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**Testimony of Vermont Assistant Attorney General Wendy Morgan
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Committee on Energy and Commerce
Subcommittee on Commerce, Manufacturing, and Trade
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Summary

Chairman Terry, Ranking Member Schakowsky, and members of the Subcommittee, thank you for the opportunity to testify today. The Vermont Attorney General's Office has been actively working to address the issue of unfair and deceptive communications made in the context of patent assertion and licensing. My office appreciates the work of Congress, and of this subcommittee in particular, in proactively addressing this issue, and we appreciate having the opportunity to share our thoughts on your draft legislation ("Discussion Draft").

State attorneys general are often the first government officials to receive complaints from small businesses and nonprofits that have received vague, confusing, and misleading patent demand letters. We appreciate the subcommittee's efforts to address the issue of troublesome patent demand letters, as part of much-needed broader reforms regarding patent assertion entities generally. My office's experience with these issues informs my testimony with respect to the Discussion Draft. My testimony is summarized below:

- Sections 2(a)(2) and (3) would both benefit from catch-all provisions, and the savings clauses in Sections 3(c) and 4(a)(2) that preserve the authority of the FTC and state attorneys general are critical. Although the practices specified in Section 2(a)(1)-(3) are some examples of the unfair and deceptive practices that my office has observed, once legislation is enacted, bad actors will likely adapt their behavior to avoid practices that are specifically prohibited. However, they may continue to engage in different unfair and deceptive acts. Our recommendations would provide needed flexibility to the FTC and state attorneys general to bring actions under state and federal law to address other practices that may develop in the future that are also unfair and deceptive.
- In order to allow greater flexibility for state enforcement, and consistent with most consumer protection law, state enforcement of any potential legislation should permit the state to act to protect the public interest generally and not limit the state to acting as *parens patriae* for particular residents or require the state to demonstrate that residents have been adversely affected.
- The rebuttable presumption in Section 2(b) seems unnecessary and could create confusion. This could be removed. If it does remain as a rebuttable presumption, the presumption should clearly be limited to compliance with Section 2(a)(4), to avoid any possible misinterpretation that it applies generally to claims of unfairness and deception.
- The definition of “bad faith” should encompass any of the representations set forth in Section 2(a)(2)-(3) that are false, deceptive, or misleading, without respect to the sender’s knowledge. There is traditionally no scienter requirement in consumer protection law. Requiring proof of “actual knowledge or knowledge fairly implied” would create an unnecessarily high bar for an enforcement action and would significantly hinder the ability to enforce the proposed standards for demand letters.
- To prevent ambiguity, it should be clarified that a cause of action under any enacted legislation does not constitute an action arising under the patent laws pursuant to 28 U.S.C. § 1338.
- Limiting the definition of “sender” to a person with a right to license or enforce the patent weakens the ability of the FTC and states to enforce Section 2 against entities that they have no right to license or enforce.
- The definition of “systems integrator” should be broad enough to encompass developments beyond websites and mobile applications that similarly incorporate retail software or services.

Preserving State Enforcement Authority to Fully Protect Consumers

Any federal statute that addresses patent assertion letters should preserve and recognize the full authority of the FTC and state attorneys general to take action against unfair and deceptive communications. The proposed legislation highlights unfair and deceptive practices and promotes increased transparency. Those provisions of the Discussion Draft would provide greater protection to businesses and nonprofits that receive patent assertion letters and will provide them with some of the tools necessary to consider their options. However, there are three areas of the Discussion Draft that my office believes could be clarified or modified to allow states to most effectively protect consumers from unfair and deceptive patent assertion and licensing communications.

First, it is important that the FTC and state attorneys general retain their current authority to protect consumers from unfair and deceptive acts and practices with respect to letters that assert patents and seek licensing fees. Commonly, states are guided in enforcing their consumer protection acts by the FTC Act,¹ but the Act does not generally preempt states' enforcement authority under their own consumer protection statutes.² Federal consumer-protection statutes commonly operate concurrently with state statutory and common law authority.³ We advocate that in the area of unfair and deceptive patent assertion and licensing

¹ See, e.g., 9 V.S.A. § 2453(b); see also Henry N. Butler, *Are State Consumer Protection Acts Really Little-FTC Acts?* 10 (Northwestern University School of Law Scholarly Commons, Faculty Working Papers, 2010) (“Twenty-eight states currently reference the FTC in their CPA.”).

