

# UNFINISHED BUSINESS: ARE TODAY'S P2P NETWORKS LIABLE FOR COPYRIGHT INFRINGEMENT?

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## ABSTRACT

*In June 2005, the U.S. Supreme Court issued the decision in Metro-Goldwyn-Mayer Studios v. Grokster Ltd., a case that asked whether peer-to-peer networks may be held liable for facilitating the illegal distribution of music over the internet. The music industry petitioned the Supreme Court to settle the disagreement between the circuit courts over the standard of liability for aiding in copyright infringement. The case was based on a clash between the protection of technological innovation and the protection of artistic works. This iBrief examines the circuit split and the Grokster opinion and discusses the questions of liability left unresolved by the Supreme Court. It argues that further clarification of the Sony rule is still needed in order to encourage the proliferation of legitimate peer-to-peer networks by protecting their services while discouraging illegitimate file-sharing activities.*

## INTRODUCTION

¶1 Last spring, the war to curb illegal file-sharing (over eighty-five million copyrighted songs a day) entered a new battleground, this time before the Supreme Court.<sup>2</sup> On December 10, 2004, the Court agreed to hear *Metro-Goldwyn-Mayer Studios v. Grokster Ltd.*<sup>3</sup> This case marked the second time the Court has visited the issue of the secondary liability of a technology manufacturer for copyright infringement; the first decision having been made over twenty years ago.<sup>4</sup> The current dispute centered on whether providers of peer-to-peer networks, who allow the illegal distribution of copyrighted songs and other media over the internet, are

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<sup>2</sup> Linda Greenhouse, *Justices Agree to Hear Case on File Sharing*, N.Y. TIMES, Dec. 11, 2004.

<sup>3</sup> *MGM Studios, Inc. v. Grokster Ltd.*, 380 F.3d 1154 (9th Cir. 2004), cert. granted, 125 S. Ct. 686 (2004).

<sup>4</sup> Elizabeth Miles, Note, *In re Aimster & MGM, Inc. v. Grokster, Ltd.: Peer-to-Peer and the Sony Doctrine*, 19 BERKELEY TECH. L.J. 21, 22 (2004); *Sony Corp. of America, Inc. v. Universal City Studios, Inc.*, 464 U.S. 417 (1984).

liable for the copyright infringement their services enable.<sup>5</sup> Finding that the defendants had no actual or constructive knowledge of infringement, the U.S. District Court for the Central District of California and the United States Court of Appeals for the Ninth Circuit found the service providers were not liable for aiding in illegal copyright infringement.<sup>6</sup>

¶2 The Supreme Court granted a writ of certiorari to resolve the split between the Seventh and Ninth Circuits over the standard of liability for aiding in copyright infringement. The split evolved from differing interpretations of *Sony Corp. v. Universal City Studios*, also known as the *Betamax* case, which has been a guidepost on copyright law to federal courts for the past two decades.<sup>7</sup> In *Betamax*, the Court found the manufacturers of video recorders were not liable for the copyright infringement committed by the user of such equipment.<sup>8</sup> The Court determined that “the sale of copying equipment, like the sale of other articles of commerce, does not constitute contributory infringement if the product is widely used for legitimate, unobjectionable purposes. Indeed, it need merely be capable of substantial noninfringing uses.”<sup>9</sup> Pronouncing that the “question is thus whether the *Betamax* is capable of commercially significant noninfringing uses,” the Court determined that, on the basis of facts presented concerning the actual use of the machine, there were substantial noninfringing uses and thus no liability.<sup>10</sup>

¶3 Over the years, the *Betamax* doctrine has guided lower courts in assessing the potential liability of technology providers for contributory copyright infringement.<sup>11</sup> Yet, as rapidly advancing technology gave rise to novel questions in copyright law, the circuits began to diverge in their interpretation and application of *Betamax*. In 2001, the Ninth Circuit considered the issue of contributory copyright infringement and affirmed Napster’s liability for facilitating the transmission of copyrighted music

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<sup>5</sup> Greenhouse, *supra* note 2.

<sup>6</sup> *MGM Studios Inc. v. Grokster, Ltd.*, 380 F.3d 1154, 1167 (9th Cir. 2004), *affirming* *MGM Studios v. Grokster, Ltd.*, 269 F. Supp. 2d 1213 (C.D. Cal. 2003).

