Statement of the

National Retail Federation

and

Shop.org

submitted to the

United States House of Representatives
Committee on Judiciary
Subcommittee on Courts, Intellectual Property and the Internet

for its hearing on

"Abusive Patent Litigation:
The Impact on American Innovation & Jobs, and Potential Solutions"

held on

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Chairman Coble, Ranking Member Watt and members of the House Judiciary Subcommittee on Courts, Intellectual Property, and the Internet, on behalf of the National Retail Federation (NRF) and its division Shop.org, I appreciate the opportunity to submit this written statement to the Committee in connection with its hearing entitled "Abusive Patent Litigation: The Impact on American Innovation & Jobs, and Potential Solutions" held on March 14, 2013.

As the world's largest retail trade association and the voice of retail worldwide, NRF represents retailers of all types and sizes, including chain restaurants and industry partners, from the United States and more than 45 countries abroad. Retailers operate more than 3.6 million U.S. establishments that support one in four U.S. jobs – 42 million working Americans. Shop.org, a division of the National Retail Federation, is the world's leading membership community for digital retail. Founded in 1996, Shop.org's 600 members include the 10 largest online retailers in the U.S. and more than 60 percent of the *Internet Retailer* Top 100 E-Retailers. Contributing $2.5 trillion to annual GDP, retail is a daily barometer for the nation's economy.

Summary of Comments

Members of the National Retail Federation believe that Congress must address the rapidly growing problem of abusive patent litigation by "patent trolls." While the majority of the patent reform conversation revolves around technology companies, we are pleased from the scope of views represented on the witness panel that the Committee recognizes the impact patent trolls are having on the retail industry. Patent trolls are stealing precious capital resources that many retailers would otherwise use to invest in their businesses, including jobs, innovation and refurbishment of their stores.

In recent years, over 200 retailers have contacted NRF about this issue because they have been, or are currently, the target of patent trolls' abusive practices. The threat typically comes from firms whose business model is buying obscure patents which are about to expire and then either licensing the patents to retailers through the threat of litigation or filing lawsuits in an effort to force a settlement. Often retailers will choose to pay the licensing fee because patent litigation is prohibitively expensive.

A patent troll's typical strategy is to go after end-users such as retailers. Why? End-users are more numerous. One manufacturer or vendor may supply a product or service to thousands of retail end-users. Thus, there are many more entities from which to demand a royalty. The end-user retailers are also easy prey because they lack the expertise to fight complex patent infringement claims. They also typically operate on thin profit margins compared to high-tech companies. Knowing that retailers lack technical expertise, operate on thin margins, and that patent litigation is enormously expensive, trolls will often price a settlement demand, which may still be in the millions, below the cost of litigating, and, thus, effectively blackmail a retailer into settling. This is an abuse of the system.

Nor can retailers always obtain indemnification from their vendors. Because of consolidation in the technology industry, sellers of technology equipment and services have more bargaining power, making it more difficult for end-users to negotiate indemnification

clauses or warranty of non-infringement clauses in their contracts when they buy such equipment or services.

Patent trolls frequently file claims that are based on broad concepts and a general way of doing something rather than specific software innovations. This enables trolls to assert infringement claims covering the use of technology in virtually every area of e-commerce and mobile retailing (for example, providing store-locator functionality on a website; clicking on an item on a website to obtain further product information; sending electronic notifications to customers that their packages have been shipped). Moreover, trolls' claims are not limited to e-commerce applications, but also affect the operations of traditional "brick and mortar" retail stores as well (for example, claims that purport to cover the printing of receipts at cash registers, the sale of gift cards, and the connection of any product such as a computer or printer to an ethernet network).

On the rare occasions these cases go to trial, it has been reported that trolls lose 92 percent of the time, but this is small comfort to the retailers who lack the resources to see these cases through to a resolution. Often, the damages claims are so exorbitant, and the prospect of relief through litigation so time-consuming, that retailers make a business decision to settle, rather than litigate. Smaller retailers may find themselves particularly ill-equipped legally or financially to defend themselves from abusive claims.