² See *Altria Group, Inc. v. Good*, 555 U.S. 70, 91 (2008) (concluding that FTC decisions did not prevent a jury from considering a state deceptive practices claim).

³ See, e.g., Telephone Consumer Protection Act, 47 U.S.C. § 227(g)(6) (“Nothing contained in this subsection shall be construed to prohibit an authorized State official from proceeding in State court on the basis of an alleged violation of any general civil or criminal statute of such State.”); Real Estate Settlement Procedures Act, 12 U.S.C. § 2616 (“This chapter does not annul, alter, or affect, or exempt any person subject to the provisions of this chapter from complying with, the laws of any State with respect to settlement practices, except to the extent that those laws

communications, federal law act as a floor and not preempt state legislative or regulatory authority, or exempt state laws already in effect as is the case in the Fair Credit Reporting Act.⁴ Vermont, along with nine other states,⁵ has passed legislation that respects the rights of patent holders while protecting consumers and end users who are targeted with deceptive, misleading, and unfair patent demand letters. In our view, these state laws are targeted only at bad actors and do not interfere with the important rights of patent holders to assert their patents honestly and in good faith.

While we prefer that any federal legislation not preempt state laws directed at patent demand letters, we understand that some patent holders object to these targeted state laws and the Discussion Draft would preempt those laws. If the Committee takes this approach, the preemption language should be carefully and narrowly crafted to preserve state authority to enforce consumer protection statutes, including any judicial interpretation of such statutes,

are inconsistent with any provision of this chapter, and then only to the extent of the inconsistency.”); Truth in Lending Act, *Williams v. First Gov’t Mortgage & Investors Corp.*, 176 F.3d 497, 500 (D.C. Cir. 1999) (finding that TILA did not preempt the District of Columbia Consumer Protection Act “and that TILA compliance does not immunize lenders . . . against CPPA [D.C. Consumer Protection Procedures Act] liability.”); Telemarketing and Consumer Fraud and Abuse Prevention Act, 15 U.S.C. § 6103(f)(1) (“Nothing contained in this section shall prohibit an authorized State official from proceeding in State court on the basis of an alleged violation of any civil or criminal statute of such state.”); Fair Debt Collection Practices Act, 15 U.S.C. § 1692n (“This subchapter does not annul, alter, or affect, or exempt any person subject to the provisions of this subchapter from complying with the laws of any State with respect to debt collection practices, except to the extent that those laws are inconsistent with any provision of this subchapter, and then only to the extent of the inconsistency. For purposes of this section, a State law is not inconsistent with this subchapter if the protection such law affords any consumer is greater than the protection provided by this subchapter.”).

⁴ *See, e.g.* 15 U.S.C. § 1781t(2) (“ . . . this paragraph shall not apply with respect to subsection (a) or (c)(1) of section 2480e of title 9, Vermont Statutes Annotated (as in effect on the date of enactment of the Consumer Credit Reporting Reform Act of 1996)”.

⁵ Georgia, Act 809, 2013-2014 Leg., Reg. Sess. (Ga. 2014); Idaho, S.B. 1354, 62nd Leg., 2nd Reg. Sess. (Id. 2014); Maine S.P. 654, 126th Leg., 2nd Reg. Sess. (Me. 2014); Oregon, S.B. 1540, 77th Leg., Reg. Sess. (Or. 2014); South Dakota, S.J. 143, 2014 Leg., Reg. Sess. (S.D. 2014); Tennessee H.B. 2117, 108th Leg., Reg. Sess. (Tenn. 2014); Utah, H.B. 117, Gen. Sess. (Utah 2014); Virginia, S.B. 150, 2014 Leg., Reg. Sess. (Va. 2014) (passed but not signed), Wisconsin, Act 339, 2013-2014 Leg., Reg. Sess. (Wis. 2014).

against unfair and deceptive patent-assertion conduct. If the proposed legislation contains preemption language – which we oppose – the preemption clause should be clearly limited to state laws and regulations that expressly regulate patent-assertion communications, and additional language should be added to clarify that state attorneys general may use existing consumer protection laws to take action against unfair and deceptive patent communications.