<sup>7</sup> Miles, *supra*, note 4, at 21; *see also* *Sony Corp. v. Universal City Studios*, 464 U.S. 417 (1984).

<sup>8</sup> *Sony*, 464 U.S. at 456.

<sup>9</sup> *Id.* at 442.

<sup>10</sup> *Id.* (finding that “time-shifting,” recording a program in order to view it later, in the home is a legitimate fair use). The Court found there was ample evidence in the record to find that “there are many important producers of national and local television programs who find nothing objectionable about the enlargement in the size of the television audience that results from the practice of time-shifting for private home use. *Id.* at 446.

<sup>11</sup> Miles, *supra* note 4, at 21.

among its users.<sup>12</sup> The Ninth Circuit found that the *Betamax* “substantial noninfringing use” test applied to constructive knowledge, or whether the defendant should have known or had imputed knowledge due to the circumstances, and it was not a bar to liability if it could still be shown that the defendant “knew or had reason to know of its users’ infringement of plaintiff’s copyrights.”<sup>13</sup> The court determined that if a system operator “learns of specific infringing material available on his system and fails to purge such material from the system, the operator knows of and contributes to direct infringement.”<sup>14</sup> The court imposed liability for vicarious infringement because Napster had the ability to control the infringement and benefited financially from it.<sup>15</sup>

¶4 In 2003, the Seventh Circuit introduced a different interpretation of *Betamax*, affirming the decision to shut down the Aimster internet service, which facilitated the sharing of music files over the internet. The court cited Aimster’s failure to demonstrate any “probable” noninfringing uses of the service as imputing knowledge of infringement and evidence of its liability.<sup>16</sup> The court insisted that even when noninfringing uses of a product exist, a service provider must still attempt preventing infringement or “show that it would have been disproportionately costly” to do so.<sup>17</sup>

¶5 This iBrief compares the decisions of the Ninth and Seventh Circuits in the *Napster* and *Aimster* cases and their differing interpretations of the *Betamax* “noninfringing use” standard. This iBrief focuses on the *Grokster* case and whether the Supreme Court’s opinion appropriately resolves the conflict between the Circuits and provides a rule to resolve the tension between artists and innovators. It concludes that while the Supreme Court has ruled in a way that prevents technology providers from intentionally avoiding liability by changing the form but not the substance or function of their services, the liability of providers remains unclear.

## I. THE CIRCUIT SPLIT OVER SECONDARY LIABILITY FOR COPYRIGHT INFRINGEMENT

### A. *Secondary Liability and the Common Law*

¶6 The various standards used to evaluate the liability of peer-to-peer services are all rooted in common, rather than statutory law. The concept of secondary liability for copyright infringement, which holds a second party

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<sup>12</sup> A&M Records, Inc. v. Napster, Inc., 239 F.3d 1004, 1021-22 (9th Cir. 2001).

<sup>13</sup> *Id.* at 1021.

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

<sup>15</sup> *Id.* at 1024.

<sup>16</sup> In re Aimster Copyright Litig., 334 F.3d 643, 653 (7th Cir. 2003).

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

liable for the direct infringement of others, has emerged from the common law tort doctrines of contributory and vicarious liability.<sup>18</sup> Contributory liability requires the tortfeasor to possess knowledge of the infringing act and to participate in the causation of, inducement or material involvement of the act.<sup>19</sup> Vicarious liability requires the actor to profit from the direct infringement of others while possessing the right and ability to control the infringing act.<sup>20</sup>

¶7 As will be discussed below, the Ninth and Seventh Circuits have based liability on different interpretations of these common law doctrines due to the gaps left by the *Betamax* case. These differences remain significant because the Supreme Court in *Grokster* did not harmonize the different interpretations of contributory and vicarious liability, but rather introduced a new “inducement theory” of secondary liability.<sup>21</sup>

### B. *The Betamax Case*

¶8 In 1984, the Supreme Court for the first time addressed the issue of secondary liability for copyright infringement in the *Betamax* case. Expressing reluctance to expand copyright protections without explicit legislative guidance, the Court construed the Copyright Act in light of its ultimate purpose, “to stimulate artistic creativity for the general public good.”<sup>22</sup>

¶9 *Betamax* recognized the existence of liability for contributory copyright infringement after finding that a parallel theory of liability exists for the Patent Act.<sup>23</sup> However, the Court warned that a business that supplies copying equipment “should not be stifled simply because the equipment is used by some individuals to make unauthorized reproductions” of another’s work.<sup>24</sup>

¶10 Consequently, the Court was careful not to create too broad a theory of liability, as imposing contributory liability upon providers inhibits innovation because “every article of commerce may be used for unlawful activities.”<sup>25</sup> Holding manufacturers liable for products that *could* be used

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<sup>18</sup> Miles, *supra* note 4, at 22. See also *MGM Studios Inc. v. Grokster, Ltd.*, 125 S. Ct. 2764, 2776 (2005).

