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Catch-As-Catch-Can: A Case Note on Grokster

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Urs Gasser*
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ABSTRACT

In summer 2005, the United States Supreme Court issued a decision which is surely destined to play a significant role in the interrelation between law and technology in the coming years. The case, *Metro-Goldwyn-Mayer Studios Inc., et al. v. Grokster, Ltd., et al.*, pitted copyright holders against the operators of certain peer-to-peer online file-sharing services and was awaited by many in both the legal and technology communities as a referendum on the landmark legal precedent set in the "Sony-Betamax" case. The Sony case came to represent the legal standard for determining when manufacturers of "dual-use technology"—technology capable of both legally noninfringing and infringing uses—should be given a safe harbor from liability for acts on the part of their consumers which violated copyright law.

Surprisingly, the Supreme Court's decision did not center around an affirmation or rejection of the Sony ruling; rather the Court based their opinion on a common law principle which, they held, was not preempted by the holding in Sony. The "inducement" to infringe copyright, although not a completely novel cause of action, has been perceived by some commentators to introduce a change in the legal landscape of secondary liability for copyright infringement. In this article, we provide an extensive exposition of the Court's decision and discuss the disposition of the decision including the implication of the two concurring opinions. We also speculate on the impact that the Court's decision will have on the technology sector and on technological innovation in particular. Ultimately, we grapple with new questions which the decision has presented for industry and the continued existence of peer-to-peer file-sharing.

Keywords: Grokster, file-sharing, peer-to-peer, Sony Betamax, Digital Entrepreneurship

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Table of Contents

I. The Problem, p. 4

II. The Ruling, p. 4

III. Comments, p.6

1. The Sony Controversy, p.7

2. (Re-)Introducing the Inducement Rule, p. 9

3. Grokster's Potential Impact, p. 12

4. Conclusion, p. 15

I. The Problem

Grokster Ltd. and StreamCast Networks, Inc. have distributed free software products¹ that allow Internet users to share electronic files through so-called *peer-to-peer (P2P) networks*. P2P networking, in essence, can be described as a system of information exchange where the transfer of data is effected directly from one user's computer to another.² P2P networks are opposed to centralized systems where users communicate through a central server that mediates the exchange of information or files among them. Software such as Grokster and Morpheus can be used by individuals to share any type of digital file, including, for instance, public domain works. However, it is common wisdom that users have prominently used P2P networks to share copyrighted materials such as music and video files without authorization. Against this backdrop, motion picture studios, recording companies, songwriters, and music publishers (a group hereinafter referred to as "MGM") sued Grokster and StreamCast for their users' copyright infringements, alleging that they knowingly and intentionally distributed their software products to enable users to reproduce and distribute copyrighted works in violation of U.S. Copyright. The District Court for the Central District of California granted partial summary judgment for Grokster and StreamCast on issues of contributory and vicarious infringement.³ MGM appealed and the United States Court of Appeals for the Ninth Circuit affirmed the District Court's ruling.⁴ The U.S. Supreme Court granted certiorari.⁵ The key question before the Supreme Court was: under what circumstances can the distributor of a product (here: software) capable of both lawful *and* unlawful use (here: sharing unprotected files as well as copyrighted materials) be held liable for acts of copyright infringement perpetrated by third parties using the product. The appeal of the case represented both a challenge of the lower court rulings in the Grokster matter but also the principle settled in the 1984 United States Supreme Court case, *Sony Corp. of America v. Universal City Studios, Inc.* as to secondary liability in copyright. Observers in the technology and media fields agreed that much hung in the balance.

II. The Ruling

In the landmark case *Metro-Goldwyn-Mayer Studios Inc., et al. v. Grokster, Ltd., et al.*,⁶ the Supreme Court held that there was sufficient evidence to find Grokster and StreamCast liable of infringement under a *theory of inducement* of infringement and remanded to the lower courts

¹ Grokster relied on FastTrack technology which had been developed and licensed to Grokster by a third party. StreamCast's software was called "Morpheus" and relied on Gnutella technology. In the course of litigation, StreamCast later switched over to Neonet technology as a basis for its software. This development, however, was apparently not deemed to be relevant to the Court's decision.

² See, e.g., Wikipedia, "Peer-to-Peer", available at <http://en.wikipedia.org/wiki/Peer-to-peer>.

³ *Metro-Goldwyn-Mayer Studios Inc., et al. v. Grokster, Ltd., et al.*, 259 F. Supp.2d 1029 (C.D. Cal., 2003). On the issue of contributory infringement, the District Court found that both Grokster and StreamCast failed to meet the elements for liability since 1) there was no evidence that either had *actual* knowledge of infringement on the part of their users at a time when they had the ability to do something about it; and 2) neither actively facilitated nor could do anything to prevent their users' infringing activities. *See id.* at 1035-43. With regard to vicarious liability, the District Court found that the initial element of direct financial benefit from the infringing activity was met with regard to both companies. *See id.* at 1043-44. Neither company, however, met the second element of liability in the court's opinion, since neither company had the requisite influence or control over the networks on which their users carried out infringing activity. *See id.* at 1044-46. Of primary significance in the court's analysis under both theories of liability was the fact that neither company controlled the platform for the exchange of files as was the case with Napster; Napster had provided an index of available files on its own server.

⁴ *Metro-Goldwyn-Mayer Studios Inc., et al. v. Grokster, Ltd., et al.*, 380 F.3d 1154 (9th Cir., 2004).

⁵ *Metro-Goldwyn-Mayer Studios Inc., et al. v. Grokster, Ltd., et al.*, 125 S. Ct. 686, 160 L.Ed.2d 518 (2004).

⁶ 125 S.Ct. 2764 (2005).

for a determination of the companies' liability. In order to understand the ruling, one must first recall an important feature of U.S. copyright law and a precedent that played an important role in the *Grokster* litigation.

