

**BEFORE THE OFFICE OF MANAGEMENT AND BUDGET
EXECUTIVE OFFICE OF THE PRESIDENT**

**RESPONSE OF NETCOALITION AND THE COMPUTER & COMMUNICATIONS
INDUSTRY ASSOCIATION TO THE INTELLECTUAL PROPERTY ENFORCEMENT
COORDINATOR'S REQUEST FOR COMMENTS ON THE JOINT STRATEGIC PLAN**

NetCoalition and the Computer & Communications Industry Association (CCIA) welcome this opportunity to respond to the request of the Intellectual Property Enforcement Coordinator (IPEC) for comments on the development of the Joint Strategic Plan for Intellectual Property Enforcement.

At the outset, we wish to indicate points of agreement and disagreement with Administration IP policy since we responded in March 2010 to the request for comments concerning the first Joint Strategic Plan. We then address the specific sections of the request for comments: strategy recommendations, threat assessment, and optional questions.

I. POINTS OF AGREEMENT

The overarching theme of our 2010 comments was the importance of balance to the U.S. IP system. We encouraged the Administration to strive to preserve that balance in domestic law while promoting the adoption of balanced frameworks overseas. We are gratified that the Administration has supported a more balanced approach to protection in the context of several significant domestic and international IP policy initiatives.

- **USTR Position on Copyright Exceptions and Limitations in TPP**

On July 3, 2012, the Office of the U.S. Trade Representative (USTR) issued a statement concerning copyright exceptions and limitations in the context of the Trans-Pacific Partnership (TPP) agreement. The USTR announced that

the balance of rights and exceptions and limitations achieved in U.S. law provides diverse benefits for large and small businesses, consumers, authors, artists, and workers in the information, entertainment, and technology sectors.

A robust copyright framework ensures that authors and creators are respected, investments (both intellectual and financial) are promoted, that limitations and exceptions provide an appropriate balance, and that enforcement measures are effective.

An important part of the copyright ecosystem is the limitations or exceptions placed on the exercise of exclusive rights in certain circumstances. In the United States, for example, consumers and businesses rely on a range of exceptions and limitations, such as fair use, in their businesses and daily lives. Further, under the U.S. Digital Millennium Copyright Act (DMCA), the United States provides safe harbors limiting copyright liability, which

help to ensure that legitimate providers of cloud computing, user-generated content sites, and a host of other Internet-related services who act responsibly can thrive online.¹

After this introduction, the USTR declared that

[f]or the first time in any U.S. trade agreement, the United States is proposing a new provision, consistent with the internationally-recognized “3-step test,” that will obligate Parties to seek to achieve an appropriate balance in their copyright systems in providing copyright exceptions and limitations for purposes such as criticism, comment, news reporting, teaching, scholarship, and research. These principles are critical aspects of the U.S. copyright system, and appear in both our law and jurisprudence. The balance sought by the U.S. TPP proposal recognizes and promotes respect for the important interests of individuals, businesses, and institutions who rely on appropriate exceptions and limitations in the TPP region.²

NetCoalition and CCIA strongly support the inclusion in the TPP agreement of a provision “that will obligate Parties to seek to achieve an appropriate balance in their copyright systems in providing copyright exceptions and limitations for purposes such as criticism, comment, news reporting, teaching, scholarship, and research.” Additionally, NetCoalition and CCIA agree with the principles concerning balanced copyright that underlie this announcement by USTR. NetCoalition and CCIA also appreciate USTR’s acknowledgment of the importance of the DMCA safe harbors to Internet services such as cloud computing.

Finally, our organizations recognize the efforts USTR has made to work more closely with a variety of stakeholders, and hope that this coordination will continue and lead to even greater transparency.

- **Administration Position on SOPA and PIPA**

On January 14, 2012, the White House issued a statement expressing concerns with certain provisions in the PROTECT IP Act (PIPA) and the Stop Online Piracy Act (SOPA). While stating “that online piracy by foreign websites is a serious problem that requires a serious legislative response,” the White House stressed that “we will not support legislation that reduces freedom of expression, increases cybersecurity risk, or undermines the dynamic, innovative global Internet.”³

The statement added that “any effort to combat online piracy must guard against the risk of online censorship of lawful activity and must not inhibit innovation by our dynamic businesses large and small,” observing that “legislation must be narrowly targeted only at sites beyond the reach of current U.S. law, cover activity clearly prohibited under existing U.S. laws,

¹ Office of the U.S. Trade Representative, USTR Introduces New Copyright Exceptions and Limitations at San Diego TPP Talks, July 3, 2012, <http://www.ustr.gov/about-us/press-office/blog/2012/july/ustr-introduces-new-copyright-exceptions-limitations-provision>.

² *Id.*

³ Victoria Espinel, Aneesh Chopra, & Howard Schmidt, *Official White House Response to Stop the E-PARASITE Act: Combating Online Piracy while Protecting an Open and Innovative Internet*, We the People, Jan. 14, 2012, <https://www.whitehouse.gov/petition-tool/response/combating-online-piracy-while-protecting-open-and-innovative-internet>.

and be effectively tailored, with strong due process and focused on criminal activity.” The statement also endorsed transparency, and cautioned against “overly broad private rights of action that could encourage unjustified litigation that could discourage startup businesses and innovative firms from growing.” We also note that the Administration statement addressed the domain name issue by observing that “we must avoid creating new cybersecurity risks or disrupting the underlying architecture of the Internet.” We share the White House’s commitment to “vigorously defending an open Internet based on the values of free expression, privacy, security and innovation.”

- **Leadership Concerning a WIPO Instrument on Limitations and Exceptions for Visually Impaired Persons**

The United States has demonstrated leadership at the World Intellectual Property Organization in the development of an international instrument on the limitations and exceptions for visually impaired persons. We hope these efforts continue and lead to the adoption of an effective instrument in the near future.

