

**UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF VERMONT**

STATE OF VERMONT)	
)	
Plaintiff,)	
)	
v.)	Civil Action No. 2:13-cv-00170-wks
)	
MPHJ TECHNOLOGY)	
INVESTMENTS, LLC,)	
)	
Defendant.)	
_____)	

**STATE OF VERMONT'S OPPOSITION TO
MPHJ'S MOTION FOR SANCTIONS UNDER RULE
11, 28 U.S.C. § 1927, AND THE COURT'S INHERENT AUTHORITY**

STATE OF VERMONT
WILLIAM H. SORRELL
ATTORNEY GENERAL

Bridget C. Asay
Ryan Kriger
Naomi Sheffield
Assistant Attorneys General
Office of the Attorney General
109 State Street
Montpelier, Vermont 05609-1001
(802) 828-5500
Counsel for Defendant-Appellee

CONTENTS

Page

ARGUMENT 1

I. MPHJ’s motion is an improper effort to test the legal sufficiency of the State’s complaint in the guise of a sanctions motion..... 1

II. An unfair and deceptive licensing campaign is an act “in commerce” under the Vermont Consumer Protection Act. 11

III. MPHJ does not have a protected right to engage in unfair and deceptive commercial speech or to disseminate demand letters in bad faith 15

 A. The First Amendment does not protect unfair and deceptive commercial speech 16

 B. The State may prove bad faith without addressing the scope or validity of MPHJ’s Patents..... 20

CONCLUSION..... 25

The Court should deny MPHJ's baseless request for sanctions. A sanctions motion is an extraordinary step, reserved for egregious breaches of a lawyer's obligations to the Court. As the Second Circuit has explained, "Rule 11 targets situations where it is patently clear that a claim has absolutely no chance of success." *Healey v. Chelsea Res., Ltd.*, 947 F.2d 611, 626 (2d Cir. 1991) (quotation omitted). MPHJ's motion, however, is based on nothing more than an unsurprising disagreement between the parties about the strength of the State's legal theories. MPHJ believes that it has a right under federal law to send patent enforcement letters that are deceptive and unfair. The State's position is that these letters violate Vermont's consumer protection law. The State's position is grounded in reasonable interpretations of state and federal law. It is also consistent with the actions of other state attorneys general, a draft complaint against MPHJ by the Federal Trade Commission aimed at precisely the same conduct that underlies this suit, and public statements by federal officials recognizing state authority in this area.

MPHJ's motion does not approach the showing necessary under Rule 11. The motion should be denied and the Court should order MPHJ to pay the State's attorneys' fees for responding to the motion.

I. MPHJ's motion is an improper effort to test the legal sufficiency of the State's complaint in the guise of a motion for sanctions.

By filing this motion, MPHJ is doing what the rule, the advisory notes, this Court, and numerous other courts all proscribe: it is using Rule 11 merely to dispute

the persuasiveness of its opponent's legal theories. As this Court has explained, "Rule 11 is not a vehicle to test the legal sufficiency of a complaint." *Akerley v. N. Country Stone, Inc.*, 2006 WL 2452640, at *6 (D. Vt. Aug. 23, 2006) (denying Rule 11 motion and noting "defendants' apparent disinclination to challenge the sufficiency of the pleadings directly").¹ It is not enough – not nearly enough – for a party to assert that an opponent's legal position is debatable, unpersuasive, or even unlikely to succeed. "The fact that a legal theory is a long-shot does not necessarily mean it is sanctionable. The operative question is whether the argument is frivolous, *i.e.*, the legal position has 'no chance of success,' and there is 'no reasonable argument to extend, modify or reverse the law as it stands.'" *Fishoff v. Coty Inc.*, 634 F.3d 647, 654 (2d Cir. 2011) (citations omitted); *see also* Fed. R. Civ. P. 11 advisory committee's note, 1993 amendment ("[T]he extent to which a litigant has researched the issues and found some support for its theories even in minority opinions, in law review articles, or through consultation with other attorneys should certainly be taken into account in determining whether [Rule 11(b)(2)] has been violated.").

Nowhere in its motion does MPHJ acknowledge or address the demanding standard for a Rule 11 motion. Instead, citing *Caisse Nationale de Credit Agricole-*

¹ *See also* Fed. R. Civ. P. 11 advisory committee's note, 1993 amendment ("Rule 11 motions should not . . . be employed . . . to test the legal sufficiency or efficacy of allegations in the pleadings; other motions are available for those purposes. Nor should Rule 11 motions be prepared to emphasize the merits of a party's position, to exact an unjust settlement, to intimidate an adversary into withdrawing contentions that are fairly debatable, [or] to increase the costs of litigation."); 5A Charles A. Wright & Arthur R. Miller, *Federal Practice & Procedure* § 1336.3 at 671 (3d ed. 2004) ("Rule 11 should not be used to raise issues as to the legal sufficiency of a claim or defense that more appropriately can be disposed of by a motion to dismiss, a motion for judgment on the pleadings, a motion for summary judgment, or a trial on the merits.").

CNCA v. Valcorp, Inc., 28 F.3d 259, 264-65 (2d Cir. 1994), it asserts that sanctions “are warranted when a party has asserted a legal theory or contention that is either not supported by, or instead is contradicted by, legal authority.” Doc. 38-1 at 11. That is not what *Caisse Nationale* says. Like *Fishoff* and scores of other cases, *Caisse Nationale* holds that an argument is frivolous only if “there is no chance of success and no reasonable argument to extend, modify or reverse the law as it stands.” 28 F.3d at 264 (quotation omitted).

