centered portfolios available for licensing. As discussed in Part II, supra, R&D entities’ patent portfolios are often of higher quality and better internal coherency, as they enable and protect licensees’ freedom to practice a certain technology. The Commission’s “strong nexus” requirement for portfolio expense asks whether the asserted patent is “particularly important or valuable within the portfolio” and gives great weight to evidence such as whether the patent has been “discussed during the licensing negotiation.”

But this requirement does not seem to reflect the business realities of R&D entities, and, in fact, it would hurt the socially desirable ability of such entities doing important innovative work to further commercialize a particular technology. This is so because, at times, a patent portfolio directed towards a specific technology may consist of a group of essential patents, none of which is more important than another. Moreover, “[o]nce the overall strength and value of a portfolio has been established in a particular segment of the market, it is not unusual that” parties would conduct and conclude a licensing negotiation “without any discussions of particular patents.” Emphasizing such evidence rather than the intrinsic technological characteristics of the patent portfolio might unnecessarily burden R&D entities as they try to come up with evidence that may be nonexistent in their normal business practice.

Furthermore, despite R&D entities’ established licensing programs and efforts to commercialize their patented technologies, there have always been players who try to practice the technology without paying first. In their

239. See supra Section II.C.
244. See, e.g., Rambus Inc.’s Responses to Complaint Counsel’s Proposed Findings of Fact at 546, In re Rambus Inc., No. 9302 (F.T.C. Oct. 1, 2003), available at http://www.ftc.gov/os/adpro/d9302/031001RespondentoCCsfactsvol2.pdf (quoting memo from a Siemens employee stating that “[o]ne day all computers will (have to) be built like this, but hopefully without the royalties going to Rambus”).
efforts to demand royalty payments from such players, R&D entities will inevitably target the *existing* products of such players. Historically, the Commission has not treated R&D entities’ enforcement activities targeting existing products differently from their technology-transfer activities that focus primarily on creating new products or industry.  

However, under the Commission’s new production/revenue dichotomy, those enforcement activities directed towards existing products may be deemed to be revenue-driven and given “less weight.” Although the mechanism of the production/revenue dichotomy is still unclear, it is hardly justifiable if the Commission gives R&D entities’ revenue-driven licensing activities “less weight” simply because a bad player has managed to get away with the patented technology for free and actually made a product out of it.

D. **INDEPENDENT INVENTORS**

Independent inventors represent the most active patent litigants. For the same reason stated in the case of patent assertion entities, the “clear link” requirement for litigation expense will also create hurdles for independent inventors seeking to enforce their IP rights at the ITC.

However, litigation may, at times, be the only way for truly independent inventors to obtain a license agreement for their invention. In the past, an ALJ rejected an independent inventor’s efforts to establish “substantial investment” based on twenty years of continuous efforts to obtain licenses, reasoning that none of those efforts resulted in any license agreements. In another case, the ALJ was satisfied that a different independent inventor's litigation expenses and royalty payments arising out of a string of litigations met the domestic industry requirement.

Under the current “clear link” test for litigation expenses, it is likely that the second independent inventor would fail to establish “substantial

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245. *See e.g.*, Certain Digital Satellite Sys. (DSS) Receivers & Components, USITC Inv. No. 337-TA-392, Initial Determination at 10–11 (Oct. 31, 1997) (treating complainant’s enforcement activities targeting the Weather Channel’s existing products the same way as their technology-transfer activities with Sony and StarSight).


247. *See supra* Section II.D.

248. *See supra* Section II.D; *supra* note 143.

249. *See Stringed Musical Instruments*, USITC Inv. No. 337-TA-586, Initial Determination on Violation at 23 (Dec. 3, 2007) (“McCabe’s investment over the span of nearly 20 years was limited to a few prototypes and short collaborations and discussions with various companies and manufacturers . . . which failed to produce any commercial products or result in any license agreements.”).

investment” in licensing because almost all of her expenses were directed towards enforcement through litigation. The first inventor’s case is more challenging: the inventor’s efforts to continuously engage manufacturing entities for collaboration opportunities over the years to commercialize the patented technology seemed to represent precisely the type of production-driven licensing activity which the Commission and Congress seek to encourage. It seems unjustified, or even unfair, to completely discredit such efforts in determining “substantial investment,” simply because they did not yield any return.251 Ironically, this would be analogous to keeping out of the ITC those thinly capitalized small enterprises that motivated Representative Kastenmeier to support the 1988 amendment to § 337 in the first place.252

On the other hand, the Commission’s latest treatment of royalty payments as “circumstantial evidence,” and not the investment itself253 may benefit independent inventors such as the first inventor, because royalty payments, as mere “circumstantial evidence,” clearly can no longer be a necessary condition to establishing domestic industry through licensing. This may afford independent inventors who engage in genuine efforts to bring the patented technology to market, but without success, an opportunity to rely on their unsuccessful licensing activities to establish domestic industry at the ITC.