Under U.S. law, not only the direct or primary infringer, but also parties with less direct involvement in the infringement might be held liable for copyright infringement. Third-party (also known as secondary) liability in copyright traditionally follows one of two theories: contributory liability or vicarious liability. Contributory liability requires that the secondary infringer knew or had reason to know of the direct infringement and that the secondary infringer materially contributed to that infringement.⁷ Vicarious liability, by contrast, does not require knowledge. Rather, it requires that the third party have some measure of control over the primary party. Further, the third party must enjoy a direct financial benefit from the infringement to be held liable under the vicarious liability doctrine.⁸

The U.S. Supreme Court has dealt with secondary copyright infringement in only one recent case—a precedent that the parties in *Grokster* as well as many *amici* regarded as key in resolving the *Grokster* controversy. In *Sony Corp. of America v. Universal City Studios, Inc.*,⁹ Universal Studios and Disney sued Sony for contributory infringement caused by consumers copying TV programs using Sony's videocassette recorders (VCRs). However, at the trial on the merits, evidence showed that the principal use of the VCR was for non-infringing uses such as time-shifting.¹⁰ Further, there was no evidence that Sony had intent to promote infringing uses.¹¹ Consequently, the only basis for imposing liability was on the theory of contributory infringement arising from the very distribution of VCRs to consumers with the knowledge that some would use them to infringe a commercial product.¹² Reflecting a traditional doctrine from patent law, the Supreme Court held Sony could not be faulted solely on the basis of the distribution of VCRs, because the device was "capable of commercially significant noninfringing uses."¹³

The Ninth Circuit applied the *Sony* doctrine in favor of *Grokster* and *StreamCast* by giving it a broad interpretation, holding that whenever a product is capable of substantial non-infringing uses, the producer or distributor can not (or only under very specific circumstances)¹⁴ be held contributorily liable for a third party's infringing use of it. Based on this view of *Sony* on the one hand and the Circuit Court's finding that the defendants software was capable of substantial lawful uses--like sharing public domain works--on the other hand, the Ninth Circuit ruled that neither company could be held liable, since there was no evidence that their software afforded them knowledge of specific unlawful uses.

⁷ *Gershwin Pub. Corp. v. Columbia Artists Management, Inc.*, 443 F.2d 1159 (2d Cir. 1971). For instance, where a concert promoter organizes a performance of copyrighted material to be performed by artists under the promoter's own management and knows that neither the artists nor local organizers would secure a copyright license, that promoter may be held liable under a theory of contributory infringement. *See generally, id.*

⁸ *Fonovisa, Inc. v. Cherry Auction, Inc.*, 76 F.3d 259 (9th Cir. 1996). Liability may attach to the provider of a file-sharing network, for instance, where the future revenue of that provider is directly dependent upon the availability of copyrighted materials and the provider has the right and ability to police the infringing activity of its users. *See A&M Records, Inc. v. Napster, Inc.*, 239 F.3d 1004 (9th Cir. 2001).

⁹ 464 U.S. 417 (1984).

¹⁰ Time-shifting refers to the practice of recording television programs so that they may be viewed at a later time--in effect "shifting" the time at which the program is viewed.

¹¹ The recording of programs for the purpose of selling them to third parties or for building a movie library, for instance.

¹² *Id.* at 439.

¹³ *Id.* at 442.

¹⁴ See *infra* Section III.1 for further discussion.

In the majority opinion, the U.S. Supreme Court disagreed with the Ninth Circuit's broad reading of *Sony*, but left further consideration of the rule “for a day when that may be required,” holding that the *Sony* doctrine did not exclusively require the distributor to have actual knowledge of specific unlawful acts on the part of third party users of the distributor's product in order for secondary liability for infringement to attach. According to this opinion, *Sony* did not eliminate or replace common law theories of liability. The question under what circumstances the distributor of a product capable of both lawful and unlawful use is liable for acts of copyright infringement by third parties using the product was ultimately answered by adopting an alternative theory of liability rooted in patent law, the so-called *inducement rule*. The Court held:

*We adopt [the inducement rule] here, holding 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.*¹⁵

The Supreme Court held that there was sufficient evidence to find Grokster and StreamCast liable of infringement under this theory of enticement or inducement of infringement. Three features of the evidence of intent were particularly important in this context: First, StreamCast and Grokster were targeting users of the former file-sharing service Napster as internal documents as well as advertisement demonstrated. Second, neither company attempted to develop filtering tools or other mechanisms to diminish the infringing activity using their software. In an important footnote, the Supreme Court made clear that this failure to take affirmative steps to prevent infringement would not be sufficient to find contributory infringement liability in cases of dual-purpose devices. However, the Court argued that this piece of evidence underscored the defendants’ intentional facilitation of their users’ infringements. Third, the fact that StreamCast and Grokster made money by selling advertising space by directing ads to the screens of computers employing their software complemented the direct evidence of unlawful objective, since “the extent of the software’s use determines the gain to the distributors, the commercial sense of their enterprise turns on high-volume use, which the record shows is infringing.”¹⁶ Again, this evidence alone would not justify an inference of unlawful intent, but acquired added significance “in the entire record’s context.”¹⁷

Based on the theory of inducement and according to this evidence, the Supreme Court remanded the case to the lower courts for a determination of StreamCast’s and Grokster’s liability.

III. Comments

The *Grokster* case raises a multitude of equally interesting and complex questions at the intersection of law, technology, and digital entrepreneurship. They range from specific doctrinal problems to policy issues, but also include a set of fact-specific questions. In this section, we focus on three aspects that are particularly interesting and controversial. First, we seek to analyze to what extent *Grokster* affects the above-mentioned *Sony* standard. Second, we take a closer look at the alternative theory of secondary liability that the Supreme Court introduced in *Grokster* (“inducement rule”). Finally, we offer some thoughts about the possible impact of *Grokster* on the digital media landscape.

¹⁵ *MGM et al.*, 125 S. Ct. at 2780.

¹⁶ *Id.* at 2782.