Any suggestion that the existence of contrary legal authority, by itself, makes a legal theory frivolous is flatly inconsistent with the language of Rule 11 and precedent applying the rule. Courts have recognized that novel legal theories are permissible and parties acting in good faith may advance arguments that other courts have rejected. Rejecting sanctions in *Kamen v. Am. Tel. & Tel. Co.*, 791 F.2d 1006 (2d Cir. 1986), the Second Circuit emphasized its reluctance “to stifle the enthusiasm or chill the creativity that is the very lifeblood of the law.” *Id.* at 1014 (quotation omitted). Sanctions were inappropriate, the court held, because the law was “quite unsettled.” *Id.* The Fourth Circuit similarly declined to sanction a plaintiff for pursuing a legal theory that had been rejected by three district courts in other circuits. See *Brubaker v. City of Richmond*, 943 F.2d 1363, 1378 (4th Cir. 1991). The *Brubaker* court noted the lack of Supreme Court or circuit precedent and

observed that the “plaintiff under such circumstances has a right to come to court seeking to obtain a different result from that reached by other districts.” *Id.*²

MPHJ also asks the court to go further and individually sanction the assistant attorneys general, citing 28 U.S.C. § 1927, which allows for the imposition of sanctions on counsel that “unreasonably and vexatiously” multiply the proceedings. *Id.* The standard for such sanctions is higher than that of Rule 11, requiring a finding of not just “objective unreasonableness,” but also bad faith. See *Star Mark Mgmt., Inc. v. Koon Chun Hing Kee Soy & Sauce Factory, Ltd.*, 682 F.3d 170, 178 (2d Cir. 2012). This bad faith element is met when an “attorney’s actions are so completely without merit as to require the conclusion that they must have been undertaken for some improper purpose such as delay.” *United States v. Int’l Bhd. of Teamsters, Chauffeurs, Warehousemen & Helpers of Am., AFL-CIO*, 948 F.2d 1338, 1345 (2d Cir. 1991) (quotation omitted). Any delay or multiplicity in this case was caused by MPHJ, which first removed the action and has now filed a meritless Rule 11 motion. MPHJ’s disagreement with the State’s legal theory does

² See also *Azurite Corp. v. Amster & Co.*, 52 F.3d 15, 16, 19 (2d Cir. 1995) (upholding trial judge’s refusal to sanction private plaintiff even though different district judge in same court had ruled in defendants’ favor in “virtually identical action” brought by SEC; holding that district judge in second action had not abused her discretion in denying Rule 11 sanctions since investor had “made a good faith effort to persuade her not to follow [first district judge’s] unappealed decision in the SEC action.”); *Sec. Indus. Ass’n v. Clarke*, 898 F.2d 318, 321-22 (2d Cir.1990), *overruled on other grounds by Cooter & Gell v. Hartmarx Corp.*, 496 U.S. 384 (1990) (“[I]t seems self-evident that when a particular point of law is unsettled, parties and (or) their attorneys need not accurately prognosticate the correct law in order to avoid sanctions.”); *In re Cross Media Mktg. Corp. Sec. Litig.*, 314 F. Supp. 2d 256, 269 (S.D.N.Y. 2004) (declining to impose Rule 11 sanctions because “there was no circuit court authority” barring plaintiffs’ legal theory).

not meet “the high standard of ‘clear bad faith’ and ‘willful misconduct,’” as MPHJ suggests, Doc. 38-1 at 17, just as it does not satisfy the requirements for Rule 11.

MPHJ’s motion essentially asks this Court – which has not even decided its own jurisdiction – to delve into the merits of the State’s legal theory, predict how the Vermont Supreme Court would apply state law to these facts, and consider whether MPHJ can plausibly assert a First Amendment right to send patent enforcement letters that are unfair and deceptive.³ In Parts II and III, below, the State has addressed these legal issues and explained the basis for the State’s positions.⁴ But that level of analysis is not even necessary to illustrate that MPHJ’s motion is baseless and should be denied.

First, MPHJ’s motion relies on inaccurate descriptions of the cases it cites. MPHJ repeatedly asserts that the Vermont Supreme Court’s decision in *Foti Fuels, Inc. v. Kurrle Corp.*, 2013 VT 11, “makes it clear” that the Vermont Consumer Protection Act (“CPA”) does not apply to MPHJ’s patent licensing activity. Doc. 38-1

³ The State does not concede that this Court may impose sanctions based on the State’s filing of a state-law complaint in state court. *Cf. Willy v. Coastal Corp.*, 503 U.S. 131, 137-39 (1992) (district court could impose sanctions for procedural violation, even though court lacked subject-matter jurisdiction, where sanctions order did not “signify a district court’s assessment of the legal merits of the complaint” (quotation omitted)). The State contends that the Court lacks subject matter jurisdiction, and in the absence of jurisdiction, the Court may not impose a sanction of dismissal. *See Hernandez v. Conriv Realty Assocs.*, 182 F.3d 121, 123-24 (2d Cir. 1999). In any event, because defendant’s motion lacks merit, the Court may deny it without deciding whether other sanctions are theoretically possible.

⁴ In its motion, MPHJ twice references *Eng’g & Inspec. Servs., LLC v. IntPar, LLC*, 2013 WL 5589737 (E.D. La. Oct. 10, 2013), *see* Doc. 38-1 at 7, 30, but does not, in its argument, assert personal jurisdiction as a basis for its Rule 11 motion. The State has previously responded to MPHJ’s motion to dismiss for lack of personal jurisdiction, *see* Doc. 27, and does not further address that issue here.

at 18-19; *id.* at 8 (asserting that it is now “beyond peradventure” that state law cannot be applied to its conduct); *id.* at 21 (asserting that *Foti* “directly contradict[s]” the State’s position). *Foti* addressed a single, customized sale of a business and says nothing at all about patent licensing activity. MPHJ sent nearly identical form letters to thousands of targets nationwide. MPHJ’s suggestion that *Foti* decides this case is, itself, unreasonable. *See infra* 11-15.

