

## HOUSE OF REPRESENTATIVES STAFF ANALYSIS

**BILL #:** CS/HB 1181 Bad Faith Assertions of Patent Infringement

**SPONSOR(S):** Judiciary Committee; Civil Justice Subcommittee; Grant

**TIED BILLS:** None **IDEN./SIM. BILLS:** CS/SB 1298

REFERENCE	ACTION	ANALYST	STAFF DIRECTOR or BUDGET/POLICY CHIEF
1) Civil Justice Subcommittee	11 Y, 0 N, As CS	Malcolm	Bond
2) Judiciary Committee	17 Y, 0 N	Malcolm	Havlicak

### SUMMARY ANALYSIS

In 2015, the Legislature enacted the "Patent Troll Prevention Act" (Act) to provide a private right of action for a person who has received a bad faith patent infringement claim. The bill amends the Act by revising when a party pursuing a private right of action under the bill may recover punitive damages, and by revising the criteria by which a demand letter is deemed to be a bad faith assertion of patent infringement in violation of the Act.

The bill also repeals the provision in the Act that authorizes a target of a bad faith assertion of patent infringement to seek a protective order or a court order requiring the plaintiff to post a bond.

The bill does not appear to have a fiscal impact on state or local government.

The bill is effective upon becoming law.

# FULL ANALYSIS

## I. SUBSTANTIVE ANALYSIS

### A. EFFECT OF PROPOSED CHANGES:

#### Current Situation

##### **Patent Law**

A patent is the grant of a property right in an invention to its inventor, issued by the United States Patent and Trademark Office generally for a term of 20 years.<sup>1</sup> A patent confers the right to exclude others from making, using, or selling the invention in the United States or importing the invention into the United States.<sup>2</sup>

Article I, s. 8, cl 8, of the United States Constitution gives Congress the power to enact laws relating to patents.<sup>3</sup> Based on this grant of power, Congress enacted a number of patent statutes, most significantly, the Patent Act of 1952.<sup>4</sup> Congress, in turn, has vested the federal courts with exclusive jurisdiction to determine patent validity and infringement.<sup>5</sup>

##### **Enforcement of Patents**

A patent holder may enforce its rights by filing infringement suits in federal court.<sup>6</sup> The patent holder bears the burden of establishing infringement by each alleged infringer.<sup>7</sup> Patent litigation is generally very expensive: the average suit in which \$1 million to \$25 million is at stake costs \$1.6 million through discovery and \$2.8 million through trial.<sup>8</sup>

Although Congress has not expressly preempted state law in all areas of patent law, federal courts have generally held that most patent litigation is implicitly preempted by Congress.<sup>9</sup> Accordingly, the Federal Circuit, which has exclusive appellate jurisdiction over patent cases, has held that state law claims against abusive patent infringement practices are mostly preempted by the federal Patent Act because

a patentee must be allowed to make its rights [under the federal Patent Act] known to a potential infringer so that the latter can determine whether to cease its allegedly infringing activities, negotiate a license if one is offered, or decide to run the risk of liability and/or the imposition of an injunction. The federal patent laws thus bar state-law liability for communications concerning alleged infringement so long as those communications are not made in “bad faith.”<sup>10</sup>

To avoid preemption, a person that raises a state law cause of action based on abusive patent infringement practices must prove that the infringement allegations were “objectively baseless,” meaning that no reasonable litigant could have expected to succeed.<sup>11</sup>

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<sup>1</sup> United States Patent and Trademark Office, *General Information Concerning Patents* (Oct. 2014) <http://www.uspto.gov/patents-getting-started/general-information-concerning-patents#heading-2> (last visited Jan. 23, 2016).

<sup>2</sup> 35 U.S.C. §154 (2012).

<sup>3</sup> “To promote the Progress of Science and useful Arts, by securing for limited Times to Authors and Inventors the exclusive Right to their respective Writings and Discoveries.” Art. I, §8, cl. 8, U.S. Const.

<sup>4</sup> P.L. 82-593, 66 Stat. 792 (codified at 35 U.S.C.).

<sup>5</sup> 28 U.S.C. §1338(a) (“No State court shall have jurisdiction over any claim for relief arising under any Act of Congress relating to patents . . .”).

<sup>6</sup> See *id.*; 35 U.S.C. §271 (2012).

<sup>7</sup> 35 U.S.C. §101 (2012).

<sup>8</sup> Brian Yeh, *An Overview of the “Patent Trolls” Debate*, Congressional Research Service (April 16, 2013).