- **Efforts Relating to Infringement Affecting Health and Human Safety**

As we recommended in 2010, a major focus of the Administration’s IP enforcement efforts have been infringement that affects health and human safety, such as counterfeit pharmaceuticals. In the past two years, U.S. Customs and Border Protection and U.S. Immigration and Customs Enforcement increased seizures of counterfeit pharmaceuticals by almost 600 percent and fake consumer safety and critical technology merchandise by 183 percent.⁴ Additionally, the National Defense Authorization Act of 2012 and the Food and Drug Administration and Safety Act incorporate several of the legislative recommendations concerning health and human safety articulated in the Administration’s White Paper on Intellectual Property Enforcement Legislative Recommendations.⁵

II. POINTS OF DISAGREEMENT

- **Leaked TPP Chapter**

As indicated above, NetCoalition and CCIA support the USTR’s position concerning a new provision in the TPP agreement addressing copyright exceptions and limitations. This new provision, however, does not address the full range of our concerns relating to the leaked TPP chapter proposed by the United States. For example, this language does not specifically address the issue of buffer and other temporary copies. It also does not reach the issue of trademark fair uses such as nominative uses. Additionally, it leaves in place troubling language concerning international exhaustion and parallel imports – in essence prejudging an issue now before the Supreme Court in *Kirtsaeng v. John Wiley & Sons*.⁶

- **Domain Name Seizures**

⁴ 2012 U.S. Intellectual Property Enforcement Coordinator Joint Strategic Plan 1 (2012).

⁵ *Id.* at 2.

⁶ *John Wiley & Sons, Inc. v. Kirtsaeng*, 654 F. 3d 210 (2d Cir. 2011), *cert. granted*, No. 11-697, April 16, 2012.

Immigration and Customs Enforcement (ICE) seized hundreds of domain names allegedly engaged in infringing activity. The legal authority for the seizures was 18 U.S.C. § 2323. Serious questions have been raised with respect to some of these seizures, including whether the sites in fact engaged in infringing activity, and how federal prosecutors have interfered with these sites' ability to resume their lawful activities.⁷ Similarly, federal prosecutors have made it difficult for innocent users to access their information stored on the Megaupload system, another website seized by federal authorities. We would like to work with the federal government to address how to protect the property rights of innocent users of systems that have been seized by law enforcement.

III. STRATEGY RECOMMENDATIONS

- **U.S. IP foreign policy should more completely reflect the balance in U.S. law.**

Although this Administration has taken positive steps in the direction of a balanced IP foreign policy, there still exist asymmetries that result in the interests of entertainment companies and other copyright owners taking precedence over policies needed to promote Internet exports. While this bias may have made sense in the pre-Internet era, it no longer reflects the national economic interest. The fastest growing sector of the economy – the Internet economy – relies as much on copyright law's exceptions as on its protections. The Internet economy benefits U.S. artists by enabling them to reach new markets at lower cost, and benefits U.S. consumers by providing them with more access to information and competitive goods and services. By forcing other countries to intensify their enforcement of IP rights without also requiring them to adopt the full range of balancing exceptions, the U.S. government has actually subjected U.S. Internet companies to greater risk overseas. This must stop.

- **The Administration should support amendments to the Copyright Act that “maintain robust information flows that facilitate innovation and the growth of the Internet economy” and “safeguard end-user interests in freedom of expression, due process, and privacy.”⁸**

A. Reassess Statutory Damages – Section 504(c)(2)

The existing framework of copyright statutory damages can have a chilling effect on innovation. Indeed, statutory damages are so arbitrary and unfair that federal judges have called for the reform of copyright statutory damages.⁹ Accordingly, the Administration should

⁷ See, e.g., *Feds Falsely Censor Popular Blog for Over a Year, Deny Due Process, Hide All Details...*, Techdirt, Dec. 8, 2011, at <http://www.techdirt.com/articles/20111208/08225217010/breaking-news-feds-falsely-censor-popular-blog-over-year-deny-all-due-process-hide-all-details.shtml> (discussing hip hop blog Dajaz1.com).

⁸ Department of Commerce, Notice of Inquiry on Copyright Policy, Creativity, and Innovation in the Internet Economy, 75 Fed. Reg. 61418 (Oct. 5, 2010). The following legislative proposals were contained in CCIA and NetCoalition's December 10, 2010 response to this notice of inquiry.

⁹ E.g., *Capitol Records v. Thomas*, 2008 U.S. Dist. LEXIS 84155 (D. Minn. Sept. 24, 2008). In the pending litigation concerning Google Books Search, the Authors Guild is seeking in excess of \$3 billion in statutory damages, although it has made no showing of any harm – not even the lost sale of a single book.

recommend that Congress re-evaluate the statutory damages provision of Title 17 to promote predictability and fairness to manufacturers, service providers, and consumers.

i. Ensure predictability of statutory damages in secondary liability cases

Currently, an Internet service provider or a consumer electronics manufacturer could be found liable for statutory damages for each work a third party infringes while using the service or product. This potential exposure to astronomical damages chills innovation and discourages capital investment in new products and services. Accordingly, Section 504(c)(2) should include the following limitation:

“The court shall remit statutory damages for secondary infringement, except in a case in which the copyright owner sustains the burden of proving, and the court finds, that the act or acts constituting such secondary infringement were done under circumstances in which no reasonable person could have believed such conduct to be lawful.”

ii. Reduce the level of minimum damages

The existing statute contains a range of damages, but the minimum is too high. For example, a consumer is liable for a minimum of \$750 for infringement of one album that he could purchase on iTunes for \$15.00. Even if the court finds the infringement is innocent, the minimum is still \$200 per work infringed. The general statutory minimum should be reduced to \$250, and the minimum for innocent infringement should be reduced to \$100. This is still more than 100 times greater than the going rate for many common works, and in the unlikely event that it is insufficient, plaintiffs may always opt for actual damages.

iii. Guide courts in awarding damages

As noted above, the statute sets forth a broad range for damages, but provides no guidance for courts on how they should exercise their discretion. The court is simply directed to make the award “as the court considers just.” When the case does not involve willful infringement, there is no economic basis for attempting ‘deterrence.’ Thus, the court in calculating statutory damages should attempt to compensate the plaintiff, not punish the defendant. The following sentence should be added to the statute to provide this guidance:

