

# Expert Report

## FILE SHARING

The copyright questions raised in the high-profile *Grokster* case made it all the way to the Supreme Court, which in June 2005 issued a decision with a much more narrow holding than many had anticipated or hoped. The following article analyzes that decision in the context of the larger concerns raised by the case and provides practical advice for those distributing technologies that may be used by third parties for copyright infringement.

### Lessons From *Grokster*: Avoiding Liability for Inducing Copyright Infringement

BY LISA M. TITTEMORE

**O**n June 27, 2005, Supreme Court Justice David Souter delivered the much-awaited decision of the Court in what has come to be known as "the *Grokster* case."<sup>1</sup> The Supreme Court, in a rare unanimous opinion, held in favor of the petitioners, MGM et al., reversing lower court decisions that had ruled, on summary judgment, in favor of the defendants *Grokster* and *StreamCast* with respect to secondary liability for copyright infringement.

The *Grokster* case had garnered significant attention and fostered intense discussion among those interested in copyright law. It had also been of great interest to those involved in developing, distributing, and using new technologies that facilitate digital data, music, and video distribution, particularly over the Internet. What brought these groups together is a case that many hoped would bring additional guidance with respect to the extent of potential secondary liability faced by distributors of these new technologies for copyright infringement by third party users of the technology.

While the Supreme Court's decision in *Grokster* does bring guidance for cases dealing with similar, relatively narrow, and rather remarkable facts relating to inducement, it provides only a glimmer as to how cases decided solely on the issue of distribution of such technology might be decided in the future. And, after all the

hoopla, the decision in *Grokster* was disappointing for many.

#### Harmonizing *Grokster* and *Sony*

In *Grokster*, the plaintiff movie studios and other owners of copyrighted works sought to prevent the distribution of software that allowed users to share files through non-centralized, peer-to-peer computer networks, which the copyright owners alleged were primarily used for illegal distribution of copyrighted works. The defendants, *Grokster* and *StreamCast*, hoped to avoid secondary liability for the infringing use of their software under the precedent of the Supreme Court's landmark decision in *Sony Corp. of America v. Universal City Studios, Inc.*, 464 U.S. 417 (1984).

In the groundbreaking 1984 *Sony* decision, the Supreme Court held that, where there was no evidence that *Sony* had any involvement with the infringing activity or that infringers were influenced or encouraged by *Sony* to infringe, the mere fact that *Sony* sold equipment (the "Betamax") that could be used for infringement did not give rise to a finding of secondary liability for the resulting infringement. The Court reasoned that liability would not attach under these circumstances as the equipment at issue was also "capable of substantial noninfringing uses."<sup>2</sup> The *Sony* rule was a tremendous victory for technology innovators, and was the result of the Court's stated desire to balance the public interest in preventing infringement and that of promoting technological advances.

Since then, there has been significant debate regarding the meaning of the phrase "capable of substantial noninfringing uses," and the meaning of the phrase was a hot button issue in the *Grokster* case. While the *Grokster* case was pending, many different suggestions for how the phrase should be interpreted were floated by a wide-variety of constituencies, including the movie industry, academics, technophiles, the U.S. government, and others. Indeed, much of the interest in the

<sup>1</sup> *Metro-Goldwyn-Mayer Studios Inc. v. Grokster, Ltd.*, 125 S. Ct. 2764 (2005) (10 ECLR 641, 6/29/05).

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<sup>2</sup> *Sony*, 464 U.S. at 442.

*Grokster* case derived from the question of how the Supreme Court would apply the *Sony* precedent to peer-to-peer, file-sharing technology at issue in the case. Some hoped and others feared that the *Sony* rule would be reconsidered.

Instead, the Court's majority opinion left *Sony* untouched. The Justices did so by distinguishing the *Grokster* and *Sony* cases on their facts. The Court determined that, unlike in *Sony*, the record in *Grokster* was "replete with evidence that from the moment *Grokster* and *StreamCast* began to distribute their free software, each one clearly voiced the objective that recipients use it to download copyrighted works, and each took active steps to encourage infringement."<sup>3</sup> The Court held:

In sum, this case is significantly different from *Sony* ... *Sony* dealt with a claim of liability based solely on distributing a product with alternative lawful and unlawful uses, with knowledge that some users would follow the unlawful course. ...

