

SENATE BILL REPORT

SHB 1495

As of March 16, 2011

Title: An act relating to the unfair competition that occurs when stolen or misappropriated information technology is used to manufacture products sold or offered for sale in this state.

Brief Description: Regarding the unfair competition that occurs when stolen or misappropriated information technology is used to manufacture products sold or offered for sale in this state.

Sponsors: House Committee on Judiciary (originally sponsored by Representatives Eddy, Rodne, Kirby, Armstrong, Hunter, Hinkle, Chandler, Pettigrew, Carlyle, Springer, Maxwell, Anderson, Clibborn, Kelley and Kenney).

Brief History: Passed House: 2/22/11, 90-4.

Committee Activity: Labor, Commerce & Consumer Protection: 3/14/11.

SENATE COMMITTEE ON LABOR, COMMERCE & CONSUMER PROTECTION

Staff: Ingrid Mungia (786-7423)

Background: Consumer Protection Act. The state's Consumer Protection Act (CPA) prohibits unfair or deceptive acts or practices and unfair methods of competition in the conduct of trade or commerce that directly or indirectly affect the people of Washington. Several statutes specify practices that constitute unfair acts, but they do not provide an exhaustive list. A court may find that conduct not specifically enumerated in statute may constitute an unfair or deceptive act.

Either private plaintiffs or the Attorney General may bring civil actions to enjoin future violations of the CPA or to recover damages caused by an unfair act. Private plaintiffs may recover actual damages and costs, including reasonable attorneys' fees. Courts also may award private plaintiffs damages of as much as three times actual damages, in an amount not to exceed \$25,000.

Personal vs. In Rem Jurisdiction. In order for a court to hear and determine a controversy, it must have jurisdiction over the matter. Often, courts have personal jurisdiction over a person sued in a civil lawsuit because the person made certain minimum contacts with the state; for purposes of the CPA, this includes transacting business within Washington.

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Foreign defendants whose actions give rise to a lawsuit in a Washington court but who have never visited the state and who have no assets within Washington might not be subject to personal jurisdiction. Yet state courts may have jurisdiction to enter judgment regarding property located within the state, even if the courts do not have personal jurisdiction over that defendant. Such actions against property are called proceedings in rem.

Intellectual Property. Federal and state laws protect certain intellectual property rights in creations, such as computer software (programs) and hardware (equipment). A federal copyright gives the owner of an original work that expresses ideas, such as certain software, exclusive rights to copy, distribute, and adapt the work. A federal patent may protect a publicly disclosed computer-related invention for a period of time. Federal and state trade secret laws prohibit misappropriation of trade secrets, such as formulas, programs, and techniques.

Some holders of software copyrights license other people to modify and redistribute source code for those programs for free. Such programs commonly are called open source software.

Summary of Bill: The bill as referred to committee not considered.

Summary of Bill (Proposed Amendment): A business that manufactures a product while using stolen or misappropriated information technology (stolen IT) in its business operations engages in unfair competition when the product is sold in Washington, either separately or as a component of another product, in competition with a product made without use of stolen IT. A new cause of action allows private plaintiffs or the Attorney General to sue businesses that engage in these unfair acts.

Stolen or misappropriated IT is defined as hardware or software that a person acquired, appropriated, or used unlawfully, unless the hardware or software was not available for stand-alone retail purchase at or before the time it was stolen. Using information technology in business operations means using IT to design, manufacture, distribution, marketing, or sales of products.

Notice. Before an injured plaintiff can file suit, the owners of stolen IT must provide written notice to the party allegedly using the stolen IT giving the party the opportunity to prove it is not using stolen IT or 90 days to stop using it or begin legalizing or replacing the stolen IT they are using, subject to any extensions approved by the owner or the court. The notice must state (1) the identity of the IT; (2) the identity of the lawful owner; (3) the identity of the applicable law being violated; (4) the manner in which the IT is being used, if known; (5) the products related to the stolen IT; and (6) the basis and evidence supporting the allegation.

Jurisdiction. A court may proceed in rem against certain products only if a court is unable to obtain personal jurisdiction over a party who violated the act.

Elements of a Claim. A person is injured by the sale of a product if the person establishes by a preponderance of the evidence that:

- the person manufactures articles or products sold or offered for sale in Washington in competition with articles or products made using stolen IT;
- the person's articles or products were not manufactured using stolen IT;

- the person suffered economic harm, which may be shown by evidence that the retail price of the stolen IT was \$20,000 or more; and
- the person is proceeding in rem or seeks injunctive relief, that they have suffered a material competitive injury.

Remedy. If the use of stolen IT continues despite the owner of the stolen IT providing the 90-days' notice, any injured person or the Attorney General may bring an action against any person, article, or product to ask the court to enjoin violations of the bill's provisions, including ordering a person not to sell certain products in Washington. A plaintiff also may ask for the greater of actual damages or statutory damages of no more than the retail price of the stolen IT. An award of damages against a third party must be the lesser of the retail price of the stolen IT or \$250,000.