Similarly, MPHJ repeatedly argues that a Nebraska district court decided the same issues presented in this case. *E.g.*, Doc. 38-1 at 8-9, 26. That is not true. The Nebraska litigation centered on a cease-and-desist order that the state attorney general issued to the law firm Farney Daniels. The order, issued without notice or findings, potentially affected the firm’s representation of a party other than MPHJ in a pending federal case. Although MPHJ later intervened in the case, “the Attorney General responded to [MPHJ’s] motion for a preliminary injunction with his argument about mootness. He filed no additional arguments regarding the motion for preliminary injunction.” Doc. 38-3 at 4 n.1. The Nebraska litigation was thus procedurally and substantively different from this case. *See infra* 24-25. The Nebraska court’s decisions – which are in any event not controlling precedent – have minimal relevance here.

Second, MPHJ relies on inaccurate descriptions of the State’s Complaint and the State’s position in prior filings with the Court. According to MPHJ, the State “artfully craft[ed]” its Complaint to “specifically avoid pleading that MPHJ enforced its patents in bad faith” and “purposely avoided pleading bad faith in its

Complaint.” Doc. 38-1 at 25-26. In fact, the Complaint expressly alleges that MPHJ’s letters were deceptive and unfair, and that MPHJ “acted in bad faith by sending these letters to Vermont businesses.” Doc. 6 at ¶ 54. MPHJ also says that the State has not pled that MPHJ’s “correspondence was objectively and subjectively baseless.” Doc. 38-1 at 23.⁵ Although the Complaint does not use that phrase, the Complaint asserts – with specific examples – that the letters were deceptive and sent in bad faith. Doc. 6 at ¶¶ 1, 56-57.

MPHJ even suggests that the State “cynically *concedes* that it has purposely so far avoided pleading bad faith, and it could not in the future make such an allegation in good faith.” Doc. 38-1 at 27 (emphasis added). That is false. The State has never made this concession. What the State has repeatedly and expressly argued to this Court is that the State’s consumer protection claims “have nothing to do with the validity of MPHJ’s patents,” Doc. 9-1 at 6, and that “[w]hatever the status of the patents, the letters sent by MPHJ were *not a good faith attempt to enforce these patents*,” Doc. 9-1 at 16 (emphasis added). MPHJ cannot base a sanctions motion on a non-existent concession.

Third, the positions taken by other state and federal officials, and MPHJ’s own conduct in settling similar claims with other states, all confirm that Vermont’s position in this case is reasonable and far from frivolous. MPHJ itself publicly disclosed the Federal Trade Commission’s draft complaint against it, Jay Mac Rust,

⁵ MPHJ states on at least eight occasions in its motion that the State failed to plead “bad faith” or objective and subjective baselessness. See Doc. 38-1 at 23, 25-28.

Farney Daniels, P.C., and attorney W. Bryan Farney. In a pleading filed in federal court in Texas, MPHJ alleged that the filing of the FTC's enforcement action was imminent. The FTC's draft complaint sets forth allegations very similar to the State's allegations in this case. It alleges, for example, that the defendants "falsely threatened thousands of small businesses with imminent patent infringement litigation." *See* State's Attach. 1, ¶ 11. The FTC's draft complaint also alleges that the defendants "falsely represented that substantial numbers of businesses had responded to their letters by purchasing licenses from the Defendants when, at the time of the representations, the Defendants had not sold any licenses to letter recipients." *Id.* According to the FTC, MPHJ sent letters to "16,465 small businesses located in all fifty states and the District of Columbia." *Id.* ¶ 20. The FTC's position that MPHJ and its counsel engaged in deceptive acts or practices "in or affecting commerce," *id.* ¶¶ 44, 47, illustrates the reasonableness of the State's similar position under the CPA. Vermont's law is generally interpreted consistently with the Federal Trade Commission Act. *See* 9. V.S.A. § 2453(b) ("courts of this State will be guided by the construction of similar terms contained in Section 5(a)(1) of the Federal Trade Commission Act").

The New York Attorney General also investigated MPHJ, set forth its findings, and stated its belief that MPHJ's practices "constitute repeated deceptive acts in violation of" New York's consumer protection law. Doc. 38-6 at 11. MPHJ settled with New York. Although MPHJ did not admit or deny the facts asserted by New York, it agreed to provide refunds to New York businesses and to substantially

change its practices. *See id.* at 12, 15-18. For example, the revised demand letters attached to the New York Assurance of Discontinuance omit many of the statements that Vermont has alleged were unfair and deceptive in the letters sent to Vermont consumers. *See id.* at 25-32. Among other things, the revised letters do not assert that the target is “likely” infringing, do not threaten litigation, and do not claim that other businesses have purchased licenses. MPHJ also reached a settlement with the Minnesota Attorney General, addressing actions by MPHJ that were substantially the same as those set forth in the State’s Complaint. State’s Attach. 2. MPHJ’s description of the State’s position as “frivolous,” “untenable,” “unlawful,” and a “textbook case of sham litigation,” Doc. 38-1 at 7-10, 28, cannot be reconciled with its decision to settle similar claims by other states.⁶