“In determining the award of statutory damages, the court shall attempt to compensate the copyright owner for the actual damages he or she suffered by virtue of the infringement.”

iv. Harmonize copyright willfulness with patent willfulness

If an infringement is committed willfully, the statutory maximum increases by a factor of five, from \$30,000 to \$150,000. However, the Copyright Act does not define willfulness, and there is a lack of uniformity in the courts concerning this important concept. The U.S. Court of Appeals for the Federal Circuit in *In re Seagate Technologies LLC*¹⁰ defined willful infringement

¹⁰ *In re Seagate Technologies LLC*, 497 F.3d 1360 (Fed. Cir. 2007).

in the patent context. This provides a helpful guide for a definition of willful copyright infringement:

“To establish willful infringement, a plaintiff must show by clear and convincing evidence that the infringer acted despite an objectively high likelihood that its actions constituted infringement of an obviously valid copyright.”

v. Require the timely election of statutory damages

Current practice permits plaintiffs to delay the election between actual and statutory damages until after the jury (or court) awards both actual and statutory damages. This allows the plaintiff to “game the system” and extract higher settlements by threatening draconian damages throughout the litigation. So as not to unfairly prejudice defendants, plaintiffs should make this election in a timely manner, before the trial or the filing of a motion for summary judgment.

vi. Reduce statutory damages for orphan works

Many copyrighted works have little or no economic value soon after their creation or publication. Nonetheless, these works may possess significant cultural, educational, or historical value. Authors of such works typically are willing to permit others to reproduce, distribute, perform, or display their works at no charge because the authors benefit in tangible and intangible ways from these uses. While the authors obviously would like to receive compensation for the use of the works, most authors would prefer uncompensated use over no use whatsoever; authors rarely want their creations to be ignored and forgotten.¹¹

Archives, libraries, and museums across the country are interested in digitizing parts of their collections to make them publicly accessible over the Internet. If it is clear that the copyright term for a particular work has not expired, and the owner of the copyright can be identified and located, then the archive as a general matter should not make the full text of the work publicly accessible over the Internet without seeking the owner’s permission. But for many works, it is not clear whether the term has expired, or the owner cannot readily be identified or located.

Under current law, the archives might be liable for copyright infringement if it were to upload the entire orphan work onto the Internet and the owner subsequently objected. Although the owner probably suffered no actual damage because the work had no economic value, he or she might still be able to recover statutory damages. And although most authors would be pleased that their long neglected works were receiving any attention, an archives’ potential exposure could be significant if it were to upload thousands of orphan works.

In the face of this potential exposure, the archives may well decide not to make the orphan works available on the Internet.¹² This represents a significant loss to the public, which

¹¹ Tim O’Reilly, *Search and Rescue*, N.Y. Times, Sept. 28, 2005, at A27, <http://www.nytimes.com/2005/09/28/opinion/28oreilly.html>.

¹² United States Copyright Office, *Report on Orphan Works* 25 (2006), <http://www.copyright.gov/orphan/orphan-report-full.pdf>.

will be denied access to socially valuable information. Keeping this wealth of material off the Internet also harms members of CCIA and NetCoalition, which benefit as more users seek more information on the Internet. Additionally, it represents a loss to most of the authors of these works, whose creations will continue to remain hidden from public sight. At the same time, keeping the works warehoused in the archives does not preserve any income stream for the owners because orphan works rarely, if ever, generate any revenue.

Accordingly, we support the amendment of the Copyright Act to reduce the barriers it places on the dissemination of orphan works. Specifically, courts should have the discretion to reduce or remit statutory damages if a user made a reasonably diligent search for a copyright owner prior to the user, but could not identify or locate her.

B. Preserve the First Sale Doctrine – Section 109(a)

For over 100 years, the first sale doctrine has been one of the basic principles of copyright law. It provides that the owner of a copy of a work may sell, rent, or otherwise dispose of that copy without infringing the copyright holder's distribution right. The first sale doctrine is under attack from several directions. First, the Second and Ninth Circuit have ruled that the first sale doctrine applies only to copies manufactured in the United States. If the Supreme Court affirms the Second Circuit in *Kirtsaeng v. John Wiley & Sons*, the scope of the first sale doctrine will be narrowed dramatically. Copyright owners will have the incentive to move their manufacturing operations overseas so as to avoid the first sale doctrine and exercise control over the secondary markets for their products – to the detriment of consumers who may be forced to pay higher purchase prices and then be unable to alienate the goods they purchase. The Administration should carefully consider amendments to the first sale doctrine to ensure its continued vitality.

C. Misuse

Some copyright owners have misused the protections afforded by the Copyright Act in an effort to prevent competition. One of the clearest examples of this misuse is *Costco v. Omega*. Omega attempted to leverage the copyright in a small logo engraved on the back of its watches into control over the importation of the uncopyrighted watch. When the case was remanded to the district court after reaching the Supreme Court, the district court found that Omega had misused its copyright.¹³ The *Omega* case follows from an equally questionable assertion of copyright in *Quality King v. L'anza*, where the copyrighted work was the label on a shampoo bottle.

Rightsholders have also taken advantage of the temporary copies made by digital technologies as a pretext for copyright infringement actions. This has occurred in cases relating to: maintenance services for computer software and hardware products;¹⁴ interoperable software;¹⁵ network digital video recorders;¹⁶ and content streaming services.

¹³ *Costco Wholesale Corp. v. Omega, S.A.*, 2:04-CV-05443-TJH-RC (E.D. Cal. Nov. 9, 2011).

¹⁴ *See, e.g., MAI Systems Corp. v. Peak Computer, Inc.*, 991 F.2d 511 (9th Cir. 1993).

¹⁵ *See, e.g., Vault Corp. v. Quaid Software*, 847 F.2d 255 (5th Cir. 1988).

Moreover, every time an American consumer opens a book, plays a DVD, or watches a broadcast of a sporting event, she is confronted by strong language warning of what she is not allowed to do with that product under copyright law. By design or effect, many of these warnings are misleading and harmful to millions of American consumers, customers, and businesses. These ubiquitous statements often include gross misrepresentations of copyright law and characterize as unlawful acts that are explicitly permitted by law. Many such warnings forbid “unauthorized” copying and sharing of any part of their works, even when such copying or sharing is “fair use” and is permitted by law and in fact by the Constitution itself.