Here, evidence of the distributors' words and deeds going beyond distribution as such shows a purpose to cause and profit from third-party acts of copyright infringement.<sup>4</sup>

Further, given the different factual situations, the Court concluded that it was unnecessary for it to revisit *Sony* and that it would "leave further consideration of the *Sony* rule for a day when that may be required."<sup>5</sup>

Thus, in *Grokster*, the majority opinion declared that "one who distributes a device with the object of promoting its use to infringe copyright, as shown by clear expression or other affirmative steps taken to foster infringement, is liable for the resulting acts of infringement by third parties."<sup>6</sup>

### Singing the Right Tune Under *Grokster*

While the opinion is narrower than many of those interested had hoped, the *Grokster* decision does provide some guidance for companies distributing products that are at risk of being used for infringing purposes by third parties.

First and foremost, as noted above, the decision leaves the *Sony* safe harbor in place, at least for now. Thus, if those Justices in the *Grokster* majority hold sway going forward, the following should still be true (but see below regarding possibilities for the future of *Sony* if other voices on the Court are dominant).

**General knowledge of infringement by third parties is not enough to confer liability when the product is capable of substantial noninfringing use.** Distribution of a product by a company with generalized knowledge that the product is being used by third parties for infringing purposes, without knowledge of specific instances of infringement, even when third parties are in fact using the product to infringe, is not enough to confer liability as long as the product is capable of substantial noninfringing uses. *Sony* knew that users of its "Betamax" VCR were using it to duplicate television programs, including illegal copying of copyrighted works. Nevertheless, that knowledge alone was not enough to confer li-

ability for third party infringement, because the VCR was capable of substantial noninfringing uses.

The majority opinion in *Grokster* cited the doctrine on which the *Sony* rule is based with approval, noting that it "limits liability to instances of more acute fault than the mere understanding that some of one's products will be misused. It leaves breathing room for innovation and a vigorous commerce."<sup>7</sup> The Supreme Court in *Grokster* further explained its decision by making the following distinction: "[t]he inducement rule, instead, premises liability on purposeful, culpable expression and conduct."<sup>8</sup> Thus, at least the majority opinion in *Grokster* leaves *Sony* standing.

**The failure to take affirmative steps to prevent infringement, if the product is capable of substantial noninfringing uses, and absent other culpable conduct, is not enough to support liability for third party infringement.** The majority opinion in *Grokster*, in what is sure to become the frequently cited "Footnote 12," stated explicitly that "[o]f course, in the absence of other evidence of intent, a court would be unable to find contributory liability merely based on a failure to prevent infringement, if the device otherwise was capable of substantial noninfringing uses."<sup>9</sup>

While the Court cited *Grokster* and *StreamCast*'s failure to take such affirmative steps (e.g., failure to develop filtering tools or like mechanisms) as underscoring their intent to facilitate infringement, the Court made clear that such failure to take affirmative steps *alone* would not support secondary liability. Thus, even if a company knows generally that its product will be used for infringing activity and does not make any attempt to develop mechanisms to diminish the infringing activity, that alone is not enough to support liability under *Grokster* and *Sony*.

That being said, what a company clearly *cannot* do is make statements and/or take affirmative steps which might be seen as evidence of an intent to encourage copyright infringement by third parties which does in fact result in infringement. The Supreme Court cited numerous instances of conduct by *Grokster* and *StreamCast* which it held to be evidence of the defendants actively seeking to advance infringement by third parties, and which provide some specific examples of what not to do.

Accordingly, a company distributing a product that can be used by third parties to infringe copyright should keep the following guidelines in mind.

**Take care not to publicly target your product to users known to engage in copyright infringement.** The Court noted that *StreamCast* and *Grokster* distributed free software hoping to attract former users of the "notorious" *Napster* file-sharing service to their own products, and specifically sought to capture the market of former *Napster* users. The Court found that the defendants' conduct in targeting these users was evidence that *Grokster* and *StreamCast* were aiming to satisfy a "known source of demand for copyright infringement."<sup>10</sup> The Court cited company documents which indicated that *StreamCast* planned to be "the next *Napster*" and that the company was positioning itself "to

<sup>3</sup> *Grokster*, 125 S. Ct. at 2766-67.

<sup>4</sup> *Id.* at 2782.

<sup>5</sup> *Id.* at 2779.

<sup>6</sup> *Id.* at 2770.