¹⁷ *Id.*

1. The *Sony* Controversy

As mentioned above, the interpretation of the *Sony* doctrine has been at the core of the litigation all the way up to the Supreme Court. Both the parties as well as many *amici* asked the Supreme Court to clarify the *Sony* doctrine and its application in the digital age – and many suggested to the Court that they ought to re-affirm its core holding.¹⁸ The Supreme Court, however, has not provided a comprehensive answer,¹⁹ but made clear that it disagrees with *Sony*'s application by the Ninth Circuit Court.

The Ninth Circuit interpreted the *Sony* doctrine broadly by ruling that “in order for limitations [to contributory liability] imposed by *Sony* to apply, a product need only be *capable* of substantial noninfringing uses.”²⁰ In the Ninth Circuit Court's reading,²¹ *Sony* provides a safe harbor even when an actual purpose to cause infringing use is shown by evidence independent of design and distribution of the product, unless the distributors had “specific knowledge of infringement at a time at which they contributed to the infringement, and failed to act upon that information.”²² The Supreme Court disagreed with this broad view and held that the Ninth Circuit had misapplied *Sony*. The Justices found that the Ninth Circuit's view was in error because *Sony* only limits “imputing culpable intent as a matter of law from the characteristics or uses of a distributed product,” but does neither displace other theories of secondary liability—including rules of fault-based liability derived from the common law—nor require courts to ignore evidence of intent if there is such evidence.²³

Justice Ginsburg's concurring opinion also concluded that the Ninth Circuit misapplied the *Sony* doctrine. In contrast to the majority opinion, however, Justice Ginsburg did not put emphasis on alternative theories of secondary liability. Rather, Justice Ginsburg took up the *Sony* question by arguing that “the evidence was insufficient to demonstrate, beyond genuine debate, a reasonable prospect that substantial or commercially significant noninfringing uses were likely to develop over time.”²⁴ In other words, Justice Ginsburg—joined by the Chief Justice and Justice Kennedy—held that *Grokster*'s activities did not pass the *Sony* test as conceived by the Court in 1984.²⁵

¹⁸ See, e.g., Brief for Petitioners, at 17, *Metro-Goldwyn-Mayer Studios Inc., et al. v. Grokster, Ltd., et al.*, 125 S.Ct. 2764 (2005) (No. 04-480); Brief for Respondents, at 13-14, (No. 04-480) (arguing that the Court should endorse the Ninth Circuit's view of *Sony*); Oral Argument, (No. 04-480) 2005 WL 832356, at *6-7, *9-12, *26-27, *30-31, *41, *65; see also generally, *Amicus Curiae* Brief of the American Intellectual Property Law Association; Brief of the Business Software Alliance as *Amicus Curiae* (No. 04-480) (urging the Court to “reaffirm” the *Sony* rule and reject the approach of the Seventh Circuit); Brief of *Amici Curiae* Law Professors, Economics Professors, and Treatise Authors (No. 04-480) (urging the Court to restore the “balance” of *Sony* which the Ninth Circuit had upset).

¹⁹ See, e.g., Electronic Frontier Foundation, *Remedying Grokster*, (July 25, 2005), available at <http://www.eff.org/deeplinks/archives/003833.php#003833>; “U.S. Supreme Court Justices rule on music downloads,” *Daily Record* (July 5, 2005) 2005 WLNR 10682073.

²⁰ *Metro-Goldwyn-Mayer Studios Inc., et al. v. Grokster, Ltd., et al.*, 380 F.3d 1154, 1162 (9th Cir., 2004).

²¹ *Compare In re Aimster*, 334 F.3d 643 (7th Cir. 2003). In an opinion by Judge Posner, the Seventh Circuit expressed a different view of the “*Sony* defense.” It suggested that, in addition to showing that the product was capable of noninfringing use, where infringement was “substantial” the defendant of a contributory infringement action should be required to “show that it would have been disproportionately costly for [it] to eliminate or at least reduce the substantially infringing uses.” *Id.* at 653.

²² *Id.*; see also *MGM et al.*, 125 S. Ct., at 2778.

²³ *MGM et al.*, 125 S. Ct., at 2778-79.

²⁴ *Id.*, at 2786 (Ginsburg, J., concurring).

²⁵ In this context, Justice Ginsburg points out a number of factual differences between the *Sony* case and that of *Grokster*:

Justice Breyer, joined by Justices Stevens and O'Connor, agreed with the majority opinion as far as the inducement rule is concerned, but disagreed with Justice Ginsburg's interpretation and application of the Sony standard in two important respects. On the one hand, Justice Breyer argued that Justice Ginsburg's approach leads to a more strict interpretation of *Sony* by requiring "defendants to produce considerably more concrete evidence ... to earn Sony's shelter."²⁶ On the other hand, Justice Breyer found that the record evidence passes the *Sony* test, that is, in Breyer's view, whether the company's product is capable of substantial or commercially significant noninfringing uses.²⁷

The following chart summarizes the positions as far as the interpretation and application, respectively, of *Sony* is concerned.

	Majority op.	Ginsberg conc. op.	Breyer conc. op.
Sony misapplied by 9th Circuit?	<i>Yes</i>	<i>Yes</i>	<i>Yes</i>
"Inducement rule" as an alternative theory of liability?	<i>Yes</i>	<i>Yes</i>	<i>Yes</i>
Sony test interpreted?	-	<i>Yes</i>	<i>Yes</i>
Record evidence passes Sony's test?	-	<i>No</i> <i>"... [E]vidence insufficient to demonstrate, beyond genuine debate, a reasonable prospect that substantial or commercially significant noninfringing uses were likely to develop over time"</i> ²⁸	<i>Yes</i> <i>"When measured against Sony's underlying evidence and analysis, the evidence now before us shows that Grokster passes Sony's test ..."</i> ²⁹

-- The amount of infringement of the plaintiff's copyrighted material in *Sony* was allegedly well below 10%, whereas in *Grokster* the plaintiffs owned approximately 70-75% of the infringed material.