These warnings intimidate average people and hinder free expression. They depict as illegal many legitimate and beneficial uses made possible by the high-tech industry, and cast a pall over the high-tech marketplace. Moreover, these misleading warnings represent an assault on the open communications and free expression vital to our society.¹⁷

The DMCA likewise has been abused by certain rightsholders. For example, manufacturers of garage door openers and computer printers have attempted to use the prohibition on circumvention in section 1201 to prevent competition in aftermarkets.¹⁸ Likewise, companies have misused the section 512 notice and takedown to force the removal of material that did not infringe copyright.¹⁹ Section 512 has also been abused to chill political speech by demanding the takedown of newsclips and ads from campaign websites.²⁰

Section 512 has two built-in, albeit relatively ineffective, mechanisms for preventing abuse. First, a user can employ the counter-notification process of section 512(g) to request that access to taken-down material be restored if the rightsholder does not initiate a copyright infringement actions against the user. Second, under section 512(f), a rightsholder who

¹⁶ *Cartoon Network LP LLP v. CSC Holdings, Inc.*, 536 F.3d 121 (2d Cir. 2008), *cert. denied*, 129 S. Ct. 2890 (2009).

¹⁷ In 2007, CCIA filed a complaint with the Federal Trade Commission, taking the position that such practices constitutes unfair and deceptive trade practices as defined by the Federal Trade Commission Act.

¹⁸ *See, e.g.*, *Chamberlain Group, Inc. v. Skylink Technologies, Inc.*, 381 F.3d 1178 (Fed. Cir. 2004); *Lexmark Int'l v. Static Control Components*, 387 F.3d 522 (6th Cir. 2004). The exemption granted by the Librarian of Congress for the “jailbreaking” of the iPhone prevents Apple from employing section 1201 to prevent the use of apps not approved by Apple.

¹⁹ *See, e.g.*, *Lenz v. Universal Music Corp.*, 572 F.Supp.2d 1150, 1154 (N.D. Cal. 2008) (record company sent DMCA notice without considering whether video was fair use); *Online Policy Group v. Diebold, Inc.*, 337 F.Supp.2d 1195 (N.D. Cal. 2004) (maker of voting machines alleged DMCA violation to silence critics). In *Design Furnishings, Inc. v. Zen Path LLC*, 2010 WL 4321568 (E.D. Cal. Oct. 21, 2010), a distributor of wicker furniture sent DMCA takedown notices to eBay with respect to the listings of a competing distributor of wicker furniture, falsely alleging that it had a copyright in the design of furniture. In granting the competing distributor a temporary restraining order in its declaratory judgment action, the district court said, “To withhold a TRO would allow anyone to effectively shut down a competitor’s business on eBay simply by filing the notice that the seller’s product allegedly infringes on the complaining party’s copyright.”

²⁰ Center for Democracy and Technology, *Campaign Takedown Troubles: How Meritless Copyright Claims Threaten Online Political Speech*, <http://cdt.org/policy/cdt-releases-report-meritless-dmca-takedowns-political-ads> (Sept. 2010). In July, BMG demanded that YouTube take down a Mitt Romney campaign ad that contained a clip of President Obama singing a few lines from Al Green’s “Let’s Stay Together.” *See* Timothy B. Lee, *Music publisher uses DMCA to take down Romney ad of Obama crooning*, *Ars Technica*, July 16, 2012, <http://arstechnica.com/tech-policy/2012/07/major-label-uses-dmca-to-take-down-romney-ad-of-obama-crooning/>.

“knowingly materially misrepresents ... that material or activity is infringing” is liable for damages.

In contrast, there is no statutory mechanism for addressing misuses of section 1201 or the Copyright Act itself. Some courts have recognized copyright misuse as a defense to infringement claims. Thus, the Fourth Circuit in *Lasercomb America v. Reynolds*²¹ found that Lasercomb, by the terms of its copyright license agreement, was attempting to monopolize something which clearly was not part of the bundle of rights granted by copyright: the right to develop competing software utilizing the same ideas. Similarly, in *DSC Communications Corp. v. DGI Technologies, Inc.*, 81 F.3d 597, 601 (5th Cir. 1996), the Fifth Circuit found copyright misuse when DSC used its copyright to indirectly gain control over a competitor’s use of its microprocessor cards. The court observed that “DSC seems to be attempting to use its copyright to obtain a patent-like monopoly over unpatented microprocessor cards.”

Because copyright misuse currently is only a defense to infringement actions, it provides little deterrent against misuse to prevent legitimate competition or to chill free speech. And courts have not yet applied the copyright misuse doctrine as a defense to section 1201 claims. The Administration should recommend that Congress consider codifying a copyright misuse provision that creates predictable and meaningful deterrents to the misuse of copyrights.

D. Music Licensing Reform – Section 115

In 2005, Marybeth Peters, the then-Register of Copyrights, testified that “the present language of Section 115, with its compulsory license to allow for the use of nondramatic musical works for the making and distribution of physical phonorecords and digital phonorecord deliveries, is outdated. Reform is necessary....”²² The Register urged that Section 115 be amended “to facilitate the licensing of nondramatic musical works in a way that will serve the interests of composers and music publishers, record companies and other providers of recorded music, and the consuming public, especially with respect to digital audio transmissions of music.” Unfortunately, the past three Congresses failed to amend section 115. This failure has led to extensive litigation among the parties in this space, and delayed the development of robust legal alternatives for consumers to access music. The Administration should work closely with the new Congress to resolve this problem.

IV. THREAT ASSESSMENT

The request for comments “seeks written submissions from the public identifying the cost to the U.S. economy resulting from infringement of intellectual property rights....” We appreciate the level of specificity the RFC requires, including “the methodology used in calculating the estimated costs and any critical assumptions relied upon,” “the source of data on which the cost estimates are based,” and “a citation to each such source of information.”

