



National Retail Federation Testimony

Hearing on

Demand Letters and Consumer Protection:
Examining Deceptive Practices by Patent Assertion Entities

Committee on Commerce, Science and Transportation
Subcommittee on Consumer Protection, Product Safety, and Insurance

United States Senate

November 7, 2013

Lary Sinewitz
Executive Vice President
BrandsMart USA

On Behalf Of
The National Retail Federation

Liberty Place
325 7th Street NW, Suite 1100
Washington, DC 20004
800.NRF.HOW2 (800.673.4692)
202.783.7971 fax 202.737.2849
www.nrf.com

Introduction and Background:

Chairman McCaskill, Ranking Member Heller, and members of the Subcommittee, I thank you for the opportunity to appear before you today. My name is Lary Sinewitz, and I am executive vice president of BrandsMart USA. Founded in 1979, BrandsMart USA is a consumer electronics and appliance retailer in the Southeast. With 11 retail stores in South Florida and the Atlanta area and a growing ecommerce presence at BrandsMart-USA.com, BrandsMart USA is the 8th largest appliance retailer in the country. We employ 2,000 people.

I am here today on behalf of the National Retail Federation (“NRF”) and the Stop Patent Abuse Now (“SPAN”) Coalition to testify about the impact of demand letters sent by patent assertion entities (“PAEs”) or “patent trolls” on small businesses and consumers. Members of the NRF and the SPAN Coalition appreciate the attention the Subcommittee is paying to this particular issue.

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. 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. The National Council of Chain Restaurants, a division of the National Retail Federation, has worked to advance sound public policy that serves restaurant businesses and the millions of people they employ for over 40 years. NCCR members include the country’s most respected quick-service and table-service chain restaurants. Contributing \$2.5 trillion to annual GDP, retail is a daily barometer for the nation’s economy. Retailers create opportunities for life-long careers, strengthen communities at home and abroad, and play a leading role in driving innovation.

The SPAN Coalition represents the interests of retailers, advertisers, advertising agencies, and direct marketers who increasingly are being targeted by patent trolls with unfair and deceptive patent infringement demand letters.

BrandsMart’s Experience with Patent Troll Demand Letters

You have invited me to testify about my company’s experience with unfair or deceptive demand letters. I am just one retailer, but I believe my experience receiving patent troll demand letters is fairly typical, not only of retailers, but also of businesses and not-for-profits of all types who are the end-users of technology.

Over the course of the last several years, my company alone has received six patent troll demand letters. For example, in 2008, I received a short, two paragraph letter from a law firm stating that it had come to their attention that my retail facilities were using debit and gift cards that were activated in a manner that may raise issues with their client's patent.

To be clear, the technology at issue in the demand letter is a ubiquitous technology that enables debit cards and gift cards to read and process information via the magnetic strip on the back of the card. Virtually every retailer uses this type of technology. So imagine my shock when some law firm sent me a vague letter accusing me of patent infringement and trying to get me to pay them some unknown sum of money for a license.

I do not believe this law firm did any due diligence truly to ascertain whether BrandsMart was infringing its client's patent. Rather, I believe, based on my conversations with other retailers in my region, that the firm simply picked the 150 biggest retailers in the Atlanta metropolitan area and sent the same vague demand letter to each of them.

So, I ask you to put yourselves in my shoes – and the shoes of retailers and similarly situated small businesses across the country. You receive a vague patent troll demand letter about some process you are using to enable credit cards to be used in your stores. What do you do? Consult a patent lawyer? BrandsMart does not have in-house patent lawyers, and we did not even have a patent lawyer on retainer. As one can imagine, just to pick up the phone to consult a patent lawyer to determine the validity of the infringement claim and evaluate the license demand could cost tens of thousands of dollars. Moreover, the cost of litigating the claim in court or going to the Patent Trademark Office to challenge the patent could be prohibitive or imprudent to a business such as mine.

Patent troll demand letters like this one put the fear in you that a costly lawsuit could be forthcoming. So what can you do? Stop accepting credit cards and gift cards? No way; that would be the death of your business. So, a business like mine either ignores the letter at our own peril (and hope the harassment goes away) or we begrudgingly try to settle for as little money as possible. In every case, we have chosen the later approach and paid.