<sup>19</sup> *Grokster*, 125 S. Ct. at 2776.

<sup>20</sup> Miles, *supra* note 4, at 23 (citing *Shapiro, Bernstein & Co. v. H.L. Green Co.*, 316 F.2d 304 (2d Cir. 1963)); see also *Grokster*, 125 S. Ct. at 2776.

<sup>21</sup> *Grokster*, 125 S. Ct. at 2776 n.9.

<sup>22</sup> *Sony*, 464 U.S. at 431-32.

<sup>23</sup> *Id.* at 435; Patent Act, 35 U.S.C. §271(c) (2000).

<sup>24</sup> *Sony*, 464 U.S. at 446.

<sup>25</sup> Lee B. Burgunder, *Reflections on Napster: The Ninth Circuit Takes a Walk on the Wild Side*, 39 AM. BUS. L.J. 683, 685 (2002).

for infringing purposes would eliminate many socially-valuable products from the market because these products would become more expensive as manufacturers accounted for the costs of such liability.<sup>26</sup> Additionally, suppliers have no absolute knowledge of how their products will be used by consumers, nor do they have control over these uses.<sup>27</sup> Nevertheless, if there are no commercially significant noninfringing uses of a product, then the supplier has notice and is liable for contributory infringement.<sup>28</sup>

¶11 Because Betamax is “capable of substantial noninfringing uses,” such as time-shifting, tape-recording a program in order to view it later,<sup>29</sup> the Court held the suppliers were not liable for contributory infringement.<sup>30</sup> Yet, in its concluding words, the Court again cautioned that it was not the Court’s “job to apply laws that have not yet been written” and invited Congress to take a second look at the new technology if a different result was more desirable.<sup>31</sup>

### C. *The Ninth Circuit’s Napster Decision*

¶12 Napster, Inc. developed software that allowed users to share files, mostly of copyrighted music, by making music files stored on one member’s computer available for copying by other users.<sup>32</sup> Napster’s software facilitated the search for music stored on other computers and transferred exact copies of files once they were located.<sup>33</sup> When users connected to the Napster service, the names of their music files were uploaded from their computers to the Napster servers, creating a directory of all files available for transfer to other users.<sup>34</sup> Hence, when a user searched for a file, the Napster servers communicated the location of the music file to the user conducting the search, and the requesting computer used it to establish a connection and download a copy of the music from the source computer.<sup>35</sup> The plaintiffs, A&M Records, who legally record, distribute and sell copyrighted music, sued Napster in California District Court and obtained a preliminary injunction barring the defendants from engaging or aiding others in the copying and distribution of illegal music.<sup>36</sup>

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<sup>26</sup> *Id.*

<sup>27</sup> *Id.*

<sup>28</sup> *See Sony*, 464 U.S. at 442.

<sup>29</sup> *Id.* at 421.

<sup>30</sup> *Id.* at 456.

<sup>31</sup> *Id.*

<sup>32</sup> *A&M Records, Inc. v. Napster, Inc.*, 239 F.3d 1004, 1011-12 (9th Cir. 2001).

<sup>33</sup> *Id.*

<sup>34</sup> *Id.*

<sup>35</sup> *Id.*

<sup>36</sup> *A&M Records, Inc. v. Napster, Inc.*, 114 F. Supp. 2d 896 (N.D. Cal. 2000), *aff’d* 239 F.3d 1004 (9th Cir. 2001).

