The once-active home page of Internet file-sharing site Grokster has been replaced by a terse message: “The United States Supreme Court unanimously confirmed that using this service to trade copyrighted material is illegal. ... There are legal services for downloading music and movies. This service is not one of them. Grokster hopes to have a safe and legal service available soon.”

The shutting down of Grokster’s downloading service was a result of a settlement in one of the most anticipated copyright cases in decades - MGM Studios Inc. v. Grokster Ltd., 125 S.Ct. 2764 (June 27, 2005), in which the Supreme Court unanimously reversed a decision of the 9th U.S. Circuit Court of Appeals and thus provided some much-needed guidance to federal courts grappling with the application of the doctrine of contributory copyright infringement to emerging technologies.

The Supreme Court decision and Grokster’s ensuing settlement do not end this debate, however, and attorneys handling ensuing copyright infringement cases will likely grapple with many of the same issues argued in Grokster - primarily because the court’s majority opinion adopted an inducement approach to contributory liability, and two concurring opinions provided contrasting views of the Sony decision, thus leaving unanswered many key questions going forward.

In the 1984 Sony ruling, the court defined the parameters for balancing the competing values of supporting creativity (through copyright protection) and promoting technological innovation (by limiting infringement liability), which later would be applied to file-sharing technologies such as Napster, Aimster, Grokster, StreamCast, Kazaa and others. In a 5-4 decision, the court ruled that Sony could not be held contributorily liable for illegal copying of movies and television programming by users of its VCRs, even though Sony was aware that its products could be used to commit copyright infringement.

The court held that knowledge of infringement - an element of the prima facie claim for contributory copyright infringement - could not be imputed...
merely from the sale of products capable of infringement if the products also are capable of substantial non-infringing uses.

In recent years, a number of federal courts have grappled with the proper application of the Sony decision to the emerging technology of peer-to-peer (P2P) networking and file-sharing software. The stakes in these disputes were high. Copyright owners sought to hold the makers and distributors of file-sharing software liable for copyright infringement committed by users of their software, largely on the basis that the software was designed and used to facilitate widespread infringement.

In three decisions, the 9th and 7th Circuits attempted to apply the Sony decision in the file-sharing context. In A&M Records Inc. v. Napster (“Napster I”), 239 F.3d. 1004 (2001), 9th Circuit held that, for products that met Sony’s standard of substantial non-infringing uses, contributory liability requires proof that the defendant (a) had reasonable knowledge of specific infringing conduct, and (b) failed to act to prevent distribution of infringing works.

Two years later, the 7th Circuit adopted a narrower (and more copyright-friendly) interpretation of Sony in In re Aimster Copyright Litigation, 334 F.3d 643 (2003), by determining that court decisions on whether a product or service is capable of substantial non-infringing uses must assess the probability that such non-infringing uses will be made, particularly in light of the extent of illegitimate uses.

Finally, in 2004, the 9th Circuit affirmed the grant of summary judgment in favor of two distributors of popular file-sharing software, Grokster and StreamCast, who had been sued by major motion picture studios, record labels, and individual copyright owners. Both the District Court and the 9th Circuit in MGM v. Grokster emphasized the decentralized architecture of the companies’ software - they maintained no central servers and no login process for end users - as a characteristic distinguishing them from Napster and evidence precluding a finding of contributory infringement.

The courts held that Grokster and StreamCast were merely software distributors. They did not materially contribute to the infringement committed by end users and could not do anything to stop it.

In its majority opinion in Grokster, the court followed the tradition of Sony and once again borrowed a principle of patent law - the inducement rule - and applied it in the copyright context, formulating a theory of secondary liability grounded in “purposeful, culpable expression and conduct.” A distributor of a product may be liable for contributory infringement, the court held, if it takes active steps to promote the product’s use to infringe copyright.

The court reconciled this new rule with the “staple article of commerce” safe harbor introduced in Sony by distinguishing between “imputed intent” (the issue in Sony) and the actual intent involved in an inducement theory of liability. Specifically, the court outlined three main features of Grokster and StreamCast’s business practices that constituted “affirmative steps taken to foster infringement,” and evinced an intent to encourage infringing use by third parties.

Despite recognizing an intent-based form of secondary liability and finding evidence of inducement in Grokster and StreamCast’s business and promotional practices, the court limited the scope of its holding in two important respects that are likely to arise again in future disputes.

First, Justice David Souter’s majority opinion highlighted the fact that internal documents and promotional materials produced by Grokster and StreamCast were unusually explicit in defining their intent to fill the void left by Napster. These “unequivocal indications of unlawful purpose” lent substantial weight to otherwise
circumstantial claims of intent, and included the types of explicit affirmations of intent that likely will not recur in the future among litigation-wary businesses, particularly in the wake of the court’s decision.