-- Evidence suggested that Grokster and StreamCast software was overwhelmingly used for purposes of infringement, whereas, in *Sony*, it was found that "[m]ost purchasers used the Betamax principally to engage in time-shifting." *MGM et al.*, 125 S. Ct., at 2784 (Ginsburg, J., concurring) (citing *Sony*).

²⁶ *Id.*, at 2792 (Breyer, J., concurring). According to the Breyer concurring opinion, Justice Ginsburg's conclusions are based on "insufficient evidence in this case of both present lawful uses and of a reasonable prospect that substantial noninfringing uses would develop over time," while the conclusion in *Sony* was based on the "likely existence of a substantial market for authorized copying upon general declarations, such as survey data, and common sense." *Id.*, at 2791.

²⁷ *Id.*, at 2788. In essence, Justice Breyer found that the statements of witnesses, which revealed a number of "authorized" types of files available on the Grokster network, established that Grokster technology was capable of substantial or commercially significant noninfringing uses. Although the volume of noninfringing use may be small ("apparently" 10%), Justice Breyer considered this figure comparable to the purported 9% of "authorized" use of the Betamax in the *Sony* record. Furthermore, he deemed the *Grokster* record to hold sufficient evidence of a "significant future market" for noninfringing uses of Grokster-type peer-to-peer software since the amount of uncopyrighted material available on such networks would grow with time. *Id.*, at 2788-90.

²⁸ *Id.*, at 2786.

²⁹ *Id.*, at 2788.

Grokster et al. liable?	<i>Yes</i> (under “inducement rule”)	<i>Yes</i> (both under “inducement rule” <u>and</u> Sony)	<i>Yes</i> (under “inducement rule,” but <u>not</u> under Sony)
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After all the back-and-forth, where does *Grokster* leave us as far as the *Sony* standard is concerned? In our view, the baseline is that *Grokster* has not changed the *Sony* standard, which was a sound decision on the part of the Court. While the majority opinion avoided revisiting *Sony*, both Justice Ginsburg’s and Justice Breyer’s concurring opinions read *Sony*—as a matter of substantive law—in the same way. “Liability under our jurisprudence,” so Justice Ginsburg, “may be predicated on actively encouraging (or inducing) infringement through specific acts ... or on distributing a product distributees use to infringe copyrights, *if the product is not capable of ‘substantial’ or ‘commercially significant’ noninfringing uses.*”³⁰ Similarly, Justice Breyer defines *Sony* as a test “whether the company’s product is capable of substantial or commercially significant noninfringing uses.”³¹ However, the concurring opinions are evidence that there is significant *disagreement* regarding the question as to when evidence satisfies *Sony*’s test. More precisely, the two concurring opinions suggest a *different level of concrete evidence* that is required to fall under the *Sony* safe harbor. It remains to be seen how this disagreement will play out and what the practical impacts on the safe harbor provided by the *Sony* doctrine will be.³² In the event that the Supreme Court adopts Justice Ginsburg’s approach, putting a heavier evidentiary burden on defendants, there are good reasons to believe that *Sony* would provide less protection for entrepreneurs engaged in the design and distribution of technologies. Indeed, we agree with the analysis³³ that a requirement to provide detailed evidence in order to earn *Sony*’s shelter is likely to increase the copyright holder’s incentive to litigate, while negatively affecting an entrepreneur’s cost-benefit analysis when deciding whether she shall engage in the development, production, or distribution of a new technology vis-à-vis the specter of extensive and expensive trials. This, in turn, would unnecessarily shift the delicate balance “between a copyright holder’s legitimate demand for effective—not merely symbolic—protection of the statutory monopoly, and the rights of others freely to engage in substantially unrelated areas of commerce.”³⁴

2. (Re-)Introducing the Inducement Rule

As discussed above, the Supreme Court disagreed in its *Grokster* ruling with the Ninth Circuit regarding the proper understanding of the limiting effect of the *Sony* rule. In essence, the disagreement boils down to the question under what circumstances a defendant can be liable for contributory infringement even when its actions are taken in connection with a product that is capable of substantial noninfringing uses. The Ninth Circuit took a narrow view of the remaining

³⁰ *Id.*, at 2783 (Citations omitted) (emphasis added).

³¹ *Id.*, at 2789 (Citations omitted).

³² See, e.g., Richard Raysman and Peter Brown, ‘MGM v. Grokster’: Finding Another Theory of Secondary Liability, N.Y. L.J., July 12, 2005 (suggesting the uncertain status of the *Sony* rule due to division within the court regarding the relative balance of infringing and non-infringing uses that would permit a technology to qualify for the *Sony* safe harbor and that changes to the *Sony* rule are possible should the rule need to be applied in a future case).

³³ *MGM et al.*, 125 S. Ct., at 2792 *et seq.* (Breyer, J., concurring).

³⁴ *Sony*, 464 U.S. at 442. See also Richard M. Myrick, Note: *Peer-to-Peer and Substantial Noninfringing Use: Giving the Term “Substantial” Some Meaning*, 12 J. INTELL. PROP. L., Spring 2005, at 539, 559-65 (arguing that the Supreme Court should adopt the Seventh Circuit’s approach).

circumstances under which contributory infringement could be found. The Supreme Court, in contrast, held that “where evidence goes beyond a product’s characteristics or the knowledge that it may be put to infringing uses, and shows statements or actions directed to promoting infringement, *Sony*’s staple-article rule will not preclude liability.”³⁵ Thus, the Supreme Court recognized that active inducement is available as an alternative theory of contributory infringement after *Sony*. As noted above, the *Grokster* court adopted the inducement rule from patent law, from which the *Sony* court also adopted the “capable of substantial noninfringing uses” standard.³⁶ As a result, the Supreme Court synchronized secondary liability under copyright law with patent law to the extent that a demonstration of substantial noninfringing uses is a defense to contributory infringement, but not a defense to liability under the (active) inducement theory.³⁷ Consequently, someone does not earn *Sony*’s safe harbor “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.”³⁸ Such a person is liable for the resulting acts of infringement by third parties whether or not their technology is capable of substantial noninfringing uses.