²¹ *Lasercomb America v. Reynolds*, 911 F.2d 970, 977 (4th Cir. 1990).

²² Statement of Marybeth Peters, The Register of Copyrights, before the Subcommittee on Courts, the Internet, and Intellectual Property, Committee on the Judiciary, United States House of Representatives 109th Congress, 1st Session (June 21, 2005).

A. Department of Commerce Study

In this context, we note that the recently released Department of Commerce study, *Intellectual Property and the U.S. Economy: Industries in Focus*, does not in any way demonstrate the cost to the U.S. economy resulting from IP infringement. The study explicitly states that it “does not contain policy recommendations and is not intended to advance particular policy issues.”²³ Moreover, the study “note[s] the importance of achieving a balanced system of IP rights that protects innovators and creators from unlawful use of their work while encouraging innovation, competition, and the markets for technology in which IP is transacted. Importantly, using IP rights to support innovation and creativity means recognizing the public domain and limits such as fair use which balance the public’s right to use content legally with IP owners’ interests.”²⁴

Turning to the substance of the study, it reports impressive numbers for the contribution of “IP-intensive industries” to the U.S. economy in terms of employment and value added. Closer examination reveals, however, that the study includes “trademark-intensive industries” within the definition of “IP-intensive industries.” Trademark-intensive industries, in turn, include industries such as grocery stores, clothing stores, sporting goods and musical instrument stores, residential building construction, dairy product manufacturing, beverage manufacturing, footwear manufacturing, and gambling.²⁵ Indeed, 83 percent of all reported IP-intensive jobs come from trademark intensive industries.²⁶ The study itself concedes that “employment in trademark intensive industries is almost six times as great as employment in patent-intensive industries.”²⁷

The study further concedes that “overall employment in IP-intensive industries has lagged other industries in the last two decades. While employment in non-IP-intensive industries was 21.7 percent higher in 2011 than in 1990, overall IP-intensive industry employment grew over 2.3 percent over this same period.”²⁸ IP-intensive industries’ share of total employment dropped from 21.7 percent in 1990 to 18.8 percent in 2010.²⁹ Employment in patent intensive industries fared even worse than other IP-intensive sectors, shrinking by 30 percent during this period.³⁰

The fact that employment in “IP-intensive industries” has lagged behind other industries over the past twenty years certainly belies the triumphalism with which the study has been greeted by some advocacy groups and Department of Commerce press releases. The study does not “show[] that intellectual property protections have a direct and significant impact on the U.S.

²³ Economics and Statistics Administration & U.S. Patent and Trademark Office, U.S. Department of Commerce, *Intellectual Property and the U.S. Economy: Industries in Focus* (2012) at vi.

²⁴ *Id.*

²⁵ *Id.* at 36-38.

²⁶ Knowledge Ecology International, *The USPTO/DOC’s liberal and misleading definition of IP-intensive industries is designed to influence policy debates*, <http://www.keionline.org/node/1432>.

²⁷ *IP and the U.S. Economy* at vi.

²⁸ *Id.* at vii.

²⁹ *Id.* at 40.

³⁰ *Id.*

economy.”³¹ Nor does it prove that “when Americans know that their ideas will be protected, they have greater incentive to pursue advances and technologies that help keep us competitive, and our businesses have the confidence they need to hire more workers.”³² Accordingly, the study provides no support for the contention that “this Administration’s efforts to protect intellectual property ... are so crucial to a 21st century economy that is built to last.”³³

B. The Cost of Overprotection

The Department of Commerce study attributes the decrease in employment in patent intensive industries to “historic losses in manufacturing jobs.” But another factor might also be in play. Recent studies demonstrate that patent litigation has imposed enormous costs on companies in patent-intensive industries. James Bessen and Michael Meurer, for example, found that the direct costs to defendants arising from the assertion of patents by non-practicing entities (also commonly referred to as “patent trolls”) totaled \$29 billion in 2011.³⁴ In 2005, the cost amounted to \$6.6 billion. They also found that 82 percent of the defendants in patent cases were small or medium sized firms with annual revenue of less than \$100 million. The median annual revenue of patent troll targets was \$10.8 million.

After presiding over one of the many smart-phone patent litigation cases, Judge Richard Posner wrote a provocative article entitled “Why There Are Too Many Patents in America.” He described how pharmaceuticals are “the poster child for the patent system,” but noted that few industries resemble pharmaceuticals:

In most, the cost of invention is low; or just being first confers a durable competitive advantage because consumers associate the inventing company’s brand name with the product itself; or just being first gives the first company in the market a head start in reducing its costs as it becomes more experienced at producing and marketing the product; or the product will be superseded soon anyway, so there’s no point to a patent monopoly that will last 20 years; or some or all of these factors are present.³⁵

For this reason, Judge Posner concluded that “most industries could get along fine without patent protection.” Judge Posner went on to stress the relatively low cost of innovation in non-pharmaceutical industries:

In an industry in which teams of engineers are employed on a salaried basis to conduct research on and development of product improvements, the cost of a specific improvement may be small, and when that is true it is difficult to make a case for granting a patent. The improvement will be made anyway, without patent protection, as part of the normal competitive process in markets where patents are unimportant. It is true that the easier it is to get a patent, the sooner inventions will be made. But ‘patent

³¹ See <http://www.commerce.gov/blog/2012/04/11/intellectual-property-intensive-industries-contribute-5-trillion-40-million-jobs-us->.

³² See <http://www.uspto.gov/news/pr/2012/12-25.jsp>.

³³ *Id.*

³⁴ James E. Bessen & Michael J. Meurer, *The Direct Cost from NPE Disputes*, http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2091210 (2012).

³⁵ Richard A. Posner, *Why There Are Too Many Patents in America*, *The Atlantic*, July 12, 2012, <http://www.theatlantic.com/business/archive/2012/07/why-there-are-too-many-patents-in-america/259725/>.

racers' (races, induced by hope of obtaining a patent, to be the first with a product improvement) can result in excessive resources being devoted to inventive activity. A patent race is winner take all. The firm that makes an invention and files for a patent one day before his competitors reaps the entire profit from the invention, though the benefit to consumers of obtaining the product a day earlier may be far less than the cost of the accelerated invention process.