¶13 On appeal, the Ninth Circuit determined that liability was based on whether Napster, “with knowledge of the infringing activity, induces, causes, or materially contributes to the infringing conduct of another.”<sup>37</sup> Thus, the court limited the application of *Betamax* to circumstances where the defendant is found to have possessed constructive knowledge of infringement. *Betamax*, therefore, does not impose the requisite level of knowledge where the product is “capable of both infringing and ‘substantial noninfringing uses.’”<sup>38</sup> The Ninth Circuit focused on whether the product is “capable of commercially significant noninfringing uses,” and placed less emphasis on the current proportion of infringing uses.<sup>39</sup>

¶14 The Ninth Circuit concluded that knowledge of the existence of infringing material, control over access to it, and a failure to remove the infringing material constitutes contributory infringement when the defendant supplies the services that enable the infringement.<sup>40</sup> The conclusion that Napster *could have* but *chose not to* end the copyright infringement occurring on its network led to the court’s finding of contributory negligence.<sup>41</sup> The Ninth Circuit also imposed vicarious liability upon a finding that Napster did have the ability to control its system, and it received a financial benefit because the infringing material was a “draw” for users.<sup>42</sup>

¶15 The problem left by *Napster* is not that the decision achieved the wrong result, but that the court based liability on notice and capacity to control, thus raising a question as to how the Ninth Circuit doctrine would apply to a service provider who slightly altered their infrastructure to eliminate their control to escape.<sup>43</sup> This ambiguous precedent contributed to the Ninth Circuit’s later problematic ruling in the *Grokster* case.

### D. The Seventh Circuit’s *Aimster* Decision

¶16 The *Aimster* service facilitated file swapping over the internet through software that, like Napster’s software, could be downloaded free of charge and enabled users to communicate with all *Aimster* users, or only with listed “buddies,” in order to exchange files.<sup>44</sup> In responding to a user’s

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<sup>37</sup> *Napster*, 239 F.3d at 1019 (quoting *Gershwin Publ’g Corp. v. Columbia Artists Mgmt., Inc.*, 443 F.2d., 1159, 1162 (2d Cir. 1971)).

<sup>38</sup> *Id.* at 1020 (quoting *Sony Corp. v. Universal City Studios*, 464 U.S. 417, 442 (1984)).

<sup>39</sup> *Id.* at 1021 (quoting *Sony*, 464 U.S. at 442-43) (distinguishing between “current uses” and “capable” uses).

<sup>40</sup> *Id.* at 1022.

<sup>41</sup> *Id.*

<sup>42</sup> *Id.* at 1023-24.

<sup>43</sup> Burgunder, *supra*, note 25, at 707.

<sup>44</sup> *In re Aimster Copyright Litig.*, 334 F.3d 643, 646 (7th Cir. 2003).

search request, Aimster's software would search all users' shared files, which, like Napster, remained on users' computers, and would instruct the source computer to send the requested file to the recipient to download.<sup>45</sup> For a small fee, Aimster users could download the most shared music files more easily than was possible using the free service.<sup>46</sup> The plaintiffs, who were recording industry owners of copyrighted music, sued Aimster in the United States District court for the Northern District of Illinois and were granted a preliminary injunction to stop Aimster from aiding in copyright infringement.<sup>47</sup>

¶17 The Seventh Circuit, in an opinion written by Judge Richard Posner, added a few new twists to the *Betamax* doctrine.<sup>48</sup> Pointing to overwhelming actual examples of copyright infringement, the court switched the burden of production to the defendant to show substantial noninfringing uses of its service and found Aimster liable for contributory infringement when it failed to demonstrate such uses.<sup>49</sup> Judge Posner acknowledged that several noninfringing uses were possible, but "the question is how probable they are."<sup>50</sup> In other words, "[i]t is not enough . . . that a product or service be physically capable . . . of a noninfringing use," rather, there must be evidence that the service "is actually used for the stated non-infringing purposes."<sup>51</sup> Even when such uses are present, the court found that "if the infringing uses are substantial then 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 reduce substantially the infringing uses."<sup>52</sup> The court noted that providers cannot avoid liability by taking reasonable care to change the architecture of their system to provide encryption features because "willful blindness is knowledge," and Aimster's deliberate encryption of files to prevent its knowing what copyrighted files were being exchanged is not a defense.<sup>53</sup>

¶18 Concerning the knowledge element of contributory liability, the Seventh Circuit disagreed with the Ninth Circuit's opinion that "actual

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<sup>45</sup> *Id.*

<sup>46</sup> *Id.*

<sup>47</sup> *In re Aimster Copyright Litig.*, 252 F. Supp.2d 634 (N.D. Ill. 2002), *aff'd*, 334 F.3d 634 (7th Cir. 2003).