Although the “inducement rule” was formally adopted in *Grokster*, one can find earlier references to the concept of “inducement” of infringement in the copyright context and with regard to contributory liability. Perhaps the most prominent formulation goes back to the Second Circuit’s decision *Gershwin Publishing Corp. v. Columbia Artists Management, Inc.*³⁹ The *Gershwin* court held that “one who, with knowledge of the infringing activity, *induces*, causes or materially contributes to the infringing conduct of another, may be held liable as a ‘contributory’ infringer.”⁴⁰ Thereafter, the attribution of liability for “inducing,” “causing” or “materially contributing” to infringement seems to have become widespread throughout the nation’s federal courts.⁴¹ The *Sony* court, too—albeit focusing on limitations to contributory liability—made references to liability based on inducement of infringement when distinguishing its own facts from other cases.⁴²

³⁵ *MGM et al.*, 125 S. Ct., at 2779.

³⁶ See 35 U.S.C. § 271(c).

³⁷ As the American Intellectual Property Law Association pointed out in its brief, inducement liability was subsumed under contributory liability in case law prior to the 1952 Patent Act. The 1952 Act codified inducement liability separately from that of contributory liability. *Amicus Curiae* Brief of the American Intellectual Property Law Association, at 16, *Metro-Goldwyn-Mayer Studios Inc., et al. v. Grokster, Ltd., et al.* (Case No. 04-480). See also in particular the reference to the *Henry* case where the defendant was held liable of inducement despite the fact that the product at issue was capable of substantial noninfringing uses. *Id.* at 17.

³⁸ *MGM et al.*, 125 S. Ct., at 2780; see also *id.*, at 2779-80.

³⁹ 443 F.2d 1159 (2d Cir. 1971).

⁴⁰ *Id.*, at 1162 (emphasis added).

⁴¹ See, e.g., *CoStar Group, Inc. v. LoopNet, Inc.*, 373 F.3d 544, 71 U.S.P.Q.2d (BNA) 1096 (4th Cir. 2004); *Broadcast Music, Inc. v. Jeep Sales & Service Co.*, 747 F Supp 1190, 17 USPQ2d 1862 (E.D. Va. 1990); *Alcatel USA, Inc. v. DGI Technologies, Inc.*, 166 F.3d 772, 49 U.S.P.Q.2d (BNA) 1641 (5th Cir. 1999), reh’g and reh’g en banc denied, 180 F.3d 267 (5th Cir. 1999); *Bridgeport Music, Inc. v. Diamond Time, Ltd.*, 371 F.3d 883, 71 U.S.P.Q.2d (BNA) 1193 (6th Cir. 2004); *Playboy Enterprises, Inc. v. Russ Hardenburgh, Inc.*, 982 F. Supp. 503 (N.D. Ohio 1997); *Marobie-Fl, Inc. v. National Ass’n of Fire and Equipment Distributors and Northwest Nexus, Inc.*, 983 F. Supp. 1167, 45 U.S.P.Q.2d (BNA) 1236 (N.D. Ill. 1997); *Burdick v. Koerner*, 988 F. Supp. 1206, 45 U.S.P.Q.2d (BNA) 1887 (E.D. Wis. 1998); *Ellison v. Robertson*, 357 F.3d 1072, 69 U.S.P.Q.2d (BNA) 1616 (9th Cir. 2004).

⁴² *Sony*, 464 U.S. at 438 and 439 (“... [the District Court] found that ‘there was no evidence that any of the copies made by Griffiths or the other individual witnesses in this suit were influenced or encouraged by [Sony’s] advertisements’”) (citing *Sony*, 480 F. Supp. 429, 460 (C.D. Cal. 1979)), (“Sony certainly does not ‘intentionally [induce]’ its customers to make infringing uses of respondents’ copyrights, nor does it supply its products to identified individuals known by it to be engaging in continuing infringement of respondents’ copyrights.”) (citation omitted).

In *Grokster*, the Supreme Court mentioned as prime examples of “active steps ... taken to encourage direct infringement” the advertisement of an infringing use or the instruction how to engage in infringing use, which in turn “show an affirmative intent that the product be used to infringe.” On the other end of the spectrum, the Court emphasized that neither the mere knowledge of infringing potential or of actual infringing uses, nor “ordinary acts incident to product distribution, such as offering customers technical support or product updates, would support liability in themselves, since “[t]he inducement rule ... premises liability on purposeful, culpable expression and conduct...”⁴³

Despite those lines of demarcation, it remains unclear what, exactly, constitutes “inducement” under the *Grokster* standard.⁴⁴ The application of the standard to the facts presented in the case itself indicates that there is an area of uncertainty surrounding the inducement rule.⁴⁵ Beyond the facts of the case, for instance, it remains an open question under what conditions a business model would be considered to effectively induce others to infringe copyright. Similarly, it is unclear what kinds of advertisement would show an affirmative intent that the product be used for infringing uses, or what reasonable steps must be taken to stop people from using the product for infringing uses in order to avoid that the lack of such steps may be regarded as evidence underscoring intentional facilitation of users’ infringements.⁴⁶ Businesses are also left without any clear guidance as to what response to take once they become aware that their products are being put to infringing uses.⁴⁷ This sort of uncertainty may have a negative impact on innovation and digital entrepreneurship, respectively.

Before we move to the discussion of *Grokster*’s impact on the digital ecosystem, however, it is noteworthy that similarly broad and vague inducement standards have been proposed by policymakers and legislators on both sides of the Atlantic.⁴⁸ In the U.S., for instance, the Intentional Inducement of Copyright Infringements Act of 2004 (INDUCE Act),⁴⁹ sponsored by a bipartisan coalition of senators, would enable civil lawsuits by copyright holders against any party that “induces” illegal copying by another. The proposed Act responded to the District Court’s decision in *Grokster*, which stated that a secondary liability theory against P2P

⁴³ *MGM et al.*, 125 S. Ct., at 2780.