Judge Posner then explained that “a firm that can get along without patent protection” may nonetheless seek patents for defensive purposes:

Defensive patenting means getting a patent not because you need it to prevent copycats from making inroads into your market, but because you want to make sure that you're not accused of infringing when you bring your own product to market. The cost of patenting and the cost of resolving disputes that may arise when competitors have patents are a social waste.

Judge Posner described another wasteful phenomenon – patent trolls. “Patent trolls are companies that acquire patents not to protect their market for a product they want to produce – patent trolls are not producers – but to lay traps for producers, for a patentee can sue for infringement even if it doesn't make the product that it holds a patent on.”

Judge Posner identified aggravating factors in the patent system: a right to a jury trial, with jurors who “tend to favor patentees, believing that they must be worthy inventors defending the fruits of their invention against copycats;” the difficulty of patent searches; and the understaffing at the Patent and Trademark Office, resulting in “perfunctory” patent examinations. He opined that the “difficulties of search, and the prospect of incurring litigation costs to defend an infringement suit, may actually discourage innovation.” In other words, the patent system may discourage the innovation that is the very purpose of its existence. Judge Posner proposed a variety of possible solutions to the “serious problems with our patent system.”

While neither CCIA nor NetCoalition necessarily endorse all of Judge Posner's views, the fact that a judge of this stature is proposing significant amendments to the patent law just ten months after the adoption of major patent reform legislation – the America Invents Act³⁶ – points toward continuing dysfunctionality in the patent system.

Trolls, with the resulting chilling effect on creativity, exist in the copyright system as well. In *Brownmark Films v. Comedy Partners*, Judge Posner's colleague on the Seventh Circuit, Judge Frank Easterbrook, noted that Brownmark's broad discovery requests gave it “the appearance of a ‘copyright troll.’”³⁷ Judge Easterbrook added that early resolution of cases by granting motions to dismiss on the basis of affirmative defenses was necessary to avoid the cost of discovery. “The expense of discovery, which [defendants] stressed at oral argument, looms over this suit. [Defendants], and amicus, the Electronic Frontier Foundation, remind this court that infringement suits are often baseless shakedowns. Ruinous discovery heightens the incentive to settle rather than defend these frivolous suits.”³⁸

³⁶ Pub. L. No. 112-29 (2011).

³⁷ *Brownmark Films v. Comedy Partners*, 682 F.3d 687 (7th Cir. 2012).

³⁸ Rightshaven is another notorious example of a copyright troll.

Copyright trolls pose a threat to the U.S. economy by posing a threat to innovative companies. Even if a plaintiff isn't a 'troll' per se, the copyright system encourages aggressive litigation positions that impose ruinous costs on prevailing defendants. Veoh, a site that hosted user generated content, had to declare bankruptcy because of litigation costs, although it ultimately was found innocent of infringement.³⁹ Our legislative recommendations for statutory damages and misuse, detailed above, would reduce this serious threat.

C. The Health of the Copyright Industries

The copyright industries argue repeatedly that the Internet poses an existential threat. The evidence shows the opposite. According to the Department of Commerce study, employment in copyright-intensive industries increased by 46.3 percent between 1990 and 2011.⁴⁰ A recent study by business and trend analysis company Floor64 found that “[b]y any measure, it appears that we are living in a true Renaissance era for content. More money is being spent overall. Households are spending more on entertainment. And a lot more works are being created.”⁴¹ During the first decade of this century, the entertainment industry’s global revenue increased 50 percent. The value of the global music industry rose from \$132 billion in 2005 to \$168 billion in 2010. The value of the global entertainment industry grew from \$449 billion in 1998 to \$745 billion in 2010.⁴²

Similarly, the Congressional Research Service (CRS) issued a report on December 9, 2011, concerning the financial condition of the U.S. motion picture industry.⁴³ The report finds that the U.S. motion picture industry is in very good health, which belies industry claims that online infringement is causing it economic devastation.

The report makes the following findings:

- The motion picture and sound recording industry’s value-added share of GDP (0.4%) did not change between 1995 and 2009. (This suggests that infringement has not harmed these industries relative to the U.S. economy as a whole.)
- Gross revenues for the motion picture and sound recording industries grew from \$52.8 billion in 1995 to \$104.4 billion in 2009.
- U.S. box office revenues for the U.S. and Canada rose from \$5.3 billion in 1995 to \$10.6 billion in 2010.

³⁹ UMG Recordings, Inc. v. Shelter Capital Partners LLC, 667 F.3d 1022 (9th Cir. 2011). Similarly, Perfect 10’s unsuccessful litigation against Google’s Image Search lasted five years and consumed vast attorney and staff resources.

⁴⁰ *IP and the U.S. Economy* at vii.

⁴¹ Michael Masnick & Michael Ho, Floor64, *The Sky is Rising* (2012), at <http://www.cciainet.org/CCIA/files/ccLibraryFiles/Filename/000000000586/TheSkyIsRising7-130.pdf>.

⁴² Derek Slater & Patrick Wruuck, *We Are All Content Creators Now*, <http://www.globalinnovationindex.org/gii/main/fullreport/files/Chap1/Chapter11.pdf>.

⁴³ Memorandum from Sue Kirchoff, Congressional Research Service, to Senator Ron Wyden, Dec. 19, 2011, available at <http://www.techdirt.com/articles/20111212/02244817037/congressional-research-service-shows-hollywood-is-thriving.shtml>.

- Worldwide box office receipts have been growing faster than U.S. domestic receipts. (This suggests that the problem of foreign infringement is overstated.)
- According to the Census Bureau, the after-tax profit of the industry increased from \$496 million for the second quarter of 2010 to \$891 million for the second quarter of 2011.
- According to the Commerce Department’s Bureau of Economic Analysis, corporate profits after taxes for the U.S. motion picture and sound recording industry grew from -\$2.7 billion in 1998 to \$937 million in 2008.
- CEO pay has increased significantly over the past 15 years. Walt Disney Company: \$10 million in 1994 to \$29.6 million in 2010; and Time Warner: \$5 million in 1994 to \$26.3 million in 2010. Other industry CEOs also received generous compensation in 2010. News Corp.: \$33.3 million; Viacom: \$84.5 million; and NBC Universal: \$21.4 million.

