

MGM v. Grokster: The Latest Battle in the War on Internet Copyright Infringement

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In a case involving peer-to-peer file sharing software, the U.S. Supreme Court has been asked to choose between competing interpretations of its seminal case on contributory copyright infringement. Its widely-anticipated decision will likely have far-reaching implications for the IT industry in the United States.

Last year saw the 20th anniversary of the U.S. Supreme Court's decision in *Sony v. Universal*, 464 U.S. 417 (1984) ("*Betamax*"), which held that a device manufacturer could not be held liable for contributory copyright infringement if the device is capable of a substantial non-infringing use. The *Betamax* safe harbor recently has come under attack, both in the courts and in the U.S. Congress. On December 10, 2004, the Supreme Court upped the ante when it granted review of the Ninth Circuit's controversial decision in *MGM v. Grokster*, 380 F.3d 1154 (9th Cir. 2004).

The *Betamax* Rule

In *Betamax*, the Supreme Court fashioned a simple rule: the sale of copying equipment does not constitute contributory copyright infringement if the product is "capable of commercially significant non-infringing uses." *Betamax* thus provided an exception to the principle that a person who knowingly makes a material contribution to an infringement committed by another person is liable for that infringement. Although the technology at issue in *Betamax* (the video tape recorder) is no longer at the cutting edge, the standard the Supreme Court enunciated has been critical to the development of the IT industry in the U.S. over the past 20 years. The legal certainty provided by the *Betamax* decision encouraged the investment in technologies such as personal computers, MP3 players, personal video recorders, and the Internet.

Recent Judicial Narrowing of *Betamax*

Ever since the *Betamax* decision, the U.S. entertainment industry has remained hostile to any new technology that provides a means of reproducing their product. Their most recent target has been peer-to-peer software which allow users to share computer files, such as digitized copies of music and movies, with others over the Internet. The most infamous of these providers (and the first to be shut down by court order) was Napster. The litigation it has spawned along with its progeny, such as Aimster, Grokster, Morpheus and Kazaa, has produced both conflicting and narrowing interpretations of *Betamax* which are now headed to the Supreme Court for resolution.

In *A&M Records v. Napster*, 239 F.3d 1004 (9th Cir. 2001), the Ninth Circuit took a step back from the bright line drawn by *Betamax*. Rather than finding that *Betamax* provided a complete defense to a provider of a dual-purpose technology (i.e., a

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technology that could be used for infringing and non-infringing purposes), the court held that the existence of a substantial non-infringing use for an accused technology was merely relevant to the knowledge prong of contributory copyright infringement and meant only that constructive knowledge of infringement could not be “presumed.” If non-infringing uses were shown, the plaintiff then had to prove that the defendant had actual knowledge of specific infringing material on its system and failed to purge the material from the system. Applying this test, Napster was found to have the requisite knowledge and ability to block the infringing material, which it had failed to do.

The Ninth Circuit based its narrow interpretation of *Betamax* on a single sentence in that decision stating that if secondary liability was to be imposed on Sony, “it must rest on the fact that it has sold equipment with constructive knowledge of the fact that its customers may use that equipment to make unauthorized copies of copyrighted works.” However, nothing in *Betamax* suggests the Supreme Court intended to limit its “capable of substantial non-infringing uses” standard to a single prong of the test for contributory infringement.

Two years later, in *In re Aimster Copyright Litigation*, 334 F.3d 643 (7th Cir. 2003), the Seventh Circuit rejected the *Napster* standard as a misreading of *Betamax* but adopted instead a complex balancing test that applied *Betamax* even more narrowly. The *Aimster* test first looks at an “estimate of the respective magnitudes” of the infringing and noninfringing uses. If the infringing uses are substantial, “to avoid liability as a contributory infringer the provider of the service must show that it would have been disproportionately costly for him to eliminate or at least substantially reduce the infringing uses.”

The Seventh Circuit’s reformulation of *Betamax* was unnecessary as the *Aimster* defendants unquestionably engaged in contributory conduct that extended far beyond the mere supply of a technology that others could use to infringe and thus fell outside the bounds of the safe harbor as originally fashioned by the Supreme Court. First, in explaining how to use its software, *Aimster*’s tutorial was an “invitation to infringement” since it gave “as its *only* examples of file sharing the sharing of copyrighted music.” Second, *Aimster* operated a “club” which enabled members “to download with a single click” the copyrighted music most often shared by *Aimster* users.