Although the list set forth in Section 2(a)(1)-(3) is a relatively comprehensive summary of the unfair and deceptive acts that the my office has observed to date, we expect that bad actors will tailor their communications to comply with these standards but will not stop engaging in unfair and deceptive practices designed to persuade small businesses and nonprofits to pay licensing fees. For example, a communication may state that the patent holder is requesting a licensing fee of \$10,000 based on the price that it has negotiated with others who were similarly situated to the recipient. If, in fact, the patent holder *had* received licensing fees from some individuals who were similarly situated to the recipient, but such licensing fees had never exceeded \$1,000, my office would argue that the statement in the letter was deceptive. However, it would not violate the requirements in the Discussion Draft. This example demonstrates the reality that it is impossible to fully anticipate the unfair and deceptive acts that individuals may engage in. Preserving the authority for the states and the FTC to protect small businesses and nonprofits, end-users of products that they have already paid for, from unfair and deceptive attempts to extort licensing fees will not encroach upon the rights of patent holders who are straightforward and honest in their enforcement efforts. It will, however, provide flexibility for enforcement agencies to address new unfair and deceptive practices that may arise.

Second, as is typically the case in consumer protection causes of action, states should not have to step into the shoes of consumers or show actual consumer harm to enforce the

provisions of Section 2. In enforcing consumer protection laws, my office acts on behalf of the State of Vermont, not any individual citizens. Therefore, unlike a private cause of action for unfair and deceptive practices, which requires the plaintiff to show injury,⁶ a claim brought by a state or the FTC does not typically require a showing of harm.⁷ The states' authority, particularly in this context, would be significantly inhibited if it is limited in this manner.⁸ Requiring states to show that residents have been adversely affected by unfair and deceptive patent assertions or licensing communications would require states to identify consumer harm. This may be particularly difficult when an attorney general's office has received a complaint but has no knowledge of whether the recipient has been sued or hired an attorney to assist in deciding how to respond. Often, the harm of an unfair or deceptive act is likely to occur in the future. Requiring proof of harm to individual consumers will prevent states from acting swiftly to *prevent* the actual harm or injury. My office would recommend that the enforcement authority granted to attorneys general under this act be consistent with typical enforcement authority and not require that the attorney general act as *parens patriae* and prove that recipients have been adversely affected.

⁶ See, e.g., 9 V.S.A. § 2461(b); Cal. Civ. Code § 1780(a); Fla. Stat. § 501.211(s); Mass. Gen. Laws Ch. 93A, § 9; N.Y. Gen. Bus. Law § 349(h).

⁷ See, e.g., *Carter v. Gugliuzzi*, 716 A.2d 17, 23 (Vt. 1998) (“Deception is measured by an objective standard, looking to whether the representation or omission had the ‘capacity or tendency to deceive’ a reasonable consumer; actual injury need not be shown.”); *In the Matter of Daniel Chapter One*, 2009 WL 4086836, *23 n.13 (F.T.C. 2009) (“the FTC need not prove actual injury to consumers”).

⁸ Federal statutes take differing approaches to concurrent state authority, some simply provide for state enforcement, while others limit states to acting in the role of *parens patriae*. Compare 47 U.S.C. § 227(g)(1) (granting states the authority to bring a civil action when a person “has engaged or is engaging in a pattern or practice of telephone calls or other transmissions to residents of that State in violation of this section . . .” without the requirement of showing that the interests of residents have been adversely affected) with 15 U.S.C. § 6103(a) (providing authority to bring a civil action as *parens patriae* when it has reason to believe “the interests of the residents of that State have been or are being threatened or adversely affected” by a person engaging in a telemarketing practice in violations of the FTC’s rule).

Third, the rebuttable presumption in Section 2(b) is unnecessary, but, if left in, could be clarified to confirm its purpose of protecting businesses acting in good faith that inadvertently send communications with a technical omission of the requirements of Section 2(a)(4). Section 2(a)(4)'s disclosure requirements provide adequate flexibility to protect patent holders that have limited information.⁹ To the extent concerns exist that a technical omission of certain disclosures set forth in Section 2(a)(4) could result in liability under this Discussion Draft, providing a very limited rebuttable presumption could address such concerns. However, as currently drafted, it is not clear whether the intent of Section 2(b) is to provide a rebuttable presumption that the patent holder has complied with the requirements set forth in Section 2(a)(4) or that the patent holder has not engaged in any unfair and deceptive act under the FTC Act generally. The latter would be very problematic and undermine the effectiveness of the proposed legislation.

