Roadblock to Innovation: The Role of Patent Litigation in Corporate R&D

Filippo Mezzanotti*

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Abstract

I examine how patent enforcement affects corporate R&D, exploiting the legal changes induced by the Supreme Court decision “eBay v. MercExchange.” This ruling increased courts’ flexibility in remedying patent cases, and effectively lowered the potential costs of patent litigation for defendants. For identification, I compare innovative activity across firms differentially exposed to patent litigation before the ruling. Across several measures, I find that the decision led to a general increase in innovation. This result confirms that the changes in enforcement induced by the ruling reduced some of the distortions caused by patent litigation. Exploring the channels, I show that patent litigation negatively affects investment because it lowers the returns from R&D and exacerbates its financing constraints.

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1 Introduction

The main goal of the patent system is to protect innovation and thus to spur growth. Whether this goal is achieved depends on how patents are defined and protected, which itself depends on how the legal system resolves intellectual-property disputes. Indeed, the courts appear to have played an increasingly important role in the patent system (Cohen et al., 2019). Over the last thirty years, lawsuits involving patents more than tripled (Figure 1) and their estimated cost surpassed $300 billion (Bessen et al., 2018). In part, this shift in patent enforcement has been connected with the increase in patent-holders’ rights over the past decades (Jaffe and Lerner, 2011).¹

In principle, increasing the rights of patent-holders should have positive effects on innovation. However, this simple logic may fail for several reasons. For instance, stronger rights for patent-holders may actually have detrimental effects on innovation when we account for the role of competition (Arrow, 1962; Aghion and Howitt, 1992) or we consider innovation as a cumulative process (Scotchmer, 1991; Bessen and Maskin, 2009). Furthermore, the idea that stronger patent rights will increase innovation also hinges on the assumption that patent enforcement is sufficiently effective in resolving legal disputes. In practice, the patent system is characterized by a lot of uncertainty (Lemley and Shapiro, 2005) and enforcement tends to be a noisy process (Jaffe and Lerner, 2011). In this context, strong patent rights may actually increase the cost that frivolous patent litigation can impose on innovative firms, which in turn may curb innovation and growth (Bessen and Meurer, 2008b; Boldrin and Levine, 2002). Therefore, to understand the connection between patent protection and innovation, we need to also consider how changes in patent rights affect enforcement. This issue is particularly crucial today, given the increasing importance of intangible assets to the modern corporation (e.g. Corrado and Hulten, 2010; Eisfeldt and Papanikolaou, 2014; Peters and Taylor, 2017).

Consistent with this hypothesis, this paper shows that a reduction of patent holders’ rights - which lowered the costs of patent litigation for defendants – may have positive effect on corporate innovation. To examine this issue, I develop a new research design that exploits a landmark Supreme Court decision “eBay v. MercExchange” (2006). The ruling ended the practice of automatically granting a permanent injunction after a patent violation. The issuance of an injunction forces the defendant firm to shut down any operation related to the violated technology, regardless of the nature or magnitude of the infringement. Given this large operational risk, the presence of automatic injunction gave patent holders a very strong bargaining position in IP disputes and negotiations (Section 2.1). With the 2006 decision, courts were allowed to decide on a case-by-case basis whether an injunction was appropriate, therefore increasing court flexibility to remedy patent disputes and lowering the potential cost for defendants.

¹A prominent example that demonstrates the important role of automatic injunction in patent litigation before
2006 is the lawsuit initiated by NTP Inc. against Research in Motion (RIM), the maker of BlackBerry, in the early 2000s. The district court sided with NTP and found RIM guilty of infringing on a few of NTP's patents. With the objective of avoiding an injunction, RIM started to negotiate with NTP. Even if the infringement covered only a small fraction of the portfolio of patents used to run the BlackBerry system, an injunction order would likely have led to a shutdown of the whole system. Leveraging on its ability to obtain an injunction, NTP was able to negotiate a record settlement of more than $610 million, approximately half of RIM's revenues in the previous year. Interestingly, years later some of the claims contained in NTP patents were deemed invalid, as RIM had argued initially. According to several experts, the presence of an automatic injunction played a fundamental role in the decision to settle early and the size of the transfer.\(^2\)

In general, the overall impact of the "eBay v. MercExchange" decision is ex-ante ambiguous. On the one hand, removing the automatic injunction may lower deterrence against violations (e.g., Epstein, 2008), therefore reducing the incentives to innovate. On the other hand, this increase in court flexibility may actually positively affect innovation by reducing the costs that patent litigation may impose on innovative firms. In fact, the presence of a "near-mandatory" injunction increases the extent to which companies can be held up by a plaintiff (Lemley and Shapiro, 2006; Shapiro, 2010, 2016a), as clear from the RIM-NTP case. In general, leveraging on the high degree of uncertainty in the patent system (Lemley and Shapiro, 2005), the injunction threat may help plaintiffs to obtain large settlements even if accusations are based on frivolous claims or minor violations.\(^3\)

In this context, the new rules should reduce the hold-up costs of litigation, therefore positively affecting the incentives and financial ability to do R&D investments.\(^4\)

The post-eBay changes in patent enforcement suggests that the impact that the decision had on litigation costs may have been substantial (e.g. Bessen and Meurer, 2008a; Holte, 2015; Shapiro, 2010; Tang, 2006; Venkatesan, 2009). In aggregate, Chien and Lemley (2012) found that the likelihood of obtaining an injunction after the Supreme Court ruling decreased by at least 25%. However, injunctions are still granted in the majority of cases, suggesting that this remedy is still available to firms in case of a violation. Furthermore, the decline in injunction rates was larger for cases where the firms involved are not competitors or when the case involves a patent assertion entity (PAE) (Seaman, 2016). In line with this result, I find that public PAEs experienced large negative returns around the time of the court decision, with average cumulative returns of about -10%.

Given the theoretical ambiguity, this paper empirically studies the effect of the ruling by estimating a difference-in-difference model that exploits variation in firm exposure to patent litigation in 2006 to identify

\(^2\)In an interview with the National Law Journal (March 13, 2006, Volume 27, Issue 77), patent litigator David Clonts of Akin Gump Strauss Hauer & Feld, stated that “If BlackBerry knew it could successfully defend against an injunction and instead have a trial on money damages, the settlement value would have been a tenth of what it was.”

\(^3\)To quote the Supreme Court majority opinion, the threat of injunction was frequently used “as a bargaining tool to charge exorbitant fees to companies that seek to buy licenses to practice the patent.”

\(^4\)This view was shared by many scholars and practitioners. According to the American Innovators Alliance, an association representing large high-tech companies, because of high injunction risk, “money that could go to productive investments is instead diverted to legal fees and settlement payments,” leading to “... less innovation.” The sentences are taken from the “amicus curiae” submitted for the Supreme Court case.
companies that are more likely to be affected by the eBay ruling. The intuition for this choice is simple: while the shock potentially touched every firm, companies that operate in areas where patent litigation is more intense should be relatively more affected by the decision. I construct this measure of exposure as a weighted-average of litigation activity across all the technology areas in which a firm operates, where the weights are given by the share of patents in each USTPO technology class for the firm. Therefore, this measure captures exposure to litigation coming from the area in which the company operates, and it is orthogonal to endogenous decisions of the firm to engage in patent litigation. As a validation, I show that heterogeneity in exposure to the shock predicts variation in abnormal returns the day in which the decision was made public. In particular, firms more exposed to litigation outperformed less exposed firms when the ruling was released.

As a first step, I use this model to examine how the decision affected patent applications for a sample of almost twenty thousand innovative firms. Firms that were more exposed to litigation before the decision increased patenting more after the decision. In particular, a one-standard-deviation increase in exposure leads to a 3% higher application rate – which translates into almost one extra patent in the two years after the shock – and a 2% increase in the probability to patent anything. As discussed in the paper, these results are not driven by differential trends across heterogeneously exposed firms, and they are robust to control for industry trends – measured by the main technology area of the firm (Hall et al., 2001) – as well as other confounding factors. Furthermore, I also argue that my findings cannot be explained by other contemporaneous legal changes.

To better characterize the effect of the decision on innovation, I then extend this analysis in different directions. First, I find that the change in enforcement led to a shift in patent quality. While increasing their patenting relatively more, firms more exposed to patent litigation did not lower the average quality of their output. Instead, they became relatively more likely to develop a potential “breakthrough innovation” (Kerr 2010; Lin et al. 2016), defined as a patent that is at the top of the citation distribution within the same patent class and year group. Second, using different metrics (Abrams et al., 2013; Srinivasan, 2018), I show that the shock also decreased the share of defensive patents for highly affected firms. Third, I show that the ruling had a positive effect on R&D investment for public innovative firms.

Altogether, these results confirm that the positive effect on patenting did not simply reflect an increase in defensive activity (Hall and Ziedonis, 2001) or a shift in the incentives to file for a patent. Instead, these results are consistent with the idea that the change in enforcement caused by the ruling positively affected innovation. This suggests that the reduction in plaintiff bargaining power reduced some of the distortions caused by the litigation environment. In line with this hypothesis, I also show that the R&D effect was more pronounced for firms that were more likely to be involved in litigation as a defendant.

Finally, I examine how an improvement in enforcement rules may affect the process of innovation. First, enforcement seems to influence innovation because it determines the relative returns of different R&D projects. Consistent with this hypothesis, I find that after the Supreme Court ruling, firms marginally reshuffled their
internal resources toward projects that are in higher litigation areas, at least at the extensive margin. Second, enforcement rules seem to also affect R&D because they exacerbate the financing problems of innovation (Brown et al., 2009; Hall and Lerner, 2010). In fact, companies operating in high-litigation environments are forced to devote a larger share of resources for defensive activities (Cohen et al., 2019, 2016b) and spend more money on settlements or licensing.\(^5\) In the presence of financial frictions, this increase in costs may negatively impact the ability to undertake investments. Consistent with this implication, firms that were more likely to be financially constrained before the decision increased R&D intensity in its aftermath. These findings establish the important role played by financial constraints in explaining the negative effects of patent litigation.

This analysis provides several contributions to the literature. First, the paper shows that the impact of a change in patent rights on innovation crucially depends on how this shift affects patent enforcement. Previous work has shown that the strength of patent system has a limited direct effect on innovation (e.g. Lerner, 2002, 2009; Moser, 2005, 2013; Sakakibara and Branstetter, 2001). At the same time, stronger patents may negatively affect innovation indirectly, for instance by reducing knowledge diffusion (e.g. Galasso and Schankerman, 2015; Murray and Stern, 2007; Williams, 2015). However, less attention has been devoted to understanding the relationship between property rights, enforcement, and innovation decisions. The eBay ruling represents a shift of patent enforcement towards principles of “proportionality.” In particular, it gives courts more flexibility to balance the interests of competing parties and therefore reduces the prerogative of a patent owner. This paper shows that in the current patent system this type of intervention may have beneficial effects for innovation by reducing distortions caused by hold-up in litigation (Shapiro, 2016a).\(^6\) Therefore, while this paper does not directly help settle the broad debate on the optimal strength of patents, it provides novel insights about the role of patent enforcement in this area.

This discussion is not surprising within the context of the law and economics literature. In general, a strict property rule – as the mandatory injunction policy in place before the ruling – works well when ownership rights are clear and easy to identify, as with tangible assets (Calabresi and Melamed, 1972). If the boundaries of the assets are hard to define, like for patents (Lemley and Shapiro, 2005), a strict property rule may fail to provide the best incentives, and it may be inferior to a hybrid system characterized by more flexibility (Kaplow and Shavell, 1996).

Furthermore, these results provide new evidence on the real costs of patent litigation – which is central in today’s research (Hall and Harhoff, 2012) and policy debate (White House 2013). Previous work in this area – in particular Smeets (2014) and Cohen et al. (2019) – has shown that innovation activity declines when a firm is

\(^5\)Litigation claims “whether meritorious or not, (...) could require expensive changes in our methods of doing business, or could require to enter into costly royalty or licensing agreements” (eBay 2006 10-K).

\(^6\)One limitation of this study – which is driven by the methodology used - is that its results cannot be directly generalized to start-ups. While more research is definitely needed to explore this dimension, in the conclusion (Section 7) I discuss how evidence from this study and other works (e.g. Mezzanotti and Simcoe, 2019) may suggest that results for that sample should not be reversed. Furthermore, it is important to highlight how established firms undertake the largest majority of R&D investment in US.
directly targeted by patent lawsuits. While my results are consistent with these papers, this work also extends this literature in several directions. First, changes to the patent litigation environment – and therefore not only the direct involvement in a lawsuit - significantly affect the quantity and the direction of innovation. One implication of this result is that focusing only on the direct costs of patent litigation (e.g. Bessen et al., 2018) will under-estimate the real impact. Second, my results expand their analyses by examining the channels through which litigation may affect R&D decisions. Lastly, in this area this paper complements the contemporaneous work by Appel et al. (2019), which examines the detrimental effects of patent litigation on business creation and start-up activity.\footnote{On top of looking at different dimensions of firm activity (innovation vs. business creation), Appel et al. (2019) also differs from this work across (at least) two important dimensions. First, the papers look at very different types of policy interventions. Second, the two works focus on different populations (established vs. new-firms), which are likely to be affected in different ways by litigation.}

More broadly, this paper shows that changes in patent enforcement can have a significant impact on the incentives of firms to invest in R&D, therefore contributing to the finance literature studying the relationship between legal institutions and economic activity (Acharya et al., 2011; Claessens and Laeven, 2003; Demirgüç-Kunt and Maksimovic, 1998; Ferreira et al., 2018; King and Levine, 1993; La Porta et al., 1997; Lerner and Schoar, 2005; Hochberg et al., 2017). Previous research has demonstrated that secure property rights favor a more efficient allocation of resources and fosters growth, but in many cases good enforcement is just as important as good rules in determining economic outcomes (e.g. Djankov et al., 2003; Ponticelli, 2016). The role of enforcement is particularly important in intellectual property because the exact boundaries of patents are hard to define (Lemley and Shapiro, 2005) and therefore lawsuits are frequent (Lanjouw and Lerner, 1998). This paper highlights the role of enforcement in innovation and suggests that, similar to other interventions (Acharya and Subramanian, 2009; Hsu et al., 2014; Lin et al., 2016; Mann, 2018; Moshirian et al., 2018), a fine-tuning of patent law can have substantial effects on fostering corporate innovation.\footnote{This analysis is also related to the body of work in finance that focuses on the effect of litigation risk - mostly shareholder litigation - on corporate policies (Appel, 2016; Arena and Julio, 2014; Kim and Skinner, 2012; Lin et al., 2016; Haslem, 2005; Rogers and Van Buskirk, 2009).}

The paper is organized as follows. In Section (2), I provide more background information about the Supreme Court decision and discuss its potential effects on corporate innovation. In Section (3), I present the data used in the paper, while in Section (4), I present the identification and discuss in detail the measurement of exposure to patent litigation at the firm level. In Section (5), I present the main results of my analysis. In Section (6), I discuss and test different channels through which patent litigation can affect innovation. Lastly, Section (7) concludes.
2 The “eBay v. MercExchange” case

This section provides background information on the Supreme Court decision “eBay v. MercExchange” and discusses its possible effects on innovation. First, I analyze the importance of injunction on the pre-ruling world and provide some background on the decision. Second, I discuss how the ruling could affect innovation, therefore setting the foundation for the hypothesis and research design. Lastly, I provide some preliminary and novel evidence of the importance of the ruling for patent enforcement.

2.1 The role of injunction and the 2006 decision

With the 2006 “eBay v. MercExchange” decision, the Supreme Court revisited the norms regulating the issuance of permanent injunction in cases involving intellectual property.\(^9\) Injunction is a remedy that can be requested by a plaintiff. If granted by a court, an injunction forces the infringer to stop using any technology covered by the contested patents, irrespective of the magnitude of the infringement. Before 2006, a plaintiff that was able to prove a violation had essentially the automatic right to obtain a permanent injunction. In other words, the norm was that “a permanent injunction should be issued when infringement was proven” (Court, 2006). Exceptions to this rule were quite uncommon and mostly due to reasons of public interest.

The availability of a quasi-automatic injunction grants a lot of power to plaintiffs in IP negotiations (Hall and Ziedonis, 2001). Experts have criticized this feature of the law arguing that the presence of automatic injunction exacerbates the hold-up problem during the negotiation between firms involved in litigation (Shapiro, 2016b). In particular, the view was that the ability to leverage on an injunction threat may allow the plaintiff to obtain transfer of resources that exceed the value of the disputed technology, either before or during a formal court proceeding. In the context of intellectual property, the hold-up problem is particularly concerning because technologies tend to be characterized by high complementarity. Therefore, even an injunction granted for a relatively small violation can deeply impair a company’s operations. Furthermore, the high uncertainty characterizing the patent system may exacerbate this issue. In fact, the discovery process in IP can be long and costly, and cases of involuntary infringements or false positives in court decisions tend to be common (Lemley and Shapiro, 2005). In this context, even when a lawsuit is based on relatively weak claims, the threat of injunction may force the defendant into costly settlements to avoid an uncertain court procedure.\(^10\)

The RIM vs. NTP case discussed in the introduction represents a very clear example of how an injunction can magnify the cost of patent litigation. First, although the dispute involved only a few patents, the settlement

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\(^{9}\)I provide some background legal information about the “eBay v. MercExchange” case in Appendix (A.1). More discussion on the background of the case and its policy implication can be also found in Mezzanotti and Simcoe (2019).

\(^{10}\)One interesting quote can be found in the analysis of the case in Wesenberg and O’Rourke (2006): “In determining whether to settle a case, a market participant must consider many factors, including (1) the expense of litigation, (2) the potential exposure, and (3) the threat of an injunction forcing the company to either terminate a product or excise a component or part from a larger product, at potential prohibition, cost or delay. Oftentimes, it is this final threat of injunctive relief that forces the market participant to settle. As a practical matter, certainty trumps justice and accused defendants agree to pay an exorbitant license fee for a questionable patent and continue to operate rather than risk discontinuing a product or operations altogether.”
was more than $600 million, almost half of RIM’s previous year revenue. This high settlement is explained by
the fact that a likely injunction would have forced RIM to completely block its Blackberry sales, increasing the
chance of bankruptcy for the firm. Second, RIM was forced to settle despite the fact that most of the NTP
claims were eventually found to be invalid. This invalidity was impossible to prove in court at the time of
the litigation. Altogether, NTP’s ability to leverage on the near-mandatory injunction was the main driver to
obtain the large settlement.

This argument – which links some of the distortion in the litigation market to the presence of automatic
injunction – was prevalent among academics (e.g., Bessen and Meurer, 2008a), practitioners, and legal experts.
For example, the American Innovators Alliance, an association of high-tech companies, claimed that, because
of automatic injunction, “money that could go to productive investments is instead diverted to legal fees
and settlement payments,” therefore having “profound implications for technological innovation in the United
States.”11 This view was also expressed by the Supreme Court in the motivation of the ruling. For instance,
Justice Kennedy wrote that the threat of injunction has been extensively used “as a bargaining tool to charge
exorbitant fees to companies that seek to buy licenses to practice the patent.” This quote is in line with the
evidence that parties accused of aggressively asserting their patents – for instance, the patent assertion entities
(PAE) discussed later – were actively using the threat of permanent injunction as a way to scare counterparties
and therefore obtain larger settlements (Lemley and Shapiro, 2006).

The ruling “eBay v. MercExchange,” which was made public on May 15, 2006, changed the landscape
by shifting negotiation power away from plaintiffs (e.g. Bessen and Meurer 2008a; Shapiro 2010, 2016a; Tang
2006; Venkatesan 2009). Specifically, the decision stated clearly that the issuance of an injunction should not
happen automatically. Instead, courts should decide on a case-by-case basis, using a four-factor test balancing
“the hardships between plaintiff and defendant” (Court, 2006). In practice, the eBay case started a new hybrid
system in which monetary damages could be used instead of an injunction to remedy violations. In other words,
the court recognized that a “damages award is sometimes sufficient to maintain incentives while preventing
patentees from amassing disproportionate rewards, significantly injuring the public, and stifling innovation”
(Carrer, 2011). In the context of the policy debate, the decision was perceived as an attempt to remove some
of the distortions that characterized the system, however leaving injunction as an option when this is the only
way to remedy a violation.

One important step is to understand the effectiveness of this decision is to examine its impact on patent
enforcement, in particular regarding the use of injunction. Quantifying this effect is challenging, because of
the obvious selection issue. In fact, the decision did not only affect how courts will make decisions, but it
also changed the balance of costs and benefits to file a lawsuit. Despite this limitation, three stylized facts are

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11 American Innovators Alliance is a lobby group that represents large tech firms, such as Microsoft, Micron, Oracle, and Intel. The sentences are taken from the “amicus curiae” that the group submitted for the Supreme Court case. Similar quotes can be found in the “amicus curiae” submitted by the Computer & Communication Industry Association (CCIA): for instance, they claim that automatic injunction did “produce anti-competitive behavior, foster more litigation, and undermine innovation.”
identified in the literature. First, the ruling in aggregate substantially reduced the likelihood of obtaining an injunction. For instance, Chien and Lemley (2012) find that the likelihood of obtaining an injunction declined by about 25%.\footnote{Similar results are also provided in an earlier empirical analysis in Grumbles III et al. (2009).} Since firms appear now less likely to seek an injunction in the first place (Gupta and Kesan, 2015), this estimate may be considered a lower bound of the actual effect. Second, despite this decline, injunction is still a valuable tool for companies seeking protection from patent violations. In fact, injunctive reliefs still granted in the majority of cases. Third, the drop in the injunction rate is mostly driven by cases that are more likely to be motivated by the strategic and opportunistic reasons. For instance, Seaman (2016) finds that injunction rates decline across all categories of plaintiffs, but this reduction is much larger when the two parties are not competitors or when the case involves a non-practicing entity. In principle, this evidence is consistent with the idea that the policy was able to reduce the risk of litigation, without however completely removing injunction as a remedy against real violations.

Therefore, the eBay decision led to a significant shift of bargaining power from plaintiff to defendants in both court cases and out-of-court negotiations (Shapiro, 2016b). Consistent with the reduction in plaintiff’s power, firms heavily involved in litigation activity have tried to change their strategies to try to limit the impact of this change on their bargaining power. For instance, Chien and Lemley (2012) find that after the eBay ruling companies started to become more active in bringing claims in front of the International Trade Commission (ITC), which – in some cases – could still issue injunctions. At the same time, Cohen et al. (2016a) discuss how firms, to make their claims more credible, increased their likelihood of filling a lawsuit rather than simply issuing demand letters.\footnote{This hypothesis may explain why the number of lawsuits kept increasing after the eBay ruling. Another proposed explanation is that defendants after eBay were less concerned with going to court and therefore became less likely to settle ex-ante.} The previous discussion in the literature – also consistent with a revealed preference argument – suggests that these changes could not undo the shift caused by eBay. Our evidence on NPE returns will corroborate these claims. However, our analyses – looking at the effect of the reform net of any strategic response – will be able to shed light on this issue.

### 2.2 Hypothesis development

Given the discussion from the previous section, it is clear how the shock led to a significant reduction in the bargaining power of plaintiffs in litigation. However, the court ruling’s effect on innovation is less obvious ex-ante. For a firm, this shock to enforcement can have two effects. On the one hand, limiting the ability of a plaintiff to hold-up a defendant in litigation implies a reduction in the cost of litigation (Shapiro, 2016b,a).\footnote{As discussed in Shapiro (2016a) injunction could lead to an excessive compensation of the patent holder both during ex-post (litigation) and ex-ante negotiation. Since both negotiations are strictly tied in practice, the language of the paper refers to both of them as being part of the “litigation channel.”} In turn, this shift should increase firms’ incentive to innovate and also allow a company to transfer more resources from the defensive activity into R&D.\footnote{Importantly, this effect does not necessarily imply that the number of lawsuits should go down, as discussed before. In fact, the number of lawsuits is an equilibrium outcome and therefore also depends on the willingness of the accused firm to settle versus}
to deter possible violations (Epstein, 2008; Holte, 2015) and, as a result, lower appropriability. Even if injunction were still available to firms facing infringements, the level of ex-ante deterrence perceived by the firms may still be lower than before. This alternative channel would lower the returns from innovation, and therefore induce firms to invest less.

In light of this discussion, it is clear that the overall effect is ex-ante ambiguous. The evidence on the changes in injunction rates discussed before provides some guidance for thinking about this problem. However, it is not sufficient to evaluate the full impact of the decision. In this context, the only way to evaluate the policy is to test how firms actually responded to the change in incentives. This analysis will inform us about how a change in patent enforcement – which effectively reduced the rights of patent owners – would affect the innovation activity. Furthermore, this type of analysis can provide important insights on how the risk of patent litigation can distort firm innovation.