Vermont’s pending lawsuit and New York’s settlement reflect the states’ longstanding authority and jurisdiction in consumer protection cases. Federal lawmakers recognize this authority as well. Senator Claire McCaskill, at a recent Senate hearing, described the practices of patent assertion entities as a “growing consumer protection concern” and expressly supported *state-by-state* efforts to

⁶ The New York Assurance of Discontinuance contains provisions apparently intended to allow MPHJ to continue disputing state jurisdiction in other cases. *See* Doc. 38-6 at 12, 20. MPHJ may, of course, settle claims with other states without conceding liability in this case. It is extraordinary, however, that MPHJ would file a Rule 11 motion describing Vermont’s lawsuit as a “sham” and “frivolous as a matter of law,” Doc. 38-1 at 10, 15, just a few days after settling similar claims with New York. The New York Attorney General described the MPHJ settlement as “groundbreaking” and said it set “guidelines for all patent trolls engaged in similar patent assertion behavior.” *A.G. Schneiderman Announces Groundbreaking Settlement With Abusive “Patent Troll,”* Jan. 14, 2014, available at: <http://ag.ny.gov/press-release/ag-schneiderman-announces-groundbreaking-settlement-abusive-%E2%80%9Cpatent-troll%E2%80%9D>

combat the problem.⁷ The former director of the United States Patent and Trademark Office, in testimony to another Senate committee, opined that “harassing conduct by patent owners in the form of unwarranted demand letters, especially against smaller and less sophisticated end users,” “may constitute a form of consumer fraud which may be very capably addressed by agencies such as the Federal Trade Commission and states’ attorneys general in the regular course of their jurisdiction.”⁸

MPHJ targeted scores of Vermont businesses and nonprofits with its threatening letters. The Attorney General conducted an investigation and filed this lawsuit to protect this State’s consumers and end MPHJ’s unlawful practices. Instead of litigating the case on the merits, MPHJ has (1) removed the case to federal court; (2) insisted that it cannot be sued in Vermont, even though it threatened to bring dozens of lawsuits here; (3) asked this Court to sanction and impose monetary fines on the individual assistant attorneys general who filed the suit; and (4) suggested that it may file a lawsuit against the lead attorney in this case.⁹ Enough. The Court should deny the Rule 11 motion and remand this case so that a state court may decide whether MPHJ’s conduct violated state law.

⁷ Video clip of Senator McCaskill’s statement available at:
<http://www.youtube.com/watch?v=hz5oL9yNf5M>

⁸ Written Testimony of O. Todd Dickinson, Senate Judiciary Committee, Dec. 17, 2013 at pp. 9-10, available at:
<http://www.judiciary.senate.gov/resources/documents/113thCongressDocuments/upload/121713QFRs-Dickinson.pdf>

⁹ See State’s Attach. 3, at 2 (Letter from Andrew Manitsky, Esq. to Bridget Asay, Assistant Attorney General).

II. An unfair and deceptive licensing campaign is an act “in commerce” under the Vermont Consumer Protection Act.

MPHJ sent nearly identical letters to seventy-five Vermont businesses and nonprofits and over 16,000 targets nationwide. The letters expressly solicited the payment of money in exchange for a license. MPHJ now claims that its nationwide licensing campaign was not an act “in commerce” for purposes of the CPA, which prohibits “unfair or deceptive acts or practices in commerce.” 9 V.S.A. § 2453(a). The question for the Court in this context is not whether the State should ultimately prevail on its claim that MPHJ violated the CPA. A Rule 11 motion is not the proper avenue for MPHJ to “test the legal sufficiency or efficacy of allegations in the pleadings; other motions are available for those purposes.” Fed. R. Civ. P. 11 advisory committee’s note, 1993 amendment. The question for the Court is whether the State’s position – namely, that the term “in commerce” includes the indiscriminate targeting of businesses with form letters in a nationwide licensing campaign – is frivolous. It is not.

MPHJ argues that the Vermont Supreme Court’s recent decision in *Foti Fuels*, 2013 VT 111, “has now confirmed, the [CPA] is limited exclusively to consumer transactions, and does not apply to patent licensing activity, at least of the type accused in this case.” Doc. 38-1 at 18. MPHJ’s description of *Foti* is inaccurate and its reliance on *Foti* is misplaced.

The Vermont Supreme Court held in *Foti* that the CPA did not apply to the sale of a fuel business. The Court reasoned that this private transaction between

two individuals was not “in the consumer marketplace.” *Foti*, 2013 VT 111 at ¶¶ 7-21. The Court emphasized that the seller’s offer was limited to the buyer and not made “to the public at large,” that it “did not involve products, goods or services purchased or sold for general consumption, . . . but rather the sale of an entire business from one party to another,” and that it involved a “high level of customization – which was achieved through particularly negotiated contract terms rather than boilerplate language.” *Id.* at ¶ 25.

MPHJ’s licensing activities are nothing like the private, customized sale at issue in *Foti*. MPHJ offered its license not to a single individual, but to seventy-five businesses and nonprofits in Vermont and over 16,000 small businesses nationwide. *See* State’s Attach. 1, ¶ 20. Businesses, like individual consumers, are protected under the CPA. *See* 9 V.S.A. § 2451a(a). MPHJ was offering its service, a license to its patents, for general consumption. Indeed, the business of seeking license fees appears to be MPHJ’s *only* business. And MPHJ was not entering into unique and customized transactions, but rather using form letters with boilerplate language. MPHJ’s far-reaching campaign to license its patents to thousands of small businesses is not comparable to the private sale of an entire business from one party to another.