<sup>7</sup> *Id.* at 2778.

<sup>8</sup> *Id.* at 2780.

<sup>9</sup> *Id.* at 2781 n.12.

<sup>10</sup> *Id.* at 2781.

capture the flood of their 32 million users" if Napster was shut down by the courts.<sup>11</sup>

**Avoid positioning the product as a way to "get around" or flaunt copyright law.** The Court referenced StreamCast draft promotional materials reading "Napster Inc. has announced that it will soon begin charging you a fee. That's if the courts don't order it shut down first. What will you do to get around it?"<sup>12</sup> Even though it was not clear whether anyone outside StreamCast ever saw the draft promotional materials, what was clear was that the Court did not appreciate this kind of challenge to its authority. The Court also quoted the StreamCast CTO stating that "the goal is to get in trouble with the law and get sued. It's the best way to get in the new[s]." as evidence of StreamCast's intent to induce infringement.<sup>13</sup>

**Avoid promoting product features that facilitate infringement.** The Court cited internal StreamCast communications indicating that the company sought to have a larger number of copyrighted songs available on its networks than other file-sharing networks. The Court noted that Grokster also sent users a newsletter promoting its ability to provide certain popular copyrighted material.<sup>14</sup> Nonetheless, the line of what is permissible with respect to promoting product uses is somewhat fine. Indeed, the Court noted that, while what Grokster and StreamCast did to encourage infringing use was over the line, Sony had apparently skirted it: "Although Sony's advertisements urged consumers to buy the VCR to 'record favorite shows' or 'build a library' of recorded programs, neither of these uses was necessarily infringing."<sup>15</sup>

**Avoid communicating the wrong message by offering technical support to users who are in the process of infringing.** The Court held that both StreamCast and Grokster had "communicated a clear message by responding affirmatively to requests for help in locating and playing copyrighted materials."<sup>16</sup> However, the Court also noted that "ordinary acts incident to product distribution, such as offering technical support or product updates [do not] support liability in themselves."<sup>17</sup> Thus, presumably as long as the technical support is not provided to help customers actively infringe copyright, providing such support would be permissible, even if the user ultimately does engage in copyright infringement.

**Even in purely internal documents, be careful what you say.** As noted above, much of the evidence cited by the Court came from internal company documents. Evidence of intent or "an object" to foster infringement was as much at issue in the Court's decision as affirmative conduct taken to encourage infringement.

**The risks are greater when the magnitude of the infringement is greater.** A study commissioned by MGM allegedly showed that nearly 90 percent of the files available for download using the software were copyrighted works. While noting that the study was contested by the software companies, the Court nonetheless concluded that "MGM's evidence gives reason to think that the

vast majority of users' downloads are acts of infringement, and because well over 100 million copies of the software in question are known to have been downloaded, and billions of files are shared across the Fast-Track and Gnutella networks each month, the probable scope of copyright infringement is staggering."<sup>18</sup> Moreover, the Court noted that "Grokster and StreamCast concede the infringement in most downloads."<sup>19</sup>

**The risks are even greater when adopting a business model that profits from an increased volume of infringement.** The Court concluded that the business models employed by Grokster and StreamCast had the principal object of profiting from the downloading of copyrighted works. Both companies generated income by selling advertising that would be streamed to users of their software. Thus, the larger the number of users of their software, the more money they made. The Court saw this as an incentive for Grokster and StreamCast to encourage infringing use. It seems unlikely, however, that such a business model alone would result in liability.

**Affirmative steps taken to try to prevent infringing use could be used to counter a claim of secondary liability.** The Court found that neither Grokster nor StreamCast had attempted to implement any tools or mechanisms to diminish infringing activity by users of their software. The Court was clear to state that, in the absence of other evidence of intent to bring about and profit from infringement by third parties, the failure to take affirmative steps to prevent infringement would not, by itself, be enough to support contributory infringement liability if the device was capable of substantial noninfringing uses. That being said, a company's attempt to implement such tools or mechanisms could help to show lack of intent to encourage infringing use.<sup>20</sup>

## Understanding the Future for Sony

While notable because it was a unanimous decision, the separate concurring opinions in *Grokster* written by Justice Ruth Bader Ginsburg (joined by Chief Justice William Rehnquist (now deceased) and Justice Anthony Kennedy) and Justice Breyer (joined by Justices John Paul Stevens and Sandra Day O'Connor (soon retiring)) provide key insights into how the Justices might view the Sony rule in a case with less extreme facts than *Grokster*.