Following most of the empirical literature in this area, the paper will start by measuring innovation activity at the firm level using patent application counts. Patents provide a multidimensional measure of innovation activity in both private and public firms and can be used to identify shifts in the quality of innovation (Lerner and Seru, 2015). However, a drawback in using patents is that this measure does not allow us to directly distinguish the impact of the shock on innovation from a shift in the incentives to file patents. In particular, one concern is that the count of patent applications may confound an increase in defensive activity with an increase in innovation. This result is particularly relevant in this case, since previous research looking at the semiconductor industry in the 1990s found that an increase in hold-up can increase firms' incentive to patent for defensive reasons (Hall and Ziedonis, 2001). Therefore, looking at patent counts in isolation may be problematic.

Because of these concerns, the paper will also explore innovation across several other dimensions. First, for the sample of public firms, I will explore the effect of the decision on R&D expenditure as well. Second, this study will examine the effect of the decision on the quality of patenting. Along this dimension, a standard model of innovation and patenting should provide different predictions depending on the firms' motives. In particular, if a higher propensity to patent caused the increase in patenting, I expect the quality of the output to decrease after the ruling, since the marginal project should be worse than the average patent. The same result should not be true if the increase in patenting is caused by more genuine innovation. Third, given the specific concerns, I will directly examine the impact on strategic patenting. If the increase in patenting were to be explain by more defensive activity, then the share of strategic patenting should actually increase. The same should not be the case otherwise. While none of these tests may be perfect, taken together they provide a great overview of the overall effect on innovation. In the last part, I will try to exploit this setting to provide

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16 While an increase in patenting may still have some positive effect -- e.g. Hegde and Luo, 2017 for the role of disclosure -- these benefits are likely to be much lower than those caused by an actual increase in innovation.
valuable insights into channels through which patent enforcement can foster or hinder innovation.

2.3 The economic importance of the decision: the case of NPE

Previous discussion presents the shock as a reduction in the bargaining power of plaintiffs in litigation. In this section, I provide evidence consistent with this hypothesis by examining the stock returns of a set of public PAEs. In particular, I find that the ruling led to a drop of about 10% in the stock price of these companies.

Following the literature (Cohen et al., 2019; Feng and Jaravel, 2015; Kiebzak et al., 2016; Tucker, 2014), I identify PAEs looking at nonpracticing entities (NPEs), which are companies that generate most of their revenue through licensing and settlement fees rather than from manufacturing.\(^\text{17}\) This setting is a useful laboratory for several reasons. First, previous research has confirmed NPEs extensively used injunction threats when negotiating licensing agreements or settlements (Chien and Lemley, 2012). Therefore, the ruling should have somehow harm their business model. Second, unlike for other companies, automatic injunction does not constitute a major risk for these firms because they generally do not directly use intellectual property to develop products or sell services.

Therefore, if the ruling had a big impact on patent enforcement, I expect NPEs to be negatively affected by the decision. In particular, I test this hypothesis by looking at the stock market returns of public NPEs around the time of the ruling. The main challenge in this type of analysis is that most NPEs are private. For instance, “Intellectual Ventures” – allegedly the largest NPE today – is a private firm. I start by combining two lists of NPEs, provided respectively by PatentFreedom, one of the most important firms in assessing NPE risk and now owned by RPX, and by EnvisionIP, a law firm involved in strategic IP consulting.\(^\text{18}\) Then, I identify the firms in these lists for which returns information is available in CRSP around the date of the event. This analysis yields a final list of ten companies.\(^\text{19}\)

Studying the returns of these companies around the decision, I identify four important stylized facts.\(^\text{20}\) First, on the day of the decision these firms experienced a drop in stock price of 3.3% – 3.8%, depending on whether I look at raw returns or abnormal returns. These effects are highly significant, with the Sharpe ratios ranging between 4.08 and 4.75. Second, firms suffered negative returns also in the couple of days before the decision (Figure 2). While the largest one-day drop occurred the day of the Supreme Court ruling, these stocks also lost value in the three days before it. Examining the abnormal returns with respect to the S&P500, the firms lost 6.3% (\(t = -4.53\)) on average the week before the ruling. One explanation for this result is that investors,

\(^{17}\)Not every NPE can be accused of acting like a “patent troll.” For instance, universities and other research institutions are in the NPE category. By the same token, not all the abusive behavior is specific to NPEs.

\(^{18}\)The first firm published a list of top NPEs active in the USA at 2014 (https://www.patentfreedom.com/about-npes/holdings/), where companies were selected based on number of patents held. The second instead published a study on stock returns on NPEs in 2013, using both public and private information for compiling a list of NPEs that are publicly traded (http://patentvue.com/2013/04/15/508-publicly-traded-patent-holding-companies-yield-impressive-returns/).

\(^{19}\)The majority of the companies appear in both list - six, and only one company is only listed by PatentFreedom. The companies are Acacia Technologies, Asure Software (formerly Forgent Network), Rambus, Tessera Technologies, Universal Display, Document Security Systems, ParkerVision, Unwired Planet (formerly Openwave), Interdigital, and Spherix.

\(^{20}\)More information about the analysis can be found in Appendix (A.3.3). One caveat of the data set is that it is compiled based on a recent list; therefore, I may have missed an NPE that was active and public in 2006, but defunct today. While I cannot exclude this possibility, I could not find any example of this phenomenon in the data.
anticipating the arrival of news regarding the case, started to require a premium to hold these stocks until the
day of the decision. Third, I find that the drop is not capturing a negative trend in the data. When I consider a
month or two months before the ruling – excluding the five trading days before it – I find no out-performance of
this group of firms with respect the benchmarks (Table A.6). Finally, these negative effects do not revert back
in the days following the decision. Even if the largest negative returns are experienced in the day in which the
news became public, the portfolio continues to experience negative returns for the following month, reaching
the bottom in mid-June. Overall, these results hold when using alternative models (Figure A.4).

In summary, these facts confirm that public NPEs suffered a great deal around the Supreme Court decision.
In particular, the shock led to a large drop in market value, which did not revert back in the weeks that followed.
The results are robust to the removal of each of the NPEs considered in the sample.\textsuperscript{21} Overall, this evidence
demonstrates that the ruling was a critical event in patent enforcement and greatly affected the players in
this market. Furthermore, these results confirm that the decision was not completely anticipated by market
participants.

\section{Data}

To estimate the impact of the “eBay v. MercExchange” Supreme Court decision on corporate innovation, I
compare innovative activity across firms that were differentially affected by the decision. In the first part of the
paper, I proxy innovation with counts of granted patents, where the timing is defined based on the application
date. This measure allows me to observe innovation for a large sample of both public and private companies.
The data come from the Fung Institute (University of California at Berkeley) patent data set, which is an
updated version of the Harvard Business School Patent Network Database (Li et al., 2014) used extensively in
literature. These data contain complete information on all patents granted between 1975 and 2014 and contain
a new disambiguate assignee ID which I use to identify a firm across different patents.\textsuperscript{22} In most of the analyses,
I focus on a sample of more than sixteen thousand firms active in patenting around the time of decision.

I also supplement the patent data with balance-sheet information from Compustat. I match Compustat
to patent information using a procedure that takes advantage of the recent data from Kogan et al. (2012). In
short, I link one or more identifiers in the patent data to one Compustat identifier using a patent level matching.
Since patent numbers are easy to match, this approach greatly reduces the probability of errors and missing
information. After applying the standard filters,\textsuperscript{23} I am left with a sample of more than one thousand public
companies active in innovation around the decision and with R&D information at the quarterly level. Lastly, I

\textsuperscript{21} For instance, the average return the day of the decision is -3.4\%. When dropping one company at the time, I get results
between -2.97\% and -3.75\%. In all cases, the result is 1\% significant.

\textsuperscript{22} Almost all the analyses are run with applications made by the end of 2008, therefore allowing more than the five years
recommended by Dass et al. (2015) to eliminate risk of truncation bias.

\textsuperscript{23} I consider firms in non-financial and non-regulated industries, headquartered in the USA, not involved in financial restructuring
and with information reported in the quarterly Compustat data. More details are available in the Appendix (A.3).
match these firms to CRSP using the standard Compustat-CRSP bridge file. In the Appendix (A.3) I provide more details on the data construction and matching.

As stated earlier, the main measure of innovation activity employed in the paper is based on the simple count of patents applied for by a firm in a specific period. I focus on the application date because this is closer to the time of the actual invention. When I focus on public firms, I supplement patent-based innovation measures with R&D intensity data, constructed as quarterly R&D expenses scaled by total assets of the firm (e.g. Mann, 2018). In the end, patent data are also used to construct a variety of measures of patent quality, which are discussed in the paper as they are used.

Furthermore, I use patent data to generate firm-level control variables. For every firm, I construct an industry classification based on the major (large) technology class in which the firm patents during the four years around the time of the decision (Hall et al., 2001). I use the addresses reported in the patent application to identify the state of location of the firm. In addition, I construct a proxy for firm age by looking at the time at which a firm first applied for a patent (“start-up”), and a proxy of patent portfolio size by counting the number of patent applications in the two years before the estimation window.

Table 1 reports the summary statistics of the main variables used. On average, the firms in the sample applied for almost 10 (granted) patents per year over the window considered. These numbers are large but they are justified by the fact that I focus most of the analysis on a subset of firms that are highly active in patenting around the time of the decision. In terms of citations, they receive an average of one citation per patent, where the number of citations is adjusted for technology-class and year. As expected, innovative public firms appear to patent more than the average firm in the full data set – around 50 patents per year – and they have on average quarterly R&D expenses of roughly 3% of their assets.

4 Empirical setting

4.1 The framework

The objective of my study is to examine how the Supreme Court decision “eBay v. MercExchange” affected the innovation of corporations. In principle, every firm patenting in the US has been affected by this legal change, and therefore there is no straightforward control group in this experiment. However, the shock should not have affected every firm in the same way. In particular, firm exposure to patent litigation should represent an important factor in determining whether the ruling was significant for a company. Firms operating in technology areas where patent litigation was non-existent should be essentially unaffected by the decision. For the same reason, the ruling was instead very salient for firms that innovate in high litigation technologies.

24This term “start-up” is likely not particularly accurate to describe the variable. To make sure readers will understand what this captures, I provide a clear definition of this variable (and the others) in each table.
Following this logic, the paper exploits variation in the intensity of the treatment – measured by the extent to which a firm was exposed to patent litigation at the time of the Supreme Court decision – to identify the effects of the decision. In this framework, firms with little or no exposure to litigation, which supposedly were not affected by the shock, provide a counterfactual for firms that were instead highly exposed to litigation. The key advantage of this approach is that it does not impose any restriction on the effect of the ruling on firms. In fact, firms more exposed to patent litigation will benefit from the decision because of a reduction in litigation distortions but will also be hurt because of the potential reduction in deterrence. The estimates will provide evidence regarding the overall net effect of the different channels.

This design is equivalent to a difference-in-difference model, where I study how innovation changed as a function of the exposure to the shock. In other words, I estimate:

\[ y_{jt} = \alpha_j + \alpha_t + \beta(\text{Exposure}_j \cdot \text{Post}) + \gamma_t X_j + \epsilon_{jt} \]  

where \( y_{jt} \) is an outcome of firm \( j \) at time \( t \), \( \text{Post} = 1\{\text{time > decision}\} \), \((\alpha_j, \alpha_t)\) is a set of firm and time fixed effects, and \( \text{Exposure}_j \) is the index of exposure to litigation, which is discussed in next section. For robustness, I can augment the specification with a matrix of controls \( X_j \). As I discuss later, the controls are a set of firm-level characteristic measured before the decision which are interacted with time dummies to allow them to have differential effects before and after the decision (Angrist and Pischke, 2008; Gormley and Matsa, 2014).

When it is not specified otherwise, I estimate this equation over a four-year window, considering the two years before and after the announcement of the Supreme Court decision on May 15, 2006.\(^{25}\) To facilitate the interpretation of the different margins and in line with the literature (Bertrand et al., 2004), I run my main results collapsing the data in one observation before and one after the decision. For instance, when looking at patenting, the outcome is the total number of applications in the windows before and after the shock.\(^{26}\) This choice does not affect in any way my results – indeed I will also show the results using the full panel dimension when presenting the estimate quarter-by-quarter – and it has the advantage of allowing me to focus on intensive and extensive margin separately. For consistency, the standard errors will be clustered at firm-level across all the analyses.\(^{27}\)

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\(^{25}\)In tables and figures dates are usually reported in terms of quarters (e.g. 2006Q1): these quarters are constructed in event time, where I artificially set the end of the first quarter of the year at May 15. The other quarters are then constructed consistent with this.

\(^{26}\)In the text, I will discuss case by case the definition of the outcome used.

\(^{27}\)As expected based on the literature (Bertrand et al., 2004), clustering the errors does not have a material impact when the sample is collapsed in two periods (pre and post), but it is important when presenting the result as dynamic effect and therefore using the panel at quarterly frequency.
4.2 Measuring exposure of litigation at the firm level

While most of the previous literature has studied the determinants of litigation at patent level (e.g. Lanjouw and Schankerman, 2001), a crucial component of my identification relies on measuring exposure to litigation at firm-level. Intuitively, a firm is more exposed to patent litigation if it operates in a technology area where patent litigation is more intense. For instance, companies that operate in software or drugs, where IP lawsuits are more frequent, will be more concerned with patent litigation than companies doing mechanical research, where litigation is much less intense. Therefore, one potential approach is to measure a firm’s exposure to litigation by looking at the absolute level of litigation in the area in which it undertakes R&D. This approach takes advantage of two features of the patent system. First, there is a lot of variation across technology fields in the intensity of patent litigation. This is true both across major technology areas – for instance between “Communications & Computer” and “Chemicals” – and within the major technology fields. Second, many companies operate across different technology fields (Bessen and Hunt, 2007). This fact implies that even firms that operate in relatively safer areas may still be influenced by litigation because of a subset of the patent portfolio.

Formalizing this intuition, I can express the exposure to patent litigation of an individual firm $j$ as a function of two quantities: (1) the technology fields $i$ in which the firm $j$ operates, defined by a vector $t(j) = [\sigma^j_i]_{i=1}^T$; and (2) the distribution of the patent litigation activity across different technology fields $i$, which is defined by a vector $p = [p_i]_{i=1}^T$. In particular, I can define $t(j)$ as a vector whose entries $\sigma^j_i$ are the share of firm $j$ patents across the different technology fields $i$. Therefore, firm $j$ exposure to litigation $Exposure_j$ can be constructed by weighting the litigation risk in each technology field by the share of activity that firm $j$ has in each of these fields. This is:

$$Exposure_j = \sum_{i=1}^T \sigma^j_i p_i$$

(2)

with $Exposure_j \in [\min(p), \max(p)]$.

While the variable $Exposure_j$ is intrinsically unobservable, its components – $t(j)$ and $p$ – can be constructed from the data. First, I use patent data to measure $t(j)$, the technology space where the company operates. The USPTO categorizes each patent across more than 400 technology classes, therefore providing a very precise and narrow definition of technology. Using this classification, I construct $\sigma^j_i$ as the share of granted patents of firm $j$ in technology class $i$ that were applied for before 2006.\footnote{For instance, if a company operates in four technology classes with two patents granted in the each of these classes, then the vector $t(j)$ will be equal to zero for every technology class where there were no patents and equal to 0.25 for the four technology classes where the company patented something.}

Second, I estimate the distribution of patent litigation across technology fields – the vector $p$ – using litigation data from WestLaw, a subsidiary of Thomson Reuters (e.g. Lerner, 2006, Lanjouw and Schankerman, 2001).\footnote{One of the advantage of WestLaw is that this data goes back to 1980, unlike other sources. For instance, RPX - another leading data source used for research in this area (Cohen et al., 2019) - generally provides data on litigation starting from 2005. The same data is also known as Derwent LitAlert data. The data were accessed through the online tool LitAlert14}
Using all filings involving IP between 1980 and 2006, I extract all the patents that were asserted by the plaintiff and then use this information to construct a proxy for \( p \). After some preliminary data cleaning, this corresponds to more than thirty thousand fillings, with the number of cases per year increasing over time (Figure 1). Similar to Kiebzak et al. (2016), I reshape the data at defendant-plaintiff-patent level to make cases comparable across filings.\(^{30}\) I then measure the size of the litigation in each of the USPTO technology classes by computing the number of patents in a specific class involved in the litigation, normalized by the total number of patents litigated. In other words, my index is:

\[
p_i = \frac{100 \sum_{c \in \text{cases}} \#\text{Patents}_i^c}{\sum_{i \in \text{Tech.
Classes}} \sum_{c \in \text{cases}} \#\text{Patents}_i^c}
\]  

where \( i \) defines one of the USPTO technology classes, and \( c \) is a specific filing. In line with the previous evidence, patent litigation is not equally spread across technology classes, but rather tends to be more concentrated. For instance, the top 50 technology classes in terms of litigation account for half of the patent level litigation (Table A.7).\(^{31}\)

I estimate \( \text{Exposure}_j \) by combining these two measures as in equation (2). My preferred measure uses litigation data and patents in the five years before the Supreme Court decision. As expected, the distribution of the score is skewed and some areas, such as “Drug” and “Computer and Communication,” have a larger share of highly exposed firms (Figure 3). However, even within this major industry there is a relatively large variation in litigation exposure. Indeed, I will show that my results are similar even when I control for this main industry effect.

This way of measuring exposure to patent litigation has three important advantages. First, this score can be calculated for every firm that is active in patenting using existing data, and its computation is relatively simple. Second, the measure is exogenous to firm \( j \)'s strategies in litigation. Unlike other approaches, this measure does not depend on the actions that firms take regarding litigation, but only on the area in which a firm operates. Third, the fact that litigation across technologies is highly persistent over time (Figure A.5) suggests that this measure does not simply reflect some heterogeneity in technology shocks in the years before the Supreme Court decision, but rather some structural characteristic of the field.

However, the validity of my approach relies on the assumption that the score captures relevant heterogeneity in exposure to litigation across firms. In general, the fact that I will find that exposure predicts a change in R&D behavior around the shock already suggests that this approach is capturing information that is relevant to http://intranetsolutions.westlaw.com/practicepages/template/ip_litalert.asp?rs=IPP2.0&vvr=1.0

\(^{30}\) First, each filing may contain multiple defendants. Firm A suing firms B and C in the same filing should carry more weight that Firm A suing only firm D. Second, each filing may contain more than one patent, because in the same case the plaintiff may sue the defendant over multiple technologies. In order to address this, I reshape the data at the single defendant-plaintiff-patent level.

\(^{31}\) Qualitative inspection also provides supportive evidence, as I find technology classes that are expected to have high level of litigation to actually be on the top of the ranking. For instance, at the top of the ranking, I find the two main classes for drugs (514, 424) and two of the prominent classes for communications technologies (379, 340), plus business method (705) and one electronic class covering illumination technologies (362).
understand the impact of the decision. However, to provide more direct evidence in this direction, I examine the stock market reaction of innovative firms around the announcement. Given the previous NPE result (Section 2.3), it is clear that the stock market thought that the patent ruling represented significant news for innovative firms. Therefore, we should expect to find a systematic correlation between this measure and stock returns of innovative firms around the event.

I explore this issue by measuring returns and abnormal returns around the Supreme Court announcement and then correlating these measures with the litigation exposure score (Katz et al., 2017). The main result of the analysis can be synthesized by Figure (4), which plots the cumulative value-weighted returns of high and low exposure firms, where the split is made at the top 25% of the litigation distribution. I find that the two groups behave in the same way in the days before the ruling. However, the day of the decision, the high-risk group outperforms the low-risk group by almost 1%. This initial out performance does not revert immediately afterward. The same results hold in a formal regression analysis (Table A.1). Appendix (A.4.1) contains a more detailed discussion of these results. These analyses suggest that our score captures significant exposure to the ruling. Furthermore, the effect appears to be positive for innovative companies. As I discuss later, this effect is consistent with the rest of evidence presented in the paper.

5 The effect of the Supreme Court decision on innovation

This section contains the main results of the analysis. I start by showing that the Supreme Court decision positively affected the ability of companies to patent new technologies. Next, I discuss the main identification assumption – in particular the parallel trend assumption – and I provide further evidence that confirms the quality of my model. Lastly, I examine the effect of the decision on the quality of innovation and on R&D intensity for public firms.

5.1 The effect on innovation output

I begin my analysis by exploring how the decision affected innovation output, measured by the count of granted patents using the application date as time reference of the patent. In particular, I construct two outcomes using this data. First, I look at $\ln(pat_{jt})$, which is the logarithm of the total number of patents that firm $j$ applied for during time $t$ (intensive margin). In order to keep the panel balanced and therefore estimate a purely intensive margin, I estimate the model using every firm in the patent data that applied for at least one patent before and

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32 To the extent that Exposure$_j$ captures just a very noisy measure of litigation, I expect measurement error to bias the results towards zero. Therefore, at the extreme, measurement error should push us towards finding no effect.

33 As discussed in detail in Appendix (A.4.1), I repeat the same analysis on the day in which the Supreme Court decided to hear the case (November 28th, 2005) and at the oral hearing (March 29, 2006). While the decision to hear the case is not associated with any significant response, the oral argument is associated with negative outperformance of firms more exposed to litigation. The magnitude of this negative effect is around one-half of the size of the positive outperformance at announcement. This effect seems to be consistent with the idea that eBay did not come out as a clear winner from the oral argument, therefore confirming that the outcome of the decision was unexpected.
Second, I examine an alternative outcome variable: a dummy equal to one when the firm has applied for any subsequently granted patent in the period, $1\{Patent_{jt} > 0\}$ (extensive margin). In this case, the sample contains every firm that applied for at least one patent in the five years before the Supreme Court decision, which is a minimal requirement to construct the measure of litigation exposure.

Table (2) starts presenting the results by estimating the baseline version of equation (1). Looking at both the intensive (column 1) and extensive (column 4) margins, I find that firms that were operating in more litigious areas increased their patent-application relatively more. These effects are not only statistically significant, but also economically relevant. A one-standard deviation increase in the exposure to litigation leads to a relative increase in patent applications of 3%. Comparing these estimates to the patenting baseline, this effect corresponds to an increase of almost one additional patent for innovative firms (0.7). Similarly, a one-standard-deviation increase also implies a 0.8% increase in the probability of patenting, which is a 2% increase relative to the baseline probability over the whole period. This result suggests that removing the threat of automatic injunction did not discourage firms from filing patent applications. If anything, those firms that were more likely to be affected by the new rules saw a relative increase in patenting activity. In particular, this evidence seems to be consistent with a “catch-up” mechanism, where firms were able to close part of the gap caused by litigation costs after the change in enforcement.

The causal interpretation of the difference-in-difference approach relies on the parallel trend assumption. In this case, the assumption requires that the relative behavior of high- and low-exposed firms would have not changed without the Supreme Court ruling. As a first test in this direction, I examine the dynamic of patenting activity in the months before and after the decision. In particular, I use patent data at quarterly frequency and I estimate the time-varying effect of exposure to litigation on patenting relative to the last quarter before the decision:

$$y_{jt} = \alpha_j + \alpha_t + \sum_{\tau=-8}^{8} \beta_{T-\tau} Exposure_j + \epsilon_{jt}$$

(4)

Consistently with the parallel-trend assumption, I expect to find that: (a) the positive effect appears only in quarters after the Supreme Court decision ($\beta_t > 0$); (b) before the decision, the changes in patenting behavior are orthogonal to the measure of exposure ($\beta_t = 0$). For completeness, I estimate this equation using a log-plus-one specification, which allows me to look at the effect at both the intensive and extensive margins. These results are presented in Figure (5): firms characterized by different exposure to litigation did not have a differential pattern of patenting before the Supreme Court decision. The estimated $\beta$ in this period is always small in size and statistically non-different from zero. However, after the Supreme Court decision, firms that

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34 In particular, in the reported table, I require the firm $j$ to have applied for at least one granted patent in the two years before and in the one year after. This choice is motivated by the fact that I want the sample in this table to be equivalent to the one I use in one of the next sections, where I estimate the same equation over different periods, from one to three years after. Results are unchanged if I consider the set of firms with at least one patent in the two years before and one in the two years after.
were more exposed to litigation increased their rate of patenting more. In particular, the effects turn positive already within a few quarters and keep rising afterward. These results are overall comparable with those in the previous regression model, confirming that choice of collapsing the data in the main model does not affect our results.\textsuperscript{35} As I discuss later, I confirm the same results looking at other metrics, like innovation quality and R\&D investments (Figure A.6 and Table A.5).