<sup>9</sup> See *Globetrotter Software, Inc. v. Elan Computer Grp., Inc.*, 362 F.3d 1367, 1374 (Fed. Cir. 2004).

<sup>10</sup> *Id.* at 1374-75 (quoting *Va. Panel Corp. v. MAC Panel Co.*, 133 F.3d 860, 869 (Fed.Cir.1997)).

<sup>11</sup> *Id.* at 1377; *Dominant Semiconductors Sdn. Bhd. v. OSRAM GmbH*, 524 F.3d 1254, 1260 (Fed. Cir. 2008).

## Patent Trolls

"Patent assertion entities," commonly referred to as "patent trolls," describes a business that focuses on purchasing and asserting patents against companies that already use the patented technology in their business operations (after infringement and lock-in have occurred), rather than developing and transferring technology to licensees.<sup>12</sup> Patent trolls frequently operate by sending notices of alleged patent infringement to large numbers of businesses to threaten litigation if the business does not pay a licensing fee.<sup>13</sup> Often defendants, especially smaller companies and startups, will choose to settle to avoid expending time and resources on costly litigation. Patent trolls simply transfer a legal right not to be sued for the transfer of money.<sup>14</sup>

## State Attempts to Limit Bad Faith Patent Infringement Claims

As of the beginning of 2016, 27 states, including Florida, have passed statutes outlawing certain acts of bad faith patent enforcement;<sup>15</sup> the majority of statutes, including Florida's, are modeled after a Vermont statute, which prohibits "bad faith" assertions of patent infringement.<sup>16</sup> Other states have outlawed assertions that "contain false, misleading, or deceptive information"<sup>17</sup> or have defined specific acts as illegal, such as threatening litigation and not filing suit or making infringement assertions that "lack a reasonable basis in fact or law."<sup>18</sup> Most of the new statutes create a private right of action for the targets of unlawful infringement assertions, and all of the statutes provide for enforcement by state officials, such as the state attorney general.<sup>19</sup> However, whether such state law attempts to curb bad faith patent claims are preempted by federal law is unknown.<sup>20</sup>

## Florida's Patent Troll Prevention Act

In 2015, the Florida Legislature passed the Patent Troll Prevention Act (Act), Part VII of ch. 501, F.S.<sup>21</sup> The Act creates a private right of action for a person who has received a bad faith assertion of patent infringement. In determining whether an assertion of patent infringement violates the Act, a court may consider a number of factors, including whether:

- the demand letter contained basic information regarding the patent, the patent owner, and the specific infringing conduct, or whether such information was provided when requested;
- the demand letter requested payment of a license fee or a response within an unreasonable period of time or requested an unreasonable license fee;
- the assertion of patent infringement is deceptive or unenforceable, and the person knew, or should have known, that the claim or assertion was unenforceable; and
- the person has previously sued or threatened to sue to enforce the claim and a court found the claim to be meritless.

Alternatively, a court may consider a number of factors as evidence that a person has not made a bad faith assertion of patent infringement, including whether:

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<sup>12</sup> Thomas A. Hemphill, *The Paradox of Patent Assertion Entities*, American Enterprise Institute (Aug. 12, 2013) <http://www.aei.org/publication/the-paradox-of-patent-assertion-entities/> (last visited Jan. 23, 2016).

<sup>13</sup> See Paul R. Gugliuzza, *Patent Trolls and Preemption*, Boston University School of Law Public Law & Legal Theory Paper No. 15-03, 1-4 (Jan. 20, 2015), available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2539280](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2539280) (last visited Jan. 23, 2016).

<sup>14</sup> Hemphill, *supra* Note 12.

<sup>15</sup> Gugliuzza, *supra* Note 13 at 4-5; Patent Progress's Guide to State Patent Legislation (Jan. 4, 2016) <http://www.patentprogress.org/patent-progress-legislation-guides/patent-progresss-guide-state-patent-legislation/> (last visited Jan. 23, 2016).

<sup>16</sup> VT. STAT. ANN., tit. 9, § 4197(a) (2014).

<sup>17</sup> WIS. STAT. § 100.197(2)(b) (2014).

<sup>18</sup> *E.g.*, 815 ILL. COMP. STAT. 505/2RRR(b)(1), (3) (2014).