E. STARTUPS

Although startups traditionally have not been active litigants at the ITC,254 the Commission’s clear preference for production-driven activities, reflected in the production/revenue dichotomy, might make the ITC a more easily accessible forum to startups. In a recent case, where a startup asserted domestic industry based on licensing, the Commission reviewed and vacated the ALJ’s initial determination that a domestic industry did not exist, despite the fact that the startup’s only domestic activities were its district court litigation against respondents and its patent prosecution activities and that it never tried to license the asserted patents.255 The Commission remanded the

251. See Staff Petition for Review at 10–13, Stringed Musical Instruments, USITC Inv. No. 337-TA-586 (Apr. 2, 2008) (finding domestic industry requirement met because, among other reasons, “the record clearly demonstrates a sustained and substantial effort by McCabe to obtain licensees for his patents over many years”).

252. See discussion supra Section I.B.2.


254. See supra Section I.E.

case back to ALJ, noting that “it may be that [the complainant] Motiva’s only recourse was to sue Nintendo to bring its product to market and that its litigation activities may in fact be related to ‘licensing’ under section 337(a)(3)(C).” It is not clear whether startups will take advantage of the ITC’s preference for production-driven activities and follow independent inventors’ contingency-fee model to bring more suits at the ITC as a tactic to fend off competitors.

F. SUMMARY

Table 1 summarizes the likely impact of each of these recent developments in establishing licensing-based domestic industry on non-practicing complainants, by indicating whether the new development will make it easier for the type of complainant to establish domestic industry (“E”) or make it more difficult (“D”).

256. *Id.* at 10. On remand, the ALJ again found an industry does not exist in the US. *See Video Game Systems*, USITC Inv. No. 337-TA-743, Notice Regarding Initial Determination on Remand at 1–2 (Nov. 2, 2011). A public version of the initial determination is not available as of November 29, 2011.
Table 1: Summary of Impact on Non-practicing Complainants

<table>
<thead>
<tr>
<th>PAE</th>
<th>Practicing company with an offensive patenting strategy</th>
<th>R&amp;D entity</th>
<th>Independent Inventor</th>
<th>Startups</th>
</tr>
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<tbody>
<tr>
<td>Small portfolio company</td>
<td>D</td>
<td>D</td>
<td>D</td>
<td>E</td>
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<tr>
<td>Mass patent aggregator</td>
<td>D</td>
<td>D</td>
<td>D</td>
<td>E</td>
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<tr>
<td>“Clear link” requirement for litigation expense</td>
<td>D</td>
<td>D</td>
<td>D</td>
<td>E</td>
</tr>
<tr>
<td>“Strong nexus” requirement for portfolio licensing expense</td>
<td>D</td>
<td>D</td>
<td>D</td>
<td>E</td>
</tr>
<tr>
<td>Royalty payments deemed “circumstantial evidence”</td>
<td>D</td>
<td>D</td>
<td>D</td>
<td>E</td>
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<tr>
<td>Production/Revenue-driven dichotomy</td>
<td>D</td>
<td>D</td>
<td>D</td>
<td>E</td>
</tr>
</tbody>
</table>

Table 1 shows that, on the whole, non-practicing complainants will have a more difficult time establishing domestic industry following these latest developments, which broadly means that the changes have the effect of making the ITC a less attractive litigation forum for most types of non-practicing complainants.

V. SCRUTINIZING THE NEW RULES

In Part IV, supra, this Note explores the potential impact on various non-practicing complainants brought by the new rules set forth in Coaxial Cable and Multimedia Display regarding licensing-based domestic industry. Some of these effects are consistent with public policy, and others are arguably not. In light of the predicted impact, this Part revisits and scrutinizes the new rules and proposes possible alternatives that are better aligned with public policy considerations.
A. REPLACE THE “CLEAR LINK” TEST WITH A “PATTERN OF LICENSING” APPROACH BASED ON NON-LITIGATION ACTIVITIES

The “clear link” requirement for litigation expenses may limit the ability of patent assertion entities, as well as that of independent inventors, to establish domestic industry. However, as it is not clear what level of pre-litigation activities is needed to establish the “clear link” between litigation and licensing, patent assertion entities may get around the rule by spending a minimum amount of resources on pre-litigation activities, later pointing to those activities as evidence of a “clear link” between litigation and licensing. This result frustrates the very policy interest underlying the “clear link” requirement that is against the business of rent seeking.