Ironically, the court that brought down Napster was the one to most recently deliver a blow to its opponents. In *MGM v. Grokster*, 380 F.3d 1154 (9th Cir. 2004), the Ninth Circuit followed its *Napster* precedent in applying the *Betamax* rule exclusively to the knowledge prong of contributory infringement. Because the software at issue was capable of substantial non-infringing uses, the court held that the defendants “could not be liable for constructive knowledge of infringement.” However, the court identified significant differences between the *Napster* and *Grokster* technologies. While *Napster* employed a central server to enable users to find the files they desired, the software in *Grokster* allows users to search other users’ computer directly, without relying upon a central server. On the basis of this technological difference, the court found that unlike the *Napster* service, the *Grokster* defendants did not have actual knowledge of infringing material on their system at a time they could do anything about it. The court noted that if

the defendants “closed their doors and deactivated all the computers within their control, users of their products could continue sharing files with little or no interruption.”

The Betamax Controversy Reaches the Supreme Court

The entertainment industry (songwriters, music publishers, record companies and motion picture studios) petitioned the Supreme Court to hear its appeal from the *Grokster* decision. The entertainment industry claimed that the Ninth Circuit misread the *Betamax* standard, and reached a decision that conflicted with *Aimster*. It argued that the Ninth Circuit ignored critical differences between the technologies at issue in *Betamax* and *Grokster* (such as the ability to block direct infringement), and rewarded willful blindness. Having refused to hear appeals in *Napster* and *Aimster*, the U.S. Supreme Court decided to hear the copyright owners’ appeal in *Grokster*. Briefing is currently underway. The oral argument will be heard on March 29, and a decision could be issued as soon as June.

The entertainment industry argues that *Grokster* court’s interpretation of *Betamax* will have a ruinous affect on copyright owners. Providers of P2P software, whose business model relies on infringement, will escape with impunity. The technology industry, on the other hand, argues that the *Aimster* court’s interpretation of *Betamax* will impede innovation by permitting copyright owners to second-guess every design decision made by an engineer. The stakes in this litigation could not be any higher.

Betamax Under Attack In the U.S. Congress

Perhaps skeptical that they will ultimately get their desired result in the courtroom, the entertainment industry has also taken its fight against Internet infringement to the U.S. Congress. Senators Orrin Hatch and Patrick Leahy introduced the Inducing Infringement of Copyrights Act (the “Induce Act”) in 2004 in direct response to the *Grokster* decision. The Induce Act would amend the U.S. copyright statute to create a new form of secondary copyright liability, “intentional inducement,” to which the *Betamax* defense would *not* apply.

Under the original, terse amendment, anyone who “intentionally aids, abets, induces, or procures” copyright infringement would be liable as an infringer. Intent could be shown “by acts from which a reasonable person would find intent to induce infringement based upon all relevant information about such acts then reasonably available to the actor, including whether the activity relies on infringement for its commercial viability.”

The Induce Act was met with a great deal of criticism (such as that it would outlaw Apple’s iPods) and suggestions for competing approaches to solve the peer-to-peer infringement problem. The U.S. Copyright Office advocated the targeting all businesses that “depend upon infringement for their commercial viability.” The Consumer Electronics Association advanced a narrow exception to *Betamax* creating liability for the distribution of programs specifically designed for use in mass infringing distribution to the public of copyrighted works. The Institute of Electrical and Electronics Engineers and a coalition of Internet companies proposed codification of all

forms of secondary liability, importing the definitions of active inducement and contributory liability from the Patent Act, and writing the *Betamax* safe harbor into the Copyright Act.

Senators Hatch and Leahy tried to broker a compromise between the entertainment and technology industries, but negotiations reached an impasse as the congressional session came to an end. Senator Hatch has vowed to renew discussions in 2005; while he no longer is chairman of the Senate Judiciary Committee, he now is chair of the new Intellectual Property Subcommittee. However, it is safe to say that Congress is not likely to act on the issue before the Supreme Court rules in *Grokster*.