



THE COMMITTEE ON ENERGY AND COMMERCE

MEMORANDUM

April 4, 2014

To: Members of the Subcommittee on Commerce, Manufacturing, and Trade
From: Majority Committee Staff
Re: Hearing on “Trolling for a Solution: Ending Abusive Patent Demand Letters”

On Tuesday, April 8, 2014, the Subcommittee on Commerce, Manufacturing, and Trade will convene a hearing at 10:00 a.m. in 2123 of the Rayburn House Office Building entitled “Trolling for a Solution: Ending Abusive Patent Demand Letters.” Witnesses are by invitation only.

I. Witnesses

Rheo Brouillard, President & CEO, Savings Institute Bank and Trust Company *on behalf of* American Bankers Association;

Mark Chandler, Senior Vice President & Chief Compliance Officer, Cisco Systems Incorporated;

Michael Dixon, Ph.D., President & CEO, UNeMed Corporation;

Dennis Skarvan, Deputy General Counsel, Intellectual Property Group *on behalf of* Coalition for 21st Century Patent Reform

Jason Schultz, Associate Professor of Clinical Law, New York University School of Law; and,

The Honorable William Sorrell, Attorney General, State of Vermont.

II. Summary

The Subcommittee will hear from stakeholders regarding the growing abuse of patent demand letters. In recent years, small businesses increasingly have been targeted with financial threats through demand letters. Businesses often are told either to pay for a license within a short period of time, or face going to court for infringing on the sender's vaguely defined and often specious intellectual property rights.

While these bad actors dominate the headlines, patent demand letters are not always abusive. Many entities with significant patent holdings use demand letters to engage other companies in lawful and productive discussions around their businesses. The hearing will examine the problem and explore ways to prevent the bad actors from abusing the process, often at the expense of small businesses, while preserving the legitimate business purposes of patent demand letters.

III. Background

Policymakers have focused increasing attention on patent assertion entities (PAEs), also known as “patent trolls,” in the last several months due to the outcry from small businesses who are on the receiving end of their demand letters. PAEs are non-practicing entities¹ (NPEs) that purchase patents from inventors or other rights-holders on the open market and then prosecute that patent against alleged infringers. While there are some PAEs that hold such rights and assert legitimate claims of patent infringement, PAEs have garnered negative attention for deceptive practices aimed at small businesses.²

These bad actors behave largely the same way: send hundreds or thousands of letters to small businesses, including coffee shops, restaurateurs, grocers, community banks, hoteliers, and realtors, containing vague claims of patent infringement and demanding payment of a relatively small amount of money within a short timeframe for a “license” to continue using the technology or the asserting entity will file suit.³ The claims often involve widely-used technology, and the infringing activity generally involves the use of another person’s product, such as scanning-to-email function on a copier or printer, or using a commercially available router for wireless internet connectivity. Often, these letters allege the assertion of patents that are expired or were invalidated. Because patent litigation can cost millions of dollars, even for a small business, the PAEs rely on the fact that their targets will decide that settling – or paying for a “license” – is more cost effective than hiring a patent attorney to verify or litigate the claim.

In addition to the attention on Capitol Hill, patent trolls have prompted action at the Federal Trade Commission (FTC) and in a number of States. In October 2013, the FTC announced it would initiate a study under its §6(b) authority to compel information from PAEs regarding their patent acquisition, rights assertion, licensing, and litigation practices, and compare those to the practices of other patent owners.⁴ The purpose of the study is to examine the competition and consumer protection implications of PAE practices and eventually will result in a report on the Commission’s findings. At the State level, at least four Attorneys General have pursued litigation against PAEs who have engaged in unfair or deceptive patent assertion practices.⁵ Additionally, five States have adopted legislation specifically pertaining to demand letters,⁶ two States passed legislation that awaits their respective governor’s signature,⁷ and legislation of varying approaches is pending before the legislatures of at least 19 other States.⁸

¹ All PAEs are NPEs because they do not practice the patent they hold, but not all NPEs are PAEs, however. For instance, a university often develops and patents their innovations, but they do not monetize – or “practice” – the technology, process, or invention that is the subject of the patent. In addition, the university’s patents are, most frequently, developed in-house rather than purchased on the open market. *See generally*, Federal Trade Commission, *The Evolving IP Marketplace* at 8 (March 2011), available at <http://www.ftc.gov/sites/default/files/documents/reports/evolving-ip-marketplace-aligning-patent-notice-and-remedies-competition-report-federal-trade/110307patentreport.pdf>.