⁴⁴ See, e.g., Andrew Deutsch, *File-Swapping Services May Be Liable for Inducing Copyright Infringement*, *Supreme Court Rules*, MONDAQ (June 29, 2005) 2005 WLNR 10370986; David Rae, *IT strategy - Downloadsamoney*, *FINANCIAL DIRECTOR* (July 4, 2005) 2005 WLNR 10486990. But, see generally, *Amicus Curiae* Brief of the American Intellectual Property Law Association, *Metro-Goldwyn-Mayer Studios Inc., et al. v. Grokster, Ltd., et al.* (Case No. 04-480) where the AIPLA lists the elements of inducement in patent law and cites case law applying the inducement rule. One can infer that application of the rule in the copyright context would not be any more difficult or unclear than it has been in the patent context. Yet, in his paper, *Inducing Patent Infringement*, Mark Lemley contends that the case law defining inducement liability within the patent context is far from clear and consistent. Thus, analogy to patent law may offer little guidance for an inducement standard within the copyright context. See generally, Mark Lemley, *Inducing Patent Infringement* (Stanford Public Law and Legal Theory Working Paper Series No. 110, July, 2005), <http://ssrn.com/abstract=772264>.

⁴⁵ As discussed above, the Supreme Court regarded three features of the evidence of intent as particularly important, but at the same time made clear that either of two of them standing alone would not be sufficient to find contributory infringement liability.

⁴⁶ John Palfrey, *The Entrepreneur in a Post-Grokster World*, available at <http://blogs.law.harvard.edu/palfrey/2005/06/27>.

⁴⁷ *Coming to Grips with Grokster*, *BUS. WK.*, July 11, 2005, 2005 WLNR 10640722.

⁴⁸ For an overview of proposed legislation in the digital media context, see Urs Gasser et al., *Copyright and Digital Media in a Post-Napster World*, Version 2, Updated January 2005, available at <http://cyber.law.harvard.edu/media/files/wp2005.pdf> and Urs Gasser, *International Supplement to Copyright and Digital Media in a Post-Napster World*, available via <http://cyber.law.harvard.edu/media/wpsupplement2005>.

⁴⁹ S. 2560, 108th Cong. (2004).

services might be warranted, but “additional legislative guidance may be well-counseled.”⁵⁰ The Ninth Circuit’s affirmation of the decision temporarily increased the support for the INDUCE Act, but it is doubtful whether the bill will make further headway in the aftermath of the Supreme Court’s decision.⁵¹

The Commission of the European Communities, finally, recently presented a proposal for an EU-Directive on criminal measures aimed at ensuring the enforcement of IP rights along with a proposal for a Council Framework Decision to strengthen the criminal law framework to combat IP offences.⁵² The proposal seeks to reduce existing disparities between the EU member states’ systems of penalties that, according to the Commission, “make it difficult to combat counterfeiting and piracy effectively.”⁵³ Article 3 of the proposed Directive requires that member states ensure that all intentional infringements of an intellectual property right on a commercial scale, *and attempting, aiding or abetting and inciting* such infringements, are treated as criminal offences.⁵⁴

For the reasons mentioned above and further discussed in the next section, the broadness and vagueness of this sort of “inducement” standard is highly problematic from the perspective of the entrepreneur – as well as the consumer and the policy-maker – in the digital age.⁵⁵

3. Grokster’s Potential Impact

At first glance, *Grokster* has gone some distance toward clarifying under what circumstances the distributor of a dual-use product can be held secondarily liable for the infringements committed by its users. Against the backdrop of *Grokster*, distributors of dual-use

⁵⁰ Metro-Goldwyn-Mayer Studios Inc., *et al.* v. Grokster, Ltd., *et al.*, 259 F. Supp.2d 1029, 1046 (C.D. Cal., 2003).

⁵¹ For criticism of the Act, see generally, Jason Schultz, *Secondary Liability Under the Copyright Act: Article: The False Origins of the Induce Act*, 32 N. KY. L. REV. 527 (2005) (suggesting that the Act was derived from the dissent in *Sony* and thus represents a departure from *Sony*'s clear safe harbor rule) and Ernest Miller, *Secondary Liability Under The Copyright Act: Article: First Amendment Scrutiny of Expanded*, 32 N. KY. L. REV. 507 (2005) (suggesting that the Act presents First Amendment issues). See also, Jay Dratler, Jr., *Common-Sense (Federal) Common Law Adrift in a Statutory Sea, or Why Grokster was a Unanimous Decision*, (Univ. of Akron School of Law, Public Law & Legal Theory Working Paper Series No. 05-13, Aug., 2005), <http://ssrn.com/abstract=792344> (arguing that the Common Law operates much more effectively in the regulation of technology than do statutory approaches).

⁵² See Bruce Gain, *Europe Follows Grokster's Lead*, WIRED NEWS, available at <http://www.wired.com/news/politics/0,1283,68418,00.html>.

⁵³ Proposal for a European Parliament and Council Directive on criminal measures aimed at ensuring the enforcement of intellectual property rights/ Proposal for a Council Framework Decision to strengthen the criminal law framework to combat intellectual property offences, COM(2005)276 (July 12, 2005), available at http://europa.eu.int/eur-lex/lex/LexUriServ/site/en/com/2005/com2005_0276en01.pdf.

⁵⁴ *Id.* (emphasis added). According to Article 2 of the proposed Framework Decision, member states must punish such offences with a maximum sentence of at least four years' imprisonment if the offence is committed under the aegis of a criminal organization or it carries a health or safety risk. The applicable maximum fine must be at least EUR 300,000 for cases involving criminal organizations or posing a risk to public health and safety, and EUR 100,000 in less serious cases. The proposal allows Member States to apply tougher penalties.