In order to prevent patent assertion entities from gaming the rule and sneaking pure litigation expenses back into the “substantial investment” consideration, the Commission should adopt a more specific and heightened standard as a prerequisite to using litigation expense for demonstrating domestic industry: complainants should establish a pattern of licensing based solely on non-litigation activities involving the patents in suit, proving that litigation is merely an extension of the complainants’ underlying and legitimate licensing activities.

This is essentially a two-part test: first, the complainant needs to make a prima facia showing that a pattern of licensing exists based on non-litigation activities, such as having a formal licensing department, personnel dedicated to drafting and negotiating licensing agreements, and a history of licensing negotiations; only when the complainant successfully establishes this pattern of licensing will the Commission turn to the actual litigation activities and examine whether litigation may be considered as an extension of the complainant’s licensing program, based on factors such as whether the complainant offers licenses to accused infringers prior to bringing the litigation or whether the complainant conducts settlement or licensing negotiations during the litigation.

The effect of this change on patent assertion entities would be to make establishing domestic industry more difficult by requiring an additional showing of a pattern of licensing based on pure licensing activities, before a complainant is even allowed to attempt linking litigation to licensing. Thus this test focuses on the underlying pure licensing activities that serve as the foundation of a licensing industry, at the same time taking into consideration

257. See supra Section IV.A.1.
258. See supra Section IV.A.1.
litigation expense which, at times, may be a necessary recourse against bad players.

Further, the Commission should allow a complainant to rely on both successful and unsuccessful licensing efforts to establish a pattern of licensing, in order to allow independent inventors, such as the one in Stringed Musical Instruments, to establish domestic industry, even if they have been wholly unsuccessful in their efforts to obtain licensees, and have no other options but to litigate.

B. FOCUS ON THE INTRINSIC TECHNOLOGICAL CHARACTERISTICS OF A PATENT PORTFOLIO

As discussed in Part IV, supra, requiring a “strong nexus” between portfolio licensing expenses and the specific patents in suit will most likely become an effective obstacle against the rent-seeking practices of both practicing entities with an offensive patenting strategy and mass patent aggregators, given the high-volume, low-quality patent portfolios that they often possess. However, this rule might also disadvantage R&D entities if the Commission continues to determine the “importance and value” of the asserted patent based primarily on extrinsic evidence, such as whether the patent was discussed during portfolio licensing negotiations, with less focus on the patent portfolio’s intrinsic technological characteristics. This is because extrinsic evidence implicating the importance of the patent in suit may not exist in R&D entities’ normal business practice.

To address this issue, the Commission should instead focus on the intrinsic technological characteristics of the patent portfolio in deciding whether a strong nexus exists. “Evidence showing how the asserted patents fit together congruently with other patents in the portfolio covering a specific technology” should be given the greatest weight, with extrinsic evidence, such as whether the patents in suit have been discussed during a licensing negotiation, relegated to a secondary role. This change will not only protect R&D entities’ socially desirable portfolio licensing practice, but also give companies an incentive to invest in tightly bound, high quality, essential patent portfolios, which will probably reduce overall uncertainty in the marketplace.

Furthermore, although limiting practicing entities’ ability to profit through offensive patent enforcement is consistent with the public policy

259. See supra Section III.C.
260. See supra Section IV.C.
against rent seeking, the Commission should act to minimize the potential chilling effect on practicing entities’ long-term allocation of R&D resources. A “strong nexus” rule focusing on intrinsic technological characteristics will not help practicing entities’ ability to establish domestic industry given their high-volume, low-quality patent portfolios. This negative impact may be offset by taking into consideration the value of cross-licensing agreements in the determination of “substantial investment,” as discussed in more detail in Section V.C.2, infra. In contrast, the less desirable activities of mass patent aggregators would likely remain shut out of the ITC because mass patent aggregators do not typically engage in cross-licensing.

C. TREATMENT OF ROYALTY PAYMENTS

Although royalty payments are deemed “circumstantial evidence” after Multimedia Display, this Note suggests that the Commission should maintain that receiving royalty payments is an important factor in determining whether substantial investment has been made and that it should find “substantial investment” based on unsuccessful licensing activities under very narrow circumstances only. However, the Commission should also take into account the intrinsic value of cross-licenses besides royalty payments, as cross-licenses promote the exchange of new ideas and also help minimize transaction costs.