<sup>19</sup> *E.g.*, VT. STAT. ANN., tit. 9, § 4199(a); WIS. STAT. § 100.197(3)(b); TENN. CODE ANN. § 29-40-103 to -104; 815 ILL. COMP. STAT. 505/7, 505/10a.

<sup>20</sup> See Gugliuzza, *supra* Note 13.

<sup>21</sup> ss. 7-13, ch. 2015-92, Laws of Fla.

- The demand letter contained the required identifying and contact information;
- The person engaged in a good faith effort to establish that the target has infringed the patent and negotiated an appropriate remedy;
- The person made a substantial investment in the patent;
- The person is the inventor of the patented product or is the original assignee;
- The person has demonstrated good faith business practices in previous efforts to enforce.

A target of a patent infringement claim that violates the Act may seek a protective order or court order requiring the plaintiff to post a bond equal to the lesser of \$250,000 or the defendant's estimated litigation expenses.

A person who prevails on a claim of bad faith assertion of patent infringement pursuant to the Act may be awarded equitable relief, damages, costs and fees, including attorney fees, and punitive damages in an amount equal to \$50,000 or three times the total damages, costs, and fees, whichever is greater.

Universities, technology transfer companies affiliated with universities, and certain patent infringement assertions related to pharmaceutical and biologic licensing and patents are exempt from liability under the Act.

### **Effect of the Bill**

The bill amends Patent Troll Prevention Act (Act) to remove those portions of the Act that provide the factors that a court uses in determining whether an assertion of patent infringement violates the Act and replaces those portions with a description of attributes that qualify a demand letter as a bad faith assertion of patent infringement.

Pursuant to the bill, a demand letter constitutes a bad faith assertion of patent infringement if it includes a claim that the target, or a person affiliated with the target, has infringed a patent and that the target is legally liable for the infringement, and one or more of the following is met:

- The demand letter falsely asserts that the sender has filed a lawsuit in connection with the claim.
- The demand letter asserts a claim that is objectively baseless because:
  - The sender, or a person the sender represents, lacks the right to license or enforce the patent against the target;
  - The patent is unenforceable pursuant to a final judgment or an administrative order; or
  - The infringing activity alleged in the letter occurred after the expiration of the patent.
- The demand letter is likely to materially mislead a reasonable person because it does not contain sufficient information to inform the target of:
  - the identity of the person asserting the claim, including his or her name and address;
  - the patent alleged to have been infringed, including the patent number; and
  - at least one product, service, or technology of the target alleged to infringe the patent, or at least one activity of the end user which is alleged to infringe the patent.

The bill provides that a court may award punitive damages up to \$75,000 for a prevailing plaintiff in a private cause of action pursuant to the Act only if the court determines that the person making the bad faith asserting has repeatedly violated the Act. The bill also repeals the provision in the Act that authorized a target of a bad faith assertion of patent infringement that violates the Act to seek a protective order or court order requiring the plaintiff to post a bond.

The bill also provides that the Act may not be construed: to limit the rights and remedies available to the state or a person under any other law; to alter or restrict the Attorney General's authority under any other law regarding patent infringement claims; or, to prohibit a person who owns a patent from notifying other parties of his or her ownership, offering to sell or license the patent, notifying other parties of such parties' infringement of the patent, or seeking compensation for infringement of, or license to, the patent.

### **B. SECTION DIRECTORY:**

Section 1 amends s. 501.991, F.S., relating to legislative intent; construction.

Section 2 amends s. 501.992, F.S., relating to definitions.

Section 3 amends s. 501.993, F.S., relating to bad faith assertions of patent infringement.

Section 4 repeals s. 501.994, F.S., relating to bond.

Section 5 amends s. 510.995, F.S., relating to private right of action.

Section 6 provides the bill will take effect upon becoming law.

## II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT

### A. FISCAL IMPACT ON STATE GOVERNMENT:

#### 1. Revenues:

The bill does not appear to have any impact on state revenues.

#### 2. Expenditures:

The bill does not appear to have any impact on state expenditures.

### B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

#### 1. Revenues:

The bill does not appear to have any impact on local government revenues.

#### 2. Expenditures:

The bill does not appear to have any impact on local government expenditures.

### C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

The bill does not appear to have any direct economic impact on the private sector.

### D. FISCAL COMMENTS:

None.

## III. COMMENTS

### A. CONSTITUTIONAL ISSUES:

#### 1. Applicability of Municipality/County Mandates Provision:

The bill does not appear to require counties or municipalities to take an action requiring the expenditure of funds, reduce the authority that counties or municipalities have to raise revenue in the aggregate, nor reduce the percentage of state tax shared with counties or municipalities.