⁵⁵ For further discussion, see, e.g., Urs Gasser, *Draft EU-Directive Sets Forth Criminal Law Provisions Aimed at Fighting IPR Infringements*, available at <http://blogs.law.harvard.edu/ugasser/2005/07/15#a102>, Urs Gasser, *Follow-up on IPR-II Enforcement Directive*, available at <http://blogs.law.harvard.edu/ugasser/2005/07/15#a103>, John Palfrey, *New Proposed EU IPR Directive*, available at <http://blogs.law.harvard.edu/palfrey/2005/07/15#a897>, and Bruce Gain, *Europe Follows Grokster's Lead*, WIRED NEWS, available at <http://www.wired.com/news/politics/0,1283,68418,00.html>.

products have to answer a series of questions in order to determine their liability exposure.⁵⁶ First, they have to determine whether they actively encouraged or promoted infringements by their users. If yes, a distributor can be held liable as a contributory infringer based on the inducement rule adopted in *Grokster*. If not, liability depends on the question whether the distributor has actual knowledge of specific infringements and the capability to stop those infringements. If yes, the distributor is liable when the Ninth Circuit's *Napster* standard applies. If no, the question becomes whether the product is capable of substantial noninfringing uses. If yes, the distributor enjoys *Sony's* safe harbor. If no, however, the distributor is liable as a contributory infringer, because courts will impute the requisite intent to encourage infringement to her.⁵⁷

However, things are less clear when taking a closer look at two specific elements in this algorithm. First, as previously discussed, it remains uncertain what activities will qualify as an "active inducement." Is an advertising slogan like "rip, mix, and burn" for Apple's iPod⁵⁸ already an inducement of copyright infringement as some observers have pointed out?⁵⁹ Or would media outlets run the risk of being held secondarily liable in a case where they direct readers of an online report via link to copyright infringing technology?⁶⁰ It is almost certain that marketing operations will at least be checking in with their general counsel's office before running a provocative advertisement of any sort.

Second, the Supreme Court has not clarified what counts as "substantial noninfringing uses." As discussed above, the majority opinion avoided addressing this question at all, while the two concurring opinions, each joined by three justices, took a different position. Justice Breyer's concurring opinion regarded evidence that showed that roughly 10% of the files shared over the networks were noninfringing as sufficient under *Sony's* "substantial noninfringing use" standard,⁶¹ especially in the light of the fact that there was a "reasonable prospect of expanded legitimate uses over time."⁶² Justice Ginsburg disagreed with this finding. According to the Ginsburg concurring opinion, the record evidence was insufficient to conclude that the software at issue was a product with substantial non-infringing uses. Rather, the software was

⁵⁶ David Post, *The Impact of Grokster*, 27 NATL. L.J. 10, (Aug. 3, 2005), at 10.

⁵⁷ See also, Post, *supra* note 566.

⁵⁸ See, e.g., Press Release, Apple, Apple Presents iPod, at <http://www.apple.com/pr/library/2001/oct/23ipod.html> (October 23, 2001) ("With iPod, Apple has invented a whole new category of digital music player that lets you put your entire music collection in your pocket and listen to it wherever you go," said Steve Jobs, Apple's CEO," and "iPod's revolutionary Auto-Sync feature makes it easy to get your entire music collection into iPod and update it whenever you connect iPod to your Mac.").

⁵⁹ See, Eric Gwinn, *File-sharing Services Can Be Held Liable For Illegal Activities of Clients*, CHI. TRIB., June 28, 2005.

⁶⁰ For such a scenario, see LG München, Decision of March 7, 2005, Az. 21 O 3220/05, available at <http://www.beckmannundnorda.de/linkhaftungpresse.html>, where the online news media outlet, Heise online, was held liable for providing a link to a site which provided illegal software for the copying of CDs and DVDs. For an English account of the case, see *Heise to File Constitutional Complaint Against Hyperlink Ban*, at <http://www.heise.de/english/newsticker/news/63474>.

⁶¹ *MGM et al.*, 125 S. Ct., at 2789 ("That leaves some number of files near 10% that apparently are noninfringing, a figure very similar to the 9% or so of authorized time-shifting uses of the VCR that the Court faced in *Sony*.").

⁶² *Id.*, at 2789. Such legitimate uses included: "swapping of: *research information* (the initial purpose of many peer-to-peer networks); *public domain films* (e.g., those owned by the Prelinger Archive); *historical recordings and digital educational materials* (e.g., those stored on the Internet Archive); *digital photos* (OurPictures, for example, is starting a P2P photo-swapping service); *"shareware" and "freeware"* (e.g., Linux and certain Windows software); *secure licensed music and movie files* (Intent MediaWorks, for example, protects licensed content sent across P2P networks); *news broadcasts past and present* (the BBC Creative Archive lets users "rip, mix and share the BBC"); *user-created audio and video files* (including "podcasts" that may be distributed through P2P software); *and all manner of free "open content" works collected by Creative Commons* (one can search for Creative Commons material on StreamCast). *Id.*, at 2790 (citing other sources).

overwhelmingly used to infringe, infringement was the primary source of revenue from the product, and, according to the Ginsburg opinion, there was no reasonable prospect that commercially significant noninfringing uses were likely to develop over time.⁶³

To sum up, *Grokster* has not clarified the reach of copyright law's existing secondary liability doctrines, but adopted a new one and presented a 3-3 split, with three abstentions, on the question whether *Grokster* was capable of substantial noninfringing uses.⁶⁴ Consequently, there is no such thing as a bright-line rule for technologists to make reliable *ex ante* determinations as to what it means to be too close to the line of secondary copyright liability in the Post-*Grokster* World.

This sort of increased legal uncertainty in a quicksilver technological environment is likely to have chilling effects on innovation and entrepreneurship, respectively, in the future.⁶⁵ Especially the prospect of extended, fact-specific, and costly litigation⁶⁶ through which arguments of the sort sketched above would be tested and that, if successful, would result in statutory damages far in excess of the actual resultant injury to copyright owners,⁶⁷ might discourage potential innovators and investors, causing them to abandon ventures that would have redounded to the benefit of society at large.⁶⁸ How this dynamic will play out is in the hands of the courts that now interpret the *Grokster* decision. In one early read, a federal court in Illinois explicitly cited *Grokster* in rejecting a claim of secondary liability brought against a software developer in a dispute over the use of typeface fonts and which implicated the inducement theory.⁶⁹

Large, established technology players such as producers of consumer electronic equipment might be able to respond to this threat by getting extensive advice from lawyers to assess the *Grokster* prong and *Sony's* test. In contrast, digital entrepreneurs in their garages might not have the resources or incentives to work out the subtle *Grokster* line or to get approval of copyright owners before launching new ventures. This, in turn, would both constrict and slow the flow of new ideas sharply.⁷⁰

⁶³ *Id.*, at 2786.

