

# SENATE BILL REPORT

## SHB 1495

---

---

As Reported by Senate Committee On:  
Labor, Commerce & Consumer Protection, March 17, 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, 3/17/11 [DPA-WM, DNP, w/oRec].

---

### SENATE COMMITTEE ON LABOR, COMMERCE & CONSUMER PROTECTION

**Majority Report:** Do pass as amended and be referred to Committee on Ways & Means.

Signed by Senators Kohl-Welles, Chair; Conway, Vice Chair; King, Assistant Ranking Minority Member; Keiser.

**Minority Report:** Do not pass.

Signed by Senator Kline.

**Minority Report:** That it be referred without recommendation.

Signed by Senator Holmquist Newbry, Ranking Minority Member.

**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.

---

*This analysis was prepared by non-partisan legislative staff for the use of legislative members in their deliberations. This analysis is not a part of the legislation nor does it constitute a statement of legislative intent.*

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.

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 (Recommended Amendments):** 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.

Remedies Against Manufacturers. If the use of stolen IT continues despite the required notice, an injured person or the Attorney General may bring an action to enjoin violations of the act's provisions, including ordering a person not to sell products in Washington. A plaintiff also may seek the greater of actual damages or the amount of the retail price of the stolen IT. The court may triple the damages if the defendant willfully used stolen IT. A court may award costs and reasonable attorneys' fees to the prevailing party for all litigation expenses incurred in actions brought by an injured person.

Remedies Against Third Parties. The plaintiff may add to the action a claim for actual damages against a third party who sells the products made with stolen IT, but only if a court has first entered judgment against the person using stolen IT. Damages may be imposed against a third party only if certain conditions are met, including the requirement that the third party received 90-days notice before entry of the judgment and the person who was found to have used stolen IT either did not appear in court or has insufficient attachable assets to satisfy the judgment.

Damages against a third party are limited to the lesser of \$250,000 or the retail price of the stolen IT, minus any amounts recovered from the person using stolen IT. The court may award attorneys' fees to a third party who qualifies for an affirmative defense if the third party notified the plaintiff of the affirmative defense prior to being added to the action.

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.

The bill creates remedies exclusive of the Consumer Protection Act.

Stay and Dismissal of Proceedings. The court must dismiss an action against a person using stolen IT or a third party if the person or third party has been subject to a final judgment, or has entered into a final settlement, in a proceeding in any federal or state court arising out of the same theft. If the person or third party is subject to a pending action in a federal or other state court, the court must stay the action pending resolution of the prior action.

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.

Affirmative Defense for Third Parties. A court may not award damages against a third party if the third party establishes that:

- it is the end consumer of a product or acquired the product after its sale to an end consumer;
- it is a business with annual revenues of less than \$50 million;
- it acquired the products in reliance on either a code of conduct that governs the commercial relationship with the manufacturer or in general undertook commercially reasonable efforts to implement a code of conduct with its manufacturer regarding the use of stolen IT; or
- it does not have a contractual relationship with the manufacturer that stole the IT.

**EFFECT OF CHANGES MADE BY LABOR, COMMERCE & CONSUMER PROTECTION COMMITTEE (Recommended Amendments as Passed Committee):** Includes in the definition of copyrightable end product, mask works protections as specified in the United States Code. Clarifies the written notice provided to a third party alleging the use of stolen IT must be properly served to a third party's agent for service of process. Clarifies in an action brought by a private plaintiff, a court may award costs and reasonable attorneys' fees to a third party for all litigation expenses, including without limitation, discovery expenses, incurred by a party that prevails when a person either manufactured the final product or produced a component equal to 30 percent or more of the value of the final product. Restructures Section 8 for clarity.

**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 on Proposed Amendments as Heard in Committee:**

**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.