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Making The Hunter The Hunted: North Carolina Gives Business Owners New Tools To Combat 'Patent Trolls'

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Litigation in federal courts under federal law is a primary weapon in the battle to protect patents from infringement. However, because of alleged abuse, certain states, including North Carolina, have taken it upon themselves to establish their own rules of conduct for patent infringement actions.

Governor Pat McCrory signed the North Carolina "Abusive Patent Assertions Act" ("Act") into law on August 11, 2014. The Act seeks to protect business owners from frivolous claims filed by "patent trolls," a term used to refer to those who use patent infringement actions solely as a means to make money instead of actually inventing products and bringing them to market. The Act is an amendment to the North Carolina Unfair and Deceptive Trade Practices Act and creates new liability for those who file frivolous patent enforcement actions.

North Carolina is among a very small group of states changing the legal climate for patent infringement and putting heat on patent trolls. Whether your company is defending a patent infringement action, seeking to prosecute one, or exercising due diligence in being prepared for either, it should take note of these changes. Doing so will allow your company to best position itself if and when an issue of patent infringement arises.

What is a "Patent Troll"?

"Patent trolls," also referred to as "non-practicing entities," are businesses that critics claim purchase patents for the sole purpose of extracting settlements from business owners. The patents are used as a springboard for filing frivolous enforcement actions. These groups or entities allegedly bank on the inability or unwillingness of the target of an infringement action to expend the funds necessary to defend the target's patent, including attorneys' and expert witness fees, court costs, and lost productivity by employees whose time and effort must be devoted to the defense instead of market activities. The idea is that the litigation will, among other things, allow the patent troll to extract licensing fees from its target. Critics of these entities claim that the majority of patent litigation can be attributed to these schemes and that such actions cut against and stymie an environment which fosters invention and protects those who invent.

On the other hand, defenders of non-practicing entities argue that small inventors do not have the wherewithal to defend their patents from corporate giants who either defensively buy patents at unconscionably low prices or simply and openly infringe on existing patents without any real fear of enforcement by the smaller patent holder. These proponents claim that the statistics used by critics are taken out of context and that the majority of infringement actions are legitimate.

Either way, patent trolls and the tactics they allegedly employ are topics that are garnishing quite a bit of national attention. Even President Obama himself appears to have commented on the topic, suggesting

during his 2014 State of the Union Address that Congress "pass a patent reform bill that allows our businesses to stay focused on innovation, not costly, needless litigation." While the issue has not yet woven its way through Congress at the federal level, a few states, including North Carolina, are taking action.

The Changed Landscape

The hallmark of the Act is that it gives North Carolina businesses targeted by patent infringement actions a legal claim in North Carolina courts against those who make bad-faith demands or file bad-faith lawsuits for patent infringement. Moreover, any demand or any lawsuit that is found to have been made or filed in bad faith exposes the patent troll to a litany of liabilities such as monetary damages and attorneys' fees.

The Act gives the state courts significant latitude in determining what constitutes "bad faith" by setting out a nonexclusive list of factors that *may* be considered by the court in making that determination, including:

- Use of a demand letter that does not contain certain information such as the patent application number or patent number, the name and address of the patent owner or owners, and the specific factual allegations concerning the specific areas of the infringement;
- A demand for payment of a license fee or response within an unreasonably short period of time;
- An offer to license the use of the patent to the target for an amount that is not based on a reasonable estimate of the value of the license, or an offer to license the patent for an amount that is based on the cost of defending a potential or actual lawsuit;
- The assertion of a meritless patent infringement claim by a clamant who knew or should have known that the claim or assertion was meritless;
- Evidence that the claimant or an affiliate of the claimant has, subject to certain conditions, previously or concurrently filed or threatened to file one or more lawsuits based on the same or similar claim of patent infringement; and,
- Evidence that the same demand or substantially the same demand was sent to multiple recipients and made assertions against a wide variety of products and systems without reflecting those differences in a reasonable manner.

The Act carries stiff penalties for those who violate its protections, including injunctive and monetary relief for the target of the violations. Specifically, the Act allows the recovery of money damages, costs, reasonable attorneys' fees, and, in certain situations, "exemplary damages" of $50,000 or three times the total of the target's damages, costs, and fees, whichever is greater.

In addition to the stiff penalties mentioned above, the Act provides two very significant deterrents to patent trolling schemes. First, the Act states that "upon a finding by the court that a target has established a reasonable likelihood that a person has made a bad-faith assertion of patent infringement in violation of this Chapter, the court shall require the person to post a bond in an amount equal to a good-faith estimate of the target's fees and costs to litigate the claim and amounts reasonably likely to be recovered."

While the required bond cannot exceed $500,000, the mere threat of the court imposing such a costly bond should act as a significant deterrent to bad-faith infringement actions. Second, and just as important, individuals associated with the patent troll making a bad-faith claim can be "joined" in the lawsuit and, if the patent troll cannot pay a judgment against it, may be made individually liable for that award by the court.

Conclusion

It remains to be seen how the Act will work in practice and what effect it will have on patent infringement litigation. North Carolina has not seen a great deal of patent infringement actions compared to other states

but, with these new protections in place, North Carolina may be the beneficiary of business relocations because of the protections extended to all businesses located in the state.

Regardless of the ultimate effect of the Act, prudent North Carolina business owners must take note of these changes in order to be better prepared to assert whatever benefits it will afford them.

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