<sup>48</sup> Miles, *supra* note 4, at 42.

<sup>49</sup> *Aimster*, 334 F.3d at 652 (finding that Aimster's tutorial, which only used examples of file sharing of copyrighted music, was an invitation to infringement). *See also* Miles, *supra* note 4, at 42.

<sup>50</sup> *Aimster*, 334 F.3d at 653.

<sup>51</sup> *Id.*

<sup>52</sup> *Id.*

<sup>53</sup> *Id.* at 650-51 (holding that service providers cannot create a defense by "using encryption to shield itself from actual knowledge of the unlawful purposes for which its service is being used").

knowledge of specific infringing uses is a sufficient condition for deeming a facilitator a contributory infringer” without examining the proportion of such uses and asserted that such a blanket rule might eliminate socially desirable products.<sup>54</sup> As the Supreme Court had suggested in *Betamax*, such a rule is dangerous because many products could be used for illegal purposes.

## II. THE GROKSTER CASE

### A. *The Ninth Circuit’s Grokster Decision*

#### 1. *Architecture of the Grokster Network and Streamcast*

¶19 The Ninth Circuit found that Grokster and StreamCast were not liable for contributory and vicarious copyright infringement.<sup>55</sup> Grokster and StreamCast freely distributed software that, like Napster and Aimster, allowed users to share computer files.<sup>56</sup> However, the architectures of the defendants’ peer-to-peer networks had important differences from Napster and Aimster, both of which maintained centralized indexes of files and control over them.<sup>57</sup> Both StreamCast and Grokster created decentralized networks to reduce their control over files exchanged using their software.<sup>58</sup> The StreamCast network used a decentralized index, meaning that the index of available files remained on the individual computer’s networks and the software conducted a search request of each index.<sup>59</sup> Grokster also uses a decentralized network with a “supernode” model that provides that select computers in the network are used as indexing servers, and the software provides that search requests are connected to an accessible supernode that then provides the results.<sup>60</sup> Grokster and StreamCast therefore remained unaware of the particular files copied using their software, yet discovery revealed that ninety percent of the available files were copyrighted works.<sup>61</sup>

#### 2. *Applying the Precedent for Liability Set by Napster*

¶20 The Ninth Circuit echoed its initial statements in *Napster* by pronouncing that in order to find the defendants liable for contributory copyright infringement, they must have knowledge of the infringement and

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<sup>54</sup> *Id.* at 649 (stating that defendants in *Sony* did have actual knowledge of infringing activities, and the Ninth Circuit erred in applying *Sony* only to the constructive knowledge element of contributory infringement).

<sup>55</sup> *MGM Studios Inc. v. Grokster, Ltd.*, 380 F.3d 1154, 1157 (9th Cir. 2004).

<sup>56</sup> *Id.* at 1158.

<sup>57</sup> *Id.* at 1159.

<sup>58</sup> *MGM Studios Inc. v. Grokster, Ltd.*, 125 S. Ct. 2764, 2771 (2005).

<sup>59</sup> *Id.*

<sup>60</sup> *Id.*

<sup>61</sup> *Id.* at 2772.

have made a material contribution to the infringement.<sup>62</sup> Applying the *Napster* precedent, the Ninth Circuit explained:

If the product at issue is not capable of substantial or commercially significant noninfringing uses, then the copyright owner need only show that the defendant had constructive knowledge of the infringement. On the other hand, if the product at issue *is* capable of substantial or commercially significant noninfringing uses, then the copyright owner must demonstrate that the defendant had reasonable knowledge of specific infringing files and failed to act on that knowledge to prevent infringement.<sup>63</sup>

¶21 This standard is at odds with the Seventh Circuit's ruling that the product must *actually* be used for substantial noninfringing uses to avoid imputing constructive knowledge to the supplier. The Ninth Circuit declined to follow the Seventh Circuit's narrower interpretation of the *Betamax* doctrine and found that since many capable substantial noninfringing uses were shown, the *Betamax* safe harbor doctrine applied.<sup>64</sup> Observing that the Grokster software was indeed "capable of substantial or commercially significant noninfringing uses," the court determined that the only way left to find the defendants liable was to show that they had "reasonable knowledge of specific infringement."<sup>65</sup>

