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PROTECTING INNOVATION AND ART WHILE PREVENTING PIRACY

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PROTECTING INNOVATION AND ART WHILE PREVENTING PIRACY

THURSDAY, JULY 22, 2004

UNITED STATES SENATE,
COMMITTEE ON THE JUDICIARY,
Washington, DC.

The Committee met, pursuant to notice, at 2:07 p.m., in room SD–226, Dirksen Senate Office Building, Hon. Orrin G. Hatch, Chairman of the Committee, presiding.

Present: Senators Hatch and Leahy.

OPENING STATEMENT OF HON. ORRIN G. HATCH, A U.S. SENATOR FROM THE STATE OF UTAH

Chairman HATCH. Well, we are happy to welcome you all here. At this hearing, leading experts on the intersection of copyright law and technology will share their views on how this Committee can best restore the ability of copyright-holders to challenge the large, for-profit global piracy rings that threaten the future of today's cinema and recording industries.

Research now suggests that these piracy rings will create billions of infringing copies this year alone. The architects of this file-sharing piracy make millions of dollars, while attempting to avoid any personal risk of the severest criminal and civil penalties for copyright infringement.

I think all here today would agree that these pernicious schemes to encourage others—and unfortunately these are mostly kids—to break Federal law allows these pirates to collect huge revenues, while subjecting users to the risk of prison or crippling damage awards.

To implement their schemes, the architects of file-sharing piracy must encourage users to infringe copyrights by either downloading infringing copies of works—an easy task—or by uploading files for distribution to millions of strangers—a more difficult task, with the sole reward being a risk of prosecution.

There can be no doubt that automating redistribution induces mass infringement that would otherwise never occur. The design of some file-sharing software enables its distributors to automate, induce and profit from copyright piracy. Unfortunately, as recent court decisions have made abundantly clear, Congress must act to resolve this situation.

Let me make clear that our aim is to stop the for-profit commercial piracy operations that threaten the future of artists, legal commerce, and all but their most cautious and expert users. I also un-

derscore that our goal is not to subject law-abiding technology interests to undue legal exposure.

To address this problem, Senator Leahy and I introduced S. 2560, the Inducing Infringement of Copyrights Act. The Act provides that the courts can impose secondary liability upon those who intend to induce copyright infringement. We developed this approach with the help and support of leading technology companies. We want to continue to work with interested parties to make refinements that will help us to achieve the bill's intent.

The approach taken in S. 2560 is intended to have three key attributes. First, S. 2560 is technology-neutral. It does not single out peer-to-peer networking technology for punitive regulation just because a few bad actors have misused it.

Secondly, S. 2560 uses a proven model for structuring secondary liability that can address cases of intent to induce infringement that were explicitly not covered or addressed by the Supreme Court in the famous *Sony* v. *Betamax* case.

And, third, it our intent that S. 2560 change the law of contributory liability only for a very narrow class of defendants. It is our expectation that most defendants will never be affected by S. 2560 because they already face broader liability for inducing copyright infringement. Nor do we intend to affect defendants for whom Congress or courts have narrowed the general rule of secondary liability for knowing inducement. It is also our intent that the bill not affect distributors of copying devices who merely know that their devices can be or are being used by others to make infringing copies.

As our hearing today will show, some technology companies have expressed concerns to Senator Leahy and me that claims for intentional inducement might be misused against companies that merely sell copying devices. We do not believe that is the case, but we are willing to enter into a constructive dialogue to ensure that the language is drawn as tightly as possible.

I want to continue working with technology industries to resolve any concerns about possible abuse of liability for intentional inducement. If there are alternative ideas, let's discuss them. Just as the *Sony* court never intended to allow the substantial non-infringing use rule to be misused as a license to enter the copyright piracy business, I don't believe Senator Leahy and I intend to allow S. 2560 to be misused against legitimate distributors of copying devices.

I have a longer statement that I will submit for the record, but this is an important hearing. It involves billions and billions of dollars in the future, and we need to resolve this problem and we would appreciate all the help that each of you can give who are experts in this field and who have particular interests in this field. We will count on you helping us to know how to do this in the very best possible way. Nobody has a desire to hurt anybody by this type of legislation. We just want it to work and to help to preserve all of these interests that deserve to be preserved.

[The prepared statement of Chairman Hatch appears as a submission for the record.]