The concerns that the Vermont Supreme Court identified in *Foti* as relevant to the scope of the CPA support the State’s position, not MPHJ’s. The *Foti* Court explained that “[i]ndividual buyers often hold less bargaining power and knowledge” than sellers, and “face barriers to pursuing their claims if they are

wronged in a transaction.” *Foti*, 2013 VT 111 at ¶ 23. Because “the costs of litigation often outweigh the rewards,” common-law remedies are “frequently inadequate” for individual consumers. *Id.* Here, the seventy-five Vermont businesses that received threatening letters from MPHJ’s forty different subsidiaries faced significant barriers to taking individual action. Even consulting a lawyer would be a substantial financial burden for these small businesses. Litigation costs would be overwhelming. In these situations, where “the consumer marketplace is tilted against buyers in favor of sellers,” the CPA provides its greatest value. *Id.*

MPHJ asserts that the letters were communications between two parties intended to determine whether a civil tort had been committed. The State disputes MPHJ’s description of a licensing campaign that reached over 16,000 small businesses and gave these businesses the phone number of a call center in which they could leave a message, *see* State’s Attach. 1, ¶ 30, as a private transaction between two parties. And the mere fact that the unfair and deceptive acts included threats of civil litigation does not preclude liability under the CPA. Similar licensing campaigns have been held to meet the “in commerce” requirement of state consumer protection laws, including in Massachusetts, a jurisdiction the Vermont Supreme Court looked to in *Foti*. In *Shirokov v. Dunlap, Grubb & Weaver, PLLC*, 2012 WL 1065578 (D. Mass. Mar. 27, 2012), the court held that a licensing campaign involving copyright demand letters was an act “in commerce.” *Id.* at *35-37. In *Shirokov*, the copyright holder had already filed a single civil action against hundreds of John Does alleging mass online infringement. *Id.* at *2. The court

reasoned that the claim of unfair and deceptive acts “is based on allegations that the defendants were engaged in a scheme to defraud him and others and used the [lawsuit] to add a veneer of legitimacy to their claims that [the copyright holder] was entitled to statutory damages.” *Id.* at *36. Even though the letters were sent in “the context of litigation,” *id.*, the court nonetheless found that such a campaign may satisfy the trade or commerce requirements of the consumer protection act. *Id.*

MPHJ, like the defendant in *Shirokov*, has created a business of sending threatening licensing letters related to intellectual property infringement as a means of extracting fees. This licensing scheme was MPHJ’s sole business and involved the sending of a voluminous number of threatening letters; it was not “individual correspondence” between it and an alleged infringer that “sought to propose resolution of such a civil tort.” Doc. 38-1 at 20. The nature of a defendant’s conduct matters in determining whether the “in commerce” requirement is satisfied. The Vermont Supreme Court, for example, has recognized the difference between “the sale of a home between non-merchants” and “a realtor engaged in the business of selling homes.” *Carter v. Gugliuzzi*, 716 A.2d 17, 21-2 (Vt. 1998). Using *Foti* for purposes of analogy, consider the difference between the business owner selling his entire business, which was a private transaction, and the owner selling fuel to customers, which was his regular business activity. MPHJ’s widespread licensing campaign – its sole business activity – is much closer to the solicitation and sale of fuel to the public. MPHJ is engaged in the ordinary trade of obtaining fees through

the use of unfair and deceptive licensing letters and that conduct is “in commerce” for purposes of the CPA.

MPHJ has not even shown that it is likely to prevail on this argument, much less established that its actions were indisputably outside of the realm of commerce. No controlling precedent precludes the position taken by the State. Accordingly, MPHJ’s motion must be denied. *See, e.g., Knight v. Sharif*, 875 F.2d 516, 518-19 (5th Cir. 1989) (upholding denial of sanctions where “no Mississippi case directly precluded” the state-law claim asserted by the party); *Knight v. H.E. Yerkes & Assocs., Inc.*, 675 F. Supp. 139, 146 n.5 (S.D.N.Y. 1987) (dismissing defendants’ third-party claim for failure to state claim, but finding sanctions inappropriate “[b]ecause the law of New York was not entirely clear as to whether” the claim was possible).

III. MPHJ does not have a protected right to engage in unfair and deceptive commercial speech or to disseminate demand letters in bad faith.

MPHJ also suggests that the State’s CPA claim is frivolous because MPHJ supposedly has a First Amendment right to send the letters described in the State’s Complaint. Again, MPHJ’s Rule 11 motion does not contest the State’s factual allegations. The State alleges that the letters were unfair and deceptive and, among other things, contained numerous false and misleading statements. Doc. 6 at ¶ 57. What MPHJ is arguing, then, is that the First Amendment protects its unfair and deceptive commercial speech. And, because MPHJ makes this argument in a sanctions motion, MPHJ has to show that its position is indisputable and any

contrary claim by the State is frivolous. MPHJ is wrong on the law and has not come close to showing that the State's position is frivolous.

A. The First Amendment does not protect unfair and deceptive commercial speech.

Whatever the scope of MPHJ's asserted "First Amendment right to enforce its patents against alleged infringers," Doc. 38-1 at 22, MPHJ does not have a First Amendment right to engage in unfair and deceptive acts in order to solicit licensing fees. "[S]tates have a generally unfettered right to prohibit inherently or actually misleading commercial speech." *Alexander v. Cahill*, 598 F.3d 79, 91 (2d Cir. 2010); *see also Florida Bar v. Went for It, Inc.*, 515 U.S. 618, 623-24 (1995) ("government may freely regulate commercial speech that . . . is misleading") (citing *Central Hudson Gas & Elec. Corp. v. Pub. Servs. Comm'n of New York*, 447 U.S. 557, 562-63 (1980)).