The analysis of the pre-trend provides a first glimpse into the timing of the effect, which is discussed more extensively in Appendix (A.4.2). Overall, there are three results to highlight. First, the effect is increasing over time, consistent with the idea that incentive changes will affect output with a lag. Relative to one year after the decision, the effect over two years increases by 38% and over three years by 50% (Table A.3). Second, while on average I find some response within one year, this short-term response is driven by companies operating in “Computer and Communications” technologies (Hall et al., 2001) (Table A.4). This result is reassuring because these technologies tend to have a much faster R\&D cycle than other areas, for instance drugs, and therefore they should respond first. Third, the effect does not appear to be short-lived. In Figure (A.1), I replicate the same dynamic plot using data on patents up to 2010, showing that the effects discussed before are still economically and statistically significant essentially five years after the decision.

Another way to provide evidence consistent with the parallel trend assumption is using placebo tests, where I replicate my analysis in periods where there is no change in the rules.\textsuperscript{36} The idea is again to show that - absent a large shock to enforcement like eBay - exposure to litigation does not predict differential changes in patenting. In order to avoid arbitrarily choosing a period in which to run the placebo, I consider as the fictional shock period every quarter in the closest two years before the shock and such that the post-period does not overlap with the post-treatment period (2002Q2-2004Q1).\textsuperscript{37} Figure (6) presents the results of this analysis by plotting the $\beta$ from the intensive margin regression and its 95% confidence interval for each quarter considered as the fictional shock. As expected, the coefficient is never positive and significant. In other words, in periods where there is no major shift in the patent enforcement law, I do not find that firms operating in high-litigation fields increase innovation more than firms in low-litigation fields. If anything, the coefficient actually tends to be negative in sign, but the size is always small and never statistically different from zero. As I discuss later, the same result holds for R\&D spending.

\textsuperscript{35}As an alternative to the previous analysis, I estimate the trends in the model by assuming that the relationship between exposure to litigation and patenting is linear. I essentially estimate $y_{jt} = \alpha_j + \alpha_t + \beta^{PRE} R_{jt} \cdot Pre + \beta^{POST} R_{jt} \cdot Post + \epsilon_{jt}$. The excluded period in this case is the quarter right before the decision, and therefore the two coefficients should be interpreted as changes relative to that quarter. While this approach is less flexible than the previous specification, it allows me to obtain more precise estimates of the trends and therefore to rule out that the lack of a pre-trend may have been due to a lack of power. As expected, exposure to litigation does not predict differential changes before the decision, but only after (columns 1 and 2, Table A.5).

\textsuperscript{36}In other words, I estimate the same model in equation (1) but center the analysis in a quarter where there is no change in patent law. In order to do so, I reconstruct the outcomes and regressors as if the shock occurred right after the quarter of interest.

\textsuperscript{37}Clearly, after 2004Q1, the post period of the placebo analysis would overlap with the post-treatment period. Because of this, a similar placebo centered after 2004Q1 would not be a true placebo, because the estimated parameters would capture part of the treatment effects. Furthermore, the closer I come to 2006Q1, the more my analysis would look like the main results. Consistent with this, I find that post 2004Q1 the $\beta$ starts converging towards the main results in Table (2). As expected, the convergence is smooth and the effects turns positive and significant at 95% only at the end of 2005.
This detailed discussion of pre-trend and placebo tests provides strong evidence in favor of the parallel trend assumption. However, these tests cannot fully exclude the presence of a shock contemporaneous to the ruling that was correlated positively (negatively) with exposure to litigation and positively (negatively) affects innovation. In this context, the main concern is the presence of technology shocks in highly litigated areas. To exclude this possibility, I augment my model with industries by time fixed effects, where industries are defined based on the main technology category within which they fall, as previously discussed (Hall et al., 2001). This set of controls removes from the data any technology trend, comparing patenting by firms with different levels of exposure to litigation within the same industry. The results – reported in columns (2) and (5) of Table (2) – show a relatively small change with respect to our main findings. In particular, at the intensive margin, the change in the estimated coefficient is minimal and this difference is not statistically different from zero. At the extensive margin, the inclusion of this control instead significantly increases the magnitude of the effects. Therefore, while industry dynamics could be important in explaining patenting behavior around this period, they do not seem to drive my results.

However, the presence of contemporaneous shocks may also materialize in other aspects of economic activity. For instance, local economic factors may be a concern to the extent that there is geographically clustering of firms that are similarly exposed to litigation. To deal with these concerns, in columns 3 and 6 of Table (2), I augment the previous specification with an extra set of firm-level controls in every case interacted with time dummies. To directly tackle the concern of geographical clustering, I consider among my controls the location of the firm’s R&D facilities - based on state of operation where I find the most patents before the decision. Furthermore, I also add controls for the size of the portfolio of the firm, measured by the number of patents published in the years before the decision, but outside the estimation window; quality of portfolio, measured by the average number of citations before the decision; and a dummy for firms that patented for the first time in the three years before the decision. In general, the addition of these extra controls do not significantly change my estimates. In Figure (A.2), I also show that the pre-trend analysis is qualitatively identical when I also add these controls interacted with post-dummy.

In terms of contemporaneous shocks, in Appendix (A.2) I also argue that our results are not explained by presence of other legal changes around the same time as eBay. In general, the federal law was stable during the period analyzed. Furthermore, the other Supreme Court decisions involving innovation are unlikely to have an effect in our setting. In fact, the scope and importance of other rulings were generally more limited than eBay. On top of this, the timing of our effects are also inconsistent with the impact of other important

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38 The z-score on the difference is small, around 0.29.
39 For consistency with the rest of the measures, I look at the patents applied for between four and two years before the decision.
40 This figure is constructed using the longer sample, but it is qualitatively identical using the same period as the main analyses. It is interesting to notice that the dynamic of the effect with and without controls are qualitative identical. The main difference is that the result with controls is characterized by slightly larger magnitude and more precise estimates.
41 One potential exception was the Medicare reform of 2003, which may have influenced the pattern of innovation, at least for healthcare related technologies. However, as discussed in Appendix (A.2), the timing of this reform would be inconsistent with our results, as the impact of Medicare reform appeared already much earlier than 2006 (e.g. Krieger et al., 2018).
Supreme Court decisions. Appendix (A.2) contains a thorough discussion on these issues. As a final step, I show that the results are also robust to three extra tests. First, I implement a simple permutation test (Chetty et al. 2009; Fisher 1922). As discussed in Appendix (A.4.3), this test allows me to provide inference based on weaker assumptions than the standard linear model and to rule out that my identification strategy is somehow mechanically capturing other spurious firm characteristics. The results are reassuring, as I find that the p-value constructed based on the random permutation test is similar to the standard one, and lower than 1% (Figure A.3). Second, these results are identical when using a fixed-effects Poisson model instead of the linear specification (Table A.9). Third, in Table (A.8) I can replicate the results estimated by equation (1) using an alternative measure of patent litigation exposure $Exposure^{LARGE}_j$. As discussed before, this measure uses data on patents applied for by the firm in the ten years before the shock and patent litigation data since 1980.

5.2 Evidence on patent quality

The previous results show that firms that were more exposed to litigation appeared to have responded to the Supreme Court decision by increasing the rate of patenting. At face value, these results seem to support the idea that removing automatic injunction did not cause a collapse in innovation activity, but instead had a positive effect. However, more work is required to interpret these results as evidence on firms’ innovation. First, an increase in patenting may simply represent an increase in the propensity to patent, rather than a real increase in innovation. Second, patent applications may increase because firms feel the need to increase their defensive patents (Hall and Ziedonis, 2001). This result could be consistent with the idea that eBay reduced protection against real violations.

As a first step, I start exploring measures of innovation quality. In order to do so, I use the same empirical model as before, but focus on a set of quality metrics that are constructed based on patent citations. Previous research has shown that forward citations are correlated with the quality of the underlying patent and its economic value (Hall et al., 2005, Kortum and Lerner, 2000). Here, I construct different measures based on citations in order to capture different aspects of quality (Appendix A.3).

First, I examine how the average quality of the patents – measured by average scaled citations – changes around the time of the decision. Since comparing number of citations across technologies and over time can be challenging (Lerner and Seru, 2015), I adjust my baseline citations by scaling them by the average number of citations received by other assigned patents in the same technology class and year. Across the three specifications, I find no change on the average patent in a firm’s portfolio (columns (1)-(3), Table 3). In general,
the coefficient is positive but never statistically different from zero. This result confirms that the new marginal patents applied for after the decision were not of worse quality than those before. Therefore, this evidence rejects the hypothesis that an increase in the innovation output was driven by a surge in low-quality patents.

Second, since the returns on innovation are highly skewed (Pakes, 1986), it may be useful to also examine whether the decision increased companies’ ability to develop breakthrough innovation (Kerr, 2010). In principle, we may expect a positive effect on this dimension because of a scale effect: firms now may have more resources to do R&D - consistent with previous findings- and therefore they are more likely to engage in at least one high-quality project. This mechanism may be magnified if firms conducting breakthrough projects are even more likely to be targeted by litigation. For instance, high quality research may require combining knowledge across different areas, and this type of activity may expose firms to a higher change of infringement. In order to look at this, I examine the probability that a company applies for a patent that is at the top 10% (or top 25%) of the citation distribution in the relevant reference group. In line with previous literature, the reference group is composed of assigned patents that are in the same USPTO technology class and were developed in the same year (e.g. Lin et al., 2016), but I also show similar results with alternative benchmarks.

As reported in Table (3), I find that around the time of the ruling firms more exposed to litigation were relatively more likely to apply for a breakthrough patent. The result holds when looking at both the top 10% and 25% of the quality distribution after the decision. In economic terms, an increase by one standard deviation in the index led to a 1% increase in the probably of applying for a patent in the top 10% of the distribution, which represents more than a 3% jump from the baseline probability. The results are qualitatively similar across the various specifications. In Table (A.11), I find that the same results hold when I construct two alternative versions of the reference groups used to compute the quality threshold. In particular, rather than bench-marking citations within both technology class and year, I also construct a version of the data where top citation patents are identified only looking at the technology class (odd columns) and the year (even columns). The results using these alternative measures are still positive and significant at the conventional level.

Overall, firms more exposed to patent litigation did not lower the average quality of their patents and they were more likely to develop breakthrough technologies. Furthermore, these findings – both average and extreme outcomes - do not appear to be driven by any pre-trend before the decision (Table A.5; Figure A.6). Overall, this evidence appears more in line with the hypothesis that the increase in patenting was caused by more innovative activity.

5.3 Evidence on strategic patenting

As the next step in the analysis, I explore the incidence of strategic patents around the time of the decision. I define as strategic those patents whose value does not rest on the intrinsic technology covered by the IP but

\[^{44}\text{In Table (A.5), where I analyze the pre-trend on this variable, I actually find that in this panel specification, there is some weak, positive effect on the average citations.}\]
instead comes from the ability to use it for litigation purposes, either offensive or defensive. If the positive effect on patenting is explained by an increase in defensive activity, then we should expect to find this increase to be explained by strategic patenting. In this section, using two alternative measures of strategic patenting, I will show that this is not the case.

To start measuring strategic patents, I count the number of patents that are low quality – measured by forward citations – but whose patent claim spans a very large set of different technologies, measured by originality (Hall et al., 2001). The intuition behind this measure is simple: the value of a defensive patent does not rest on the quality of the innovation covered by the patent, but rather on its ability to be used in court. Consistent with this argument, Abrams et al. (2013) find that patents with a high strategic value are actually characterized by lower quality, measured by forward citations. Instead, patents are more valuable for court cases when they are characterized by high originality (Hall et al., 2001), which is a measure used in the literature to identify patent claims that span a large set of different technologies. In practice, my outcome is the share of granted patent applications that are in the top 25% in terms of originality among patents in the same technology class and year, but also are in the bottom three quartiles in terms of citations for the same group. In these Tables, I refer to this variable as the share of defensive patents.

The results are reported in second panel of Table (3). I find that firms more exposed to litigation actually experienced a reduction in the share of defensive patents around the decision time (columns 1, 2, and 3). The results are consistent in size and significance across the different specifications, but they are larger when I add controls. Looking at the most saturated model (column 3), the estimates show that a one-standard-deviation increase in exposure to litigation translates to a reduction in the percentage of defensive patents by roughly 1%, which corresponds to a 5% reduction in defensive patents relative to the average for the period.

To validate the previous results, I provide an alternative definition of strategic patents based on business-methods patents. With this approach, rather than trying to identify strategic or defensive patents across the whole sample, I focus on a specific set of technologies – business method patents – where the strategic value of patents is generally considered to be one of the key determinants of firms’ patenting behavior (Srinivasan, 2018). In line with the previous analyses, in columns (4), (5) and (6) of the second panel of Table (3), I examine how the share of business method patents changed around the decision. Across all the specifications, I find that companies that were more exposed to litigation applied for a lower share of business method patents after the decision time. In these results, business method patents are defined as simply patents in the official

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45 In line with the rest of the literature, originality is measured as one minus the Herfindahl index of technology class dispersion of citations made by the patent to other patents. In other words, this is a measure of the dispersion of the patent’s references across the different technologies.

46 I cannot specify a general threshold in terms of citations, because the threshold depends on the comparable set of patents, which are patents in the same technology and year. However, the bottom three quartiles in terms of citations capture the bulk of patents of very low quality. The median patent in this group has zero citations and the average only 0.4.

47 For the average firm in the sample, the share of defensive/strategic patents is in fact 21%. For the median firm, the same value is about 8%.

48 This approach builds on the recent work by Srinivasan (2018), who shows that the development of business method patents appear to be mostly related to strategic considerations.
business method technology class – technology class 705. For further robustness, in the last three columns I consider an alternative definition of business method patents, as discussed in Hall (2003).⁴⁹ Also in this case, I find a negative relationship between firm exposure and the change in the share of business method patents. However, the effects appear to be statistically weaker, particularly in the baseline specification.

Overall, this evidence on strategic patents appears at odds with the hypothesis that the change in enforcement rules led to more patenting because it increased firms’ defensive activity. In fact, firms that were more exposed to litigation appear to lower their efforts on strategic patents, suggesting that they perceived a decline in the need for building up a defensive portfolio. Together with the results on the quality of the innovation output, these analyses support the interpretation of the patenting results as an increase in innovation. Furthermore, this result also help squaring this paper with the previous evidence on the relationship between patenting and injunction risk from Hall and Ziedonis (2001), which documented that an increase in injunction risk in the semiconductor industry led to an increase in defensive patenting. In the same way, I show that a decrease in injunction risk overall led to a decline in the intensity of defensive patenting.⁵⁰

5.4 R&D investment for public firms

As a further step to nail down the effects of the decision, I next look at the effects of the ruling on R&D investment. This aspect is important for two reasons. First, looking at R&D investment provides more insight on how the ruling affected firms’ activity in innovation. Second, consistent with the discussion in the previous section, evidence on R&D investment would help to interpret the patenting results. In fact, if the decision really increased innovation activity, we would expect a response at both the input and output ends of innovation. The same would not hold if the motives behind the increase in patenting were simply an increase in the propensity to patent or enhance defensive activity. One important constraint in this analysis is data. While previous analysis has the advantage of focusing on a very large, heterogeneous set of firms, the amount of information that is available is limited to patent data. Looking at public firms, I can instead observe the total amount of monetary resources that a company has devoted to R&D. In particular, I focus on a set of around one thousand firms active in patenting around the time of the decision (section 3).

Using this sample, I estimate the same equation (1) looking at R&D investment. As a preliminary check, in columns (1), (2), and (3) of Table (4) I find that patent counts positively respond to the ruling for this group of firms as well. In magnitude, these effects are larger than those estimated using the full sample, in principle

⁴⁹The list of these other technology classes is in Hall (2003) Table 3. In particular, these are technology classes: 84, 119, 379, 434, 472, 380, 382, 395, 700, 701, 702, 703, 704, 705, 706, 707, 709, 710, 711, 712, 713, 714, 715, 717, 902.

⁵⁰One difference with Hall and Ziedonis (2001) is that the overall patenting activity did not decrease. This difference can be probably explained by two important differences between this experiment and the setting in Hall and Ziedonis (2001). First, the two papers study completely different time periods, with a very different litigation landscape: in particular Hall and Ziedonis (2001) focus on the 1980s. Second, Hall and Ziedonis (2001) focus on the semiconductor industry. This is an industry characterized by very specific business conditions that are hard to generalize outside the specific context. Interestingly, despite these big differences, both papers find consistent results on the direction of the elasticity between injunction use and defensive patenting.
suggesting that public firms were particularly affected by the decision.\footnote{However, I want to be cautious in this interpretation. First, public firms operate to a much larger scale than the average company in the full sample. This difference in scale may be important to compare adjustments across groups, therefore affecting the relative magnitude of the effects. Second, this comparison only accounts for intensive margin of adjustment, and I know from the previous results that extensive margin also plays an important role in the full sample.} This result would be consistent with the idea that public firms are perceived as very profitable target for strategic litigation.\footnote{For instance, Cohen et al. (2019) suggests that a large part of strategic litigation is driven by the presence of “extra cash” on targets’ balance sheet, therefore linking aggressive behavior of NPEs to the ability to extract large profits through settlements. While Cohen et al. (2019) examines variation within-public firms, it is reasonable to assume that public firms in general can be perceived as being more profitable targets for litigation.} Then, in columns (4), (5), and (6) I show that the same result holds for R&D investment. Specifically, firms that were more exposed to litigation at the time of the Supreme Court decision experienced a larger increase in R&D spending around the same period. A one-standard-deviation increase in litigation exposure leads to an 8% increase in R&D intensity relative to the baseline model. These results are essentially unchanged when I add the usual controls (columns 5 and 6).

Also in this case, the results do not appear to be driven by a failure of the parallel trend assumption. This is true both when looking at the non parametric test – where I plot the quarter specific coefficient across time (Figure 7) - and when I assume linear trends in the model Table (A.13). Similar to our previous results, I find that the differential among firms appears within one year from the decision and it does not seem to close in the following quarters. If anything, the gap seems to increase over time. Lastly, the same type of placebo analysis discussed before also works for R&D, as reported in Figure (A.7). Overall, this result confirms that the decision had a significant impact on the R&D decisions of innovative firms.

5.5 Plaintiff vs. defendant: heterogeneous effect of the ruling

As a final robustness test to the main mechanism, I examine how the firms’ reactions differ depending on whether a company was more or less likely to be active as a plaintiff in litigation around the time of the ruling. This test is motivated by the simple intuition that a company that expects to be more active as a plaintiff rather than a defendant should benefit far less from the enforcement changes. In fact, even if permanent injunction were still available to plaintiffs, its strength as a bargaining tool was weakened by the decision. This analysis is, however, constrained by a few theoretical and empirical issues. First, the data do not allow us to observe whether a firm will be more likely to be involved as a plaintiff or a defendant in the future: all we can observe is whether or not a firm was involved in a lawsuit in the past. Second, the decision to enter into a formal lawsuit is clearly endogenous (Cohen et al., 2019). As pointed out above, the number of lawsuits that end up in court are just a fraction of the overall litigation activity, and the decision to go to court rather than settle is clearly a function of the expected costs and benefits of the different actions. Third, data do not allow us to understand the real motives of the dispute (i.e. strategic vs. defensive lawsuits).

With these caveats in mind, I use the lawsuits data at the firm level to explore this dimension. Starting with the lawsuits files from Westlaw discussed earlier, I obtain the list of all the firms that were involved in
litigation – either as a defendant or a plaintiff – and I name-match them to the patent data with the help of a research assistant. Information on this matching is available in Appendix (A.3.4). Using this information for the period 2001-2005, I define a firm as being more likely to be the plaintiff if it appeared more times in the filings as a plaintiff than as defendant.

In Table (5), I start exploring these analyses for R&D intensity. First, I look at the effect of exposure to litigation separately for companies that I identify as more likely to be a plaintiff (column 2) versus the rest, which I define by complementarity as the group of firms more likely to be a defendant (column 1). Consistently with the hypothesis presented before, I find that the effect is mostly driven by those firms that were more likely to be on the defensive side of a lawsuit. In fact, within this sample the effect of exposure is significant and positive, while for firms more likely to be a plaintiff the result is null. In column (3), I pull together the sample and formally test for the difference in the effects across the two groups. As expected, I confirm that the difference between the two groups is statistically significant. In the remaining columns (columns 4-6), I show that this result is qualitatively identical when I add the usual set of controls.

As the final step, in Table (A.14), I use the same type of analysis, but for patenting. In the two panels, I explore this separately for my full sample and for public firms only. The results across the two data sets are very consistent. As before, I find that firms more exposed to patent litigation responded positively to the shock, but only in the sample of firms that were more likely to be defendants. In particular, the effect for firms more likely to be a plaintiff is always small – if not negative – and highly insignificant statistically. However, unlike before, these differences are not statistically significant at the conventional level. While these results are not completely in line with the R&D estimates, they seem to confirm that the subset of firms that were more likely to be involved in a lawsuit as plaintiffs did not benefit much from the new rules.

Overall, these results provide a final robustness test for the mechanism of the paper, which suggests that the new rules regarding injunctions had an impact on innovation activity by affecting the balance of enforcement in patent litigation. Consistent with this mechanism, firms that were more likely to be a defendant appeared to have responded more positively than those that were more likely to be a plaintiff.

6 How does litigation exposure affect innovation?

In the previous sections, I showed that the Supreme Court decision led to an increase in patenting, both at the intensive and extensive margins. Furthermore, this change in enforcement also positively affected patent quality and R&D investments. Overall, this evidence suggests that patent litigation had real distortive effects on firms' ability to innovate in 2006, and the decision was able to reduce some of this burden faced by innovative firms.

In this section, I explore why patent litigation affects innovation by firms.

53 I thank Matthew Nicholas Nicholson for the excellent support on the name matching.
6.1 Litigation lowers innovation returns: evidence from the composition of innovation

Firms exposed to litigation may reduce innovation for different reasons. The most intuitive channel is that patent litigation lowers the returns from investing in innovation. Since direct involvement in patent litigation can be very expensive (Bessen and Meurer, 2013), firms will take into account this risk when assessing whether to invest in a project. As a result, when the risk of patent litigation is too high, firms may choose to forgo some good investment opportunities. If this channel is quantitatively important, I should expect to find two results in the data. First, firms operating in more intensively litigated areas should be more positively affected. This is what I found in the main results. Second, within a firm, projects in an area where patent litigation is more intense should become relatively more valuable. This reshuffle should happen in every firm, irrespective of whether it is more or less exposed to litigation. In other words, every firm should perceive the investment in riskier patents to be more valuable.

In order to provide evidence in favor of this idea, I study whether firms experienced a relatively increase in risky patents after the decision. In order to focus on within-firm resource allocation, I sort patents applied for by each firm across two categories – risky and non-risky – depending on whether they belong to one of the USPTO technology classes in the top 10% (or 25%) of litigation. This reshape of the data implies that each firm has two observations per period. Since I am interested in the within-firm allocation, I can now test whether risky patents increased relatively more after the decision conditional on a full set of firm-by-time fixed effects. In practice, I estimate the following equation:

\[ y_{jtr} = \alpha_{jr} + \alpha_{jt} + \beta 1\{Risk_r\} \cdot Post \]  

(5)

where \( \alpha_{jt} \) is a set of firm-time fixed effects, \( \alpha_{jr} \) is a set of fixed effects at the firm-group level, \( 1\{Risk_r\} \) is a dummy for riskier groups. As mentioned above, I group patents in two classes, such that \( r = \{high risk; low risk\} \). If the return channel is the driving force behind the response of innovation to the ruling, I would expect risky patents to grow substantially more than non-risky patents within the firm portfolio, which is \( \beta > 0 \). Standard errors are clustered at firm-level.

In this analysis, I consider two outcomes: first, I explore the intensive margin of the effect by looking at \( \ln(\text{pat}_{jtr}) \), which is the logarithm of the grant patent that firm \( j \) applied for during time \( t \) in the class of risk \( r \). To obtain a purely intensive margin, I estimate this regression with a subset of firms that are simultaneously active in both risk classes around the decision time. Second, I look at the extensive margin with \( y_{jtr} \) equal to \( 1\{\text{Pat}_{jtr} > 0\} \), which is a dummy equal to one if the firm \( j \) applies for any subsequently granted patent in risk-group \( r \) at time \( t \). In this case, my sample is much larger, since I consider every firm that has applied for at least one patent in the ten years before the decision.
Results are reported in Table (6). When I look at the intensive margin, I find that patents belonging to more intensively litigated patent classes do not appear to increase relatively more within a firm’s portfolio. Estimates are very small and noisy. On the other hand, I find that firms are more likely to patent in a risky class in the two years after the decision, rather than in the two before. The results are similar whether risky patents are defined as being in the top 10% or the top 25%. Lastly, in Table (A.12) I use the full panel dimension – without collapsing pre- and post – and I estimate the effect differentially for pre- and post- relative to the quarter before the decision. This analysis shows that this effect is not driven by differential trends in patenting before the decision.