¶22 The Ninth Circuit found that due to the decentralized nature of Grokster's architecture, any attempt to give the defendants notice to satisfy the "reasonable knowledge" requirement would be "irrelevant" because the notice would arrive at a time when the defendants "do nothing to facilitate, and cannot do anything to stop" the infringement.<sup>66</sup> The court distinguished Grokster from Napster because, while both networks were found *capable* of noninfringing uses, the software design was different.<sup>67</sup> Napster's service employed a centralized set of servers that contained an index list of available files, whereas Grokster and StreamCast used decentralized networks and maintained neither central indexes nor control over index files.<sup>68</sup> If the defendants "closed their doors and deactivated all computers

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<sup>62</sup> *Grokster*, 380 F.3d. at 1160.

<sup>63</sup> *Id.* at 1161 (emphasis added).

<sup>64</sup> *Id.* at 1162, n.9 (concluding that the Seventh Circuit analysis was flawed because it thought a finding of substantial noninfringing uses in the Seventh Circuit would prevent a finding of contributory infringement, regardless of the defendant's level of knowledge).

<sup>65</sup> *Id.* at 1162.

<sup>66</sup> *Id.*

<sup>67</sup> *Id.* at 1163.

<sup>68</sup> *Id.*

within their control, users of their products could continue sharing files with little or no interruption.”<sup>69</sup>

¶23 The Ninth Circuit also found the defendants made no material contribution to the infringement. It observed that unlike the defendants in *Napster*, the defendants in *Grokster* did not possess files, or lists of files, to delete, nor could they control access to their networks, and thus they did not provide the “sites and facilities” to contribute to direct infringement.<sup>70</sup>

### 3. Problems with the Ninth Circuit’s Interpretation of *Betamax*

¶24 The Ninth Circuit found the fact that the defendants could have altered their technology to maintain control and limit infringement irrelevant.<sup>71</sup> Applying the circuit precedent, the court found the defendants not liable due to the architecture of their decentralized systems. The most alarming feature of this result is that “both a party’s level of knowledge of and its right and ability to control infringing activity,” the factors that the Ninth Circuit found the *Grokster* defendants lacked, “are a function of the design of its technology, and of how [a software provider] has defined its legal relationship with end users”<sup>72</sup> and therefore can easily be manipulated by the software providers to avoid liability. The Seventh Circuit’s analysis also would not encounter the problems the Ninth Circuit faced in finding that the defendants had control over their networks. The Seventh Circuit’s approach considers “how the defendant designed the technology and whether it could have made (and could still make) design changes to eliminate or decrease direct infringement.”<sup>73</sup>

### B. The Supreme Court’s Decision: The Inducement Theory

¶25 Faced with the task of clarifying the doctrines of contributory and vicarious liability and whether the substantial noninfringing uses must be probable or just capable, the Supreme Court evaded the issue by applying

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<sup>69</sup> *Id.* (citing *MGM Studios, Inc. v. Grokster, Ltd.*, 259 F.Supp. 2d 1029, 1041 (C.D. Cal. 2003)).

<sup>70</sup> *Id.*

<sup>71</sup> See Brief by Amici Curiae Law Professors in Support of Issuance of Writ of Certiorari at 11, *MGM Studios Inc. v. Grokster, Ltd.*, 125 S. Ct. 2764 (2005) (No. 04-480) [hereinafter “*Professors’ Brief*”] (“The Ninth Circuit . . . views the [Grokster] technology as static—fixed in time and in design”). See also *MGM Studios, Inc. v. Grokster Ltd.*, 380 F.3d 1154 (9th Cir. 2004), *cert. granted*, 73 U.S.L.W. 3247 (U.S. Dec. 10, 2004) (No. 04-480).

<sup>72</sup> *Professors’ Brief* at 15.