Here, the State has alleged seven unfair acts and nine deceptive statements in MPHJ's demand letters. A few examples:

- MPHJ told each target that "[w]e have identified your company as one that appears to be using the patented technology." Doc. 6-1 at 1. The State alleges that MPHJ did little or nothing to identify the targeted businesses. *See* Doc. 6 at ¶ 35.
- MPHJ said that it "had a positive response from the business community to our licensing program." Doc. 6-1 at 4. The State alleges that MPHJ

received a very limited response and that this response was not positive.

See Doc. 6 at ¶¶ 37-38; see also State's Attach. 1, ¶ 27.

- MPHJ's counsel states that "we must hear from you within two weeks of the date of this letter" or "litigation will ensue otherwise." Doc. 6-1 at 6. It is the State's contention that MPHJ did not intend to file lawsuits against thousands of targeted businesses and never filed any lawsuits in Vermont. See Doc. 6 at ¶¶ 41-44. In fact, out of 16,000 targeted businesses, MPHJ has sued only one, nearly a year later, in Texas. See Complaint, *MPHJ Technology Investments, LLC v. Research Now, Inc.*, No. 2:13-cv-00962 (E.D. Tex. filed Nov. 19, 2013).

These are just a few of the alleged actions that the State believes collectively constitute MPHJ's unfair and deceptive licensing campaign. The State may, consistent with the First Amendment, regulate and penalize commercial speech that is deceptive or misleading. See, e.g., *Virginia State Bd. of Pharmacy v. Virginia Citizens Consumer Council, Inc.*, 425 U.S. 748, 771-72 (1976) ("The First Amendment. . . does not prohibit the State from insuring that the stream of commercial information flow cleanly as well as freely.").

MPHJ asserts a First Amendment right to petition the government through litigation. See *California Motor Transport Co. v. Trucking Unlimited*, 404 U.S. 508, 510 (1972) ("The right of access to the courts is indeed but one aspect of the right of petition."). According to MPHJ, its right to petition the government extends to its licensing campaign because the letters included threats of litigation.

While some pre-litigation activity may be protected under what is known as the *Noerr-Pennington* doctrine, see *Primetime 24 Joint Venture v. Nat'l Broadcasting Co.*, 219 F.3d 92 (2d Cir. 2000), the *Noerr-Pennington* doctrine does not allow MPHJ to engage in unfair acts and make deceptive statements in an attempt to solicit licensing fees. Even assuming *Noerr-Pennington* has some relevance to this case,¹⁰ the State's claim against MPHJ falls within the sham litigation exception to that doctrine. The Second Circuit has concluded that, in the context of voluminous threats of litigations, analyzing the sham litigation exception to *Noerr-Pennington* requires the court to ask “[w]ere the legal filings made, not out of a genuine interest in redressing grievances, but as part of a pattern or practice of successive filings undertaken essentially for purposes of harassment?” *Primetime*, 219 F.3d at 101. The *Primetime* court refused to dismiss plaintiff's complaint on the pleadings, noting that the plaintiff alleged “‘automatic petitioning . . . without regard to and regardless of the merits of said petitions,’ that ‘if proven, would be sufficient to overcome the [defendants'] *Noerr-Pennington* defense.’” *Id.* (citation omitted). This decision supports the State's position that MPHJ's unfair and

¹⁰ On issues of federal law, the Vermont state court is bound by the United States Supreme Court, but not any particular federal circuit. See *State v. Kulzer*, 2009 VT 79, ¶ 13, 186 Vt. 264, 269, 979 A.2d 1031, 1035 (noting that there is no controlling federal precedent where “[t]he United States Supreme Court has not ruled on this issue.”). The United States Supreme Court has not decided whether the *Noerr-Pennington* doctrine applies to prelitigation communications, and at least one circuit has held that “prelitigation threats communicated solely between private parties” were not afforded immunity under the First Amendment. See *Cardtoons, L.C. v. Major League Baseball Players Ass'n*, 208 F.3d 885, 891 (10th Cir. 2000) (“A letter from one private party to another private party simply does not implicate the right to petition, regardless of what the letter threatens.”).

deceptive acts, including the indiscriminate threats of litigation, are outside of any immunity provided by *Noerr-Pennington*.

Other courts, in light of the policy concerns of the *Noerr-Pennington* doctrine – to protect a person’s right to petition the government – have not applied it in the context of an unfair and deceptive commercial campaign in which litigation or the threat of litigation plays a role. For example, the court in *Shirokov* addressed the application of the *Noerr-Pennington* doctrine to facts similar to the facts here. The court explained that the issue was “not the defendants’ right to use demand letters . . . but rather their use of false or misleading statements in the demand letters.” 2012 WL 1065578, at *21. The court denied *Noerr-Pennington* immunity, explaining that subjecting the defendants to liability would not discourage settlement, but would rather “encourage defendants to investigate carefully their accusations and to be precise in the language they use when attempting to settle with suspected infringers.” *Id.*

Other courts have similarly acknowledged that *Noerr-Pennington* immunity is not available when “[plaintiff] is not challenging [defendant’s] rights to send pre-litigation demand letters, file suit . . . or litigate its claims fully,” but rather seeking “to hold [defendant] to account if the manner in which it allegedly undertook these activities was unfair, deceptive, and in violation of the UTPA.” *Pepper v. Routh Crabtree, APC*, 219 P.3d 1017, 1022 (Alaska 2009); *see also DirectTV, Inc. v. Cephas*, 294 F. Supp. 2d 760, 767 (M.D.N.C. 2003) (not applying *Noerr-Pennington* in the context of a claim of unfair and deceptive acts related to pre-litigation demand

letters because “counterclaims brought under . . . the UDTPA . . . prevent only unfair and deceptive acts, parties bringing or threatening to bring meritorious, good faith claims cannot by definition be subject to liability under . . . the UDTPA.”).