As I discussed above, my office has significant concerns with the possibility that patent holders who seek to deceive small businesses and nonprofits will comply with the requirements set forth in Section 2(a), but nonetheless engage in unfair acts or include deceptive statements in their patent assertion letters. If Section 2(b) were interpreted broadly to create a rebuttable presumption that the patent holder has not engaged in any unfair and deceptive acts, enforcement agencies would face a higher-than-normal burden of proof in prosecuting even blatantly unfair and deceptive practices by such a patent holder.¹⁰ If the rebuttable presumption is removed, or,

⁹ See Section 2(a)(4)(C) & (D) (both limited “to the extent reasonable under the circumstances”).

¹⁰ The typical burden of proof in a consumer protection case is a preponderance of the evidence *See, e.g., Koch v. Greenberg*, 2014 WL 1284492, at *7 (S.D.N.Y. Mar. 31, 2014) (requiring plaintiff to prove elements in consumer protection case by a preponderance of the evidence); *F.T.C. v. Commerce Planet, Inc.*, 878 F. Supp. 2d 1048, 1055 (C.D. Cal. 2012) (finding that the FTC had proven by a preponderance of the evidence that individual was liable for deceptive and unfair marketing in violation of FTC Act); *State v. Hulsey*, 249 P.3d 468 (Kan. App. 2011) (table)

short of that, references to unfair or deceptive acts or practices and to the FTC Act are stricken from Section 2(b), this drafting problem would be eliminated.

Amend “Bad Faith” to be consistent with consumer protection laws

There are many practices employed by certain patent holders that are unfair and deceptive to recipients of patent assertion and licensing communications. These practices include: indiscriminately sending letters to businesses without particularized understanding of the business’s activities; sending letters that are so vague that the recipient cannot discern the patents being asserted, the alleged infringement, or the party making the assertion; and making express statements in the letters that are factually untrue or misleading.

The Discussion Draft makes it unfair and deceptive to send communications that include the representations in Section 2(a)(2)-(3) if the sender knows, or knowledge can be implied, that the representations were false. My office agrees with the general principal of these requirements but, from an enforcement perspective, believes that the requirements of actual falsity and knowledge or implied knowledge of the falsity will create unnecessary challenges to enforcement actions even where the communications are clearly deceptive and misleading.

Bad actors who wish to send unfair and deceptive patent assertion communications will find ways to comply with the delineated requirements in the Discussion Draft. For example, a statement may be deceptive and misleading without being technically “false.” Requiring actual falsity, as the Discussion Draft presently contemplates, may make it difficult to prove a case against a sender who carefully crafts its letters to avoid outright falsehoods. A letter may state

(distinguishing a criminal charge which must be proven beyond a reasonable doubt, the court noted that “a KCPA [consumer protection act] claim must only be proven by a preponderance of the evidence.”); *Poulin v. Ford Motor Co.*, 513 A.2d 1168, 1172 (Vt. 1986) (explaining that while common law fraud requires clear and convincing proof, consumer fraud requires application of the preponderance of the evidence standard).

that the sender is aggressively pursuing all legal remedies to enforce its patents against other persons instead of expressly stating that the sender has filed litigation against other persons. If the sender has, in fact, only sent initial letters, and has not taken and lacks the capacity to take any further steps to enforce the patent, it is a deceptive and misleading statement. Similarly, a sender may state that it is an agent for enforcing the patents and attach a draft complaint listing itself as the plaintiff. This misleads the recipient into believing the sender is, in fact, an owner or exclusive licensee of the patent, even though it was never expressly stated. Therefore, my office would recommend that the definition of bad faith be amended to include representations that are deceptive or misleading in addition to false.¹¹

Additionally, my office would recommend that the definition of “bad faith” not impose a knowledge requirement that states are not typically required to prove.¹² While the FTC Act has a knowledge requirement for the imposition of civil penalties,¹³ a person that violates an FTC rule, even without knowledge, is liable for injury caused to a consumer irrespective of knowledge.¹⁴ Although we believe civil penalties would be appropriate, as is common in most state consumer protection law, if the relief is limited to injunctions and consumer restitution, the knowledge

¹¹ The FTC has clarified that a “deceptive” practice must have “a representation, omission or practice that is likely to mislead the consumer,” be evaluated “from the perspective of a consumer acting reasonably in the circumstances,” and the “representation, omission, or practice must be a ‘material’ one.” See *Matter of Cliffdale Assocs., Inc.*, 103 F.T.C. 110, at *45 (1984). Including representations that are deceptive and misleading in the definition of “bad faith” would be consistent with traditional understandings of deceptive practices.