These concurring opinions make clear that had the Justices not been able to distinguish the *Grokster* case from Sony on its facts, it is unlikely that the decision in *Grokster* would have been unanimous, and the Sony rule might well have been modified.

Unfortunately, the majority and concurring decisions do not provide much clear guidance for how the Court as a whole would come out on Sony if that had been the case. But some insights can be gleaned.

**At least two Justices appear inclined to interpret Sony more narrowly in the future.** Justice Ginsburg's concurring opinion suggests that, given a case with the right facts, she and Justice Kennedy might reconsider Sony to require that a product be more than "capable of substantial noninfringing use." Instead, they would require evidence sufficient "to demonstrate, beyond genuine

<sup>11</sup> *Id.* at 2773.

<sup>12</sup> *Id.*

<sup>13</sup> *Id.*

<sup>14</sup> *Id.* at 2774.

<sup>15</sup> *Id.* at 2777 (quoting Sony, 464 U.S. at 459 (Blackmun, J., dissenting)) (emphasis added).

<sup>16</sup> *Id.* at 2781.

<sup>17</sup> *Id.* at 2780.

<sup>18</sup> *Id.* at 2772.

<sup>19</sup> *Id.*

<sup>20</sup> See *id.* at 2781.

debate, a reasonable prospect that substantial or commercially significant noninfringing uses were likely to develop over time."<sup>21</sup> Thus, the term "capable" as used in *Sony* may be read much more strictly (or replaced entirely) in the future. This would put defendants to a much more difficult burden of proof, as they would not only need to show that the technology at issue *could* be used for substantial noninfringing purposes but also that it was *likely* to be used for substantial noninfringing purposes (and perhaps to require that such use be in a commercial context).

**At least two Justices may want to make Sony even stronger in the future.** Justice Stephen Breyer, joined by Justices Stevens and O'Connor, claims "a strong demonstrated need for modifying *Sony* (or for interpreting *Sony*'s standard more strictly) has not yet been shown."<sup>22</sup> Justice Breyer wrote that "*Sony*'s rule is strongly technology protecting."<sup>23</sup> He added that "the law disfavors equating the two different kinds of gain [of protecting copyright] and loss [of technological innovation]; rather, it leans in favor of protecting technology."<sup>24</sup> These Justices also favor the *Sony* rule because it "is mindful of the limitations facing judges where matters of technology are concerned."<sup>25</sup> While these Justices were strongly pro-*Sony*, they concurred in the *Grokster*

<sup>21</sup> *Id.* at 2786 (Ginsburg, J., concurring).

<sup>22</sup> *Id.* at 2796 (Breyer, J., concurring).

<sup>23</sup> *Id.* at 2791 (Breyer, J., concurring) (emphasis in original).

<sup>24</sup> *Id.* at 2793 (Breyer, J., concurring).

<sup>25</sup> *Id.* at 2792 (Breyer, J., concurring) (emphasis in original).

judgment on the narrow ground of *Grokster*'s and *StreamCast*'s conduct and statements which were seen as evidence of inducing their customers to use the product illegally.

**Three Justices did not indicate clearly their position on Sony.** Other than agreeing that it should be left to be considered another day, Justices Souter, Antonin Scalia, and Clarence Thomas did not provide much indication regarding how they might rule on *Sony* in the future.

Given this outcome, it is certainly possible that the next time around the *Sony* rule might be modified or interpreted more strictly. Until then, companies distributing new technologies that are used by third parties for copyright infringement must take care not to run afoul of the guidelines set out in *Sony* and *Grokster*, and hope that this is enough to keep them in the "safe-harbor."

Indeed, given the major changes on the Court since the decision was issued, namely, Justice O'Connor's retirement and the recent passing away of the Chief Justice, analysis of how the Supreme Court might rule on a case with facts closer to *Sony* than *Grokster* can only be even more speculative. Nevertheless, while disappointing for its lack of answers on the broader questions, the *Grokster* case remains important for the guidelines it does provide for avoiding liability under similar facts to those distributing technology that may be used for copyright infringement by others. Thus, *Grokster* sets a minimum floor, posts red flags, and leaves open many issues for further discussion.