B. The State may prove bad faith without addressing the scope or validity of MPHJ’s Patents.

MPHJ contends that the State’s claim is preempted unless the State proves bad faith, and to prove bad faith, the State must prove “that the asserted patent(s) was objectively invalid, objectively not infringed, or both.” Doc. 38-1 at 25. It also wrongly asserts that “the State, by its own admission, has purposefully avoided pleading bad faith in its Complaint.” Doc. 38-1 at 26. MPHJ’s understanding of preemption is flawed and its description of the Complaint is inaccurate.

The State specifically alleges bad faith, Doc. 6 at ¶ 54, and contends that MPHJ’s actions, described in detail in the Complaint, show its patent licensing campaign was conducted in bad faith. In pleading bad faith, the State identified specific activities and communications by MPHJ, satisfying the federal pleading requirement. *See Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009) (“To survive a motion to dismiss, a complaint must contain sufficient factual matter, accepted as true, to state a claim to relief that is plausible on its face.” (quotation omitted)).¹¹

¹¹ MPHJ cites extensively to cases that set forth the federal pleading requirements. As discussed above, it is not appropriate to utilize a Rule 11 motion as a de facto motion to dismiss. Moreover, although the State’s Complaint satisfies the federal pleading standard, that standard does not apply in Vermont state courts, where the Complaint was filed and the case should be litigated. *See Colby v. Umbrella, Inc.*, 2008 VT 20, ¶ 5, 184 Vt. 1, 6, 955 A.2d 1082, 1087, n.1 (reaffirming Vermont’s “minimal notice pleading standard” and rejecting *Ashcroft/Twombly* standard).

MPHJ disregards the State's specific and detailed Complaint and instead argues that the State's claim is preempted unless the State proves that it was objectively baseless for MPHJ to conclude that its patents were valid or being infringed. The "objective baselessness" standard is one way to prove bad faith, but it is not the only way. The Federal Circuit has acknowledged that other conduct, beyond asserting invalid patents or asserting valid patents against parties that clearly do not infringe, may nonetheless demonstrate bad faith. "Exactly what constitutes bad faith remains to be determined on a case by case basis." *Zenith Elecs. Corp. v. Exzec, Inc.*, 182 F.3d 1340, 1354 (Fed. Cir. 1999).

To the extent the State is required to prove bad faith in this case, the State may reasonably do so by proving that MPHJ's letters contained false statements and MPHJ engaged in unfair and deceptive conduct. The Federal Circuit case that MPHJ principally relies on, *Globetrotter Software, Inc. v. Elan Computer Group, Inc.*, 362 F.3d 1367 (Fed. Cir. 2004), does not stand for the position that *any* statement, regardless of how misleading, untrue or deceptive, is protected simply because it is in a letter that asserts a valid patent that is being infringed.¹² This

¹² In most cases that address state-law claims relating to patent assertion, the state-law claims turn on the invalidity of the patent, lack of infringement, and subjective bad faith. *See, e.g., Globetrotter*, 362 F.3d at 1375 (state-law claim alleged only "subjective bad faith," including an allegation that patent holder subjectively intended to interfere with a pending acquisition and that patent holder "believed that the patent was invalid," but never attempting to show that the claims asserted by the patent holder regarding the patents were objectively baseless); *Zenith*, 182 F.3d at 1343 (explaining that unfair competition claims arose because patent holder should have known that the "patents are limited . . . and that [defendant's system] . . . does not infringe the . . . patents"). The State's claim in this case, however, is not directed to the validity or scope of MPHJ's patents, but rather the

would mean that a holder of a valid patent is immune from liability for making any false statements in demand letters. For example, the patent holder could do the following without risk of recourse:

- specify that significantly more businesses had licensed the patent than had actually done so;
- lie about the fees that other businesses had paid for a license; or
- falsely state that it had successfully brought infringement actions against other businesses that refused to purchase a license.

This cannot be the case. The State does not dispute the right of a patent owner to enforce its patents and litigate infringement claims. But that does not mean that a patent owner is free to engage in unfair acts and make deceptive statements of the type described in the Complaint.

The State's position, that MPHJ's unfair practices and deceptive statements are sufficient to prove bad faith, is reasonable and, in fact, more persuasive than MPHJ's extreme view of the rights of a patent holder. In the context of patent enforcement, the Federal Circuit has noted that "[i]nfringement notices have been enjoined when the patentee acted in bad faith, for example by making threats without intending to file suit." *Mallinckrodt, Inc. v. Medipart, Inc.*, 976 F.2d 700, 710 (Fed. Cir. 1992) (citing *Betmar Hats, Inc. v. Young America Hats, Inc.*, 116 F.2d

unfair and deceptive statements in the demand letters. It would be illogical for the State to be required to prove the patents are invalid in order to prove MPHJ's unrelated claims in the letters were deceptive.

