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PTAB Misconduct Rule Won't Deter Hedge Fund Attacks

By **Erin Coe**

Law360, San Diego (September 1, 2015, 11:18 PM ET) -- The latest rule package for America Invents Act reviews would arm the Patent Trial and Appeal Board with the ability to sanction attorneys for not doing an adequate prefiling investigation and for making representations to the board for an "improper purpose," a new tool that attorneys say won't likely thwart patent challenges by hedge funds that some view as an abuse of the system.

Attorneys already have a duty of candor and good faith when they practice before the PTAB, but one of the proposed new rules announced by the U.S. Patent and Trademark Office in August would impose a requirement for attorneys to sign petitions, responses and all other filings, similar to a Rule 11 standard in district courts. They also would have to make sure any representation to the board is not made for any improper purpose, "such as to harass, cause unnecessary delay or needlessly increase the cost of the proceeding," as well as ensure that legal contentions are warranted and factual contentions have evidentiary support — or they could face sanctions.

"The proposed rule requires attorneys to perform a policing function on their clients ... and I think if you're a reputable attorney, it will make you think twice about the purpose of a filing," said Dorothy Whelan, a principal at Fish & Richardson PC. "By actually putting the onus on attorneys that when they sign papers, they are certifying a filing is not meant for an improper purpose, that's putting some skin in the game for attorneys."

Whelan said that a recent spate of filings by a coalition that has ties to hedge fund manager Kyle Bass has been one of the driving forces behind the proposed requirement.

"This rule is designed in part to address these abusive filings," she said.

But many attorneys told Law360 that even if the USPTO is attempting to use the proposed rule to put a stop to AIA challenges launched by hedge funds, it would have little deterrent effect.

The rule package comes as patent validity challenges are shifting from the district courts to the PTAB, with the USPTO noting last month that the board has received 3,655 petitions in the three separate AIA review programs since the proceedings became available in September 2012.

"One of the concerns as inter partes reviews and post-grant proceedings increase in popularity is whether this process could become rife with misuse," said Steve Lendaris, a partner at Baker Botts LLP. "There also are concerns that patent owners will face waves of frivolous inter partes reviews."

And one set of inter partes review filings is already causing a stir among patent owners, particularly pharmaceutical companies. The Coalition for Affordable Drugs, a wholly owned subsidiary of Bass' Hayman Credes Master Fund LP, has launched about two dozen AIA challenges of various drug patents. Bass has said invalidating the patents not only would lower the price of drugs by opening the door for generic-drug competitors, but also was part of an investment strategy to grow his fund, which he said has taken a short position on the drugmakers' stock and stands to gain if the stock price drops.

Pharmaceutical companies have argued that the group is misusing the inter partes review process to manipulate the stock market. Celgene Corp. in July filed a motion for sanctions against the coalition, and the PTAB on Tuesday asked for more briefing by the coalition and a Shire PLC unit on whether two of the coalition's petitions over Shire's patent for treating short bowel syndrome should be dismissed for abusing the AIA review program.

But under the current inter partes review system, parties are permitted to challenge patents even if they haven't been accused of infringing them, and the hedge fund filings aren't likely the sanctionable conduct the USPTO had in mind when it came up with its proposed rule, according to Neil Smith, a partner at Rimon PC and a former PTAB administrative patent judge for the USPTO's Silicon Valley office.

He also pointed out that the board last month denied two of the coalition's inter partes review petitions over Acorda Therapeutics Inc.'s multiple sclerosis drug patents on substantive grounds.

"I have faith in the board, which has already denied a couple of those petitions," he said. "The market shouldn't necessarily see every one of these filings to mean the petitioner is going to win."

Even if the rule is adopted, filings by hedge funds aren't necessarily going to slow down, according to Joseph Palys, a partner at Paul Hastings LLP.

"I don't see anything in the rule that would hinder the filing of a petition by a party that aggressively believes it has the right to pursue petitions in this way," he said. "But it might prevent other potential petitioners that are not as aggressive, or at least help them to make sure that the positions they take in a petition are warranted."

The proposal would implement more court-like procedures in the AIA system that should make it easier for the board to impose sanctions if a petitioner hasn't done sufficient research before filing an AIA review or tries to advance baseless arguments, according to John Murphy, a partner at BakerHostetler.

The development is a positive one for patent owners with valuable patent rights at stake in the reviews, but the rule also would require patent owners to make sure their filings are well-supported.

"The proposed rule helps protect patent owners' property rights from bad faith arguments, but it imposes the same requirement on patent owners to mind their Ps and Qs as well," he said. "It ought to impact both parties at all stages of a proceeding for many different reasons."

The provision requiring attorneys not to make representations for "any improper purpose, such as to harass" might be a tool that the PTAB uses to deny petitions filed by hedge funds, but a solution may ultimately have to come from Congress, according to Dion Bregman, a partner at Morgan Lewis & Bockius LLP. A pending bill in the U.S. House of Representatives, the Innovation Act, seeks to bar AIA reviews from being filed by hedge funds seeking to manipulate stock prices by challenging patents.

"Under the current rules, I don't believe that the board can reject petitions simply because it doesn't like the fact that patents are being challenged to lower the patent owner's stock price so that the petitioner can hedge the stock," he said. "Congress likely needs to fix this issue, such as by requiring a party to be sued before being able to file an inter partes review, which is already a requirement for covered business method reviews."

But Whelan said the proposed rule could be a way for the PTAB to deal with the hedge fund filings on its own without the need for legislation, though an adverse ruling for the coalition in the Celgene cases also had the potential to scale back such filings. The board is expected to rule in those cases in October.

"If those petitions aren't granted, filing an inter partes review doesn't become an attractive strategy for hedge funds, and they might die away anyway," she said. "It will be interesting to see what the PTAB does with Celgene's motion for sanctions, what framework it sets up for evaluating the motion and what constitutes sanctionable behavior."

Bregman doubted there would be much overall effect from the proposed rule if it was implemented, noting that AIA challenges don't leave a lot of room for misconduct in the first place.

"In these patent proceedings, you're already at the mercy of the panel, and you don't want to do anything to upset them," he said. "For the most part, attorneys behave. And inter partes review petitions require so much detail, including a claim chart that explains why each claim is unpatentable. If the petitioner fails to present a compelling case, the board will simply deny the petition."

--Additional reporting by Ryan Davis. Editing by Katherine Rautenberg and Philip Shea.
