MGM v. Grokster: The U.S. Supreme Court Decision (2005)

On June 27, 2005, nine justices of the Supreme Court agreed, in *MGM v. Grokster*, that the distributors of devices capable of both lawful and unlawful uses are liable for the infringing acts of third parties, where, as shown by clear expression or other affirmative steps, the distributors promote the infringement.

Distinguishing *Sony,* the Court held that secondary liability may be predicated on actively encouraging -- or inducing -- infringement. The Court noted that Grokster and StreamCast, the distributors of peer-to-peer [P2P] software used for widespread infringement of copyrighted audio and video works, were not passive recipients of information about infringing use. Rather, MGM had notified the distributors that 8 million copyrighted files could be obtained using their software and, with minimal effort, the companies could have used their P2P software to determine what content was available on the networks that the software reached. The justices also agreed that the Ninth Circuit had misapplied *Sony*, and vacated the lower court's opinion.

In two concurring opinions, however, Justices Ginsburg (joined by Chief Justice Rehnquist and Justice Kennedy) and Breyer (joined by Justices Stevens and O'Connor) disagreed about whether the *Grokster* facts supported an inducement finding.

Justice Ginsburg concluded that summary judgment was not warranted at the trial level, since there were material factual issues. More significantly, reading *Sony* to require that a court examine how products are currently being used instead of viewing the potential capability of the technology, she concluded that the evidence did not demonstrate any reasonable prospect that substantial noninfringing uses were likely to develop over time, since the P2P software was used overwhelmingly to infringe.

By contrast, Justice Breyer would have upheld the grant of summary judgment, since in his view no facts asserted by MGM in the summary judgment filings would support a different outcome after trial. *Sony* requires that a product "need merely be *capable of* substantial noninfringing uses," and the percentages of noninfringing uses in *Grokster* and *Sony* were comparable: 10% vs. 9%. And although this percentage may prove insufficient over time, there is a significant future market for noninfringing uses of P2P software. Similarly, the *Grokster* and *Sony* records were both based on general declarations, survey data and common sense. Finally, the "capable of" language in *Sony* requires the plausible possibility of a significant future market for noninfringing uses, rather than, as Justice Ginsburg reads the case, a significant current market. The latter reading raises the *Sony* standard of proof.

THE NINTH CIRCUIT MISREADS SONY

The Court held 21 years ago in *Sony* that the manufacturers and distributors of videocassette records [VCRs] were not secondarily liable for the infringing videotaping of the VCR users. Incorporating patent law's "staple article of commerce" doctrine into the copyright regime, the Court concluded that even though Sony knew that the VCRs would be used for infringement, the products were capable of substantial lawful uses. For more than 20 years, this decision has provided a safe harbor for technological innovation. Even under *Sony*, however, there would still be secondary liability for distributing a product that is *incapable* of substantial or commercially significant noninfringing uses.

The Ninth Circuit read *Sony* to mean that the P2P software distributors would be liable as contributory infringers only if they had knowledge of direct infringement and materially contributed to that infringement. Since the P2P software is capable of substantial noninfringing uses, the distributors were not liable for third-party infringement because the companies had no actual knowledge of infringement, based on the decentralized architecture of the software. The companies did not materially contribute to the infringement because they only provided the software, while users performed most actions involving the content. The Ninth Circuit also held that the companies were not vicarious infringers, since they did not monitor or control use of the software, had no right or ability to supervise its use, and had no independent duty to police infringement.

The Supreme Court disagreed with the Ninth Circuit's reading, and distinguished *Sony* from *Grokster* on the basis that Sony, unlike the Grokster distributors, did not induce infringement. Since Sony did not promote infringing uses, its knowledge alone that VCRs would be used to infringe was not actionable, since the VCRs were "*capable* of commercially significant noninfringing uses (emphasis added).

INDUCEMENT AND OTHER THEORIES OF SECONDARY LIABILITY

Because the scope of infringement was too broad to go after direct infringers, the *Grokster* Court observed, the only practical alternative was to pursue the distributors for secondary liability. Such liability is based on long-established common law principles of contributory or vicarious infringement. Contributory infringement predicates liability on inducing or encouraging direct infringement; vicarious infringement requires profiting from direct infringement, while declining to exercise a right to stop or limit the infringement.

Sony still permits secondary liability when an actual purpose to cause infringing use is shown independent of the design and distribution of a product, the Court concluded. In other words, the staple article of commerce doctrine does not displace fault-based liability, based on statements or actions directed to promoting infringement. However, mere knowledge of infringing potential or of actual infringing uses would not be enough to subject a distributor to liability, nor would offering customers technical support or product updates.