Seeing a court case through to final adjudication can easily cost a retailer millions of dollars, but even a settlement agreement can be expensive. Some of our members report that they spend as much as one million dollars annually on patent troll-related expenses and settlement agreements. While licensing fees might seem nominal compared with the cost of a lawsuit, these fees take away from a retailer's ability to use capital to reinvest in the business, grow and create jobs.

The recent Newegg case[1] demonstrates the many costly steps involved in litigating a case. Over two years ago Soverain Software sent Newegg, and other retailers, a demand letter asserting broad infringement claims relating to the functionality of online shopping carts. One large retailer had previously settled for millions of dollars, and another had also settled with Soverain for an undisclosed amount. Newegg, however, fought the claim. At trial a jury awarded Soverain $2.5 million. Newegg appealed the decision, and the Federal Circuit Court of Appeals invalidated all of the asserted patent claims on the basis of obviousness in January 2013.[2] Although Newegg proved ultimately successful, the case took nearly two years and millions of dollars to resolve.

The Newegg case is just one example of the broad infringement claims trolls are asserting against retailers. There are over one million software patents in the United States. Many software patents contain broad concepts dealing with Internet functionality and have extraordinarily vague claims. Past asserted patents include activities as mundane as (1) a

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[1] *See supra* note 3.

[2] Chole Albanesius, "Newegg Crushes Patent Troll in Online 'Shopping Cart' Suit" PCMag. Com, January 28, 2013, last accessed March 5, 2013, available at http://www.pcmag.com/article2/0,2817,2414778,00.asp.

retailer's mobile application linking to their website[3], (2) using a search function as part of the retail website[4], or even (3) scanning a document to PDF and then emailing the file[5].

Legislative Solutions

The members of the National Retail Federation appreciate the efforts of Congress to reform the United States patent system through the America Invents Act in 2011. Retailers believe, however, that true patent reform will not be complete until Congress has devised a way to combat the alleged infringement claims made by patent trolls.

The Saving High-Tech Inventors from Egregious Legal Disputes (SHIELD) Act, recently introduced by Representative DeFazio (D-OR) and Representative Chaffetz (R-UT), will provide relief to retailers because the losing party is obligated to cover the fees and costs of the prevailing party. We feel this proposal would deter patent trolls from filing frivolous lawsuits and shift the financial risk calculus for all parties involved. In addition, the bill provides retailers the opportunity to defend against an infringement claim by taking a case to trial with the opportunity to recover their costs and attorneys' fees because the patent trolls would be required to pay if their case was unsuccessful.

Other deterrents to frivolous litigation might be found in modest process reforms for handling patent litigation. One proposal, for example, would be to limit the scope of discovery in patent cases, because abusive discovery requests are another expensive tactic trolls use to drive up the costs of fighting these claims in order to compel retailers to agree to an early settlement. By limiting a patent troll's ability to utilize endless discovery requests, it might be possible to strike the proper balance between protecting legitimate patent claims and the rights of retailers and others who must defend themselves from abusive litigation.

Conclusion

Patent trolls inhibit innovation and growth in the retail industry. Scarce resources that could be used to open new stores, create jobs or improve the customer experience are being drained away to fight claims by predatory and abusive patent trolls. The National Retail Federation commends the Committee's attention to this issue, and we look forward to working with you and your colleagues as you seek viable solutions to help end abusive patent litigation.

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[3] USPTO **7,441,196** http://patft.uspto.gov/netacgi/nph-Parser?Sect2=PTO1&Sect2=HITOFF&p=1&u=/netahtml/PTO/search-bool.html&r=1&f=G&l=50&d=PALL&RefSrch=yes&Query=PN/7441196

[4] Mark Brohan, "A big patent win for e-tailers" InternetRetailer.com, May 22, 2012, http://www.internetretailer.com/2012/05/22/big-patent-win-e-retailers

[5] Mark Gibbs, "A Patent Troll Wants to Charge You for Emailing Your Scans!" Forbes.com, January 5, 2013, http://www.forbes.com/sites/markgibbs/2013/01/05/a-patent-troll-wants-to-charge-you-for-emailing-your-scans/