#### 2. Other:

As explained above, Congress has not expressly preempted state law in all areas of patent law; however, federal courts have generally held that most patent litigation has been implicitly preempted by Congress.<sup>22</sup> Accordingly, state law claims against abusive patent infringement practices are mostly preempted by the federal Patent Act.<sup>23</sup> To avoid preemption, an accused infringer that raises a state law cause of action based on abusive patent infringement practices must prove that the

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<sup>22</sup> See *Globetrotter*, 362 F.3d at 1374.

<sup>23</sup> *Id.* at 1377.

infringement allegations were “objectively baseless,” meaning that no reasonable litigant could have expected to succeed.<sup>24</sup> Because the bill provides that a demand letter that, among other things, asserts a claim that is objectively baseless, it appears the bill may avoid preemption.

Additionally, for a Florida court to exercise personal jurisdiction over a non-resident defendant, it must comply with the two-step analysis articulated by the Florida Supreme Court:<sup>25</sup> First, the court must determine whether the complaint satisfies the requirements of Florida’s long-arm statute<sup>26</sup>, and second, it must determine “whether the complaint alleges sufficient minimum contacts to satisfy [constitutional] due process requirements.”<sup>27</sup>

The Federal Circuit has consistently held that the act of sending a cease and desist letter into a state is not sufficient to justify an exercise of personal jurisdiction over the non-resident patent owner. The Federal Circuit has stated,

Principles of fair play and substantial justice afford a patentee sufficient latitude to inform others of its patent rights without subjecting itself to jurisdiction in a foreign forum. A patentee should not subject itself to personal jurisdiction in a forum solely by informing a party who happens to be located there of suspected infringement. Grounding personal jurisdiction on such contacts alone would not comport with principles of fairness.<sup>28</sup>

Based on this precedent, to the extent the bill would apply to a non-patent owner whose sole contacts with the state are sending cease and desist notices or letters offering to license a patent, a Florida court may lack personal jurisdiction over such a person.<sup>29</sup>

**B. RULE-MAKING AUTHORITY:**

The bill does not appear to create a need for rulemaking or rulemaking authority.

**C. DRAFTING ISSUES OR OTHER COMMENTS:**

None.

**IV. AMENDMENTS/ COMMITTEE SUBSTITUTE CHANGES**

On January 26, 2016, the Civil Justice Subcommittee adopted three amendments and reported the bill favorably as a committee substitute. The amendments:

- require a demand letter to include specific patent information and provide specific information when requested by the target;
- remove the Attorney General enforcement provision and restores the private cause of action, which provides a recipient of a bad faith demand letter to equitable relief, actual damages, and attorney fees and costs; and
- restore the exemption in current law for universities and technology transfer companies affiliated with universities.

On February 18, 2016, the Judiciary Committee adopted one amendment and reported the bill favorably as a committee substitute. The amendment:

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<sup>24</sup> *Id.*; *Dominant Semiconductors*, 524 F.3d at 1260.

<sup>25</sup> *Venetian Salami Co. v. Parthenais*, 554 So. 2d 499, 502 (Fla. 1989).

<sup>26</sup> s. 48.193, F.S.

<sup>27</sup> 554 So. 2d at 502.

<sup>28</sup> *Red Wing Shoe Co. v. Hockerson-Halberstadt, Inc.*, 148 F.3d 1355, 1360-61 (Fed. Cir. 1998); see also *Genetic Implant Sys., Inc. v. Core-Vent Corp.*, 123 F.3d 1455, 1458 (Fed. Cir. 1997)(“sending infringement letters, without more activity in a forum state, is not sufficient to satisfy the requirements of due process. Other activities are required in order for a patentee to be subject to personal jurisdiction in the forum.”).

<sup>29</sup> Memorandum from The Patent Troll Prevention Task Force, Re: Technical Input Memorandum to The Patent Troll Prevention Act, HB 1103, Senate Amendment to SB 1362 (April 15, 2015)(on file with the Civil Justice Subcommittee).

- removes language that made a person's failure to respond to a request from the target for information related to the alleged infringing conduct a factor in determining whether a demand letter violates the Act;
- provides for the award of punitive damages against individuals who repeatedly violate the Act; and
- changes the effective date of the bill from July 1, 2016, to upon becoming law.

This analysis is drafted to the committee substitute as passed by the Judiciary Committee.