¹² See Carolyn Carter, *Consumer Protection in the States*, 17 (National Consumer Law Center) (Feb. 2009) (“Most states do not require the state agency to prove the business’s intent or knowledge.”).

¹³ See 15 U.S.C. § 45(m)(1)(A).

¹⁴ See 15 U.S.C. § 57b; see also *A Brief Overview of the Federal Trade Commission’s Investigative and Law Enforcement Authority*, Section II(A)(1)(b) (2008), available at <http://www.ftc.gov/about-ftc/what-we-do/enforcement-authority>.

requirement should be eliminated. This would be consistent with both traditional state enforcement authority and the FTC authority relating to such relief.

Other Recommendations

The primary concerns of my office are retaining enforcement authority under Vermont's general prohibition on unfair and deceptive acts and practices in commerce and structuring the prohibitions in the Discussion Draft in a manner that would make enforcement actions under an enacted statute tenable from the perspective of state attorneys general. We also have a limited number of additional suggestions that we believe would provide clarification and would help prevent unnecessary litigation over any enacted legislation.

First, Section 2(a) should include a catch-all provision for communications that otherwise include representations or omissions that are likely to materially mislead reasonable recipients. For many of the same reasons discussed in the my earlier testimony, this provision would provide enforcement authorities with the flexibility necessary to address unfair and deceptive practices, even as they change to technically conform with specific examples in any enacted legislation.

Second, because the cause of action proposed in the Discussion Draft would arise under the FTC Act, it would be helpful to clarify that the cause of action would not arise under the patent jurisdiction statute, 28 U.S.C. § 1338. This clarification would not change any authority of the United States district courts, but would provide clarity regarding the appropriate appellate court.

Third, defining the term "sender" is unnecessary. A sender is any person who sends patent assertion communications. By limiting the definition of sender to a person with the right to enforce or license the patents, a person with no such right who sends a patent assertion letter

that, for example, falsely describes existing litigation, would not violate Section 2(a)(2). The same concern arises under Section 2(a)(3). Additionally, because a “recipient” is defined to include only those consumers, end users, or systems integrators who have “no established business relationship with the sender” the definition suggests that a recipient requires a “sender.” Limiting the definition of sender in this way will, at a minimum, create uncertainty regarding the applicability of any provision in Section 2(a) to individuals who send patent assertion or licensing communications without the authority to enforce or license the patent. The State sees no reason to exclude such persons from the prohibitions in Section 2(a)(2)-(3) or to risk debate and judicial and legal resources over whether a recipient requires a sender who is a legitimate patent enforcer. Consequently, if the definition of “sender” remains, it should be amended to include persons that either state or imply a right to enforce or license a patent.

Finally, my office recognizes that the subcommittee has sought to address the concerns faced by many mobile application and website developers that integrate retail software or services into their products or services and face threatening infringement communications relating to the integrated technology. Protection of these systems integrators is similar to protection of end-users and consumers, as such terms are defined in the Discussion Draft, as they are simply incorporating a third party’s retail technology. In light of the fast-changing pace of technology, my office recommends that the subcommittee consider eliminating the limitation of this definition to websites and mobile applications, as it may preclude persons developing future technologies that similarly incorporate retail software or services.

Conclusion

The states, because of their ongoing connection with local businesses and nonprofits, play an important role in protecting against unfair and deceptive patent assertion and licensing

communications. The State of Vermont has fought hard to protect consumers and end-users of retail products from abusive practices and seeks to continue coordinating with other states and the FTC in these efforts. The legislation in the Discussion Draft would provide an additional tool for such efforts, which we support, but we do seek to clarify the existing and ongoing authority of states to utilize their consumer protection statutes to address new and changing unfair and deceptive acts as they arise.

While addressing patent demand letters alone will not resolve all of the issues raised in this field, it is a helpful step toward addressing overall patent demand reform. My office greatly appreciates the work that this subcommittee has done to advance this issue, and I thank you for the opportunity to testify.