<sup>73</sup> *Id.* at 11.

another patent liability rule, the “inducement theory” of liability, in the copyright context.<sup>74</sup>

¶26 The Court recognized that the *Betamax* safe harbor only applied to cases of “constructive knowledge.” Further, the Court found the *Betamax* safe harbor barred a finding of secondary liability based on presuming knowledge and intent to cause infringement solely from the design of a product that is capable of substantial lawful uses, even if the distributor has actual knowledge that the product is used for infringement.<sup>75</sup> However, the Court clarified that when a product is capable of substantial noninfringing uses, this doctrine does not prevent a finding of contributory liability “when an actual purpose to cause infringing use is shown by evidence independent of design and distribution of the product.”<sup>76</sup>

¶27 Similar to inducement in the patent context, the Court pronounced that “one who distributes a device with the object of promoting its use to infringe copyright, as shown by clear expression or other affirmative steps taken to foster infringement, is liable for the resulting acts of infringement by third parties.”<sup>77</sup> “[M]ere knowledge of infringing potential or of actual infringing uses would not be enough here to subject a distributor to liability.”<sup>78</sup> This theory of liability was based on “purposeful, culpable expression and conduct, and thus does nothing to compromise legitimate commerce or discourage innovation having a lawful promise.”<sup>79</sup>

¶28 The Supreme Court observed that the record was replete with evidence demonstrating inducing messages sent to users. StreamCast targeted former Napster users to use its programs and advertisements, and internal communications revealed its unlawful purpose.<sup>80</sup> Grokster also targeted former Napster users and even used metatags to attract users searching for Napster to its website.<sup>81</sup> The Court also noted that neither defendant attempted to filter files or reduce infringing activity and that both profited from the high-volume of infringing uses.<sup>82</sup> In sum, the Court found

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<sup>74</sup> *MGM Studios Inc. v. Grokster, Ltd.*, 125 S. Ct. 2764, 2778-79 (2005) (warning that the Ninth Circuit had adopted an overly broad view of the *Betamax* doctrine, and that the *Betamax* safe harbor only applied to “imputed intent”).

<sup>75</sup> *Id.*

<sup>76</sup> *Id.* at 2778.

<sup>77</sup> *Id.* at 2780.

<sup>78</sup> *Id.*

<sup>79</sup> *Id.*

<sup>80</sup> *Id.* at 2781 (finding evidence that defendant’s purposes were communicated to the public irrelevant because the purpose was unlawful).

<sup>81</sup> *Id.*

<sup>82</sup> *Id.* at 2781-82.

“[t]he unlawful objective is unmistakable” and the defendants were not protected from liability.<sup>83</sup>

### III. UNRESOLVED QUESTIONS AFTER GROKSTER

#### A. *The Unresolved Circuit Split*

¶29 While the Supreme Court noted that the Ninth Circuit erred in its broad application of the *Sony* safe harbor, the Court declined to clarify the *Sony* rule.<sup>84</sup> The Supreme Court did affirm that the *Sony* rule only applies in determining liability based upon “constructive knowledge.”<sup>85</sup> Yet, whether to avoid a finding of constructive knowledge a defendant must demonstrate that its product is *capable* of substantial noninfringing uses, as the Ninth Circuit found, or that substantial noninfringing uses are *probable*, as the Seventh Circuit found, has not been resolved. The Court left “further consideration of the *Sony* rule for a day when that may be required”<sup>86</sup> and noted that *Sony* did not clarify “the question of how much [actual or potential] use is commercially significant.”<sup>87</sup> Instead, the Court found that insufficient evidence was presented to show that there was a “reasonable prospect that substantial or commercially significant noninfringing uses were likely to develop over time.”<sup>88</sup>

#### B. *Existing Problems*

¶30 Another opportunity to clarify the *Betamax* rule may be approaching the Court faster than it wishes. While the inducement rule resolves the problem of distributors who attempt to “turn a blind eye” by altering the structure of their systems to decrease control yet still actively encourage and rely on infringement to profit, it does not clarify liability rules in the situation where inducement is absent. Several problems arise from this ambiguity.

¶31 First, since proving active inducement is enough for liability, copyright litigation will become much more complicated and costly due to more in depth discovery by plaintiffs (including emails, internal documents,

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<sup>83</sup> *Id.* at 2782 (remanding the case for reconsideration of MGM’s motion for summary judgment).

<sup>84</sup> *Id.* at 2779.

<sup>85</sup> *Id.*

<sup>86</sup> *Id.* at 2779.

<sup>87</sup> *Id.* at 2784 (Ginsberg, J., concurring) (citing *Sony Corp. v. Universal City Studios*, 464 U.S. 417, 464 (1984)).