Incidentally, we did incur the expense of consulting a patent lawyer about this letter, and when BrandsMart informed the PAE that we used a different technology to read cards, they still demanded a settlement, but reduced the amount. We ended up paying this particular PAE for five figures, and our legal fees were five figures as well. I have submitted the redacted letter with my testimony today.

Regrettably, in the past ten years, BrandsMart has spent approximately \$500,000 consulting with attorneys on infringement claims and settling with patent trolls.

BrandsMart's Experience with Patent Troll Demand Letters is not Unique

What NRF and the SPAN Coalition have learned is that BrandsMart's experience with patent troll demand letters is not unique. Patent trolls are increasingly harassing businesses and not-for-profits of every size, across a wide swath of industries, with demand letters. These letters come out of nowhere, and often allege that the mere use of everyday technology violates the patent holders' rights. Further, these questionable letters typically state vague or hypothetical theories of infringement, often overstate or grossly reinterpret the patent in question, and, in some cases, make allegations of infringement of expired or previously licensed patents.

At their core, demand letters use the threat of litigation as leverage to extract a "licensing fee" from the recipient business. Businesses like BrandsMart often simply settle these nuisance claims rather than run the risk of protracted litigation in federal court. Put simply, it is often much more expensive to hire a lawyer to review or defend against a suspect claim than it is to pay the requested "fee." This is the trolls' business model.

No one knows just how many thousands of patent-related demand letters are sent out by trolls each year; statistics only track actual patent infringement litigation in federal courts. The troll has to actually file a case in court before a judge is even made aware of the infringement claim, therefore it is impossible to get an accurate understanding of the full breadth of this problem.

End-user businesses such as retailers also appear to be easy prey because they often lack the legal resources and expertise to fight complex patent infringement claims. Many retailers do not even employ legal counsel in-house, let alone a highly specialized patent attorney. Ninety-one percent of retail companies operate with fewer than 20 employees and 95% of retail companies operate just one location.¹ Further, most retailers also do not have the time or money to engage in a lengthy battle with patent trolls. The average cost of fighting a patent troll is around \$2 million and takes about 18 months.² Patent trolls knowingly exploit their targets' tactical disadvantages, often pricing a settlement

¹ 2007 Economic Census, thisisretail.org.

² Mark Gibbs, "A Patent Troll Wants to Charge You for Emailing Your Scans," Forbes.com, January 5, 2013.

demand (which may still be in the millions) just below the cost of litigation, effectively blackmailing a retailer into settlement. This is an abuse of the system.

Trolls' claims not only affect e-commerce applications and the everyday use of technology, but also affect the storefront operations of traditional "brick and mortar" retailers, like BrandsMart. Some real world examples of the latter are claims that purport to cover point of sale and inventory control equipment, including; scanning barcodes, printing receipts, the sale of gift cards, and the connection of any product, such as a computer or printer, to an Ethernet network.

Today, too many businesses like BrandsMart are diverting precious capital resources to settle with or fight patent trolls. This is capital that they could otherwise use to invest in their businesses and in their communities, including; creating jobs, fostering innovation, and maintaining their stores. Because the retail industry contributes \$2.5 trillion to our nation's annual GDP, loosening the grip of patent trolls on retailers and others will allow innovation and growth to flourish, and undoubtedly benefit the overall U.S. economy.

NRF and SPAN Coalition members support legislative proposals to have the Federal Trade Commission ("FTC") look into these unfair or deceptive demand letters and, using their current consumer protection enforcement powers, rein in bad actors that target main street businesses. Patent trolls should not have free reign to assert expired patents, make repeated and false threats of litigation to extort fees, and materially mislead the recipients of these demands. At the very least, patent trolls should be required to provide more details in their letters. Currently, the letters are so effective because they lack specificity. Requiring greater and truthful disclosure will provide greater certainty to businesses, saving them time and money as they investigate the person or entity asserting the patent and determine the overall merits of the infringement claim.

Combating the rise of patent trolls is a top priority for retailers and the SPAN Coalition as a whole. We look forward to discussing meaningful legislative solutions and demand letter relief as patent litigation reform legislation moves forward this year. We appreciate the Subcommittee's attention to this issue, and look forward to continuing our work together.