At least partially, these results are consistent with the return channel: the decision also shifted the patenting behavior of firms across classes, in particular by making companies more likely to patent in a more risky area after the decision. While a similar effect is not identified at the intensive margin, these results are in line with the reshuffle idea that should occur if the decision were to increase the perceived returns of R&D investment.

6.2 Litigation exacerbates financial constraints

Operating in a high-litigation environment can also hinder innovation by reducing the amount of resources available for R&D. The idea that exposure to litigation can deplete corporate resources is intuitive. Firms in sectors where litigation is more intense are more likely to pay large settlements or overpays for licensing agreements. This happens because companies want to avoid the escalation of legal conflicts to courts or just limit their negative consequences, as in the BlackBerry case discussed previously. Furthermore, ex-ante these companies may be forced to devote larger resources to monitor potential threats and modify their products to minimize the risk of litigation. For example, eBay in the 2006 10-K recognizes that litigation claims “whether meritorious or not, are time consuming and costly to resolve, and could require expensive changes in our methods of doing business, or could require to enter into costly royalty or licensing agreements.” In response to this, companies may invest more intensively in defensive tools, such as a large legal department within the company, which seems to have some effects on deterring attacks (Cohen et al., 2019).

If the financing of innovation were frictionless, this shift of monetary resources should not affect firms’ ability to invest in good projects. In reality, firms face constraints in funding innovation (Brown et al., 2009; Hall and Lerner, 2010), and therefore a reduction in internal resources has an impact on firms’ ability to innovate. When this is the case, intense patent litigation exacerbates this financing problem and therefore it increases the inefficiency in funding R&D. To test whether this theory is true in the data, I examine the heterogeneity...

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54 In particular, the effect is non-significant when looking at the 10% split, and borderline significant but negative when looking at the 25% split. Overall, I interpret this evidence as consistent with a lack of response at this margin. First, the effect is small in size with both outcomes. Second, the borderline negative effect does not appear to be particularly robust. For instance, when we use the full panel dimension to study the pre-trend (Table A.12), we do not find any significant effect across both outcomes.

55 One view on this difference is that an intensive margin is harder to trace down empirically. Alternatively, it is possible that firms that already operate across areas with both high and low risk of litigation are endogenously less sensitive to patent litigation. As a result, the positive NPV effect for these firms may be smaller and empirically not relevant.
of the decision effects across firms characterized by a differential likelihood of being financially constrained. If this channel is relevant, I expect companies that are more likely to be financially constrained to react more positively to the shock. In other words, this story would predict a higher elasticity between investment in R&D and a reduction in litigation costs for companies facing more financial frictions.

In order to study this, I modify the standard model described by equation (1) by adding an interaction with a dummy $\text{FinCon}_j$, which is equal to one for firms that are more likely to be financially constrained. More specifically, I estimate:

$$y_{jt} = \alpha_j + \alpha_t + \beta_1 (\text{Exposure}_j \cdot \text{FinCon}_j \cdot \text{Post}) + \beta_2 (\text{FinCon}_j \cdot \text{Post}) + \beta_3 (\text{Exposure}_j \cdot \text{Post}) + \gamma X_{jt} + \epsilon_{jt} \quad (6)$$

Furthermore, I separately study the behavior of the two groups of firms. In line with previous discussion, I would expect $\beta_1 > 0$.

Following the relevant literature in finance, I identify firms that are more likely to be financially constrained in three different ways. First, I study the differential behavior of small versus large firms. Previous research has found that smaller firms tend to have a harder time accessing external funding (Fazzari et al., 1988; Chodorow-Reich, 2014; Bottero et al., 2015). In my setting, I focus on smaller firms within the public firm sample. In particular, I construct two definitions of small firms, looking at whether they are below the median of employment or revenue. Second, I identify firms with no rating on public debt as companies that are more likely to be financially constrained (Kashyap and Lamont, 1994; Almeida et al., 2004). More specifically, I look at firms with no rating reported in the three years before the Supreme Court decision. Lastly, I examine the heterogeneity across firms that pay and do not pay cash dividends, looking at the three years before the decision.

The results are reported in Tables (7) and (8). The decision led to an increase in R&D intensity only for firms more likely to be financially constrained. When splitting the sample across the two groups, I systematically find that the coefficient is positive and significant for the financially constrained group, while non-significant and small for the other group. When using the full sample, more financially constrained firms increase R&D intensity more. This is true across all the measures, although it is not statistically significant in some cases. Lastly, I find that more financially constrained firms did not respond more than non-financially constrained firms in terms of patent applications.56

As a robustness, I show that, in my case, the results are not simply capturing heterogeneity across firms in growth (Farre-Mensa and Ljungqvist, 2015). To rule this out, I augment equation (6) by fully interacting

56The presence of multiple (risk vs. financial) channels may explain this null effect on patenting. In particular, if the risk channels explains a large portion of the patent changes, it is possible to detect no effect on patenting across financial constrain despite the change in R&D. Alternatively, the null effect may hide a shift in the type of project. For instance, financially constrained firms may have invested less in R&D before, but they still have patented the same and simply shuffled resources towards less expensive projects.
measures of firm growth in the two years before the decision to my treatment. In particular, in Table (A.15) I report the results looking at revenue growth. I find that, if anything, the main coefficient $\beta_1$ is estimated more precisely when I add the growth controls. In an unreported Table, I find the same when looking at asset growth. Overall, my analysis is not just capturing a spurious correlation of these measure of financial constraint with different growth trajectories.

These results suggest that a decline in R&D returns is not the only channel through which patent litigation may affect innovation. Instead, financial constraint is an important dimension to consider when evaluating the effect of operating in area where litigation is intense.

7 Conclusion

This paper examines how patent rights affect innovation using the 2006 Supreme Court decision in “eBay v. MercExchange” as an exogenous shock to patent enforcement. The evidence provided suggests that this intervention had a positive effect on innovation. Firms that were more exposed to the change in rules – companies operating in areas where patents were more intensively litigated – increased innovation output more after the decision. Similarly, for a sub-sample of public firms, I found that R&D intensity was positively affected. This is consistent with the idea that patent litigation may have negative, distortive effects on firm investment in innovation. The effects were large in magnitude, suggesting that these distortions can be substantial. While the average quality of the patents did not change, firms more exposed to patent litigation increased the likelihood of patenting breakthrough technology. Similarly, firms exposed to the shock saw a lower increase in the share of defensive patents. Overall, these results are consistent with the idea that patent litigation may have negative, distortive effects on firm investment in innovation.

Furthermore, I investigate the specific channels through which patent litigation reduced innovation. First, I show that patent litigation reduces innovation because it lowers the returns from performing R&D activities. Consistent with this idea, firms partially reshuffled their portfolios toward patents with higher risk of lawsuits after the decision. Second, I explore whether patent litigation also reduces investment in R&D because it diminishes the amount of internal resources available for productive activities, therefore exacerbating the financing problem of innovation (Brown et al., 2009; Hall and Lerner, 2010). In line with this hypothesis, I find that the increase in R&D is mostly concentrated in firms that are more likely to be financially constrained.

There are several avenues for future research in this area. A primary question is to examine the effectiveness of recent policy interventions, such as the America Invents Act (2011). In addition, more work can be done to examine the role of patent litigation in start-up. The nature of my identification strategy focuses on established firms and therefore the results do not directly apply to start-up companies. However, there are good reasons to think ex-ante that the results on this set of companies should not be reversed. First, the importance of
financial constraints in explaining the results suggests that the litigation channel may have been relevant also for start-ups, since these firms are generally more financially constrained that established companies. Second, aggregate evidence is also consistent with the fact that eBay did not significantly harm start-up investments. For instance, Mezzanotti and Simcoe (2019) suggest that VC investments and aggregate innovation did not slow down during this period (and if anything grew at a faster rate).

The results presented in this paper support the idea that patent litigation can significantly affect companies’ innovation. As a result, policies that mitigate the overhang of litigation can have beneficial effects on technology advancement. In particular, improvements in the quality of patent enforcement, which reduces the legal uncertainty around patents and limits abusive behaviors in this market, can increase firms’ ability and incentives to invest in R&D. Recent efforts in the United States, such as the America Invents Act (2011) or Alice v. CLS (2014), have started to take steps in this direction. However, more comprehensive policy work needs to be done to further addresses the various problems in the patent system today.

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57 There are also more direct application of this paper. For instance, there has been some recent attempts to moderate the effect of the eBay case on the US legal system. One example is the recent bill titled “STRONGER Patent Act,” which would introduce a presumption of irreparable harm when making injunction in patent cases. For references, see “Congress Shouldn’t Overturn eBay Patent Injunction Standard” by Thomas Cotter (2018).
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Figure 1: Number of cases involving patents

This plot reports the number of filings involving patents of any type per year of filing, between 1980 and 2012. The data comes from WestLaw-ThomsonReuters, which collected filings information from public records. Data are plotted at the docket-number level, therefore, they do not account for the fact that each case can involve multiple defendants. More information on the data is available in Section (3).

Figure 2: NPEs stock returns around the decision

This figure plots the average cumulative returns, for the sample of NPEs identified in the paper. The sample of firms used are 10 companies that are (a) identified as NPEs; (b) public at the time of the Supreme Court decision. The companies are Acacia Technologies, Asure Software (formerly Forgent Network), Rambus, Tessera Technologies, Universal Display, Document Security Systems, ParkerVision, Unwired Planet (formerly Openwave), Interdigital, and Spherix. Information on the sample constructions are provided in Section (2). More information on this analysis is in Appendix (A.3.3). The straight red line corresponds to the trading day right before the decision.
This figure reports the pie chart of the patents by industry, across the full sample and the sample of firms that are more exposed to litigation. Industries are identified based on patent applications across macro-technology areas (Hall et al., 2001) and the construction is discussed in detail in Appendix (A.3). The first chart is constructed using only firms in the top 50% of litigation exposure, where litigation is measured using $\text{Exposure}_j$. This is constructed using litigation in the five years before the decision, and using patents since 2000. The second chart is instead constructed using the full sample. Furthermore, the sample that was used to construct this plot is the sample of innovative firms that applied for at least one patent in the two years before or two years after the decision.

This figure plots the value-weighted cumulative returns across high- and low-exposure firms. High litigation firms are firms in the top 25% of the litigation distribution. Cumulative returns are normalized to zero for both groups two days before the decision. The straight red line is plotted between the day before and the day of the decision (which is defined to be zero in calendar time). The value-weights are based on the market value of traded stocks, and they are kept fixed five days before the decision.
This figure plots the $\beta_t$ from equation (4). The red vertical line corresponds to the last period of the pre-decision period. Every $\beta_t$ is plotted with the corresponding CI at 5%. Every period is labeled with the corresponding quarter. Notice that quarters are in “event time” not calendar time: in fact, I set the end of the first quarter artificially to be the one ending in May 15th (the other quarters are constructed relative to this). The data used corresponds at the two years before and after the decision, in event time. The sample used corresponds to the one of the extensive margin. Standard errors are clustered at the firm-level.

This figure presents the results from a set of placebo tests. In particular, I construct a series of placebo samples, centered around fictional shocks in the two years that are completely outside the period after the decision. The date in the x-axis is the quarter around which the analysis is centered. In each case, I reconstruct the data around this placebo shock, both the outcomes and the measures of exposure $Exposure_j$. Then, I run the standard regression. The figure plots the $\beta$ from equation (1), as well as the 95% confidence intervals, estimated over different samples. For clarity, I estimate the simple equation without further controls, and looking at the intensive margin. Notice that quarters are in “event time” not calendar time: in fact, I set the end of the first quarter artificially to be ending in May 15th (the other quarters are constructed accordingly). Data used corresponds to the two years before and after the decision, in event time. Standard errors are clustered at the firm level.
This figure plots the $\beta_t$ from equation (4) with the standard controls, where the outcome is R&D over asset. The red vertical line correspond to the last period of the pre-decision period. Every $\beta_t$ is plotted with the corresponding CI at 5%. Every period is label with the corresponding quarter. Notice that quarters are in “event time” not calendar time: I set the second quarter to be the first quarter ending after the Supreme Court decision (and the other are defined relative to this quarter). The data used corresponds to the two years before and after the decision. The sample is the standard Compustat sample of innovative firms used in the paper.
Table 1: Summary Statistics

(a) Full sample

<table>
<thead>
<tr>
<th>Variable</th>
<th>Obs.</th>
<th>Mean</th>
<th>S.D.</th>
</tr>
</thead>
<tbody>
<tr>
<td>#Patent_{jt}</td>
<td>32,128</td>
<td>20.28</td>
<td>164.41</td>
</tr>
<tr>
<td>1{Patent_{jt} = Top^{10%}}</td>
<td>32,128</td>
<td>0.30</td>
<td>0.46</td>
</tr>
<tr>
<td>1{Patent_{jt} = Top^{25%}}</td>
<td>32,128</td>
<td>0.48</td>
<td>0.50</td>
</tr>
<tr>
<td>Exposure_{j}</td>
<td>32,128</td>
<td>0.77</td>
<td>0.79</td>
</tr>
<tr>
<td>Exposure_{j}^{OLD}</td>
<td>32,128</td>
<td>0.68</td>
<td>0.56</td>
</tr>
<tr>
<td>Average Citation Pre</td>
<td>32,128</td>
<td>1.19</td>
<td>1.81</td>
</tr>
<tr>
<td>1{Years first Patent ≤ 3}</td>
<td>32,128</td>
<td>0.29</td>
<td>0.46</td>
</tr>
<tr>
<td>Size Pre Portfolio</td>
<td>32,128</td>
<td>18.97</td>
<td>146.74</td>
</tr>
</tbody>
</table>

(b) Public Firms

<table>
<thead>
<tr>
<th>Variable</th>
<th>Obs.</th>
<th>Mean</th>
<th>S.D.</th>
</tr>
</thead>
<tbody>
<tr>
<td>#Patent_{jt}</td>
<td>2,034</td>
<td>101.97</td>
<td>463.87</td>
</tr>
<tr>
<td>R&amp;D/Asset</td>
<td>2,034</td>
<td>0.03</td>
<td>0.04</td>
</tr>
<tr>
<td>Exposure_{j}</td>
<td>2,034</td>
<td>0.93</td>
<td>0.81</td>
</tr>
<tr>
<td>Exposure_{j}^{OLD}</td>
<td>2,034</td>
<td>0.77</td>
<td>0.55</td>
</tr>
<tr>
<td>Average Citation Pre</td>
<td>2,034</td>
<td>1.50</td>
<td>2.06</td>
</tr>
<tr>
<td>1{Years first Patent ≤ 3}</td>
<td>2,034</td>
<td>0.04</td>
<td>0.19</td>
</tr>
<tr>
<td>Size Pre Portfolio</td>
<td>2,034</td>
<td>90.72</td>
<td>375.06</td>
</tr>
</tbody>
</table>

These two panels report the summary statistics for the two main samples used in the main analyses. Therefore, a period t is defined as a two-year window either before or after the ruling. In the first panel, I present the summary statistics for the variables that are used for the first set of analysis, where I employ both private and public firms active in innovative around the time of the decision. In particular, I use the sample that is used in the regressions, which is the sample of firms that applied to at least one granted patent in the two years before and in the year after the time of decision. In the second panel, instead, I report summary statistics for the sample that is used in the second part of the analysis, which focuses on public firms that patented around the decision. More information on the sample construction is available in the Appendix (A.3). The variable construction is described in detail in the Appendix (A.3), for outcomes, and in the Section (3) for the measures of exposure.
Table 2: Effect of the policy change on patenting: main results

<table>
<thead>
<tr>
<th>OLS</th>
<th>(1)</th>
<th>(2)</th>
<th>(3)</th>
<th>(4)</th>
<th>(5)</th>
<th>(6)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Post $\cdot$ Exposure$_{j}$</td>
<td>ln(Patents$_{jt}$)</td>
<td>1{Patent$_{jt}$ &gt; 0}</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>0.040***</td>
<td>0.036***</td>
<td>0.034***</td>
<td>0.010***</td>
<td>0.027***</td>
<td>0.027***</td>
</tr>
<tr>
<td></td>
<td>(0.008)</td>
<td>(0.011)</td>
<td>(0.011)</td>
<td>(0.002)</td>
<td>(0.002)</td>
<td>(0.002)</td>
</tr>
<tr>
<td>Firm F.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td>Time F.E.</td>
<td>Y</td>
<td>N</td>
<td>N</td>
<td>Y</td>
<td>N</td>
<td>N</td>
</tr>
<tr>
<td>Indu. $\times$ Time F.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td>Controls$_{j} \times$ Time F.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td>$R^2$</td>
<td>0.005</td>
<td>0.007</td>
<td>0.033</td>
<td>0.216</td>
<td>0.282</td>
<td>0.290</td>
</tr>
<tr>
<td>Observations</td>
<td>32,128</td>
<td>32,128</td>
<td>32,128</td>
<td>155,876</td>
<td>155,876</td>
<td>155,876</td>
</tr>
</tbody>
</table>

This table reports the estimate of the linear difference-in-difference specification (equation 1), where I estimate the effect of the decision on quantity of innovation. In particular, I estimate $y_{jt} = \alpha_j + \alpha_t + \beta(\text{Exposure}_j \cdot \text{Post}) + \gamma X_{jt} + \epsilon_{jt}$, where $y_{jt}$ is: (a) the (natural) logarithm of granted patent that firm $j$ applied for during period $t$ for Columns (1)-(3); (b) a dummy equal to one if the firm $j$ applied to at least one patent in period $t$. The data set is a balanced two-period panel. Each period collapses firm information in the two years before and two years after the Supreme Court decision. The sample depends on the outcome: when looking at the intensive margin (columns 1-3) I use every firm that applied to at least one patent in the two year before and in the year after the decision; when I look at the extensive margin (columns 4-6) I use the sample of every firm with at least one patent in the five year before the decision, which is the minimal requirement to construct the measure of exposure. The variable Exposure$_{j}$ captures the exposure of firm $j$ to patent litigation, using patent application in the five years before the decision and patent litigation at technology class since 2000. In Columns (1) and (4), I control for firm fixed-effects and time effects. In Column (2) and (5), I add industry-time fixed effect to the equation. Industry are constructed based on the macro technology area where the company patented the most over the four years before the decision, where macro technology classes are constructed as in Hall et al. (2001). In Columns (3) and (6), I further augment the specification using location dummies of the firm (constructed using the modal location reported in patent data), the size of the portfolio before the estimation period, the start-up status (looking at whether a firm applied for the first patent ever within the previous three years) and average quality of the patent portfolio in the pre period, measured by average citations. All these controls are interacted with a time dummy to allow the variable to have a differential effect before and after. More information on the variables is provided in the Appendix (A.3). Standard errors are clustered at firm level. All regressions include a constant. *** denotes significance at the 1% level, ** at the 5%, and * at the 10%.
Table 3: Evidence on patent quality

(a) Panel A

<table>
<thead>
<tr>
<th>OLS</th>
<th>(1)</th>
<th>(2)</th>
<th>(3)</th>
<th>(4)</th>
<th>(5)</th>
<th>(6)</th>
<th>(7)</th>
<th>(8)</th>
<th>(9)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Post - Exposure_j</strong></td>
<td>0.013</td>
<td>0.014</td>
<td>0.016</td>
<td><strong>0.010</strong>***</td>
<td><strong>0.016</strong>***</td>
<td><strong>0.016</strong>***</td>
<td><strong>0.018</strong>***</td>
<td><strong>0.022</strong>***</td>
<td><strong>0.021</strong>***</td>
</tr>
<tr>
<td><strong>Firm F.E.</strong></td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td><strong>Time F.E.</strong></td>
<td>Y</td>
<td>N</td>
<td>N</td>
<td>N</td>
<td>N</td>
<td>N</td>
<td>Y</td>
<td>N</td>
<td>N</td>
</tr>
<tr>
<td><strong>Indu. \times Time F.E.</strong></td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td><strong>Controls _j \times Time F.E.</strong></td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td><strong>R^2</strong></td>
<td>0.001</td>
<td>0.001</td>
<td>0.004</td>
<td>0.001</td>
<td>0.001</td>
<td>0.005</td>
<td>0.001</td>
<td>0.001</td>
<td>0.004</td>
</tr>
<tr>
<td><strong>Observations</strong></td>
<td>32,128</td>
<td>32,128</td>
<td>32,128</td>
<td>32,128</td>
<td>32,128</td>
<td>32,128</td>
<td>32,128</td>
<td>32,128</td>
<td>32,128</td>
</tr>
</tbody>
</table>

(b) Panel B

<table>
<thead>
<tr>
<th>OLS</th>
<th>(1)</th>
<th>(2)</th>
<th>(3)</th>
<th>(4)</th>
<th>(5)</th>
<th>(6)</th>
<th>(7)</th>
<th>(8)</th>
<th>(9)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Post - Exposure_j</strong></td>
<td>-0.008**</td>
<td>-0.011**</td>
<td>-0.010**</td>
<td><strong>-0.004</strong>***</td>
<td><strong>-0.006</strong>***</td>
<td><strong>-0.006</strong>***</td>
<td><strong>-0.002</strong></td>
<td><strong>-0.004</strong></td>
<td><strong>-0.004</strong></td>
</tr>
<tr>
<td><strong>Firm F.E.</strong></td>
<td>(0.004)</td>
<td>(0.005)</td>
<td>(0.005)</td>
<td>(0.001)</td>
<td>(0.001)</td>
<td>(0.001)</td>
<td>(0.001)</td>
<td>(0.001)</td>
<td>(0.002)</td>
</tr>
<tr>
<td><strong>Time F.E.</strong></td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td><strong>Indu. \times Time F.E.</strong></td>
<td>Y</td>
<td>N</td>
<td>N</td>
<td>N</td>
<td>N</td>
<td>Y</td>
<td>N</td>
<td>Y</td>
<td>N</td>
</tr>
<tr>
<td><strong>Controls _j \times Time F.E.</strong></td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td><strong>R^2</strong></td>
<td>0.001</td>
<td>0.001</td>
<td>0.005</td>
<td>0.002</td>
<td>0.003</td>
<td>0.007</td>
<td>0.001</td>
<td>0.003</td>
<td>0.006</td>
</tr>
<tr>
<td><strong>Observations</strong></td>
<td>32,128</td>
<td>32,128</td>
<td>32,128</td>
<td>32,128</td>
<td>32,128</td>
<td>32,128</td>
<td>32,128</td>
<td>32,128</td>
<td>32,128</td>
</tr>
</tbody>
</table>

These panels report the estimate of the linear difference-in-difference specification (equation 1), where I estimate the effect of the decision on the quality of innovation. In particular, I estimate \( y_{jt} = \alpha_j + \alpha_t + \beta(\text{Exposure}_j \cdot \text{Post}) + \gamma X_{jt} + \epsilon_{jt} \), where \( y_{jt} \) is a measure of patent quality. In particular, in panel A, I consider three outcomes: (a) the average number of scaled citations received by firms \( j \) in period \( t \); (b) a dummy which is equal to one if firm \( j \) has published in period \( t \) at least one patent that is in the top 10% of the distribution of citations among patents granted in the same year in the same technology class; (c) similar dummy, but constructed considering the top 25% of the distribution. In panel B instead I look at other measures of defensive patenting. In particular, I have three outcomes: (a) the share of defensive patents, where the defensive patents are patents in the top 25% in terms of dispersion across technology (originality) among patents of same technology class and year, despite being in the bottom three quartiles in terms of citations for the same group; (b) the share of business method (BM) patents, which are defined as patents in technology class 705; (c) alternative share of BM patents with broader definition, where BM patents are defined in Hall (2003) Table 3 (i.e. technology classes: 84, 119, 379, 434, 472, 580, 382, 395, 700, 701, 702, 703, 704, 705, 706, 707, 709, 710, 711, 712, 713, 714, 715, 717, 902). As before, the data set is a balanced two-period panel where I employ every firm that published at least one patent in the two year before and in the year after the decision. The variable \( \text{Exposure}_j \) captures the exposure of firm \( j \) to patent litigation, using patent application in the five years before the decision and patent litigation at technology class since 2000. I always control for firm fixed-effects and time effects. Furthermore, I always augment the specification with industry-time fixed effect, which are constructed based on the macro technology area where the company patented the most over the four years before the decision (Hall et al. (2001)). Lastly, I further augment every specification with location dummies of the firm, the size of the portfolio before the estimation period and the start-up status. More information on the variables is provided in the Appendix (A.3). Standard errors are clustered at firm level. All regressions include a constant. ** denotes significance at the 1% level, *** at the 5%, and * at the 10%.
denotes significance at the 1% level, ** at the 5%, and * at the 10%.