In sum, the CRS reports that the financial condition of the U.S. motion picture industry is very solid.⁴⁴ This, in turn, suggests that industry complaints about the harm caused by copyright infringement are overstated.⁴⁵ While Internet-based infringement may cause some companies

⁴⁴ Motion picture ticket sales have continued to surge since the release of the CRS report. International motion picture tickets in 2011 increased three percent over 2010 and 35 percent over 2006. Richard Verrier, *International movie ticket sales reach new peak in 2011*, L.A. Times, March 25, 2012, <http://latimesblogs.latimes.com/entertainmentnewsbuzz/2012/03/international-movie-ticket-sales.html>. The Chinese box office grew 35 percent in 2011 alone. Motion Picture Association of America, *Theatrical Movie Statistics 2011*, <http://www.mpa.org/resources/5bec4ac9-a95e-443b-987b-bff6fb5455a9.pdf>. In March, *The Hunger Games* set multiple sales records, including the strongest opening weekend for a spring release. Brooks Barnes, *‘Hunger Games’ Ticket Sales Set Record*, N.Y. Times, March 25, 2012, <http://www.nytimes.com/2012/03/26/movies/hunger-games-breaks-box-office-records.html>. In May, *The Avengers* broke the record for the biggest opening weekend in North America by \$30 million. Brooks Barnes, *‘Avengers’ Vanquish Box-Office Rivals*, N.Y. Times, May 6, 2012, <http://www.nytimes.com/2012/05/07/movies/marvels-the-avengers-top-box-office-record.html>. In July, *‘The Dark Knight Rises’* broke the record for the biggest opening weekend in North America for a 2D movie, notwithstanding the tragedy in Aurora, Colorado. *‘The Dark Knight Rises’ sets box-office record*, Wash. Post, July 24, 2012, http://www.washingtonpost.com/lifestyle/style/the-dark-knight-rises-sets-box-office-record/2012/07/24/gJQAE7jr6W_story.html.

⁴⁵ Many studies have demonstrated this conclusion. See Francis Bea, *Study Suggests U.S. Box Office Not Affected by BitTorrent*, Digital Trends, Feb. 11, 2012, <http://www.digitaltrends.com/international/study-suggests-u-s-box-office-not-affected-by-bittorrent/> (stating that a study by researchers from Wellesley College and the University of Missouri found that U.S. box office sales are not affected by BitTorrent pirating. The study also revealed that movie studios hold the power to curb piracy by decreasing international box office release windows); Timothy B. Lee, *Swiss Government: File Sharing No Big Deal, Some Downloading Still OK*, Ars Technica, Dec. 5, 2011, <http://arstechnica.com/tech-policy/news/2011/12/swiss-government-file-sharing-no-big-deal-some-downloading-still-ok.ars>. A report written by the Swiss Federal Council, pursuant to a request by the Swiss legislature, concluded that file-sharing does not have a negative impact on Swiss culture. Because consumers spend a constant share of their disposable income of entertainment, money they save buying CDs and DVDs are instead spent on concerts, movies, and merchandising. The Hargreaves Review in the United Kingdom stated that a detailed survey of U.K. and international data concerning online copyright infringement “finds that very little of it is supported by transparent research criteria. Meanwhile sales and profitability levels in most creative business sectors appear to be holding up reasonably well. We conclude that many creative businesses are experiencing turbulence from digital copyright infringement, but that at the level of the whole economy, measurable impacts are not as stark as is sometimes suggested.” Ian Hargreaves, *Digital Opportunity: A Review of Intellectual Property and Growth* 47 (2011), available at <http://www.ip.gov.uk/ipreview-finalreport.pdf>. The Government Response to the Hargreaves Review agreed that “too many past decisions on IP have been supported by poor evidence, or indeed poorly

some harm, the size of the problem must be properly understood to ensure that the “solutions” do not cause unnecessary collateral damage.⁴⁶

To the extent that there is a problem, the content industries assume without proof that more laws, and more enforcement of those laws, are the most effective means of reducing online infringement. However, according to a study by Joe Karaganis, “we have seen no evidence – *and indeed no claims* – that enforcement efforts to date have had *any* impact on the overall supply of pirated goods.”⁴⁷ The seizure of the Megaupload servers and domain name did not reduce infringement because the filesharing traffic simply migrated elsewhere.⁴⁸

This suggests that in the long run, the real solution to the problem of online infringement relies on business models that are attractive to users rather than ever more draconian copyright regulation. Numerous industries have developed business strategies that have had the effect of reducing the demand for infringing products. Software companies, for example, have licensed computer manufacturers to preload software on their computers prior to consumer purchase. Video game companies offer multi-player game platforms accessible only to authorized users. Some entertainment companies license their content for online distribution at low or no cost. These strategies succeed when they are designed and implemented by industry participants with a deep understanding of the relevant products, technology delivery platforms, and consumers.⁴⁹ Studies show that the vast majority of consumers desire legal sources of online content. They turn to infringing content when convenient and affordable legitimate content is not available.⁵⁰

supported by evidence. This is true at an international level as well as domestically.” *The Government Response to the Hargreaves Review of Intellectual Property and Growth* 3 (2011), <http://ipo.gov.uk/ipresponse-full.pdf>.

⁴⁶ According to reports about a leaked presentation from the Recording Industry Association of America (RIAA), 70 percent of the infringement of music occurs offline, *e.g.*, the ripping and burning of CDs or the trading of hard drives. 23 percent occurs on peer-to-peer networks and 6 percent on digital lockers. Dan Tynan, *The RIAA Knew SOPA and PIPA Were Useless, Yet Supported Them Anyway*, PCWorld, July 31, 2012, http://www.pcworld.com/article/260087/the_riaa_knew_sopa_and_pipa_were_useless_yet_supported_them_anyway.html. Hence, even if online infringement could be completely eradicated, the vast majority of infringement would continue.