956 (2d Cir. 1941)). And it has more recently confirmed that the threatening of a lawsuit for infringement when one “did not intend to initiate suit . . . may or may not provide a basis from which a reasonable jury could infer bad faith.” *Golan v. Pingel Enter., Inc.*, 310 F.3d 1360, 1372 (Fed. Cir. 2002) (the issue was not decided because the plaintiff was not the party against whom the lawsuit was threatened). Additionally, bad faith may be found “when the patentee sent notices indiscriminately to all members of the trade.” *Mallinckrodt*, 976 F.2d at 710 (citing *Int’l Indus. & Devs., Inc. v. Farbach Chemical Co.*, 241 F.2d 246 (6th Cir. 1957)); see also *RDP Techs., Inc. v. N-Viro Int’l Corp.*, 2001 WL 1083762, at *6 (D. Del. Sept. 17, 2001) (finding a genuine issue of material fact as to whether defendant asserted his patent rights in bad faith based on a record that included a “long history of threatening suit to [plaintiff’s] customers and then failing to file suit”).

MPHJ also contends that the State’s allegations are insufficient because a federal district court in Illinois found that “general [mis]statements about the number of licenses it has granted, the cost of those licenses, the reputation of the inventors of its patents, and the number of times its patents had been adjudicated are all peripheral to the question of infringement,” and, therefore, did not make the licensing campaign a sham. *In re Innovatio IP Ventures, LLC Patent Litig.*, 921 F. Supp. 2d 903, 921-22 (N.D. Ill. 2013). A district court decision from a different district, in a different circuit, is not the type of binding precedent necessary to justify a Rule 11 motion. See *S.E.C. v. All Know Holdings, Ltd.*, 949 F. Supp. 2d 814, 825 (N.D. Ill. 2013) (“A single district court opinion cannot constitute

controlling precedent sufficient to support a sanctions motion.”); *In re Cross Media Mktg. Corp. Sec. Litig.*, 314 F. Supp. 2d 256, 269 (S.D.N.Y. 2004) (declining to impose Rule 11 sanctions when “there was no circuit court authority” barring plaintiffs’ legal theory); *Neighborhood Research Inst. v. Campus Partners for Cmty. Urban Dev.*, 212 F.R.D. 374, 379 (S.D. Ohio 2002) (“This Court will not impose sanctions on the Plaintiffs for asserting claims contrary to existing law when the only existing law comes from jurisdictions whose precedent is not binding on the Court.”).

Similarly, MPHJ contends that “[t]he Nebraska District Court has now found this identical conduct to be protected by the First Amendment,” Doc. 38-1 at 26, and that the State cannot pursue its claims “unless the State can show that the protections of the First Amendment somehow do not apply in Vermont in the same manner that they do in Nebraska,” *id.* at 9. The State disputes MPHJ’s characterization of *Activision TV, Inc. v. Pinnacle Bancorp, Inc.*, 2013 WL 5466956 (D. Neb. Sept. 30, 2013). In that case, the Nebraska Attorney General issued a cease-and-desist order to Farney Daniels, counsel to MPHJ and Activision, prohibiting the initiation of new patent infringement enforcement efforts. *Id.* at *1. The court expressed particular concern with the issuing of “cease and desist orders, prior to the conclusion of the investigation, prior to any negative findings, prior to any hearings, and prior to permitting submission of documents and evidence by the Farney Daniels law firm.” *Id.* at *6. It emphasized that a cease and desist order was akin to a prior restraint on speech, requiring “certain safeguards.” *Id.* (quotation

omitted). Vermont filed a lawsuit against MPHJ; it did not restrain MPHJ's activities in the state without process. Addressing preemption, the *Activision* court concluded that "as there is no claim of bad faith," Nebraska's cease-and-desist order was preempted. *Id.* at *7. In fact, in a later decision the court invites Nebraska to show bad faith, stating: "[i]f, however, at some point during the investigation evidence supports a claim of bad faith, the Attorney General is free to revisit this preliminary injunction with the court." *Activision TV, Inc. v. Pinnacle Bancorp, Inc.*, 2014 WL 197808, at *4 (D. Neb. Jan. 14, 2014). But again, Vermont *does* claim that MPHJ acted in bad faith. Contrary to MPHJ's assertions, the Nebraska court did not address the same issues presented by this case. Regardless, the Nebraska district court's decisions are not controlling precedent and cannot be the basis of a Rule 11 motion.

CONCLUSION

MPHJ's Rule 11 motion should be denied. Given the lack of a plausible basis for MPHJ's sanction demand, the Court should find that the motion was filed for an improper purpose and should grant the State attorneys' fees to cover the costs associated with responding to this motion. Fed. R. Civ. P. 11(c)(2) (court may award attorney's fees to prevailing party).

Dated: February 21, 2014

STATE OF VERMONT

WILLIAM H. SORRELL
ATTORNEY GENERAL

By: /s/ Bridget C. Asay
Bridget C. Asay
Ryan Kriger
Naomi Sheffield
Assistant Attorneys General
Vermont Attorney General's Office
109 State Street
Montpelier, VT 05609
Tel. (802) 828-5500
basay@atg.state.vt.us
rkriger@atg.state.vt.us
nsheffield@atg.state.us

CERTIFICATE OF SERVICE

I hereby certify that on this date, I electronically filed the foregoing document and attachments with the Clerk of the Court using the CM/ECF system. The CM/ECF system will provide service of such filing via Notice of Electronic Filing (NEF) to Andrew D. Manitsky, Esq., W. Bryan Farney, Esq., and Cassandra L. Klingman, Esq.

Dated: February 21, 2014

WILLIAM H. SORRELL
ATTORNEY GENERAL

By: /s/ Naomi Sheffield
Naomi Sheffield
Assistant Attorney General
Office of the Attorney General
109 State Street
Montpelier, VT 05609-1001
(802) 828-6906
nsheffield@atg.state.vt.us

Counsel for Plaintiff