⁶⁴ See also, Fred von Lohmann, *Remedying Grokster*, July 25, 2005, available at <http://www.eff.org/deeplinks/archives/003833.php#003833>; Post, *supra*, note 56.

⁶⁵ See Brief of Amici Curiae Internet Law Faculty in Support of Respondents, Metro-Goldwyn-Mayer Studios Inc., *et al. v. Grokster, Ltd., et al.* (Case No. 04-480), available at <http://cyber.law.harvard.edu/briefs/groksteramicus.pdf>.

⁶⁶ Especially if the Ginsburg approach, which requires more detailed evidence, would prevail. See, *supra* note 32 and accompanying text.

⁶⁷ Brief of Amici Curiae Internet Law Faculty, *supra* note 65, at 10-11.

⁶⁸ Examples of potentially negative effects on innovative products and services and their further development include Slingbox, a "place-shifting" device that enables TV viewers to route the live TV signal incoming into their homes to a portable device via broadband connection. See Andre Wallenstein, *Slingbox could spark new lawsuits*, THE HOLLYWOOD REPORTER.COM, July 06, 2005, available at http://www.hollywoodreporter.com/thr/article_display.jsp?vnu_content_id=1000973572. Other observers have argued that *Grokster* might put emerging podcasting services such as Apple's podcast service on iTunes Music Store at risk. See Katie Dean, *Grokster May Haunt Podcasting*, Wired New, June 29, 2005, available at <http://www.wired.com/news/digiwood/0,1412,68034,00.html>. See also, Fred von Lohmann, *Post-Grokster Cold Front*, July 6, 2005, available at <http://www.eff.org/deeplinks/archives/003784.php>.

⁶⁹ See *Monotype Imaging, Inc., et al. v. Bitstream, Inc.* Civ. No. 03 C 4349 (N.D. Ill., July 12, 2005) at http://www.phillipsnizer.com/library/cases/lib_case398.cfm. One pending case which may also involve the application of the *Grokster* inducement rule is that brought by Marvel Entertainment against NCSOFT and Cryptic Studios for the design of their online game *City of Heroes*. Marvel charges that the game's character creation engine "facilitates, and indeed, encourages players to create and utilize heroes that are nearly identical in name, appearance and characteristics to characters belonging to Marvel." Daniel Terdiman, *Marvel Battles Role Players*, WIRED NEWS, Nov. 16, 2004, at <http://www.wired.com/news/games/0,2101,65722,00.html>.

⁷⁰ Brief of Amici Curiae Internet Law Faculty, *supra* note 65, at 12.

Last but not least, it remains an open question as to what *Grokster's* impact on the P2P software and file-sharing is. On the one hand, it seems straightforward that the Groksters of this world will avoid advertising messages that suggest infringing uses. The producers of services such as eDonkey, a large P2P service, have begun to make the move away from a free service to a pay-per-use model, which itself may not be a terrible thing.⁷¹ Reportedly, P2P advocates began discussing ways to distribute P2P applications without suggesting intent to induce infringement.⁷² Some argue that the developers of P2P software, many of them sharing values represented by certain elements of the global open source community, are relatively unconcerned about the end uses of their creations and “are motivated primarily by a set of norms that emphasize creative problem solving and contributions to the coding community.”⁷³ Viewed from that angle, it does not come as a surprise that new “closed networks” (also known as “darknets”) like Freenet have started to proliferate—networks, where only individuals get connected who trust each other and that are much more difficult to “police.”⁷⁴ On the other hand, it seems unlikely that *Grokster*—targeting distributors of P2P software—will shape persistent file-sharing norms which even seem to survive legal actions against individual file-sharers.⁷⁵

4. Conclusion

The United States Supreme Court’s *Grokster* decision added *new questions* and has not, as many wished for, eliminated uncertainty with regard to traditional doctrines of secondary liability. These questions at the intersection of law and technology with potential impact on the culture of digital entrepreneurship must ultimately be answered by the lower courts in the months and years to come. In this light, today’s clear winners of the *Grokster* opinion are IP lawyers, while entrepreneurs, consumers, and society at large alike share the risks and costs of chilling effects on innovation.⁷⁶ The true impact of the *Grokster* decision may not be known for decades.

⁷¹ Nate Mook, *P2P Future Darkens as eDonkey Closes*, BETA NEWS, September 28, 2005, available at http://www.betanews.com/article/P2P_Future_Darkens_as_eDonkey_Closes/1127953242

⁷² David Opperbeck, *Peer-to-Peer Networks, Technological Darwinism, and Intellectual Property Reverse Private Attorney General Litigation*, July, 2005, at 33, n. 138 and accompanying text, <http://ssrn.com/abstract=764825>.

⁷³ *Id.*, at 33.

⁷⁴ See, e.g., J.D. LASICA, DARKNET: HOLLYWOOD’S WAR AGAINST THE DIGITAL GENERATION (2005). For an analysis in the aftermath of the *Grokster* ruling, see John Markoff, *New File-Sharing Techniques Are Likely to Test Court Decision*, N. Y. TIMES, August 1, 2005.

⁷⁵ See, e.g., Andrew Parker, *The True Picture of Peer-to-Peer Filesharing*, available at <http://www.cachelogic.com/research/slide1.php>.

⁷⁶ See also John Palfrey, *The Entrepreneur in a Post-Grokster World*, available at <http://blogs.law.harvard.edu/palfrey/2005/06/27>.