If a person found to have violated the bill's provisions lacks sufficient attachable assets in Washington, a court may enjoin the sale or offering for sale in the state of any products made using stolen or misappropriated IT. A person subject to an order for injunctive relief must be given reasonable notice and opportunity to be heard.

A court may award as much as three times the damages normally allowed when it finds that the defendant willfully used stolen IT. A court also may award costs and reasonable attorneys' fees to the prevailing plaintiff in actions brought by an injured individual, or to a prevailing defendant in action brought by an injured person.

Exceptions. A person may not sue under this cause of action when:

1. the end product sold or offered for sale in Washington is:
 - a. a copyrightable work under the United States Copyright Act;
 - b. merchandise manufactured by or on behalf of a copyright owner and that displays a component or copyrightable element of a copyrighted work;
 - c. merchandise manufactured by or on behalf of a copyright owner or trademark owner and that displays a component or copyrightable elements relating to a theme park or theme park attraction; or
 - d. packaging or promotional material for such copyrightable works or merchandise.
2. the allegation that the IT is stolen is based on a claim that the IT infringes on patents or trade secrets;
3. the allegation that the IT is stolen is based on a claim that the use of the IT violates the terms of an open source software license; or
4. the allegation that a person aided, facilitated, or otherwise assisted someone else to acquire or use stolen IT.

A court may not award damages against a third party when they establish by a preponderance of the evidence that they:

- are the end consumer of a product or acquired the product after its sale to an end consumer;
- are a business with annual revenues of less than \$50 million;
- are pursuant to an agreement between the person and a manufacturer before 180 days after the effective date of the bill or acquired the products in good-faith reliance on either a code of conduct that governs the commercial relationship with the

manufacturer or written assurances from the manufacturer that the products were made without the use of stolen IT, as long as within 180 days of receiving written notice that satisfies the requirements of the bill, the person implements commercially reasonable efforts to confirm stolen IT is not being used, direct the manufacturer to cease theft or misappropriation or that prevent future acquisition of products from such a manufacturer or supplier; or

- have made commercially reasonable efforts to implement practices and procedures to require a manufacturer not to use stolen IT; or
- do not have a contractual relationship with the manufacturer that stole the IT.

A court may not enforce an award of damages against a third party for a period of 18 months from the effective date of the bill.

Consumer Protection Act. The bill creates remedies exclusive of the Consumer Protection Act.

Appropriation: None.

Fiscal Note: Available.

Committee/Commission/Task Force Created: No.

Effective Date: Ninety days after adjournment of session in which bill is passed.

Staff Summary of Public Testimony: PRO: This bill will help many companies which are in the business of developing information technology that is used in the manufacturing of goods worldwide. While many companies purchase their back office software, there are some manufacturers that do not purchase their back office software. We have not been able to contain the misappropriation of property when it is used in manufacturing. International law has failed us and we have a duty to protect the information technology of American companies. This is an important piece of legislation that will give the technology industry the ability to keep growing and provide jobs. The problem of piracy has been an impractical one. This bill will provide an important tool to address the unfair competition and level the playing field by providing a cause of action by the manufacturers playing by the rules against those that are not. It also provides various incentives through notice and cure provisions to correct the problem before litigation. This bill will level the playing field. The latest amendments address the concerns of various companies. We have broadened the safe harbor provisions and added protection against multiple litigation by strengthening the notice provisions and opportunity to cure. This bill has a number of safe harbor defenses to address the concerns. This cannot be enforced without a notice and opportunity to cure the problem. Software piracy hurts economic growth and limits jobs. Intellectual property has to be protected. It is not unusual for the Legislature to regulate intellectual property rights. Without protections like these in the bill, there are no incentives for companies to produce products.

CON: This bill does not accomplish its intended goal and will tie businesses up in litigation. Software compliance is difficult and complex. This bill is flawed because it includes many provisions that are broad and undefined and will lead to unintended consequences. This bill

will discourage competition in this state. The Retail Association wants to work on this issue during the interim and ask Congress to work on this issue at a national level. This bill will not help curb the piracy of software products because legitimate retailers do not want to buy pirated products. There are already national laws that address this issue. Most legitimate retailers will have representations and warranties in their sale agreements which require a vendor to sell products that do not violate any laws. Retailers do not want to be the policing force for another company that they believe is using pirated software internationally. There should be an absolute defense written into the legislation. Protections of brands is a high priority for General Motors. Motor vehicle manufacturing is a complex process and complex supply chain. We are concerned that the provisions in the bill could interrupt the supply chain and interrupt the timely delivery of vehicles to dealers. The extra territorial effect in the bill leads to concerns about the bill's constitutionality.

Persons Testifying: PRO: Representative Eddy, prime sponsor; Nancy Anderson, Microsoft; Lew McMurrin, Washington Technology Industry Association; TK Bentler, Motion Picture Association of America.

CON: Jim Halstrom, IBM; Rene Albury, Software Information Industry Association; Mark Johnson, Washington Retail Association; Cliff Webster, General Motors.