In fact, the court expressly noted that under normal circumstances, such “ordinary acts incident to product distribution” would not give rise to liability. As a result, it is unlikely that future parties who may be subject to claims for contributory copyright infringement will leave a sufficient “paper trail” to permit a finding of intentional inducement.

Second, in a footnote, the court asserted that “in the absence of other evidence of intent, a court would be unable to find contributory infringement liability merely based on a failure to take affirmative steps to prevent infringement,” claiming that “such a holding would tread too close to the Sony safe harbor.” Thus, the Grokster majority seemed to take great pains to stop short of imposing an affirmative duty on technology companies to police the use of their products for the benefit of content owners.

In addition to these express limitations on the majority opinion, the fact that the court stopped short of using an imputation of intent to reverse the 9th Circuit is a troubling development for copyright owners. Many copyright owners had hoped the court would rule that P2P and file-sharing technologies were themselves illegal per se and mere “tools of infringement,” or at least would adopt the view that the technology had not reached the threshold level of substantial non-infringing capabilities required for protection under Sony. Instead, the court avoided relying on Sony, and emphasized that inducement would be rooted in an evaluation of “purposeful, culpable expression and conduct” by companies distributing the technology.

In so doing, the majority essentially sidestepped the issue of when, if ever, a technology would fail to exhibit a sufficient potential for substantial non-infringing uses and therefore warrant an imputation of knowledge of infringing intent.

Going forward, attorneys and their clients are likely to continue grappling with the following issues in the wake of Grokster.

- Clear evidence of intentional inducement of infringement cannot be trumped by non-infringing uses. The Supreme Court stressed that “nothing in Sony requires courts to ignore evidence of intent,” and that “a showing that infringement was encouraged overcomes the law’s reluctance to find liability when a defendant merely sells a commercial product suitable for some lawful use.”
- Decentralized peer-to-peer systems may attempt to escape liability by avoiding evidence of intent to induce infringement. By grounding its reversal on issues of inducement and intent, the court essentially left undisturbed the 9th Circuit’s evaluation of Grokster and StreamCast’s liability under a Napster-type conception of contributory infringement. Thus, the 9th Circuit’s determination that the decentralized architectures of Grokster and StreamCast’s software were incapable of providing the “site and facilities” necessary for material contribution to infringement under Napster may remain good law.
- Grokster, then, may serve as a blueprint for a savvy technology company to render itself “liability-proof” by patterning its peer-to-peer system after the diffusive platforms of Grokster or StreamCast.
- There are implications for the attorney-client privilege and attorney work product doctrine. The application of Grokster’s “active inducement” test may warrant additional discovery requests regarding the intent of the technology developer. This presents challenges for attorneys that represent
companies with new devices and/or
technology. Attorneys who wish to
protect their clients from liability,
post-Grokster, must grapple with the
question of whether memos about the
technology itself (including marketing
and business plans) should be written
to counsel for advice and approval so
as to try and invoke the attorney-
client privilege and attorney work
product doctrine.

This would be burdensome and
disruptive to the business decision-
making process itself and could lead to
costly, protracted discovery fights to
determine (on a document-by-document
basis) whether the privilege was
properly asserted. However, this step
may be necessary because there are no
assurances as to how a district court will
apply the active inducement test in the
future.

• Corporate policies regarding the
appropriate, legal use of intellectual
property should be reviewed, revised
and adequately explained to all
employees on a regular basis.
Companies should consider
instituting a sign-off for all employees
to prove their compliance. Because
Grokster’s inducement test will look
to the intent of the alleged infringer,
all policies must clearly state the
company’s respect for the intellectual
property rights of others.

These policies, and documented
evidence of steps taken to ensure
compliance, will be key pieces of
evidence in the defense to any future
copyright infringement claims.

What’s next? In addition to shutting
down its Web site, Grokster has
reportedly agreed to pay the plaintiffs
$50 million as part of the settlement.
This may end Grokster’s involvement in
the copyright infringement debate for
now, but it does not definitively resolve
the issue. Going forward, the true
impact of the ruling will inevitably turn
on how future courts (including the
District Court presiding over what
remains of the Grokster case on
remand) will define inducement,
particularly the amount and types of
evidence courts require as proof of
intent to induce infringement.

For its part, StreamCast has not
indicated any immediate intent to join in
the settlement. Even after the
announcement of Grokster’s decision to
settle, its home page still displayed a
message stating that “StreamCast
Networks Vows to Continue its Fight for
Freedom to Innovate.”

The possibility exists that a jury could
conclude that MGM failed to show
active steps taken by StreamCast to
foster infringement, which might enable
StreamCast to escape liability
altogether. However, the court did stress
that “there is substantial evidence in
MGM’s favor on all elements of
inducement,” and noted that “on
remand, reconsideration of MGM’s
motion for summary judgment will be in
order.”

No doubt the Supreme Court’s strongly
worded holding influenced Grokster’s
decision to settle and will be carefully
weighed by StreamCast, as well as all
future parties engaged in the copyright
infringement debate.

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