The variables is provided in the Appendix (A.3). Standard errors are clustered at firm level. All regressions include a constant.

This table reports the estimate of the linear difference-in-difference specification (equation 1), where I estimate the effect of the decision on patenting and R&D intensity. In particular, I estimate \( y_{jt} = \alpha_j + \alpha_t + \beta \text{Exposure}_{jt} \times \text{Post} + \gamma X_{jt} + \epsilon_{jt} \), where \( y_{jt} \) is: (a) the (natural) logarithm of granted patents that firm \( j \) applied during period \( t \) for Columns (1)-(3); (b) \( \text{R&D/Asset}_{jt} \) is the average over the period of the quarterly R&D expenses scaled by total assets for Columns (4)-(6). Outcomes are winsorized at 1% and the exact construction of the variables is discussed in the paper and in Appendix (A.3). The variable \( \text{Exposure}_{jt} \) captures the exposure of firm \( j \) to patent litigation, using patent application in the five years before the decision and patent litigation at technology class since 2000. The data set is a balanced two-period panel, where each period collapses firm information in the two years before and two years after the Supreme Court decision. The sample is a set of non-financial, US located public firms that applied to at least one patent in the two years before and one after (see Appendix A.3). I always control for firm fixed-effects and time effects. In Columns (2) and (5) I augment this with industry-time fixed effect. Industry are constructed based on the macro technology area where the company patented the most over the four years before the decision, where macro technology classes are constructed as in Hall et al. (2001). In Columns (3) and (6) I further augment the specification using location dummies of the firm (constructed using the modal location reported in patent data), the size of the portfolio before the estimation period, quality of the patent portfolio before the decision (measured by average citations) and the “start-up” status (looking at whether a firm applied to at least one patent ever within the previous three years), which would be more correct to refer as firm age in this sample. All these controls are interacted with a time dummy to allow the variable to have a differential effect before and after. More information on the variables is provided in the Appendix (A.3). Standard errors are clustered at firm level. All regressions include a constant.*** denotes significance at the 1% level, ** at the 5%, and * at the 10%.

### Table 4: Effect of the decision on public firms

<table>
<thead>
<tr>
<th>OLS</th>
<th>(1)</th>
<th>(2)</th>
<th>(3)</th>
<th>(4)</th>
<th>(5)</th>
<th>(6)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Post · Exposure(_{jt})</td>
<td>0.062**</td>
<td>0.092**</td>
<td>0.096**</td>
<td>0.003***</td>
<td>0.004***</td>
<td>0.004***</td>
</tr>
<tr>
<td></td>
<td>(0.033)</td>
<td>(0.044)</td>
<td>(0.045)</td>
<td>(0.001)</td>
<td>(0.001)</td>
<td>(0.002)</td>
</tr>
<tr>
<td>Firm F.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td>Time F.E.</td>
<td>Y</td>
<td>N</td>
<td>N</td>
<td>Y</td>
<td>N</td>
<td>N</td>
</tr>
<tr>
<td>Indu. × Time F.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td>Controls(_{jt}) × Time</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td>(\text{R&amp;D/Asset}_{jt})</td>
<td>0.007</td>
<td>0.017</td>
<td>0.081</td>
<td>0.010</td>
<td>0.018</td>
<td>0.063</td>
</tr>
<tr>
<td>Observations</td>
<td>2,034</td>
<td>2,034</td>
<td>2,034</td>
<td>2,034</td>
<td>2,034</td>
<td>2,034</td>
</tr>
</tbody>
</table>

This table reports the estimate of the linear difference-in-difference specification (equation 1), where I allow the effect of the exposure to the decision to be heterogeneous across firm likelihood of being a plaintiff at the time of the decision. The outcome is always \( \text{R&D/Asset}_{jt} \), which is the average over the period of the quarterly R&D expenses scaled by total assets. As usual, this is winsorized at 1%. The variable \( \text{Exposure}_{jt} \) captures the exposure of firm \( j \) to patent litigation, using patent application in the five years before the decision and patent litigation at technology class since 2000. The dummy Likely Plaintiff is equal to one if the firm has been involved in more lawsuits as a plaintiff rather than a defendant. I first report the regressions as split between likely plaintiff and the complementary group – which I call likely defendant – and then I report the fully interacted regression in the whole sample. I always control for firm and time fixed effects, but in Columns (4)-(6) I add extra controls interacted with time dummies. As in the previous analyses, I control for industry, location dummies of the firm, the size of the portfolio before the estimation period, a dummy for “start-up”, which in this context is firms that published the first patent in the three years before the decision, and average quality of the patent portfolio in the pre period, measured by average citations. More information on the variables is provided in the Appendix (A.3). Standard errors are clustered at firm level. All regressions include a constant.*** denotes significance at the 1% level, ** at the 5%, and * at the 10%.

### Table 5: Effect across defendant status

<table>
<thead>
<tr>
<th>Public firms</th>
<th>(1)</th>
<th>(2)</th>
<th>(3)</th>
<th>(4)</th>
<th>(5)</th>
<th>(6)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Post · Exposure(_{jt})</td>
<td>0.003***</td>
<td>-0.002</td>
<td>0.003***</td>
<td>0.005***</td>
<td>-0.002</td>
<td>0.005***</td>
</tr>
<tr>
<td></td>
<td>(0.001)</td>
<td>(0.002)</td>
<td>(0.001)</td>
<td>(0.002)</td>
<td>(0.002)</td>
<td>(0.002)</td>
</tr>
<tr>
<td>Post · LikelyPlaint.</td>
<td>0.004***</td>
<td>0.003**</td>
<td>-0.005*</td>
<td>-0.004*</td>
<td>(0.003)</td>
<td>(0.003)</td>
</tr>
<tr>
<td></td>
<td>(0.002)</td>
<td>(0.002)</td>
<td>(0.002)</td>
<td>(0.002)</td>
<td>(0.002)</td>
<td>(0.002)</td>
</tr>
<tr>
<td>Firm F.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td>Time F.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>N</td>
<td>N</td>
<td>N</td>
</tr>
<tr>
<td>Indu. × Time F.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td>Controls(_{jt}) × Time</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td>(\text{R&amp;D/Asset}_{jt})</td>
<td>0.016</td>
<td>0.013</td>
<td>0.016</td>
<td>0.078</td>
<td>0.273</td>
<td>0.068</td>
</tr>
<tr>
<td>Observations</td>
<td>1,642</td>
<td>392</td>
<td>2,034</td>
<td>1,642</td>
<td>392</td>
<td>2,034</td>
</tr>
</tbody>
</table>

This table reports the estimate of the linear difference-in-difference specification (equation 1), where I allow the effect of the exposure to the decision to be heterogeneous across firm likelihood of being a plaintiff at the time of the decision. The outcome is always \( \text{R&D/Asset}_{jt} \), which is the average over the period of the quarterly R&D expenses scaled by total assets. As usual, this is winsorized at 1%. The variable \( \text{Exposure}_{jt} \) captures the exposure of firm \( j \) to patent litigation, using patent application in the five years before the decision and patent litigation at technology class since 2000. The dummy Likely Plaintiff is equal to one if the firm has been involved in more lawsuits as a plaintiff rather than a defendant. I first report the regressions as split between likely plaintiff and the complementary group – which I call likely defendant – and then I report the fully interacted regression in the whole sample. I always control for firm and time fixed effects, but in Columns (4)-(6) I add extra controls interacted with time dummies. As in the previous analyses, I control for industry, location dummies of the firm, the size of the portfolio before the estimation period, a dummy for “start-up”, which in this context is firms that published the first patent in the three years before the decision, and average quality of the patent portfolio in the pre period, measured by average citations. More information on the variables is provided in the Appendix (A.3). Standard errors are clustered at firm level. All regressions include a constant.*** denotes significance at the 1% level, ** at the 5%, and * at the 10%.
Table 6: Evidence on patent mix

<table>
<thead>
<tr>
<th></th>
<th>(1)</th>
<th>(3)</th>
<th>(5)</th>
<th>(7)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Extensive Margin</td>
<td>Intensive Margin</td>
<td></td>
<td></td>
</tr>
<tr>
<td>$\ln(Patents_{jtr})$</td>
<td>$0.005$</td>
<td>$-0.027^*$</td>
<td>$0.280^{**}$</td>
<td>$0.170^{***}$</td>
</tr>
<tr>
<td>$\text{Post} \cdot 1{Risk_{r}}$</td>
<td>$(0.020)$</td>
<td>$(0.015)$</td>
<td>$(0.003)$</td>
<td>$(0.004)$</td>
</tr>
<tr>
<td>$\text{Split}$</td>
<td>$10%$</td>
<td>$25%$</td>
<td>$10%$</td>
<td>$25%$</td>
</tr>
<tr>
<td>$\text{Firm} \times \text{Time F.E.}$</td>
<td>$Y$</td>
<td>$Y$</td>
<td>$Y$</td>
<td>$Y$</td>
</tr>
<tr>
<td>$\text{Firm} \times \text{Risk F.E.}$</td>
<td>$Y$</td>
<td>$Y$</td>
<td>$Y$</td>
<td>$Y$</td>
</tr>
<tr>
<td>$R^2$</td>
<td>$0.981$</td>
<td>$0.976$</td>
<td>$0.834$</td>
<td>$0.810$</td>
</tr>
<tr>
<td>Observations</td>
<td>$8,712$</td>
<td>$15,572$</td>
<td>$219,616$</td>
<td>$219,616$</td>
</tr>
</tbody>
</table>

This table estimates equation (5), which is: $y_{jtr} = \alpha_{jt} + \alpha_{jr} + \beta 1\{Risk_{r}\} \cdot \text{Post}$, where where $\alpha_{jt}$ is a set of firm-time fixed effects, $\alpha_{jr}$ is a set of fixed effects at the firm-group level, 1\{Risk_{r}\} is a dummy for more risky groups. Data are reshaped for this analysis at the firm-time-riskiness group level. In practice, I group patent within a firm in a certain time across two classes depending on the level of riskiness $r$, such that $r = \{\text{high risk}; \text{low risk}\}$. Patents are assigned to one of the two groups based on the intensity of litigation of their technology class after 2000 based on the WestLaw Litigation data. In particular, I split the data across both 10% and 25%. Furthermore, data are collapsed before and after the decision: therefore every firm is in the data exactly four times. I consider two outcomes: in columns (1)-(2) I use $\ln(Patents_{jtr})$, which is the logarithm of the patent applications that firm $j$ filed to during time $t$ in the class of risk $r$. Since this should capture the intensive margin of the treatment, I use all firms that are simultaneously active in both risk classes, around the decision time. Then, in columns (3)-(4) I have $y_{jtr}$ to be equal to $1\{Patents_{jtr} > 0\}$, which is a dummy equal to one if the firm $j$ applies to any granted patent in risk-group $r$ at time $t$. In this case, my sample is much larger and I consider every firm that has applied to at least one patent in the ten years before the decision. Standard errors are clustered at firm level. All regressions include a constant. $^{***}$ denotes significance at the 1% level, $^{**}$ at the 5%, and $^{*}$ at the 10%.
Table 7: Effect of the decision across firm size

(a) Heterogeneity by size: revenue

<table>
<thead>
<tr>
<th>Median Revenue</th>
<th>(1)</th>
<th>(2)</th>
<th>(3)</th>
<th>(4)</th>
<th>(5)</th>
<th>(6)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Small</td>
<td>Large</td>
<td>All</td>
<td>Small</td>
<td>Large</td>
<td>All</td>
</tr>
<tr>
<td>Post · Exposure(_j)</td>
<td>0.004**</td>
<td>-0.001</td>
<td>-0.001</td>
<td>0.005***</td>
<td>-0.001</td>
<td>0.002*</td>
</tr>
<tr>
<td></td>
<td>(0.002)</td>
<td>(0.001)</td>
<td>(0.001)</td>
<td>(0.002)</td>
<td>(0.001)</td>
<td>(0.001)</td>
</tr>
<tr>
<td>Post · Small(_j)</td>
<td>-0.004**</td>
<td>-0.003*</td>
<td>(0.002)</td>
<td>(0.002)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Post · Exposure(_j) · Small(_j)</td>
<td>0.004**</td>
<td>0.003*</td>
<td>(0.002)</td>
<td>(0.002)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Firm F.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td>Time F.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>N</td>
<td>N</td>
<td>N</td>
</tr>
<tr>
<td>Indu. × Time F.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Controls, (_j) × Time F.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(R^2)</td>
<td>0.017</td>
<td>0.007</td>
<td>0.022</td>
<td>0.120</td>
<td>0.076</td>
<td>0.072</td>
</tr>
<tr>
<td>Observations</td>
<td>956</td>
<td>1,078</td>
<td>2,034</td>
<td>956</td>
<td>1,078</td>
<td>2,034</td>
</tr>
</tbody>
</table>

(b) Heterogeneity by size: employment

<table>
<thead>
<tr>
<th>Median Employment</th>
<th>(1)</th>
<th>(2)</th>
<th>(3)</th>
<th>(4)</th>
<th>(5)</th>
<th>(6)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Small</td>
<td>Large</td>
<td>All</td>
<td>Small</td>
<td>Large</td>
<td>All</td>
</tr>
<tr>
<td>Post · Exposure(_j)</td>
<td>0.003**</td>
<td>-0.001</td>
<td>-0.001</td>
<td>0.005***</td>
<td>-0.001</td>
<td>0.002**</td>
</tr>
<tr>
<td></td>
<td>(0.002)</td>
<td>(0.001)</td>
<td>(0.001)</td>
<td>(0.002)</td>
<td>(0.001)</td>
<td>(0.001)</td>
</tr>
<tr>
<td>Post · Small(_j)</td>
<td>-0.004**</td>
<td>-0.003*</td>
<td>(0.002)</td>
<td>(0.002)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Post · Exposure(_j) · Small(_j)</td>
<td>0.004**</td>
<td>0.003*</td>
<td>(0.002)</td>
<td>(0.002)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Firm F.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td>Time F.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>N</td>
<td>N</td>
<td>N</td>
</tr>
<tr>
<td>Indu. × Time F.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Controls, (_j) × Time F.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(R^2)</td>
<td>0.016</td>
<td>0.003</td>
<td>0.021</td>
<td>0.112</td>
<td>0.058</td>
<td>0.073</td>
</tr>
<tr>
<td>Observations</td>
<td>969</td>
<td>1,065</td>
<td>2,034</td>
<td>969</td>
<td>1,065</td>
<td>2,034</td>
</tr>
</tbody>
</table>

These tables report the estimate of the linear difference-in-difference specification (equation 1), where I allow the effect of the exposure to the decision to be heterogeneous across firm size. The outcome is always R&D/Asset, which is the average over the period of the quarterly R&D expenses scaled by total assets. As usual, this is winsorized at 1%. The variable Exposure\(_j\) captures the exposure of firm \(_j\) to patent litigation, using patent application in the five years before the decision and patent litigation at technology class since 2000. Panel (a) reports the result measuring size based on revenue before the decision and in particular I divide the sample above and below the median. In Panel (b), I do the same but using employment as sorting variables. I first report the regressions as split between large and small firms, and then I report the fully interacted regression in the whole sample. I always control for firm and time fixed effects, but in Columns (4)-(6) I add extra controls interacted with time dummies. As in the previous analyses, I control for industry, location of the firm, the size of the portfolio before the estimation period, a dummy for “start-up”, which in this context is firms that published the first patent in the three years before the decision, and average quality of the patent portfolio in the pre period, measured by average citations. More information on the variables is provided in the Appendix (A.3). Standard errors are clustered at firm level. All regressions include a constant.*** denotes significance at the 1% level, ** at the 5%, and * at the 10%.
Table 8: Effect of the decision across measures of financial constraint

(a) Heterogeneity by dividend payers

<table>
<thead>
<tr>
<th></th>
<th>(1)</th>
<th>(2)</th>
<th>(3)</th>
<th>(4)</th>
<th>(5)</th>
<th>(6)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>No Dividend</td>
<td>Dividend</td>
<td>All</td>
<td>No Dividend</td>
<td>Dividend</td>
<td>All</td>
</tr>
<tr>
<td>Post · Exposure&lt;sub&gt;j&lt;/sub&gt;</td>
<td>0.003**</td>
<td>-0.002</td>
<td>-0.002</td>
<td>0.006***</td>
<td>-0.002</td>
<td>0.001</td>
</tr>
<tr>
<td></td>
<td>(0.001)</td>
<td>(0.002)</td>
<td>(0.002)</td>
<td>(0.003)</td>
<td>(0.002)</td>
<td>(0.001)</td>
</tr>
<tr>
<td>Post · 1{Div&lt;sub&gt;j&lt;/sub&gt; = 0}</td>
<td>-0.005***</td>
<td></td>
<td>(0.002)</td>
<td></td>
<td>-0.004**</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(0.002)</td>
<td></td>
<td></td>
<td></td>
<td>(0.002)</td>
<td></td>
</tr>
<tr>
<td>Post · Exposure&lt;sub&gt;j&lt;/sub&gt; · 1{Div&lt;sub&gt;j&lt;/sub&gt; = 0}</td>
<td>0.005**</td>
<td>0.005*</td>
<td>0.005*</td>
<td>0.005*</td>
<td>0.005*</td>
<td>0.005*</td>
</tr>
<tr>
<td></td>
<td>(0.002)</td>
<td>(0.003)</td>
<td>(0.003)</td>
<td>(0.003)</td>
<td>(0.003)</td>
<td>(0.003)</td>
</tr>
<tr>
<td>Firm F.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td>Time F.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>N</td>
<td>N</td>
<td>N</td>
</tr>
<tr>
<td>Indu. × Time F.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td>Controls&lt;sub&gt;j&lt;/sub&gt; × Time F.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td>R&lt;sup&gt;2&lt;/sup&gt;</td>
<td>0.019</td>
<td>0.016</td>
<td>0.019</td>
<td>0.105</td>
<td>0.092</td>
<td>0.069</td>
</tr>
<tr>
<td>Observations</td>
<td>1,322</td>
<td>712</td>
<td>2,034</td>
<td>1,322</td>
<td>712</td>
<td>2,034</td>
</tr>
</tbody>
</table>

(b) Heterogeneity by rating status

<table>
<thead>
<tr>
<th></th>
<th>(1)</th>
<th>(2)</th>
<th>(3)</th>
<th>(4)</th>
<th>(5)</th>
<th>(6)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>No Rating</td>
<td>Rating</td>
<td>All</td>
<td>No Rating</td>
<td>Rating</td>
<td>All</td>
</tr>
<tr>
<td>Post · Exposure&lt;sub&gt;j&lt;/sub&gt;</td>
<td>0.003**</td>
<td>-0.001</td>
<td>-0.001</td>
<td>0.005***</td>
<td>-0.001</td>
<td>0.002*</td>
</tr>
<tr>
<td></td>
<td>(0.001)</td>
<td>(0.001)</td>
<td>(0.001)</td>
<td>(0.002)</td>
<td>(0.001)</td>
<td>(0.001)</td>
</tr>
<tr>
<td>Post · 1{Rating&lt;sub&gt;j&lt;/sub&gt; = NO}</td>
<td>-0.003***</td>
<td></td>
<td>(0.001)</td>
<td></td>
<td>-0.001</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(0.002)</td>
<td></td>
<td>(0.001)</td>
<td></td>
<td>(0.001)</td>
<td></td>
</tr>
<tr>
<td>Post · Exposure&lt;sub&gt;j&lt;/sub&gt; · 1{Rating&lt;sub&gt;j&lt;/sub&gt; = NO}</td>
<td>0.004**</td>
<td>0.002</td>
<td>0.002</td>
<td>0.002</td>
<td>0.002</td>
<td>0.002</td>
</tr>
<tr>
<td></td>
<td>(0.002)</td>
<td>(0.002)</td>
<td>(0.002)</td>
<td>(0.002)</td>
<td>(0.002)</td>
<td>(0.002)</td>
</tr>
<tr>
<td>Firm F.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td>Time F.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>N</td>
<td>N</td>
<td>N</td>
</tr>
<tr>
<td>Indu. × Time F.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td>Controls&lt;sub&gt;j&lt;/sub&gt; × Time F.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td>R&lt;sup&gt;2&lt;/sup&gt;</td>
<td>0.014</td>
<td>0.012</td>
<td>0.014</td>
<td>0.092</td>
<td>0.089</td>
<td>0.066</td>
</tr>
<tr>
<td>Observations</td>
<td>1,336</td>
<td>698</td>
<td>2,034</td>
<td>1,336</td>
<td>698</td>
<td>2,034</td>
</tr>
</tbody>
</table>

These panels report the estimate of the linear difference-in-difference specification (equation 1), where I allow the effect of the exposure to the decision to be heterogeneous across firms characterized by different rating status or dividend policies. The outcome is always R&D/Asset, which is the average over the period of the quarterly R&D expenses scaled by total assets. As usual, this is winsorized at 1%. The variable Exposure<sub>j</sub>captures the exposure of firm <i>j</i> to patent litigation, using patent application in the five years before the decision and patent litigation at technology class since 2000. Panel (a) reports the result dividing the sample across firms that paid positive cash dividends in any quarters in the three years before the decision and firms that did not. In Panel (b), I do the same but sorting based on whether the firm has any rating reported in Compustat in the three years before, looking at S&P Domestic Long Term Issuer Credit Rating. I first report the regressions as split between the two groups, and then I report the fully interacted regression in the whole sample. I always control for firm and time fixed effects, but in Columns (4)-(6) I add extra controls interacted with time dummies. As in the previous analyses, I control for industry, location dummies of the firm, the size of the portfolio before the estimation period, a dummy for “start-up,” which in this context is firms that published the first patent in the three years before the decision, and average quality of the patent portfolio in the pre period, measured by average citations. More information on the variables is provided in the Appendix (A.3). Standard errors are clustered at firm level. All regressions include a constant.** denotes significance at the 1% level, * at the 5%, and * at the 10%.
Roadblock to Innovation: The Role of Patent Litigation in Corporate R&D

Appendix For Online Publication

Filippo Mezzanotti

A Appendix

A.1 Background information on “eBay v. MercExchange”

The main object of the dispute in the 2006 “eBay v. MercExchange” case was a patent on the popular “Buy It Now” function on the eBay platform (patent # 5,845,265). In the early 2000s, MercExchange accused eBay of infringing some of the company’s online auction patents. In 2003, the Virginia Circuit Court agreed with these accusations, but then decided to reject MercExchange’s request to issue an injunction on eBay’s technologies (Court, 2003). However, this decision was subsequently reversed by the Court of Appeals, which clearly stated that the issuance of a permanent injunction, “absent exceptional circumstances,” was a general rule in the U.S. intellectual property enforcement system. In 2005, eBay decided to petition this decision in front of the Supreme Court, which agreed to discuss the case in the following year. As I discuss in the paper, the final ruling of the Court rejects the idea that injunction should always be issued in normal cases after a patent violation.

In general, before 2006 injunction was issued almost automatically after a violation was proved. This legal practice dates back to a 1908 Supreme Court case between Continental Paper Bag and Eastern Paper Bag (Court, 1908). In this case, the Supreme Court clearly states that “exclusion may be said to have been of the very essence of the right conferred by the patent, as it is the privilege of any owner of property to use or not use it, without question of motive.” In practice, the only cases where a firm would not receive injunction is when the firm could successfully argue in favor of the public interest of its products. Otherwise, the ruling granted to patent owner full ability to exclude others from using the technologies covered by the patent.

A.2 Innovation and the law around the Supreme Court decision

An important threat to identification in this setting is the presence of other legal shocks that may affect innovation similarly to eBay. In order to be a relevant confounding factors, these legal shocks need to satisfy three conditions. First, these legal decisions need to be economically important. Second, we need to have some
prior that these changes will differentially affect firms along their exposure to patent litigation. Third, they need to happen around the same time as eBay, so they can explain the timing of our effects. In order to explore this potential issue, I examine other legal changes that happened around the same time (2003-2008) as eBay. Since I want to focus on legal changes that may have a large impact, I am going to look into other Supreme Court cases as well as other federal legislation.