1. Receipt of Royalty Payments Should Remain an Important Factor in Determining Substantial Investment

The Commission’s latest treatment of royalty payments, as mere “circumstantial evidence” and not the investment itself, might benefit independent inventors, like the one in Stringed Musical Instruments, who fail to secure royalty payments despite continuous efforts to obtain licensees. With royalty payments no longer a necessary condition to establish domestic industry through licensing, these independent inventors may have a chance to rely on their investment in unsuccessful licensing efforts to satisfy the “substantial investment” requirement.

However, to avoid opening the floodgate of frivolous complaints filed on the basis of half-hearted licensing efforts that fail to yield any agreement, the Commission should still maintain that the successful negotiation of royalty-bearing licenses remains an important factor in determining whether substantial investment has been made. “[U]nsuccessful licensing activities [may] require nothing more than approaching another party to ask if they

262. See supra Section IV.B.
263. See supra Section III.D.
would like to take a license,” meaning that although the absence of license does not always indicate no licensing effort at all, the licenses are often not difficult to obtain with a meritorious IP right. The Commission should therefore find “substantial investment” based on unsuccessful licensing activities under only very narrow circumstances where the evidence of licensing efforts is clear, such as those of the independent inventor in *Stringed Musical Instruments* who demonstrated continuous and genuine efforts directed at licensing his legitimate rights over the patented technology.

2. Recognition of the Value of Cross-licenses in Evaluating Substantiality of Investment

In addition to viewing royalty payments as important evidence of “substantial investment” in licensing, the Commission should also take into consideration the value of cross-licenses and treat them similarly to royalty payments. Many technology companies grant licenses in exchange for royalty-free cross-licenses, saving transaction costs and promoting the exchange of new ideas, which leads to innovation. In that sense, cross-licenses have an intrinsic value to the company, just like royalty payments, and so the two should be viewed somewhat interchangeably when the Commission evaluates “substantial investment” in licensing. Taking into account the value of cross-licenses may also help to offset the negative impact imposed by the “strong nexus” requirement on practicing entities’ ability to recoup R&D investment.

D. THE PRODUCTION/REVENUE DICHOTOMY

Finally, by putting forth the production/revenue dichotomy, the Commission expressed a clear preference for production-driven licensing activities that seek to bring patented technology to the marketplace and an aversion to revenue-driven licensing activities that target existing products. This is largely consistent with the stated Congressional purpose in enacting the amendments to §337, and it also roughly traces the Federal Trade Commission’s (“FTC”) distinction between *ex ante* patent transaction and

265. *See* text accompanying *supra* note 249.
267. *Id.* at 5 (“To deny the Commission’s protection of patents merely because the patent owner chooses to exploit the value of its portfolio through cross-licensing, rather than through a royalty-based licensing program, would disregard an economic reality of the portfolio patent licensing business.”).
268. *See supra* Section III.E.
269. FTC REPORT, *supra* note 76, at 40.
**ex post** patent transaction. In its report on the evolving IP marketplace, the FTC defined **ex ante** patent transactions as

>[p]atent transactions that occur as part of a technology transfer agreement [and that] occur before the purchaser has obtained the technology through other means. Such ex ante patent transactions accompanied by technology transfer have great potential for advancing innovation, creating wealth and increasing competition among technologies.

It defined **ex post** patent transactions as “patent transactions . . . [that] occur after the user of the technology has invested in its independent invention and development, without input from the patentee.” Thus both the FTC and the ITC appear to recognize two types of licensing or transactional activities that bear opposite effects on the public interest that favors the propagation and commercialization of new technology. The two agencies’ preferences for production-driven licensing activities or **ex ante** patent transactions are also aligned.

As discussed in Part IV, supra, the production/revenue dichotomy will, to some extent, undercut patent assertion entities’ ability to establish domestic industry based on their rent-seeking licensing activities, though the effect is largely uncertain due to the ambiguities related to how the Commission will apply the dichotomy to a specific set of facts. On the other hand, for R&D entities that engage in both production-driven and revenue-driven licensing activities, it is hardly justifiable to cast aside their licensing investment that targets the existing products of bad players.

To give proper weight to hybrid licensing activities, such as those of the R&D entities, application of the production/revenue dichotomy should focus on the overall effect of the complainant’s licensing activities on the U.S. market and on U.S. consumers.