<sup>88</sup> *Id.* at 2786 (Ginsberg concurrence).

and other communications revealing the intent behind every decision made.<sup>89</sup>

¶32 Second, the fate of self-proclaimed well-intentioned programmers and distributors is left unknown. Several programmers are currently developing systems that will make it easier to share digital information anonymously and avoid detection by third parties.<sup>90</sup> For example, some programmers insist that their objective is to create software to benefit society by circumventing censorship and political repression, rather than aiding in copyright infringement.<sup>91</sup> Will the inducement theory of liability leave anyone who posits a lawful goal for their service and who does not encourage infringement free from liability? Certainly not, as constructive knowledge may still be imputed. Yet, unfortunately the standard for imputing constructive knowledge is not certain. If a network is created to and does facilitate the lawful exchange of files, yet it also enables copyright infringement, does liability rest on how *probable* the legal uses are or just that they could occur?

¶33 Congress' rejection of the Induce Act,<sup>92</sup> which would have criminalized distribution of products that enabled infringement, falls in line with the *Betamax* rule that some level of constructive or actual knowledge of the distributor is required.<sup>93</sup> At the other extreme, *Grokster* imposes liability when knowledge and intent to encourage infringement is shown. Yet, it is likely that future defendants may not possess such obvious intent to induce infringement, and the standard for when to impute constructive knowledge remains unclear and will be the subject of ongoing debate.

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<sup>89</sup> Jason Krause, *Grokster Ruling Means Change Supporters Must Rethink Use of File-Sharing Programs*, 4 NO. 26 A.B.A. J. E-REPORT 5 (July 1, 2005). (suggesting that the large amount of time the Supreme Court spent analyzing evidence of internal emails will cause the discovery in copyright litigation to more closely resemble the discovery in securities litigation that examines millions of emails).

<sup>90</sup> John Markoff, *File Sharers Anonymous: Building a Net That's Private*, N.Y. TIMES, August 1, 2005, at C1.

<sup>91</sup> *Id.* (claiming the classic use is for political opponents in China or even the United States, but admitting that copyright infringement is inevitable).

<sup>92</sup> Inducing Infringements of Copyrights Act (Induce Act), S. 2560, 108th Cong. (2004).

<sup>93</sup> See Michael Grebb, *Toe-to-Toe Over Peer-to-Peer*, WIRED NEWS (Oct. 21, 2004); <http://www.wired.com/news/politics/0,1283,65414,00.html>.

### C. Proposed Solution

¶34 As *Grokster* confirms,<sup>94</sup> and as the Seventh Circuit found, the proportion of noninfringing uses must be part of the analysis, otherwise there would be no redress against networks created to facilitate legitimate exchanges, but that were dominated by illegal file swapping. Sanctioning the existence of networks with a majority of illegal files would not only allow them to compete with and make the proliferation of legitimate networks more difficult, but would send the message to users that copyright infringement is acceptable, and even desirable. Such a result could not possibly be the better choice for the public good.

¶35 All distributors could be required to take reasonable care to regulate and prevent illegal file sharing on their networks or face liability, similar to the approach Judge Posner suggested in the Seventh Circuit.<sup>95</sup> Yet, for non-profit programmers seeking to encourage free speech and the sharing of information and ideas, the costs of regulating the networks may be too great to sustain their existence. In this case, regulated profit seeking networks may replace non-profit networks.

### CONCLUSION

¶36 The Supreme Court's recent decision in *Grokster* corrects the Ninth Circuit's misunderstanding of the *Betamax* rule by introducing the inducement theory of secondary copyright liability that holds those actively encouraging infringement liable. However, the failure to clarify the standard for holding liable those defendants lacking an obvious intention to facilitate infringement leaves uninformed those actors who need notice of the law to determine whether to distribute innovations. Until the standard is clarified by Congress or the Supreme Court, the tension between artists and innovators remains unresolved. It is argued that too strict a rule will stifle innovation, but as Gresham's law<sup>96</sup> supports, perhaps a rule crafted by Congress that only applies to peer-to-peer networks and eliminates unregulated networks will not inhibit society's access to information, but simply increase the number of legitimate regulated networks available.

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<sup>94</sup> *MGM Studios Inc. v. Grokster, Ltd.*, 125 S. Ct. 2764, 2786 (2005) (finding defendants' assertions that many noninfringing files, such as works in the public domain, existed was not sufficient to show substantial non-infringing uses were likely to develop).

<sup>95</sup> *In re Aimster Copyright Litig.*, 334 F.3d 643, 653 (7th Cir. 2003).

<sup>96</sup> Gresham's law states that "bad money drives good money out of circulation."