Looking at other Supreme Court cases, I identify ten decisions that were related to patent law or covered R&D related issues. After examining these decisions, I think there are at least three reasons why these rulings are not likely to be an important confounding factor in my setting. First, the timing of the effect allows me to reasonably exclude that my results are driven by these legal changes. Combining the different margins, in the paper I start finding some effect of the policy by the end of 2006 or beginning of 2007. Therefore, it is hard to think that our results could be driven by other Supreme Court cases that happened sufficiently before or after eBay. In particular, it is unlikely that our estimates may be capturing the response to the Supreme Court cases happened in 2005 or earlier (Corp. of Am. Holdings v. Metabolite Labs., Inc or Merck KGaA v. Integra Lifesciences I, Ltd,...) because if that were the case, we would have expected to see some response, even minimal, before the end of 2006. Furthermore, this timing also allows us to exclude that our results may be capturing legal changes happening from the end of 2006 onwards (“MedImmune, Inc. v. Genentech, Inc” onward). In fact, this would imply that I start observing some effect in the data before or too close to the final decision of the policy.

The second reason why these Supreme Court cases should not affect my results is instead related to the scope of the decisions. One important aspect about eBay is that the ruling was relevant for essentially any firm active in intellectual property, since essentially every firm (with different degrees of exposure) was interested by patent litigation. This feature is unique in this period, since the scope of the other Supreme Court decisions generally appear narrower. In some cases, these decisions are narrower because they affect a specific feature of the law that are likely to be salient only for a small subset of firms. For instance, the case “Ill. Tool Works Inc. v. Indep. Ink, Inc” only affects firms that are considering tying behavior of two products, one at least covered by patents. While hard to quantify, tying behavior is not very common among innovative firms, and it is probably a minor concern in most technologies. In other cases, these alternative decisions are narrower because they are likely to apply only for a specific technology. For instance, “Microsoft Corp. v. AT&T Corp.”

59In order of time, these decisions are: Boeing Co. v. United States (March 4, 2003); Pharm. Research & Mfrs. of Am. v. Walsh (May 19, 2003); Lab. Corp. of Am. Holdings v. Metabolite Labs., Inc (February 28th, 2005); Johanns v. Livestock Mktg. Ass’n (May 23, 2005); Merck KGaA v. Integra Lifesciences I, Ltd. (June 13th, 2005); Ill. Tool Works Inc. v. Indep. Ink, Inc (March 1st, 2006); MedImmune, Inc. v. Genentech, Inc. (January 09, 2007); KSR Int’l Co. v. Teleflex Inc. (April 30th, 2007); Microsoft Corp. v. AT&T Corp. (April 30th, 2007); Quanta Computer, Inc. v. LG Elecs., Inc. (June 9th, 2008).

59The only decision that could potentially be consistent with the same timing as the one of the main results is “Ill. Tool Works Inc. v. Indep. Ink, Inc” (March 1st, 2006). However, as I discuss below, this intervention is not likely to affect our results, given the nature of the decisions.

60Another example is “MedImmune, Inc. v. Genentech, Inc.” is another example in this dimensions. In this case, the ruling was relevant only for firms actively licensing a technology. In general, only a small fraction of patents tend to be covered by licensing agreements (Gambardella et al., 2007) and this contract tends to be more prevalent for large firms.
is a case that is relevant only for software. At the same time, “Merck KGaA v. Integra Lifesciences I, Ltd.” is mostly of relevance for biomedical research.\textsuperscript{61} This narrower scope makes it hard to imagine that our exposure to litigation would actually end up capturing the effect of any of these policies, in particular once I consider the presence of the controls that characterize the analyses.\textsuperscript{62}

The third (and related) reason why my results are unlikely to be driven by the other decisions is that – in general – these other cases are considered to be less important than eBay. In general, eBay stands out as the most cited case when you examine the debate by lawyers and academics. In fact, among the cases considered, eBay is number one in terms of law review citations (1787 citations), before “KSR Int’l Co. v. Teleflex Inc.” (1178) and “MedImmune, Inc. v. Genentech, Inc.” (599). Similarly, eBay is also first in terms of Google Scholar references, identified using the online search tool (2990 citations), also in this case before “KSR Int’l Co. v. Teleflex Inc.” (1630) and “MedImmune, Inc. v. Genentech, Inc.” (884). Looking at the impact on the practice of law is clearly difficult, however one idea is to look at the citations by court documents. In this setting, I find that eBay is the second most cited decision in court documents (2529 citations). In this case, the most cited appears to be “KSR Int’l Co. v. Teleflex Inc.” (16347 citations), with “MedImmune, Inc. v. Genentech, Inc.” taking the third place (2104). Clearly, this evidence is neither a necessary nor sufficient condition for my argument. However, it supports to the notion that eBay was likely to be the main force driving the estimated effects.

On top of looking at other Supreme Court cases, I also look at federal legislation over the same period. The key takeaway is that there were no major changes in legislation that may explain our results. In general, the federal changes that were implemented had – at best – only a minor impact of the overall R&D incentives.\textsuperscript{63}

To be clear, the period considered was characterized by several attempts to undertake a deep change of patent law but these attempts were not successful. The most notable attempts were the 2005 and the 2007 Patent Reform Acts. However, these legislative attempts failed. In practice, most of the bills were funding bills that did not represent any large change relative to the status quo and were mostly focused on specific technologies.

Altogether, it is therefore very unlikely that my results can be explained by a concurrent legal change. In general, the federal law was stable during this period. Similarly, there was no clear candidate for Supreme Court decisions during this period that – looking at timing, scope, and importance – may have explained the results presented in the paper.

\textsuperscript{61}Lastly, in other cases – like “Boeing Co. v. United States” or “Lab. Corp. of Am. Holdings v. Metabolite Labs., Inc.” – the Court ended up more or less confirming the status quo, therefore it did not affect much the incentives to do innovation.

\textsuperscript{62}For instance, if a decision only affected one technology area (i.e. drugs), our controls for the major technology area interacted with time should control for this level of variation.

\textsuperscript{63}One potential caveat to this statement could be the “Medicare Prescription Drug, Improvement, and Modernization Act of 2003,” which caused a structural change in the funding of medical research and therefore could be (in theory) sufficiently important to affect our setting. However, I think that this bill is unlikely to affect our results for two main reasons. First, the policy may have affected the incentive to do R&D, but this shift in incentive is specific to the drug industry. Therefore, our specifications including the technology fixed-effects should take care of this. Second, the timing of our effects are completely inconsistent with the potential effects of this policy. In their study of the effect of the Medicare Act of 2003, Krieger et al. (2018) finds that the impact of the law can be identified within one year after its enactment (i.e. 2004). Therefore, to the extent that the policy was a confounding factor in our context, we should have detected its impact on the pre-period, but as discussed before, this was not the case.
A.3 Data

A.3.1 Samples

This is a more detailed clarification on Section (3) in the paper, where I discuss the data and variable construction.

Firm level data comes from two sources. Patent data comes from the Fung Institute (University of California at Berkeley),\textsuperscript{64} and they are an updated version of the Harvard Business School Patent Network Database (Li et al., 2014). In particular, I use all the assigned granted patents in the data, for which there are not missing information on the grant date, application date, assignee ID and technology class.\textsuperscript{65} It is worthy to point out that all analyses are carried based on application date, since I am interested in capturing a date closer to the time of an investment. The data were download in August 2014 and they contain all patents that were granted before 29th April 2014. For the full sample, I define a firm based on the assignee identifiers in the data for the analysis using the full set of innovative firms. For this identifier, I rely on the ID provided by the original Fung Institute data, based on name disambiguity (Li et al., 2014). To evaluate quality of the data, I compare them to the aggregate statistics that USPTO provides online.\textsuperscript{66} In particular, I compare patents granted to corporations according to USPTO aggregate data to the data used in this paper. I find that the two series almost overlap across the whole period and strongly co-move over 2002-2008 period. In the year, where they differ the most, the difference is only about of 2%.\textsuperscript{67}

Most of the analyses in the paper are carried using a sample of innovative firms, which are firms active in patenting before and after the decision. In particular, I define innovative firms as firms that applied to at least one patent in the two years before the decision and one in the year after this. The advantage of this approach is to have a sample that is the same when analyzing different sample period (one, two or three years after the decision). Furthermore, this sample is intrinsically balanced when I do the analysis considering data collapsed before and after the decision. When I am interested in the intensive margin, I need to consider a larger set of firms. In particular, I take firms that have at least one patent in the four years before the decision, but not necessarily anything afterwards.

In the second part of this work, I supplement patent level data with information on R&D at firm level for the subset of innovative firms, for which public information are available. Data on firms’ financials come from Compustat quarterly data. This allows me to construct pre and post period windows that are exactly around the Supreme Court decision. In order to add patent information to Compustat data, I use the data provided in Kogan et al. (2012). I construct a bridge file which is based on patent ID: this approach does not have the

\textsuperscript{64}Data can be found: http://funginstitute.berkeley.edu/tools-and-data (downloaded in August 2014).

\textsuperscript{65}To minimize the loss of information, I have supplemented missing information on the dates and technology class with data from Google USPTO patent data, which were nicely shared with me by Josh Feng.

\textsuperscript{66}Table can be found here: http://www.uspto.gov/web/offices/ac/ido/oeip/taf/h_at.htm#PartA2_1

\textsuperscript{67}This difference can stem from two things. First, it is not super clear how USPTO categorize companies, so there may be some discrepancy in this dimension. Second, the aggregate data looks at patent granted at a time different than April 2014. Third, part of difference is probably made up of patents that had missing info in the micro data, such as missing date or technology.
concerns of a matching performed by name. Essentially, I match the two data sets based on USPTO patent ID - as defined in the Fung Institute data - and then I use this match to bridge the assignee IDs to the ID used in Kogan et al. (2012). Since the assignee ID in the patent data is based on name disambiguity, one firm in patent data may correspond to more than one company ID in Compustat: therefore, the analysis at firm level use the more aggregate Compustat ID (gvkey). Furthermore, in about 90% of the cases, the company ID in the patent data corresponds to only one Compustat ID. In the remaining cases, I use the Compustat ID that received more unique matching over the period considered. An hand-check of the data supports the quality of this choice.

The final sample in the public firm data set is subject to some standard filters. In particular, I focus on non-financial companies and non-government related companies, with the headquarter in USA. Furthermore, I exclude firms that do not have a balance reporting around the decision. In particular, while some data entry may be missing for acceptable reasons, total assets and revenue should always be populated. I therefore eliminate those firms that do not have balance reporting on these variables in the four-year symmetric window around the shock, which is the same period I use for the analyses. Furthermore, I want to exclude those companies that may be under financial distress or restructuring: in order to do this, I exclude companies that systematically report negative equity over the usual period. Lastly, as in the rest of the paper, I focus only on innovative firms. All in all, I have a sample of more than one thousand firms. Using the Compustat IDs, I then also match the firm to stock returns information from CRSP.

In the end, as discussed in Section (3), I use patent lawsuits data from public filings to construct the measure of litigation size at technology class level. The data are collected from WestLaw, a subsidiary of Thomson Reuters. WestLaw is one of the primary provider of legal data in United States and use public records to develop a complete overview of lawsuits in United States. The same data, also known as Derwent LitAlert data, were previously used by other empirical work on patent litigation (e.g. Lerner 2006; Lanjouw and Schankerman 2001). Using the online tool LitAlert, I searched for all the litigation involving patents between 1980 and 2006. Every filing should report the date of the filing, the plaintiffs, the defendants and information on the intellectual property that is used to go to court. As a preliminary step, I eliminate the few filings with missing information about the date. To avoid issues with duplicates, I keep only one case in situations where multiple observations share the same entries for plaintiff, defendant, filing data and patents. Since I am interested in utility patents, at this point I keep only filings that report at least one utility patent. As discussed in Section (3), I make filings comparable across each other by reshaping the data at plaintiff-defendant-patent level. Then, I match patents with their technology fields and I aggregate them at technology class level over different periods of time. Lastly, I use equation (3) to construct the final score at technology class level.

68http://intranetsolutions.westlaw.com/practicepages/template/ip_litalert.asp?rs=IPP2.0&cvr=1.0
A.3.2 Variables definition

In the analysis involving the full sample of innovative firms, I use various outcomes.

For measuring intensity of innovation, I look at two measures. First, I look at the logarithm of the patents produced by the firm $j$ at time $t$, $\ln(\text{pat}_{jt})$, which is consistent to an intensive margin of our treatment. Using this outcome, I consider the sample of every firm, either private or public, which applied to at least one patent before and after the shock, as previously discussed. In this sample, there are slightly more than 16 thousand firms that satisfy this condition. Consistent with the literature, I count patents weighting them based on the number of assignee to which the patent is granted. In particular, I weight assignee equally. However, results are completely unaffected when I use a normal patent count, where I count patents as one even when assigned to multiple parties. Second, in order to estimate something closer to an extensive margin of the treatment, I consider an alternative outcome variable, which is a dummy equal to one when the firm has applied to any granted patent in the period, $1\{\text{Patent}_{jt} > 0\}$. In order to measure exposure to litigation for a firm, this has to have to at least one (applied) patent before the shock. Because of this, as I discussed before, I consider the set of firms that has at least one patent in the four years before the Supreme Court decision, for a total of around 77 thousand firms.\footnote{The outcome variable is constructed looking only at the two years before and after the shock, as in the intensive margin measure.} Results do not change if I shrink the window by looking only at three years before the decision or I increase it to six years before the decision.

For measuring quality of innovation, I construct few metrics based on patent citations. Following the literature in this area, I count patent citations at a fixed window - 3 years - after the granting (e.g. Bernstein, 2015). I then construct various outcomes based on this. I consider two main outcomes. First, I measure the average quality of the portfolio, by looking at the average number of adjusted citations. The citation adjustment is made to take care of the fact that the number of citations is highly heterogeneous across technology and across time. Following the literature, I make citations comparable by scaling them by the average number of citation received by a patent of the same vintage and technology class (Lerner and Seru, 2015). Second, I look at the probability that a company applies to patents that are at the top of the citation distribution in the relevant reference group as a proxy for breakthrough innovation. The reference group is composed by assigned patents that are the same USPTO technology class and were developed by the company in the same year, based on application date. I then look at whether the company has applied to any patent which is on the top 10% and 25% of the distribution of citations.

To analyze defensive patents, I also construct two other patent based measures. First, I measure the share of defensive patents by counting the number of patents that have low quality – measured by forward citations – but whose patent claim spans a very large set of different technologies, measured by originality (Hall et al., 2001). In practice, my outcome - which I refer as share of defensive patents - is the share of granted patent.
applications that are in the top 25\% in terms of originality among patents of same technology class and year, despite being in the bottom three quartiles in terms of citations for the same group. Second, I also construct a measure of the share of business method patents, looking at both patents are specifically in the business method category (class 705) or using a broader definition developed in Hall (2003).\textsuperscript{70}

I also use the patent data to construct a set of other controls. I construct a new measure of industry of the firm, which is based on patent application, rather than self-reporting industry. The main advantage of this measure is that I can use it both across public and private firms. Firm \( j \) is assigned to a certain industry by looking at the major industry in which the firm has applied to the highest number of patents. In line with the literature, major industries are defined as in the Appendix (1) of Hall et al. (2001). I use patents in the four years around the decision for the analysis. Similarly, I define a measure of location of the firm based on patent data. In particular, I assigned to firm \( j \) the location \( c \) if location \( c \) is the modal location for the patents applied in the four years before the Supreme Court decision. An extra code is used for firms for which no state location can be determined. I also construct a measure of size of the portfolio of the firm in question, looking at patents that were filled in the two years before the estimation window. The reason I use patent over this period is that I cannot use patenting before the decision inside the estimation window because this measure would be collinear with the outcomes.

In the second part of the paper, I then use a set of balance sheets variables. All balance sheet ratios are winsorize at 1\% (quarter-by-quarter) to ensure that results are not driven by outliers. My main measure of R&D intensity is R&D/Asset. R&D expenditure is measured using quarterly Compustat data (variable xrdq) and it is adjusted for acquisition of in process R&D expenses (variable rdipq), as in Mann (2018). Notice than the adjustment does not produce first-order effects in the outcome, as the share of firm-quarter with non-zero in process R&D expenses is, as expected, very small. The quarterly data are augmented, if missing, with yearly data to allow a more consistent coverage of firm R&D. Similarly, we also fill in missing quarterly observations with averages of the variable in adjacent quarters. Lastly, in line with the literature, missing R&D data is replaced with zero. Similarly to the patent data, the quarters in the Compustat data are created relative to the Supreme Court event. In particular, I re-label the second quarter of 2006 to be the first available quarter ending after the Supreme Court decision. I then rename the other quarters around this accordingly.

A.3.3 Stock Market data

When dealing with stock market data, I usually report the results both as raw returns and abnormal returns.

Raw returns are simply computed based on the standard stock returns. Abnormal returns are instead constructed relative to a benchmark, which is usually either the S&P500 or the NASDAQ. The S&P500 returns are also obtained from CRSP, while the NASDAQ data are obtained online from Yahoo Finance. In order

\textsuperscript{70}The list of these other technology classes is in Hall (2003) Table 3. In particular, these are technology classes: 84, 119, 379, 434, 472, 380, 382, 395, 700, 701, 702, 703, 704, 705, 706, 707, 709, 710, 711, 712, 713, 714, 715, 717, 902.
to construct abnormal returns, I compute the predicted returns estimating the $\beta$ of each stock using daily returns between 343 trading days before (January 1st 2005) and 30 trading days before the the eBay decision. Conditional on providing a sufficiently large window to estimate the $\beta$ precisely, results are not affected by the choice of the estimation window. When considering cumulative returns, I compute them as simple sum of the returns. Furthermore, when I use value-weights, I compute the weights based on equity capitalization seven trading days before the event considered (i.e. the eBay decision) and keep them constant throughout. Data on stock price and number of shares is collected through CRSP.

When I test the returns of NPEs around the event I report t-statistic, that tests the difference of the average returns from zero. This is constructed based on heteroskedasticity robust errors, and the estimation is implemented for simplicity using least-squares.

### A.3.4 Matching lawsuits to firm

This section explains how I identify in the data those patenting companies that were more likely to be plaintiff at the time of the ruling. The first step is to match companies by name across the assignee names available in the patent data and the information on plaintiff and defendant from Westlaw. Specifically, I use Westlaw to generate two lists of companies involved in patent litigation – one for defendant and one for plaintiff companies – using the filings between 2001 and 2005. There are a number of challenges in establishing this link. The primary challenge is the lack of standardization in the name of firm across the datasets. For example, a firm may be listed in the patent dataset as “The XYZ Company,” while in the defendant dataset, the same firm is listed as “XYZ, LLC.” Firms in the two data sets may be part of the same economic group, but file for patent or litigation under a different legal entity. Additionally, there may also be cases of firms’ names that are incorrectly transcribed.

To address these concerns, I use a combination of automatic and manual matching techniques. Each of the following procedures are performed for the plaintiff and defendant separately. First, I use automatic matching to divide the sample of plaintiffs in different groups depending whether a matching is sure, likely or unlikely. Using “pandas” package for Python 3.5, I clean every name in each dataset by first removing all punctuation and common abbreviations, such as AG, BV, INC, LLC, LTD, etc. The same cleaning procedure is applied to both patent and litigation data. Each cleaned name in the defendant (plaintiff) set was compared with the every cleaned name in the patent data via the “quick_ratio()” function of the “SequenceMatcher” class in the “difflib” package for Python 3.5. This procedure returns a number between 0 and 1 that measures the similarity between two strings. If the similarity was above 0.9, the two strings are said to be a probable match and are marked as such. If the two strings had a computed similarity of less than, or equal to 0.9, they are said to be an unlikely match and are marked as such. After this automatic matching, a final manual matching is completed using a research assistant. First, I assume that the pair where similarity equal to one is a true matching. Then,
we manually look at the other pairs, with particular interests to those that were categorize as a probable match (similarity above 0.9). As I find firms in the plaintiff and defendant lists that have a counterparty in the patent data, I also link this to the correspondent assignee ID in the patent data.

After completing this matching process, I use the information collected to construct a dummy that determines whether a company is more likely to be a plaintiff at the time of the ruling. Specifically, this variable is equal to one if the firm has been involved in (strictly) more litigation fillings during 2001-2005 as a plaintiff, rather than a defendant. For exposition purposes, I define the complementary group as the set of firms that are more likely to be defendant rather than plaintiffs.

A.4 Other analyses

A.4.1 The Supreme Court decision and stock prices

Announcement date

In the paper, I also examine the stock market reactions around some of the key events of the Supreme Court hearing. The key result is on the response around the announcement date. In particular, I find that firms that were more exposed to litigation experienced a small, positive out-performance right around the decision’s announcement. This result confirms that the shock was an economically relevant phenomenon and furthermore it confirms the quality of my empirical setting.

Previous research in finance has shown that innovation can positively affect the stock market valuation of firms (Kogan et al., 2012). If this is the case, an improvement in the enforcement of patents should positively affect the stock prices of innovative firms. This should be particularly the case for companies for which this dimension is particularly relevant, such as firms that operate in areas where patent litigation is intense. To start studying this question, I measure returns and abnormal returns around the announcement and I correlate these measures with the measure of litigation exposure. Then, I test how these returns correlate with the measures of exposure to litigation. Consistent with the previous results, I would expect an out-performance of firms operating in technologies that are more intensively litigated.

The main result of the analysis can be synthesized by Figure (4), which plots the cumulative value-weighted returns of high and low exposure firms, where the split is made at the top 25% of the litigation distribution. I find that the two groups behave in the same way in the days before the ruling. However, the day of the decision, the high-risk group outperforms the low-risk group by almost 1%. This out performance does not revert afterwards, and the two groups seem to present similar growth rates in the following dates.

In Table (A.1), I explore the same issue within a regression framework, where I run cross-sectional value-weighted regression between firm returns and ex-ante exposure to litigation. I use daily returns, since information from Supreme Court decisions tend to affect prices at relatively low frequency (Katz et al., 2017). As usual, I
focus on the sample of innovative public firms for which I find return information on CRSP around the time of decision. In columns (1) and (2), I find that companies that are more exposed to litigation performed better on the day of the decision. A one-standard deviation difference in exposure translates in 1% difference in returns. The results are essentially identical for both raw and abnormal returns. Furthermore, I obtain very similar coefficients when I look at a one-day window around the event (columns 3 and 4). This fact confirms that most of the movement in stock prices happen on the first day after the ruling was made public. I also show that the results are similar – albeit a bit smaller – when using the returns from the entire week after the decision (columns 5 and 6). Lastly, a formal test in columns 7 and 8 also rejects the presence of differential returns across firms in the week prior to the decision, confirming that the results were not driven by differential trends in returns.\textsuperscript{71}

**Case selection and oral hearing dates**

To better interpret these results, I repeat the same analysis looking at other dates that may carry important information about the final decision of the Court. In particular, I examine how the market moved during the date in which the Court agreed to hear the case (November 28th, 2005) and when they held the oral hearing (March 29th, 2006). Across the two dates, I repeat the same type of analysis that was conducted before.

Considering the date in which the Court agreed to hear the case, it is not clear ex-ante how I should expect the market to react. On the one hand, the fact that the Court decides to rule on this topic may be a good sign for eBay, which was the party that was petitioning to the Supreme Court. However, there are two factors that may counter-balance this effect. First, I do not know the ex-ante probability assigned by the market to this event. Second, the access to the Court does not necessarily imply anything about the direction of the decision. In this case, the lower courts provided conflicting views about the use of injunction. This implies that there were reasons for the Court to intervene in both directions. The estimates seem to support this mixed view. In fact, I do not find any systematic correlation between the exposure measures and returns around the data (columns (1)-(4), Table A.2). This is true when looking at both one day and three day returns, both raw and abnormal, following the same procedure of the paper. Importantly, these effects are not only non-significant, but also small in magnitude. This result suggest that the information provided by this event was not sufficient to change the expectation regarding the future of injunction.

The effects of the oral argument are also not easy to predict ex-ante. A key aspect to consider is that the new information will be positive and negative only in relationship with the expectation. Therefore, before going to the data, it could be useful to examine the qualitative information on the oral hearing. In general, the most common assessment of the hearing discussion is that it did not provide a clear insight on the intention of the

\textsuperscript{71}The only difference between the results is that for NPE some of the negative effects can also be seen on the trading day before the news. One explanation for this difference is that the content of the decision was uncertain, but it was known that the Supreme Court was going to release a decision soon. This effect may have triggered an increase in uncertainty for NPE, for which the decision was more salient and riskier.
Court. One reference to this claim is the reputable patent law blog Patently-O, which claimed “based on oral arguments, pundits see a potential split decision in the eBay v. MercExchange injunction case.”

However, some aspects of the debate may also suggest a more negative outcome for eBay. In particular, it was clear during the debate that some Justices were thinking about the issue within the context of traditional property right. This approach clearly was not particularly favorable to eBay’s case. For instance, Justice Scalia explicitly said during the discussion: “we’re talking about a property right here, and a property right is the exclusive right to exclude others.” At the same time, others pointed out the positive “momentum” of the MercExchange side, which was able to collect strong endorsements in the form of supportive amicus curiae by both the US Government and the American Bar Association. This hypothesis appears consistent with some of ex-post (relative to the decision) reactions. In fact, many news outlets reported that the later decision of the Supreme Court in favor of eBay was surprisingly. For instance, in May MarketWatch defined the ruling “a surprising turn” of the Court.