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270. Id. at 40.
271. Id. at 40.
272. Id. at 40 n.43. Arguably, the FTC’s ex post patent transaction is more narrowly defined than the Commission’s revenue-driven licensing, which includes acts that “take[] advantage of the patent right solely to derive revenue by targeting existing production,” regardless of whether the user of the technology independently invented it. *Multimedia Display*, USITC Inv. No. 337-TA-694, Commission Opinion at 25 n.20 (Aug. 8, 2011).
273. See FTC REPORT, supra note 76, at 52 (“Ex post patent assertions and transactions also provide essential support to business models based on ex ante licensing and technology transfer.”).
274. As the Federal Circuit noted in *Spansion*, protecting the need of U.S. consumers has always been a recurring theme in the Commission’s deep policy consideration. *Spansion*, Inc. v. Int’l Trade Comm’n, 629 F.3d 1331, 1360 (Fed. Cir. 2010).
Take, for example, a small portfolio company’s licensing activities. By solely targeting existing products, without any contribution to innovation, such licensing activities will inevitably increase the cost of producing existing products, and U.S. customers may eventually have to bear the burden of those cost increases assuming the existing producer can still operate its business. Such licensing activities which are purely driven by rent seeking have an overall negative effect on the U.S. market and consumers. Therefore, from a policy perspective, these activities would furnish an improper basis upon which to establish domestic industry. If, on the other hand, a different entity type such as an “idea house” comes up with a truly innovative idea and actively seeks to commercialize the product through licensing to manufacturers, the licensing activities will have a positive effect on the U.S. market and consumers because it would lead to the replacement of old products with new ones, and consumers would benefit from access to new technologies and industries that did not exist before.

For R&D entities which engage in a hybrid licensing practice regarding the patents in suit, the components of that practice that are driven purely by rent seeking will likely increase an existing production firm’s input costs and may lead to price increases or decreased consumer choice. However, these same entities’ other licensing activities, which promote the adoption of the patented technologies into new products, will have an opposite effect. For instance, introducing more new products into the market will increase competition among similar products and drive down prices. Of course, the overall effect of such complainants’ licensing activities on the U.S. market and consumers hinges on multiple factors, such as price, product, and accessibility. Complainants seeking to establish domestic industry through licensing activities bear the burden to prove the overall positive effect of their licensing activities on the U.S. market and U.S. consumers.

VI. CONCLUSION

Nearly twenty-five years after the 1988 amendment to § 337 extending the ITC’s protection to licensing-based domestic industries, a recent FTC report once again acknowledges the positive effect of licensing and technology transfer on the whole innovation ecosystem. This reaffirms the validity of the congressional intent behind the 1988 amendment, which recognized that certain industries, though not directly engaging in production, are still worthy of the Commission’s protection for actively commercializing their intellectual property through licensing. However, after the Federal Circuit’s holding that the eBay permanent-injunction decision does not apply to the ITC, non-practicing patent owners have been filing a rising number of complaints at the ITC asserting a domestic industry based
on licensing. In accordance with the widely accepted notion that the ITC is fundamentally a trade forum instead of an IP forum, the Commission faces a complex gate-keeping function of identifying worthy complainants that have truly established a licensing-based industry. The complexity arises partly out of the various licensing practices of different entities, as well as the rapid evolution of the licensing industry itself in terms of size, revenue stream, business model, etc.

In its two recent opinions, *Coaxial Cable* and *Multimedia Display*, the Commission seeks to clarify and refine the rules governing the establishment of a domestic industry based on licensing activity. These refinements have had varying degrees of impact on the several types of non-practicing complainants that come before the Commission. For the most part, it looks like the latest changes are consistent with a public policy that is defined with respect to the U.S. innovation policy. However, there remain some ambiguities and unclear applications of the various tests and future investigations will probably further refine these standards.

Notably, the rationale behind the Commission’s new production-driven/revenue-driven licensing dichotomy is more akin to a public interest consideration than statutory interpretation. Traditionally, the Commission only considers public interest factors at the conclusion of an ITC litigation, after a finding of both the existence of a domestic industry and infringement. The production/revenue dichotomy may signal the Commission’s willingness to take into consideration at least some public interest at the stage of determining domestic industry. Though there is much left to be observed as to how the dichotomy will eventually play out, going forward, such public-policy considerations may be crucial in facilitating the Commission’s efforts to properly perform its gate-keeping function.