² One estimate places the number of threatening demand letters sent in 2012 at over 100,000. *See* Executive Office of the President, *Patent Assertion and U.S. Innovation* at 6 (June 2013), available at http://www.whitehouse.gov/sites/default/files/docs/patent_report.pdf.

³ For examples of actual demand letters sent by a PAE, visit <https://trollingeffects.org/search/node/>.

⁴ Federal Trade Commission, *FTC Seeks to Examine Patent Assertion Entities and Their Impact on Innovation, Competition* (September 27, 2013), available at <http://www.ftc.gov/news-events/press-releases/2013/09/ftc-seeks-examine-patent-assertion-entities-their-impact>.

⁵ Minnesota, Nebraska, New York, and Vermont.

⁶ Alabama, Idaho, Oregon, South Dakota, and Vermont.

⁷ Georgia, and Utah.

⁸ Connecticut, Illinois, Kansas, Kentucky, Louisiana, Maine, Maryland, Mississippi, Missouri, Nebraska, New Hampshire, New Jersey, Oklahoma, Pennsylvania, Rhode Island, South Carolina, Tennessee, Virginia, and Wisconsin.

IV. Committee and Legislative History

On November 14, 2013, the Committee's Oversight and Investigations Subcommittee held a hearing titled, "The Impact of Patent Assertion Entities on Innovation and the Economy."⁹ Members received testimony from an association of franchisees, an internet company, a mobile device applications developer, a consumer group, and an academic regarding the growing problem of demand letters from PAEs.

House Judiciary Committee Chairman Goodlatte introduced H.R. 3309, the "Innovation Act," on October 23, 2013. The House approved the measure on December 5, 2013. The proposal as reported out of Committee included a provision on demand letters. The provision lays out specific requirements that must be included in a demand letter if a claimant intends to use receipt of the letter by a defendant as evidence of willful infringement.¹⁰ The bill also included a sense of Congress that "purposely evasive demand letters to end users" are an abuse of the patent system, and that demand letters should include "basic information" about the patent.¹¹ During floor debate, Chairman Terry and Mr. Chaffetz engaged in a colloquy discussing the Committee on Energy and Commerce taking a broader look at vague demand letters and any potential remedies enforceable by the Federal Trade Commission.

V. Questions for Consideration

- What are examples of activities engaged in by PAEs that constitute outright fraud?
- What elements or claims could be required for inclusion or exclusion in a demand letter?
- What differentiates legitimate demand letters from abusive letters?
- What are the possible negative unintended consequences on legitimate businesses of such requirements or exclusions of elements or claims in demand letters?
- Are there any First Amendment implications of requiring the inclusion or exclusion of any language in demand letters?

Please contact Paul Nagle, Brian McCullough or Shannon Taylor of the Committee staff at (202) 225-2927 with questions.

⁹ Hearing notice, background memo, and archived video of the hearing is available at <http://energycommerce.house.gov/hearing/impact-patent-assertion-entities-innovation-and-economy>.

¹⁰ Section 3(f) of the Innovation Act would require a claimant's demand letter "identif[y] with particularity the asserted patent, identif[y] the product or process accused, identif[y] the ultimate parent entity of the claimaint, and explain[] with particularity, to the extent possible following a reasonable investigation or inquiry, how the product or process infringes one or more claims of the patent."

¹¹ Section 3(e) of the Innovation Act expresses the sense of Congress that it is an abuse of the patent system and against public policy for a party to send out purposely evasive demand letters to end users alleging patent infringement.

Demand letters sent should, at the least, include basic information about the patent in question, what is being infringed, and how it is being infringed. Any actions or litigation that stem from these types of purposely evasive demand letters to end users should be considered a fraudulent or deceptive practice and an exceptional circumstance when considering whether the litigation is abusive.