Following the same approach as before, I explore how stock prices responded to this shock. Looking at innovative firms, I find across the usual specification a consistent negative relation between exposure to litigation and returns (columns (5)-(8), Table A.2). This suggests a pattern that is opposite to what I detect when the actual final decision was released. Within the framework discussed in the paper, this seems to suggest that the information released around the oral argument was generally perceived as relative bad news for firms operating in high litigious areas. However, the magnitude of these effects is about one half of the positive effects that the same firms experienced during the announcement, therefore suggesting that the positive effect experienced once the outcome of the decision was released were more than sufficient to compensate this initial under-performance. Altogether, this evidence seems to be consistent with the idea that eBay did not come out as a clear winner from this phase. One interpretation is that the market was thinking that eBay was in need of a particularly successful argument to be able to turn the case in their favor, and that the market did not perceive this to happen. This seems to be generally consistent with the qualitative evidence described before, which seems to rule out that the oral argument moved the needle in favor of eBay. Furthermore, this seems also consistent with the general prior that the Supreme Court is on average more likely to avoid to create a precedent.

Altogether, this analysis of returns around the key dates of the Supreme Court decision “eBay v. MercExchange” provides two main takeaways. First, the results reinforce the idea that the actual decision was unexpected and economically relevant. Consistent with this hypothesis, I find large response in the stock prices of innovative firms around the announcement and oral hearing dates. Indeed, these dates are the moments

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72 https://patentlyo.com/patent/2006/03/ebay_v_mercexch_3.html
73 In particular, on March 10th – two weeks before the oral argument of the case - the Office of the Solicitor General (OSG), on behalf of both the Federal Trade Commission and the antitrust division of the Justice Department, asked to confirm the injunction to eBay See for reference, Washington Post article on this issue “Government Sides Against eBay in Patent Dispute,” March 11th 2006. A copy is available online at the following link: http://www.washingtonpost.com/wp-dyn/content/article/2006/03/10/AR2006031001918.html. See also https://patentlaw.typepad.com/eBay/MercGovt.pdf.
74 American Bar Association: https://patentlaw.typepad.com/patent/MercABA.pdf
with the highest information content. Second, our measure of litigation exposure seems to capture relevant information. Furthermore, this evidence appears also consistent with the idea that the new rules was perceived as value-enhancing for innovative firms. In fact, I find that firms more exposed to litigation risks outperformed during the announcement, and this outperformance was double the size of the underperformance during the hearing date.\footnote{The interpretation as “value-enhancing” – as measured by stock prices – is not a necessary condition for the overall policy evaluation. It is possible that a policy that increases innovation ex-post may not be perceived ex-ante as value-enhancing.}

### Table A.1: Stock Market returns at the Announcement and Litigation Exposure

<table>
<thead>
<tr>
<th>Exposure_j</th>
<th>Event Day</th>
<th>Event [−1; +1]</th>
<th>Event [0; +5]</th>
<th>Event [−5; −1]</th>
</tr>
</thead>
<tbody>
<tr>
<td>0.008***</td>
<td>0.008***  0.013***  0.011***  0.009**  0.006*  0.001  -0.001</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(0.001)</td>
<td>(0.002)   (0.002)   (0.002)   (0.003)  (0.004)  (0.003)  (0.003)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Observations</td>
<td>992 992 992 992 992 992 992 992</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

The table reports cross-sectional value-weighted regressions between litigation exposure and returns. Returns are measured either raw or as abnormal returns, where this is constructed as \( r_j - \beta_j r^{S&P 500} \), where \( \beta \) are estimated by firm regressions between one month and twelve months before the decision. Furthermore, returns are measured over different windows, which are reported in the header of the table. Returns are winsorized at 1%. The variable \( \text{Exposure}_j \) captures the exposure of firm \( j \) to patent litigation, using patent application in the five years before the decision and patent litigation at technology class since 2000. The weights are given by the firm market value of equity seven days before the decision. Standard errors are robust to heteroskedasticity. More info on the variables are provided in the Appendix (A.3). All regressions include a constant. *** denotes significance at the 1% level, ** at the 5%, and * at the 10%.

### Table A.2: Stock Market returns around other dates

<table>
<thead>
<tr>
<th>Exposure_j</th>
<th>Announcement Hearing Oral Argument</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Event Day</td>
</tr>
<tr>
<td>0.001</td>
<td>0.001     -0.003    -0.003    -0.004*** -0.003*** -0.006*** -0.007***</td>
</tr>
<tr>
<td>(0.002)</td>
<td>(0.002)   (0.002)   (0.002)   (0.001)   (0.001)   (0.002)   (0.002)</td>
</tr>
<tr>
<td>Observations</td>
<td>992 992 992 992 992 992 992 992</td>
</tr>
</tbody>
</table>

The table reports cross-sectional value-weighted regressions between litigation exposure and returns. The first four columns explore the returns around the date in which the Supreme Court announced that the case was going to be heard (November 28th, 2005). In columns (1) and (2), I look at the returns in the day, while in columns (3) and (4) I look at the returns between the day before and the day after. The next four columns explore the returns around the date of the oral argument (March 29th, 2006). In columns (5) and (6), I look at the returns in the day, while in columns (7) and (8) I look at the returns between the day before and the day after. Standard errors are robust to heteroskedasticity. More info on the variables are provided in the Appendix (A.3). All regressions include a constant. *** denotes significance at the 1% level, ** at the 5%, and * at the 10%.

### A.4.2 The timing of the effects

In this section, I discuss more carefully the timing of the effects. This set of analyses are also presented in short in the main body of the paper and they complement the pre-trend analyses.

The first result is provided by Table (A.3). In this Table, I study how the effects change across different time windows. In particular, I repeat the same estimation as before, keeping the pre-period fixed and moving the post-period to one, two and three years after the Supreme Court decision. Consistent with the patterns

\[ \text{Equation 1} \]
shown in Figure (5), there are two results to highlight. First, the effect is increasing over time. Relative to one year after the decision, the effect over two years increases by 38% and over three years by 50%. This is consistent with the idea that changes in the production function of innovation will reflect in the output with a lag. Second, the model measures some positive effect on innovation output already after one year. While this quick response around the decision is reassuring in terms of identification, this result also raises the concerns that – at least partially – the increase in the rate of patent applications may stem from a shift in patenting incentive rather than a true change in the innovation.

To shed light on this issue, I explore the heterogeneity of the results across industries. In Table (A.4), I show that the whole positive result in the first year is driven by companies whose main industry is “Computer and Communications” (Hall et al., 2001). For this area, the R&D cycle is faster than the other technologies and therefore it is not surprising that these companies can react quicker to a change in incentives. However, the difference between this industry and the rest of the sample fades away over time. This confirms that the larger one-year effect does not reflect that this industry was, all else equal, more impacted by the ruling, but rather a different timing of the R&D cycle.

Lastly, I also show that results are not short-lived. In Figure (A.1), I replicate the main figure reporting the dynamic of the effects using data on patents application up to 2010. In general, I find that our effects are still economically and statistically significant almost five years after the decision. This result confirms that our estimates do not capture a short-lived spike in patenting, but rather a persistent shift in the incentives to innovate. By the same token, Figure (A.2) replicates the same result adding the various controls interacted with the post-variable, as in the main table. As expected, the result is qualitatively the same. If anything, these results appear more precisely estimated and larger in magnitude.

<table>
<thead>
<tr>
<th>1 Year After</th>
<th>2 Years After</th>
<th>3 Years After</th>
</tr>
</thead>
<tbody>
<tr>
<td>ln(Patentsjt)</td>
<td>ln(Patentsjt)</td>
<td>ln(Patentsjt)</td>
</tr>
<tr>
<td>Post · Exposure_{LARGE}</td>
<td>Post · Exposure_{LARGE}</td>
<td>Post · Exposure_{LARGE}</td>
</tr>
<tr>
<td>0.037***</td>
<td>0.050***</td>
<td>0.058***</td>
</tr>
<tr>
<td>(0.012)</td>
<td>(0.012)</td>
<td>(0.012)</td>
</tr>
<tr>
<td>Firm F.E.</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td>Time F.E.</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td>$R^2$</td>
<td>0.209</td>
<td>0.005</td>
</tr>
<tr>
<td>Observations</td>
<td>32,118</td>
<td>32,118</td>
</tr>
</tbody>
</table>

In this table I report the estimation of the equation 1. The data set is constituted by a balanced two-period panel. The first period is fixed to the two year before the decision, while the second period depends on the specification and in particular it moves from 1 to 3 years after. The outcome is always the (natural) logarithm of granted patent that firm $j$ applied during period $t$. In this case, I use every firm that applied to at least one patent in the two year before and in the year after the decision. The variable Exposure$_{j}$ captures the exposure of firm $j$ to patent litigation, using patent application in the five years before the decision and patent litigation at technology class since 2000. Similarly, the variable Exposure$_{LARGE}^{LARGE}$ captures the exposure of firm $j$ to patent litigation, using patent application in the ten years before the decision and patent litigation at technology class since 1980. More information on the variables is provided in the Appendix (A.3). Standard errors are clustered at firm level. All regressions include a constant.*** denotes significance at the 1% level, ** at the 5%, and * at the 10%.
This figure plots the $\beta$ from equation (4). Relative to Figure (5), the only difference is that I use a longer post-period. The red vertical line corresponds to the last period of the pre-decision period. Every $\beta_t$ is plotted with the corresponding CI at 5%. Every period is labeled with the corresponding quarter. Notice that quarters are in “event time” not calendar time: in fact, I set the end of the first quarter artificially to be the one ending in May 15th (the other quarters are constructed relative to this). The data used is between two years before eBay up to the end of 2010. The sample used corresponds to the one of the extensive margin. Standard errors are clustered at the firm-level.
In this table I report the estimation of the equation 1, where I interact the shock measure with a dummy for firms that are in the Computer industry, as defined in Appendix A.3. The data set is constituted by a balanced two-period panel. The first period is fixed to the two year before the decision, while the second period depends on the specification and in particular it moves from 1 to 3 years after. The outcome is always the (natural) logarithm of granted patent that firm $j$ applied during period $t$. In this case, I use every firm that published at least one patent in the two year before and in the year after the decision. The variable $Exposure_j$ captures the exposure of firm $j$ to patent litigation, using patent application in the five years before the decision and patent litigation at technology class since 2000. Similarly, the variable $Exposure^{LARGE}_j$ captures the exposure of firm $j$ to patent litigation, using patent application in the ten years before the decision and patent litigation at technology class since 1980. Standard errors are clustered at firm level. All regressions include a constant.*** denotes significance at the 1% level, ** at the 5%, and * at the 10%.

<table>
<thead>
<tr>
<th></th>
<th>1 Year After</th>
<th>2 Years After</th>
<th>3 Years After</th>
</tr>
</thead>
<tbody>
<tr>
<td>$Post \cdot Exposure_j$</td>
<td>0.002</td>
<td>0.037***</td>
<td>0.051***</td>
</tr>
<tr>
<td></td>
<td>(0.009)</td>
<td>(0.009)</td>
<td>(0.010)</td>
</tr>
<tr>
<td>$Post \cdot Exposure_j \cdot Computer$</td>
<td>0.093***</td>
<td>0.008</td>
<td>-0.004</td>
</tr>
<tr>
<td></td>
<td>(0.019)</td>
<td>(0.030)</td>
<td>(0.022)</td>
</tr>
<tr>
<td>$Post \cdot Exposure^{LARGE}_j$</td>
<td>0.004</td>
<td>0.052***</td>
<td>0.072***</td>
</tr>
<tr>
<td></td>
<td>(0.013)</td>
<td>(0.014)</td>
<td>(0.010)</td>
</tr>
<tr>
<td>$Post \cdot Exposure^{LARGE}_j \cdot Computer$</td>
<td>0.085***</td>
<td>0.016</td>
<td>-0.009</td>
</tr>
<tr>
<td></td>
<td>(0.027)</td>
<td>(0.029)</td>
<td>(0.030)</td>
</tr>
<tr>
<td>Firm F.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td>Time F.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td>$R^2$</td>
<td>0.215</td>
<td>0.215</td>
<td>0.006</td>
</tr>
<tr>
<td>Observations</td>
<td>32,128</td>
<td>32,128</td>
<td>32,128</td>
</tr>
</tbody>
</table>
This figure plots the $\beta_t$ from equation (4). Relative to Figure (5), here I use a longer period and I also include all the controls interacted with the post-variable, as in the main table. The red vertical line corresponds to the last period of the pre-decision period. Every $\beta_t$ is plotted with the corresponding CI at 5%. Every period is labeled with the corresponding quarter. Notice that quarters are in “event time” not calendar time: in fact, I set the end of the first quarter artificially to be the one ending in May 15th (the other quarters are constructed relative to this). The data used is between two years before eBay up to the end of 2010. The sample used corresponds to the one of the extensive margin. Standard errors are clustered at the firm-level.

A.4.3 Permutation test

As quickly presented in Section 5), I develop a permutation test (Chetty et al. 2009; Fisher 1922) as a further robustness on my results. With this test, I compare the t-statistic from my analysis to a non-parametric distribution of statistics that I obtain by randomly assigning technology classes to firms. The objective of this test is twofold. First, this methodology allows me to provide inference based on weaker assumptions than the standard linear model. Second, this test can be used to evaluate whether my analysis is capturing some other spurious firm characteristic that is different than litigation exposure but somehow correlated with it. For instance, this analysis allows me to reject that my results are somehow driven mechanically by the way the exposure index is constructed.

The intuition for this test is simple: if my results correctly capture the exposure to litigation through the technology fields, I would expect to find no results when technology exposure is randomly assigned. Rather than a one-to-one comparison, I implement this test by constructing a full distribution of test statistics obtained in this way. If my model is correctly capturing true exposure to patent litigation, I would expect the true statistic to be on the top percentiles of this distribution.

In short, the procedure is implemented in the following way: I start by re-assigning randomly the technology
classes in which a company operates for every firm in the sample. Then, based on this, I reconstruct the exposure index $Exposure_j$ and I run the main specification presented before. I repeat this procedure for a thousand random iterations and then I plot the non-parametric distribution of the t-statistic I obtain from this. I compute the p-value of my true model by looking at the percentile in which my true t-statistic is within the constructed distribution. As expected, I find that the p-value constructed based on the random permutation test is similar to the standard one, and lower than 1% (Figure A.3). Also this test confirms the quality of my empirical framework.

Figure A.3: Permutation Test: distribution of test statistic

This figure reports the results of the permutation test, where I compare the value of the t-statistic to the “true results” - shown by the straight red line - to the distribution of statistics that are constructed randomly assigning industries to firms. The procedure is the following (discussed extensively in Appendix A.4.3). For every iteration of the procedure, I randomly assign technology class to firms. Then, I run the standard regression and store the t-statistic. Finally, after one thousand iterations, I plot them in a histogram as above. As mentioned, I plot the true estimates using the red line: in this case belongs to the top 1% of the distribution of coefficients.

A.5 Other Figures and Tables

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77For instance, a firm that has obtained two patents in class 131 (Tobacco) and three in 428 (Stock material or miscellaneous articles) can be assigned to have two patents in class 432 (Heating) and three in 125 (Stone working).
This figure plots the average cumulative abnormal returns, for the sample of NPEs identified in the paper. The sample of firms used are 10 companies that are (a) Identified as NPEs; (b) Public at the time of the Supreme Court decision. The companies are Acacia Technologies, Asure Software, Rambus, Tessera Technologies, VirnetX Holding Corp., Universal Display, Document Security Systems, Pendrell, ParkerVision, Unwired Planet, Interdigital, Spherix. Information on the sample constructions are provided in Section (2.2). Abnormal returns are constructed with respect to the S&P500, as discussed in the Appendix (A.3.3). The straight red line correspond to the trading day right before the decision.
Figure A.5: Persistence of patent litigation over time

This figure provides a scatter plot of the size of litigation technology class level, as measured by equation (3), measured over two samples. In the vertical axis, I measure it using lawsuits between 1980 and 2000. In the horizontal axis, I use data between 2000 and 2006 (excluded). More information for the construction of this measure is provided in Section (3). For the clarity of the figure, I used every technology class with score $p_c$ lower than 1.5. The blue line in the figure is the linear fit of the data, which has a coefficient of 1.05 in this case.

Figure A.6: Effect of litigation over time

This figure plots the $\beta_t$ from equation 4, using the usual sample. With respect to the other Figure (A.6), this is identical but with different outcomes. In order, I consider as outcomes the scaled number of patents (as alternative to the main patent outcomes), average scaled citation and dummies for firm patenting at top of the distribution (10% and 25%). More detailed description of the outcomes are in Appendix (A.3). The red vertical line correspond to the last period of the pre-decision period. Every period is label with the corresponding quarter. Notice that quarters are in “event time” not calendar time: in fact, I set the end of the first quarter artificially to be the one ending in May 15th (the other quarters are constructed relative to this). Data used corresponds at the two years before and after the decision.
Table A.5: Robustness: differential linear effect before and after the shock

<table>
<thead>
<tr>
<th></th>
<th>(1)</th>
<th>(2)</th>
<th>(3)</th>
<th>(4)</th>
<th>(5)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>( \ln(Patents_{jt} + 1) )</td>
<td>( Patent_{jt}^{scaled} )</td>
<td>( 1{Patent_{jt} = Top^{10%}} )</td>
<td>( 1{Patent_{jt} = Top^{25%}} )</td>
<td>Average Scaled Citations</td>
</tr>
<tr>
<td>( Post \cdot Exposure_{jt} )</td>
<td>0.011***</td>
<td>0.013***</td>
<td>0.004*</td>
<td>0.010***</td>
<td>0.025*</td>
</tr>
<tr>
<td></td>
<td>(0.004)</td>
<td>(0.003)</td>
<td>(0.002)</td>
<td>(0.003)</td>
<td>(0.014)</td>
</tr>
<tr>
<td>( Pre \cdot Exposure_{jt} )</td>
<td>0.003</td>
<td>0.002</td>
<td>0.001</td>
<td>0.001</td>
<td>0.013</td>
</tr>
<tr>
<td></td>
<td>(0.004)</td>
<td>(0.003)</td>
<td>(0.002)</td>
<td>(0.003)</td>
<td>(0.014)</td>
</tr>
<tr>
<td>Firm F.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td>Indus. \times Time F.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td>( R^2 )</td>
<td>0.001</td>
<td>0.010</td>
<td>0.001</td>
<td>0.002</td>
<td>0.001</td>
</tr>
<tr>
<td>Observations</td>
<td>257,024</td>
<td>257,024</td>
<td>257,024</td>
<td>257,024</td>
<td>257,024</td>
</tr>
</tbody>
</table>

In the table, I report the estimation of an equation where I use the data as a panel and I estimate the same specification as equation (1). The key difference is that I estimate differential trends both before and after the shock. To be precise, I look at the effect of \( Exposure_{jt} \) (constructed as in the main analyses) interacted with two dummies: (a) the post dummy is equal to one after the decision (equal to one for quarters after May 15th 2006); (b) the dummy pre is equal to one starting two quarters before the decision. In other words, the quarter right before the decision is set to zero for both dummies, and therefore it represents the control period in this analysis, and all the effects can be interpreted as changes relative to this quarter. The specification is augmented with technology trends, using the major technology of the firm interacted with time dummies, as in the main analysis. The data set is constituted by a panel with eight quarter and it is balanced in any specification. In any case, I use every firm that published at least one patent in the two year before and in the year after the decision. Column (1) has the (natural) logarithm plus one of granted patent that firm \( j \) applied during period \( t \). Column (2) has granted patent that firm \( j \) applied during period \( t \), scaled by the total number of patents in the two years before the decision. Columns (3) and (4) have the dummy which is equal to one whether the firm \( j \) applied during period \( t \) at least to one patent that is in the top 10% or 25% of the matched patents (same year and same technology class). Column (5) has the (natural) logarithm plus one of granted patent that firm \( j \) applied during period \( t \) weighted by citations received in the first three years of life. Citations are scaled by the average number of citations received by the patents in the same technology class and year. More information on the data is available in the Appendix (A.3). All regressions include a constant. Standard errors are clustered at firm level. All regressions include a constant.*** denotes significance at the 1% level, ** at the 5%, and * at the 10%.
This figure presents the results from a set of placebo tests. In particular, I construct a series of placebo samples, centered around fictional shocks in the two years that are completely outside the period after the decision. The date in the x-axis is the quarter around which the analysis is centered. In each case, I reconstruct the data around this placebo shock, both the outcomes and the measures of exposure $Exposure_j$. Then, I run the standard regression. The figure plots the $\beta$ from equation (1), as well as the 95% confidence intervals, estimated over different samples. For clarity, I estimate the simple equation without further controls and looking at R&D as outcome, like in the main analyses. Notice that quarters are in “event time” not calendar time: in fact, I set the end of the first quarter artificially to be ending in May 15th (the other quarters are constructed accordingly). Data used corresponds to the two years before and after the decision, in event time. Standard errors are clustered at the firm level.
Table A.6: Stock Market returns for NPEs around the shock

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Event [-1; +1]</td>
<td>-0.034***</td>
<td>-0.038***</td>
<td>-0.036**</td>
<td>-0.033**</td>
<td>-0.076***</td>
<td>-0.064***</td>
<td>-0.026</td>
<td>-0.071</td>
<td>0.129*</td>
<td>0.063</td>
</tr>
<tr>
<td>Event [-5; -1]</td>
<td>(0.008)</td>
<td>(0.008)</td>
<td>(0.012)</td>
<td>(0.013)</td>
<td>(0.015)</td>
<td>(0.014)</td>
<td>(0.045)</td>
<td>(0.046)</td>
<td>(0.057)</td>
<td>(0.054)</td>
</tr>
<tr>
<td>Event [-20; -5]</td>
<td>10</td>
<td>10</td>
<td>10</td>
<td>10</td>
<td>10</td>
<td>10</td>
<td>10</td>
<td>10</td>
<td>10</td>
<td>10</td>
</tr>
<tr>
<td>Event [-40; -5]</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

This Table reports the average returns -either raw or abnormal-over a specific time span for the set of NPEs considered in Section (2), and a t-test for the difference from zero of the average. Standard errors are robust to heteroskedasticity. Abnormal returns refer to abnormal returns with respect to the S&P 500. More info on the test is available in Appendix (A.3.3). *** denotes significance at the 1% level, ** at the 5%, and * at the 10%.
This table reports construction of technology-class size of patent litigation, as it is described in Section (2), and in particular by equation (3).
Table A.8: Effect of the policy change on patenting: robustness with alternative *Exposure* measure

<table>
<thead>
<tr>
<th>OLS</th>
<th>(1)</th>
<th>(2)</th>
<th>(3)</th>
<th>(4)</th>
<th>(5)</th>
<th>(6)</th>
</tr>
</thead>
<tbody>
<tr>
<td><em>Post · Exposure\textsubscript{LARGE}^j</em></td>
<td>0.050***</td>
<td>0.049***</td>
<td>0.047***</td>
<td>0.014***</td>
<td>0.037***</td>
<td>0.037***</td>
</tr>
<tr>
<td></td>
<td>(0.012)</td>
<td>(0.016)</td>
<td>(0.015)</td>
<td>(0.003)</td>
<td>(0.003)</td>
<td>(0.003)</td>
</tr>
<tr>
<td><em>Firm F.E.</em></td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td><em>Time F.E.</em></td>
<td>Y</td>
<td>N</td>
<td>N</td>
<td>Y</td>
<td>N</td>
<td>N</td>
</tr>
<tr>
<td><em>Indu. × Time F.E.</em></td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td><em>Controls\textsubscript{j} × Time F.E.</em></td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td><em>R^2</em></td>
<td>0.005</td>
<td>0.007</td>
<td>0.033</td>
<td>0.216</td>
<td>0.282</td>
<td>0.290</td>
</tr>
<tr>
<td><em>Observations</em></td>
<td>32,128</td>
<td>32,128</td>
<td>32,128</td>
<td>155,876</td>
<td>155,876</td>
<td>155,876</td>
</tr>
</tbody>
</table>