Viewed in the context of the entire record, the Court found clear evidence of unlawful inducement, even though any element alone was not sufficient to establish contributory infringement. First, each company showed itself to be aiming to satisfy a known source of demand for copyright infringement -- former Napster users - - indicating a principal, if not exclusive, intent on the part of each company to bring about infringement. StreamCast engineered software that was compatible with Napster and sought to capture Napster users, in the event that the latter was shut down. There was less evidence that Grokster attempted to piggyback on Napster fame, but Grokster's name is a derivative of Napster and Grokster used computer code in its website to capture searchers using the terms "Napster" or "[f]ree file sharing." Second, neither company attempted to develop filtering tools or other mechanisms to diminish the infringing activity using their software, underscoring the intentional facilitation of users' unlawful copying. Third, the companies provided guidance to customers who had specific questions about copyrighted movies they had downloaded. Finally, the business models of both companies showed that their principal objective was to encourage use of their software to download copyrighted works. Both companies generate income by selling advertising space, and as the number of users of each program increases, advertising opportunities become worth more.

On remand, the distributors' liability would be based on a purpose to cause and profit from third-party acts of infringement. Inducement liability would be predicated on statements and actions, rather than presumed or imputed fault.

CONCLUSION

Despite all the sound and fury surrounding the *Grokster* case, the notion of secondary liability founded on encouraging or inducing infringement has long existed in copyright law. As noted by Justice Breyer in his concurrence, *Sony* distinguishes between the creation of technology that *permits* unlawful copying from the acts of *engaging* in (or encouraging) unlawful copying. But commentators expected a *Grokster* analysis considering the many noninfringing uses of P2P software, rather than a fault-based approach focused on the particular actions of Grokster and StreamCast.

And the effect of *Grokster* on *Sony* is not clear. One can say that *Sony* applies to products with substantial noninfringing uses, unless you actively encourage third parties to use your product to infringe, in which case you are liable under *Grokster.* Thus, the argument would go, the Court left *Sony* untouched, even going so far as to decline the invitation of MGM and a number of interested parties filing friend-of-the-court briefs to quantify the necessary substantiality required for noninfringing uses. Moreover, *Grokster* does not hold that P2P software is intrinsically infringing. Rather, the decision focuses on the behavior of Grokster and StreamCast in encouraging users to infringe the copyrighted works of others. Indeed, the *Grokster* Court greatly limits its inducement holding by clarifying that the mere knowledge of infringing potential or of actual infringing uses would not be enough to subject a distributor to liability, nor would offering customers technical support or product updates.

Yet a more nuanced reading underscores that the Court all but ignored any analysis of the noninfringing uses of P2P software under the "staple article of commerce" approach. Instead the Court summarily distinguished *Sony* because the facts there evidenced no inducement. But *Grokster* leaves unanswered a number of fundamentally crucial questions: How do you distinguish between promoting use and promoting infringement, and how does this answer vary depending upon specific knowledge of infringement? Is the distinction based upon advocating the unlawful uses of the product? Is the *potentiality* of a significant market for noninfringing uses replaced by the requirement that such a market *currently exists*? If an innovator does not trigger any of the inducement elements described by the Court, is he safe in selling a product that has substantial noninfringing uses? What is the order of legal analysis: would a court determine first whether a product has substantial noninfringing uses, then focus on the company's behavior in its marketing, customer support and business models? Or would the court not even get to the use analysis, if there is evidence showing that the innovator is encouraging infringing use of his product by third parties? What if the innovator has specific knowledge, but can't do anything to prevent the infringement?

The last question particularly is not a simple one, since the *Grokster* Court warns that "[t]he classic instance of inducement is by advertisement or solicitation that broadcasts a message designed to stimulate others to commit violations, " yet Sony's own advertising encouraged consumers to buy VCRs to "record favorite shows" or "build a library" of recorded programs – almost all of which would be copyrighted by television networks.

Perhaps most importantly, the *Grokster* Court blurs the line between encouraging product use and inducing infringement. The Court found inducement liability through four factors: the software distributors aimed to satisfy a known source of demand for copyright infringement, showing an intent to bring about infringement; neither company attempted to develop filtering tools or other mechanisms to diminish infringing activity; both companies provided guidance to customers about specific infringing downloads; and their respective business models encouraged use of their software to download copyrighted works.

Yet it can be convincingly argued that Justice Breyer's analysis, which more logically focuses on the potential for a viable market in noninfringing uses for the P2P software, is better reasoned than the plurality opinion and Justice Ginsburg's concurrence, and is more consistent with the *Sony* notion of a safe harbor for technological innovation. Instead of focusing on the potential legitimate uses for the software, the *Grokster* Court considers the target audience for mailings and advertising. But would it still constitute inducement, for example, if a record company licensed its content to a software distributor, then the distributor targeted mailings and advertising to former Napster users, hoping to convert them? And as noted in the Ninth Circuit's opinion and in Justice Breyer's concurrence, it is at least an open question whether, given the architecture of P2P systems, filtering is even technologically possible. In addition, how does an entrepreneur distinguish between the permitted offering of technical support or product updates to customers and the forbidden guidance about specific infringing downloads? Don't ask, don't tell? Finally, the *Grokster* facts also support the conclusion that the companies' business models encouraged widespread use of their software -- rather than widespread infringement -- particularly because there are substantial noninfringing uses for the P2P software.