⁴⁷ Joe Karaganis, *Media Piracy in Emerging Economies: Price, Market Structure and Consumer Behavior* 7 (2010), at http://www.wipo.int/edocs/mdocs/enforcement/en/wipo_ace_6/wipo_ace_6_5.pdf. Indeed, even the RIAA reportedly believed SOPA and PIPA were “not likely to have been an effective tool for music.” Tynan, *id.*

⁴⁸ See Mike Masnick, *Evidence Shows that Megaupload Shutdown had No Real Impact on Infringement*, Techdirt Feb. 8, 2012, <http://www.techdirt.com/articles/20120208/04122017699/evidence-shows-that-megaupload-shutdown-had-no-real-impact-infringement.shtml> (quoting the analysis by Deepfield Networks that the new traffic flow is “staggering less efficient from a network standpoint, because much of it moved to offshore locations over expensive transatlantic links”).

⁴⁹ Certain strategies designed to prevent infringement, such as the use of digital rights management (DRM) technologies, may ultimately harm entertainment companies’ long term interests. The record labels, for example, required Apple’s iTunes service to include DRM in sound recordings it sold. This had little impact on infringement, because users could still upload to the Internet tracks from unprotected CDs. At the same time, the DRM in effected locked consumers into the Apple platform, which ultimately gave Apple enormous leverage over the record labels. The publishing industry appears to be repeating the same mistake by requiring DRM in eBooks, thereby locking consumers into platforms, whose vendors can then dominate the publishers. See <http://www.techdirt.com/articles/20120210/01364817725/how-publishers-repeated-same-mistake-as-record-labels-drm-obsession-gave-amazon-dominant-position.shtml>.

⁵⁰ Michael D. Smith, *Converting Pirates Without Cannibalizing Purchasers: The Impact of Digital Distribution on Physical Sales and Internet Piracy* (2010), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1381827. See also *Pirates Want to Go Legal But Convenience, Choice and Availability Come First*, July 19, 2012, <http://torrentfreak.com/pirates-want-to-go-legal-but-convenience-choice-availability-come-first-120719>.

Indeed, Justice Breyer in his dissent in *Golan v. Holder* recognized that the high administrative costs for locating hard-to-find owners of copyrighted works “will tempt some potential users to ‘steal’ or ‘pirate’ works rather than do without.”⁵¹

V. OPTIONAL QUESTIONS

10. As laid out in IPEC’s 2011 Annual Report on Intellectual Property Enforcement, using our resources as efficiently as possible is a priority. Are there additional ways in which the U.S. Government could make more efficient use of its resources in protecting intellectual property?

In our 2010 comments, we argued that the federal government should intervene in IP enforcement “only in areas where: 1) the infringement is unambiguous; 2) the harm to the public is clear; 3) industry is incapable of addressing the infringement; and 4) federal intervention is likely to have a positive impact.” On this basis, we argued that the federal government should spend its IP enforcement resources fighting infringement that harms human health and safety – for example, combating counterfeit drugs rather than counterfeit handbags.

As noted above, over the past two years, the federal government has commendably devoted significant energy to addressing the problem of counterfeit drugs and other threats to health and safety. At the same time, however, the federal government has also expended resources on what we believe should be lower priority targets – websites that infringe copyrights and trademarks owned by highly-profitable, often foreign-controlled,⁵² corporations. We are not condoning the infringing activity that occurs on such sites. Rather, we do not believe federal law enforcement resources should be spent protecting entities that are perfectly capable of protecting themselves. In addition to bringing infringement actions in federal court, they can avail themselves of the DMCA’s notice and takedown procedures.⁵³

Inexpensive legitimate distribution models are also essential to reducing infringement in the developing world. Karaganis, *supra* note 47, at 5 (stating that “the key question for media access and the legalization of media markets ... has less to do with enforcement than with fostering competition at the low end of media markets – the mass market that has been created through and largely left to piracy”). Karaganis explains that a critical feature of this competition “is neither strong enforcement nor the innovative use of digital distribution, but rather the presence of firms in national markets that actively compete on price and services for local audiences.” *Id.* at 4. Karaganis adds that local firms are much more likely than multinational firms “to aggressively compete for audiences on price and service – the domestic market is their market.” *Id.*

⁵¹ See *Golan v. Holder*, 132 S.Ct. 873, 900 (2012) (Breyer, J., dissenting).

⁵² Many of the largest copyright and trademark owners are foreign companies: three of the four major record labels – Sony Music Entertainment (Japan), EMI (UK), and Universal Music Group (Vivendi, France) (the fourth major label, Warner Music Group, is owned by Len Blavatnik, who lives in the UK and the U.S.); eight of the ten largest book publishers – Pearson (owner of Penguin, UK), Reed Elsevier (UK-Netherlands), Thomson Reuters (Canada), Wolters Kluwer (Netherlands), Hachette (France), Grupo Planeta (Spain), Random House (Bertelsmann – Germany), and Holtzbrink (Germany); two of the largest video games companies – Nintendo (Japan), Sony (Japan); two of the largest database publishers – Reed Elsevier (owner of Lexis-Nexis, UK-Netherlands), Thomson-Reuters (owner of West, Canada); and many of the largest luxury goods manufacturers – Louis Vuitton (France), Hermes (France), Chanel (France), Gucci (Italy).

⁵³ In June 2012 alone, Google reported receiving DMCA removal requests with respect to 2,268,743 URLs on 25,986 specified domains in its Search service. *Google Transparency Report*, July 13, 2012, <https://www.google.com/transparencyreport/removals/copyright/>. Estimates indicate that there are well over a trillion URLs on the World Wide Web, meaning that these takedown requests apply to less than .0002 percent of the

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August 10, 2012

URLs on the Web. Google complies with 97 percent of the takedown requests it receives. Parker Higgins, *Google Releases New Copyright Transparency Report*, May 24, 2012, <https://www.eff.org/deeplinks/2012/05/google-releases-new-copyright-transparency-report>. Google does not comply with requests that do not meet the DMCA's requirements.