In this table I replicate the estimates from Table (2), using an alternative measure to firm exposure to litigation, *Exposure\textsubscript{LARGE}^j*. In particular, this alternative variable captures the exposure of firm *j* to patent litigation, using patent application in the ten years before the decision and patent litigation at technology class since 1980. I estimate equation (1), which is *y\textsubscript{jt} = \alpha_j + \alpha_t + \beta(Exposure\textsubscript{j} · Post) + \gamma X\textsubscript{jt} + \epsilon\textsubscript{jt}*, where *y\textsubscript{jt}* is: (a) the (natural) logarithm of granted patent that firm *j* applied during period *t* for Columns (1)-(3); (2) a dummy equal to one if the firm *j* applied to at least one patent in period *t*. The data set is a balanced two-period panel. Each period collapses firm information in the two years before and two years after the Supreme Court decision. The sample depends on the outcome: when looking at the intensive margin (columns 1-3) I use every firm that published at least one patent in the two year before and in the year after the decision; when I look at the extensive margin (columns 4-6) I use the sample of every firm with at least one patent in the five year before the decision, which is the minimal requirement to construct the measure of exposure. In Columns (1) and (4), I control for firm fixed-effects and time effects. In Column (2) and (5), I add industry-time fixed effect to the equation. Industry are constructed based on the macro technology area where the company patented the most over the four years before the decision, where macro technology classes are constructed as in Hall et al. (2001). In Columns (3) and (6), I further augment the specification using location dummies of the firm (constructed using the modal location reported in patent data), the size of the portfolio before the estimation period, the start-up status (looking at whether a firm applied for the first patent ever within the previous three years) and average quality of the patent portfolio in the pre period, measured by average citations. All these controls are interacted with a time dummy to allow the variable to have a differential effect before and after. More information on the variables is provided in the Appendix (A.3). Standard errors are clustered at firm level. All regressions include a constant.*** denotes significance at the 1% level, ** at the 5%, and * at the 10%.
Table A.9: Effect of the policy change on patenting: Poisson model

<table>
<thead>
<tr>
<th></th>
<th>(1)</th>
<th>(2)</th>
<th>(3)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Poisson</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Post \cdot Exposure_j)</td>
<td>0.043***</td>
<td>0.046**</td>
<td>0.039**</td>
</tr>
<tr>
<td></td>
<td>(0.015)</td>
<td>(0.021)</td>
<td>(0.020)</td>
</tr>
<tr>
<td>Firm F.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td>Time F.E.</td>
<td>Y</td>
<td>N</td>
<td>N</td>
</tr>
<tr>
<td>Indu. \times Time F.E.</td>
<td>Y</td>
<td>Y</td>
<td></td>
</tr>
<tr>
<td>Controls(j) \times Time F.E.</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Observations</strong></td>
<td>257,024</td>
<td>257,024</td>
<td>257,024</td>
</tr>
</tbody>
</table>

This table reports the estimate of the standard difference-in-difference specification (equation 1) using an equivalent fixed-effect Poisson model. The properties of the Poisson model implies that the parameter \(\beta\) on the main variable of interest \(Post \cdot Exposure_j\) can be interpreted as a semi-elasticity, similarly to the log-linear difference-in-difference model previously estimated. In this model, the outcome is the number of granted patent applications made by firm \(j\) in period \(t\). The data set is a balanced quarterly panel over the same set of innovative firms employed before. The variable \(Exposure_j\) captures the exposure of firm \(j\) to patent litigation, using patent application in the five years before the decision and patent litigation at technology class since 1990. In every specification, I essentially control for both firm and quarter fixed effects. In Column (2), I add industry-time fixed effect to the equation. Industry are constructed based on the macro technology area where the company patented the most over the four years before the decision, where macro technology classes are constructed as in Hall et al. (2001). In Columns (3), I further augment the specification using location dummies of the firm (constructed using the modal location reported in patent data), the size of the portfolio before the estimation period, the start-up status (looking at whether a firm applied for the first patent ever within the previous three years) and average quality of the patent portfolio in the pre period, measured by average citations. All these controls are interacted with a time dummy to allow the variable to have a differential effect before and after the decision. More information on the variables is provided in the Appendix (A.3). Standard errors are clustered at firm level. All regressions include a constant. *** denotes significance at the 1% level, ** at the 5%, and * at the 10%.

Table A.10: Evidence on patent quality: alternative citation measure

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<tr>
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<tbody>
<tr>
<td><strong>OLS</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Post \cdot Exposure_j)</td>
<td>-0.010</td>
<td>0.090***</td>
<td>0.091***</td>
</tr>
<tr>
<td></td>
<td>(0.016)</td>
<td>(0.027)</td>
<td>(0.027)</td>
</tr>
<tr>
<td>Firm F.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td>Time F.E.</td>
<td>Y</td>
<td>N</td>
<td>N</td>
</tr>
<tr>
<td>Indu. \times Time F.E.</td>
<td>Y</td>
<td>Y</td>
<td></td>
</tr>
<tr>
<td>Controls(j) \times Time F.E.</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>R^2</strong></td>
<td>0.007</td>
<td>0.010</td>
<td>0.013</td>
</tr>
<tr>
<td><strong>Observations</strong></td>
<td>32,128</td>
<td>32,128</td>
<td>32,128</td>
</tr>
</tbody>
</table>

These panels report the estimate of the linear difference-in-difference specification (equation 1), where I estimate the effect of the decision on the quality of innovation. In particular, I estimate \(y_{jt} = \alpha_j + \alpha_t + \beta(Exposure_j \cdot Post) + \gamma X_{jt} + \epsilon_{jt}\), where \(y_{jt}\) is a proxy of average quality of innovation in the two years before and after the decision. In particular, this table provides a robustness where I check how the result on average citations change once I do not adjust citations by technology class. In particular, the outcome on this analysis is the average number of citations, without any further adjustment. As before, the data set is a balanced two-period panel where I employ every firm that published at least one patent in the two year before and in the year after the decision. The variable \(Exposure_j\) captures the exposure of firm \(j\) to patent litigation, using patent application in the five years before the decision and patent litigation at technology class since 2000. I always control for firm fixed-effects and time effects, Furthermore, I always augment the specification with industry-time fixed effect, which are constructed based on the macro technology area where the company patented the most over the four years before the decision (Hall et al. (2001)). Lastly, I further augment every specification with location dummies of the firm (constructed using the modal location reported in patent data), the size of the portfolio before the estimation period and the start-up status (looking at whether a firm applied for the first patent ever within the previous three years). More information on the variables is provided in the Appendix (A.3). Standard errors are clustered at firm level. All regressions include a constant. *** denotes significance at the 1% level, ** at the 5%, and * at the 10%. 

25
Table A.11: Evidence on patent quality: alternative breakthrough measure

<table>
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<tr>
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<th>(3)</th>
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</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>$1{\text{Patent}_{jt} = \text{Top}^{10%}}$</td>
<td>$1{\text{Patent}_{jt} = \text{Top}^{25%}}$</td>
<td></td>
<td></td>
</tr>
<tr>
<td>OLS</td>
<td>Only Tech.Class.</td>
<td>Only Year</td>
<td>Only Tech.Class.</td>
<td>Only Year</td>
</tr>
<tr>
<td>Post $\cdot$ Exposure$_j$</td>
<td>0.019*** (0.006)</td>
<td>0.010* (0.006)</td>
<td>0.017** (0.007)</td>
<td>0.015** (0.007)</td>
</tr>
<tr>
<td>Firm F.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td>Indu $\times$ TimeF.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td>Controls$_j \times$ TimeF.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td>Observations</td>
<td>32,128</td>
<td>32,128</td>
<td>32,128</td>
<td>32,128</td>
</tr>
</tbody>
</table>

This table reports the estimate of the linear difference-in-difference specification (equation 1), where I estimate the effect of the decision on the quality of innovation using alternative breakthrough measures. In particular, I estimate $y_{jt} = \alpha_j + \alpha_t + \beta(\text{Exposure}_j \cdot \text{Post}) + \gamma X_{jt} + \epsilon_{jt}$, where $y_{jt}$ is a proxy of average quality of innovation in the two years before and after the decision. In the first column, the outcome is a dummy which is equal to one if firm $j$ has published in period $t$ at least one patent that is in the top 10% of the distribution of citation relative to patents in the technology class, but either the same vintage or different vintages. In the second column, the outcome is a dummy which is equal to one if firm $j$ has published in period $t$ at least one patent that is in the top 10% of the distribution of citations relative to patents that are granted in the same year, both inside and outside the same technology class. In the third and fourth column, I reconstruct the same outcomes using a top 25% threshold. Also for these two columns, the odd column considers a reference group of patent in the same technology, while the even column consider patents from the same year. As before, the data set is a balanced two-period panel where I employ every firm that published at least one patent in the two year before and in the year after the decision. The variable Exposure$_j$ captures the exposure of firm $j$ to patent litigation, using patent application in the five years before the decision and patent litigation at technology class since 2000. I always control for firm fixed-effects and time effects. Furthermore, I always augment the specification with industry-time fixed effect, which are constructed based on the macro technology area where the company patented the most over the four years before the decision (Hall et al. (2001)). Lastly, I further augment every specification with location dummies of the firm (constructed using the modal location reported in patent data), the size of the portfolio before the estimation period and the start-up status (looking at whether a firm applied for the first patent ever within the previous three years). More information on the variables is provided in the Appendix (A.3). Standard errors are clustered at firm level. All regressions include a constant.*** denotes significance at the 1% level, ** at the 5%, and * at the 10%.
This table provides a study of pre-trending for results reported in Table (3). In order to do so, I estimate the same specification as before without collapsing the data and estimating a differential effect for the treatment before and after the decision. Data are at quarterly level in a four year around the decision, for a total of 16 periods. In practice, I estimate:

$$y_{jt,r} = \alpha_{jt} + \alpha_{jr} + \beta_{\text{Post}}1\{\text{Risk}_r\} \cdot \text{Post} + \beta_{\text{Pre}}1\{\text{Risk}_r\} \cdot \text{Pre},$$

where $\alpha_{jt}$ is a set of firm-time fixed effects, $\alpha_{jr}$ is a set of fixed effects at firm-group level, $1\{\text{Risk}_r\}$ is a dummy for more risky groups. Here Post identifies quarters after the decision and Pre those before the decision. The quarter of the decision - 20061- is the reference period for interpreting the coefficients. Data are reshaped for this analysis at the firm-time-riskiness group level. In practice, I group patent within a firm in a certain time across two classes depending on the level of riskiness $r$, such that $r = \{\text{high risk}; \text{low risk}\}$. Patents are assigned to one of the two groups based on the intensity of litigation of their technology class after 2000 based on the litigation data. In particular, I split the data across both 10% and 25%. I consider two outcomes: in columns (1)-(2) I use $\ln(\text{Patents}_{jt,r})$, which is the logarithm of the patent applications that firm $j$ filed to during time $t$ in the class of risk $r$. Since this should capture the intensive margin of the treatment, I use all firms that are simultaneously active in both risk classes around the decision time (i.e. like in Table 6, we consider all and only firms with at least one patent in high and low risk group, both in the two years before and after). Then, in columns (3)-(4) I have $y_{jt,r}$ to be equal to $1\{\text{Pat}_{jt,r} > 0\}$, which is a dummy equal to one if the firm $j$ applies to any granted patent in risk group $r$ at time $t$. In this case, my sample is much larger and I consider every firm that has applied to at least one patent in the ten years before the decision. The number of observation is the number used in the computation. Standard errors are clustered at firm level. All regressions include a constant.*** denotes significance at the 1% level, ** at the 5%, and * at the 10%.

Table A.12: Evidence on Patent Mix: pre-trend analysis

<table>
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<tr>
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<th>(2)</th>
<th>(3)</th>
<th>(4)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Extensive Margin</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>$\ln(\text{Patents}_{jt,r})$</td>
<td>-0.003</td>
<td>-0.019</td>
<td>0.042***</td>
<td>0.027***</td>
</tr>
<tr>
<td></td>
<td>(0.026)</td>
<td>(0.021)</td>
<td>(0.002)</td>
<td>(0.002)</td>
</tr>
<tr>
<td>Intensive Margin</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>$1{\text{Patents}_{jt,r} &gt; 0}$</td>
<td>-0.003</td>
<td>0.013</td>
<td>-0.002</td>
<td>0.001</td>
</tr>
<tr>
<td></td>
<td>(0.027)</td>
<td>(0.021)</td>
<td>(0.002)</td>
<td>(0.002)</td>
</tr>
<tr>
<td>Split</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>10%</td>
<td>25%</td>
<td>10%</td>
<td>25%</td>
<td></td>
</tr>
<tr>
<td>Firm × Time F.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td>Firm × Risk F.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td>$R^2$</td>
<td>0.925</td>
<td>0.937</td>
<td>0.687</td>
<td>0.687</td>
</tr>
<tr>
<td>Observations</td>
<td>22,816</td>
<td>39,546</td>
<td>1,756,928</td>
<td>1,756,928</td>
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</table>
Table A.13: Robustness: differential linear effect before and after the shock

<table>
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<th>(4)</th>
</tr>
</thead>
<tbody>
<tr>
<td>$R^2$</td>
<td>0.005</td>
<td>0.027</td>
<td>0.006</td>
<td>0.029</td>
</tr>
<tr>
<td>Observations</td>
<td>16,272</td>
<td>16,272</td>
<td>16,272</td>
<td>16,272</td>
</tr>
<tr>
<td>$Post \cdot Exposure_{jLARGE}$</td>
<td>0.004**</td>
<td>0.006**</td>
<td>(0.002)</td>
<td>(0.003)</td>
</tr>
<tr>
<td>$Pre \cdot Exposure_{jLARGE}$</td>
<td>0.001</td>
<td>0.001</td>
<td>(0.002)</td>
<td>(0.002)</td>
</tr>
<tr>
<td>$Post \cdot Exposure_j$</td>
<td>0.003**</td>
<td>0.004**</td>
<td>(0.001)</td>
<td>(0.001)</td>
</tr>
<tr>
<td>$Pre \cdot Exposure_j$</td>
<td>0.002</td>
<td>-0.001</td>
<td>(0.001)</td>
<td>(0.002)</td>
</tr>
<tr>
<td>Firm&amp;Time F.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td>Indu. × Time F.E.</td>
<td>Y</td>
<td>Y</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Controls$_j$ × Time F.E.</td>
<td>Y</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

In the table, I report the estimation of an equation where I use the data as a panel and I estimate the same specification as equation (1). The key difference is that I estimate differential trends both before and after the shock. To be precise, I look at the effect of firm-exposure interacted with two dummies: (a) the post dummy is equal to one after the decision (equal to one for quarters after May 15th 2006); (b) the dummy pre is equal to one starting two quarters before the decision. In other words, the quarter right before the decision is set to zero for both dummies, and therefore it represents the control period in this analysis, and all the effects can be interpreted as changes relative to this quarter. The data set is constituted by a panel with eight quarter and it is balanced in any specification. The variable $Exposure_j$ captures the exposure of firm $j$ to patent litigation, using patent application in the five years before the decision and patent litigation at technology class since 2000 and the variable $Exposure_{jLARGE}$ captures the exposure of firm $j$ to patent litigation, using patent application in the ten years before the decision and patent litigation at technology class since 1980. In any case, I use every firm that published at least one patent in the two year before and in the one year after the decision. The table has have $R&D/Asset$, measured at quarterly frequency. The even columns are augmented with industry, as constructed in the Appendix, interacted with time dummies (per quarter). More information on the data is available in the Appendix (A.3). All regressions include a constant. *** denotes significance at the 1% level, ** at the 5%, and * at the 10%.
Table A.14: Effect across defendant status

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<th>(4)</th>
<th>(5)</th>
<th>(6)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>LikelyDef.</td>
<td>LikelyPlaint.</td>
<td>All</td>
<td>LikelyDef.</td>
<td>LikelyPlaint.</td>
<td>All</td>
</tr>
<tr>
<td><strong>Post · Exposure_j</strong></td>
<td>0.0644*</td>
<td>0.0355</td>
<td>0.091*</td>
<td>0.107**</td>
<td>0.005</td>
<td>0.094**</td>
</tr>
<tr>
<td></td>
<td>(0.0376)</td>
<td>(0.0462)</td>
<td>(0.048)</td>
<td>(0.050)</td>
<td>(0.101)</td>
<td>(0.047)</td>
</tr>
<tr>
<td><strong>Post · LikelyPlaint._t</strong></td>
<td>-0.090</td>
<td>-0.063</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>(0.073)</td>
<td></td>
<td></td>
<td>(0.074)</td>
</tr>
<tr>
<td><strong>Post · Exposure_j · LikelyPlaint.</strong></td>
<td>-0.029</td>
<td>-0.0071</td>
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<tr>
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<td></td>
<td>(0.059)</td>
<td></td>
<td></td>
<td>(0.062)</td>
</tr>
<tr>
<td>Firm F.E.</td>
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<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td>Time F.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>N</td>
<td>N</td>
<td>N</td>
</tr>
<tr>
<td>Indu. × Time F.E.</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td>Controls_j × Time F.E.</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(R^2)</td>
<td>0.005</td>
<td>0.051</td>
<td>0.011</td>
<td>0.089</td>
<td>0.294</td>
<td>0.083</td>
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<tr>
<td>Observations</td>
<td>1,642</td>
<td>392</td>
<td>2,034</td>
<td>1,642</td>
<td>392</td>
<td>2,034</td>
</tr>
</tbody>
</table>

(a) Public firms

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<tbody>
<tr>
<td></td>
<td>LikelyDef.</td>
<td>LikelyPlaint.</td>
<td>All</td>
<td>LikelyDef.</td>
<td>LikelyPlaint.</td>
<td>All</td>
</tr>
<tr>
<td><strong>Post · Exposure_j</strong></td>
<td>0.043***</td>
<td>0.019</td>
<td>0.019</td>
<td>0.040***</td>
<td>-0.037</td>
<td>0.037***</td>
</tr>
<tr>
<td></td>
<td>(0.009)</td>
<td>(0.033)</td>
<td>(0.033)</td>
<td>(0.011)</td>
<td>(0.047)</td>
<td>(0.034)</td>
</tr>
<tr>
<td><strong>Post · LikelyPlaint._t</strong></td>
<td>-0.161***</td>
<td></td>
<td>-0.161***</td>
<td></td>
<td>-0.083**</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>(0.04)</td>
<td></td>
<td>(0.040)</td>
<td></td>
</tr>
<tr>
<td><strong>Post · Exposure_j · LikelyPlaint.</strong></td>
<td>-0.023</td>
<td></td>
<td>-0.023</td>
<td></td>
<td>-0.028</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>(0.034)</td>
<td></td>
<td>(0.034)</td>
<td></td>
</tr>
<tr>
<td>Firm F.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td>Time F.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>N</td>
<td>N</td>
<td>N</td>
</tr>
<tr>
<td>Indu. × Time F.E.</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td>Controls_j × Time F.E.</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(R^2)</td>
<td>0.007</td>
<td>0.021</td>
<td>0.008</td>
<td>0.033</td>
<td>0.123</td>
<td>0.034</td>
</tr>
<tr>
<td>Observations</td>
<td>30,328</td>
<td>1,800</td>
<td>32,128</td>
<td>30,328</td>
<td>1,800</td>
<td>32,128</td>
</tr>
</tbody>
</table>

(b) Full Sample

These panels report the estimate of the linear difference-in-difference specification (equation 1), where I allow the effect of the exposure to the decision to be heterogeneous across firm likelihood of being a plaintiff at the time of the decision. The outcome is always \(\ln(Patents_{jt})\), which is the log of the total number of patents over the period. As usual, this is winsorized at 1%. The variable \(Exposure\_j\) captures the exposure of firm \(j\) to patent litigation, using patent application in the five years before the decision and patent litigation at technology class since 2000. The first panel reports the analysis on the sample of public companies. The second panel instead reports the analysis over the full sample. The dummy Likely Plaintiff is equal to one if the firm has been involved in more lawsuits as a plaintiff rather than a defendant. I first report the regressions as split between likely plaintiff and the complementary group - which I call likely defendant -, and then I report the fully interacted regression in the whole sample. I always control for firm and time fixed effects, but in Columns (4)-(6) I add extra controls interacted with time dummies. As in the previous analyses, I control for industry, location dummies of the firm, the size of the portfolio before the estimation period, a dummy for “start-up”, which in this context is firms that published the first patent in the three years before the decision, and average quality of the patent portfolio in the pre period, measured by average citations. More information on the data is available in the Appendix (A.3). Standard errors are clustered at firm level. All regressions include a constant.*** denotes significance at the 1% level, ** at the 5%, and * at the 10%.
Table A.15: Heterogeneity of the effects: growth

<table>
<thead>
<tr>
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<th>(1)</th>
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<th>(3)</th>
<th>(4)</th>
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</thead>
<tbody>
<tr>
<td></td>
<td>Standard</td>
<td>Controls</td>
<td>Standard</td>
<td>Controls</td>
</tr>
<tr>
<td></td>
<td>Growth</td>
<td>Growth</td>
<td>Growth</td>
<td>Growth</td>
</tr>
<tr>
<td>Post \cdot Exposure_j \cdot Small_j^{Revenue}</td>
<td>0.004**</td>
<td>0.004**</td>
<td>0.003*</td>
<td>0.003**</td>
</tr>
<tr>
<td></td>
<td>(0.002)</td>
<td>(0.002)</td>
<td>(0.002)</td>
<td>(0.002)</td>
</tr>
<tr>
<td>Post \cdot Exposure_j \cdot Small_j^{EMP}</td>
<td>0.004**</td>
<td>0.004**</td>
<td>0.003</td>
<td>0.003*</td>
</tr>
<tr>
<td></td>
<td>(0.002)</td>
<td>(0.002)</td>
<td>(0.002)</td>
<td>(0.002)</td>
</tr>
<tr>
<td>Post \cdot Exposure_j \cdot 1{Dividend_j = 0}</td>
<td>0.005**</td>
<td>0.007***</td>
<td>0.005*</td>
<td>0.007***</td>
</tr>
<tr>
<td></td>
<td>(0.002)</td>
<td>(0.002)</td>
<td>(0.003)</td>
<td>(0.002)</td>
</tr>
<tr>
<td>Post \cdot Exposure_j \cdot 1{Rating_j = NO}</td>
<td>0.004**</td>
<td>0.003*</td>
<td>0.002</td>
<td>0.003</td>
</tr>
<tr>
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<td>(0.002)</td>
<td>(0.002)</td>
<td>(0.002)</td>
<td>(0.002)</td>
</tr>
<tr>
<td>Firm F.E. &amp; Time F.E.</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
<td>Y</td>
</tr>
<tr>
<td>Indu. \times Time F.E.</td>
<td>Y</td>
<td>Y</td>
<td></td>
<td></td>
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<tr>
<td>Other Controls_j \times Time F.E.</td>
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<td>Y</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Observations</td>
<td>2,034</td>
<td>2,034</td>
<td>2,034</td>
<td>2,034</td>
</tr>
</tbody>
</table>

These Tables report the estimate of the coefficient $\beta_1$ of the following equation:

$$y_{jt} = \alpha_j + \alpha_t + \beta_1(\text{Exposure}_j \cdot \text{FinCon}_j \cdot \text{Post}) + \beta_2(\text{FinCon}_j \cdot \text{Post}) + \beta_3(\text{Exposure}_j \cdot \text{Post})$$

$$+ \beta_4(\text{Growth}_j \cdot \text{Post}) + \beta_5(\text{Growth}_j \cdot \text{FinCon}_j \cdot \text{Post}) + \gamma X_{jt} + \epsilon_{jt}$$

across different specifications. First, different rows measure financial constraint in different ways. In particular, I use: (1) size, as measure by firm below the median revenue in my sample; (2) size, as measure by firm below the median employment in my sample; (3) dividend, where I look at firms that paid no cash dividends in any quarters in the three years before the decision; (4) rating, where I sort based on whether the firm has any rating. Second, in columns (1)-(3), I report the standard results I have already reported, and in columns (2)-(4) I introduce a fully interacted control for firm growth over the pre-period. This measure is the simple growth of revenue over the two years of pre-period. Even if not reported, all the regressions are estimated as fully interacted. The outcome is always $R\&D/\text{Asset}_t$, which is the average over the period of the quarterly R&D expenses scaled by total assets. As usual, this is winsorized at 1%. The variable $\text{Exposure}_j$ captures the exposure of firm $j$ to patent litigation, using patent application in the five years before the decision and patent litigation at technology class since 2000. I always control for firm and time fixed effects, but in Columns (4)-(6) I add extra controls interacted with time dummies. As in the previous analyses, I control for industry, location dummies of the firm, the size of the portfolio before the estimation period, a dummy for “start-up”, which in this context is firms that published the first patent in the three years before the decision, and average quality of the patent portfolio in the pre period, measured by average citations. More information on the data is available in the Appendix (A.3). Standard errors are clustered at firm level. All regressions include a constant. *** denotes significance at the 1% level, ** at the 5%, and * at the 10%.