Chairman HATCH. Senator Leahy, we will turn to you.

STATEMENT OF HON. PATRICK J. LEAHY, A U.S. SENATOR FROM THE STATE OF VERMONT

Senator LEAHY. Thank you, Mr. Chairman. I thank you for holding this hearing today and, of course, thank the witnesses who have come here, who are probably like many in counting the moments for the Congress to get out of town because while most of you, of course, live for these appearances and the days and times of being sent up here, you may actually have things to do, like a life.

I hope you all have a good August. I am willing to show great dedication and am even willing to spend the whole month of August in the State of Vermont, a very difficult assignment, as you can imagine.

I am glad you are here and I am glad we can discuss the Inducing Infringement of Copyrights Act, with legitimately an eye toward moving the legislation in the fall. The issues facing the copyright and technology communities in the digital age are daunting, as so many of you know. And I see so many familiar faces here in all branches of this industry, so you know how daunting it is.

I think Congress has a role in trying to bring the various communities together. Senator Hatch and I recognize that legislating in such an area is going to be tense and intense, certainly from the e-mails I have gotten from many of you telling me that is the case. But we are committed to building the consensus that is the hallmark of successful and useful legislation. We are going to make sure that our commitment results in law.

I am glad to hear from the Register of Copyrights, Marybeth Peters. I think we Americans are fortunate that she is there. She is going to testify about the need for this bill and about how it clarifies longstanding principles of contributory copyright liability without targeting technology. I would encourage other witnesses to study her statement.

Mr. Bainwol says that while technology is not to blame, we need to target those who have hijacked technology and undermined the rights of copyright-holders. I agree. Mr. Holleyman declares that mere knowledge of a given technology's potential to be used to infringe another's copyright should not by itself constitute inducement. I agree, and I wish to offer the Business Software Association my sincere thanks for bringing open-minded cooperation and considerable expertise to the earlier drafting stages of this bill.

I am heartened even by the testimony of those who are skeptical of the bill. Mr. Shapiro says that the *Sony-Betamax* is good law. I agree. Mr. Greenberg and Mr. McGuiness urge Congress to craft our intellectual property laws so that they promote technological growth. I agree, and I believe we have done this with our bill.

Just as Senator Hatch and I have worked to promote the great possibilities of the Internet and the technologies that capitalize on its potential, one problem consistently appears, and I hear this from my State where we use the Internet a great, great deal in commerce, as well as in pleasure. The copyright-holders often fear these very same new and exciting technologies.

We have a lot of people who are in the creative community in my State and their reticence is not without merit. Our copyright industries lose billions of dollars each year to copyright piracy, and just

as importantly our artists lose the rights to their own works. By clarifying the longstanding principle of secondary copyright liability, this bill can give copyright-holders reason to embrace new technologies.

While the legal principle is an old one, the problems of inducement for copyright are a relatively new product of the digital age, an age in which it is easy and, for some, very profitable to induce others to violate copyrights through illegal downloading from the Internet.

The 1976 Copyright Act codified the principle that copyright-holders not only have exclusive rights inherent in their copyrights, but that only they can authorize others to exercise those rights, such as the right to distribute and the right to make copies of their works. Since the advent of the Internet, some have harnessed peer-to-peer technology to run roughshod over those rights.

The courts have grappled, and are still grappling with how to apply existing common law principles to the resulting legal cases. At the same time, the courts are asking the Congress to give guidance. I hope this bill does that by reaffirming Congress' intent in the 1976 Act.

The Patent Code already provides liability for inducing infringement, and our experience there shows us that such provisions work. Over the years, the number of patents has steadily grown and patent-related industries continue to thrive. But while it has long been simple and economically worthwhile to induce patent infringement, only recently has the ability to illegally download music and books and software and films made it necessary for Congress to clarify that the principle also applies to copyrights.

Of course, there are significant differences between patents and copyrights. We are not transplanting one liability regime to another part of the code, but we have learned some useful things in the patent realm and we want to use them.

I apologize for the length of this statement, but I want to make sure everybody understands what we are doing.

In making this clarification, our bill does not undermine the *Sony-Betamax* decision. It does not undermine the fair use doctrine. It does not target or penalize any technology. In fact, our bill will help companies like Apple, who, through their iToons service and iPod devices, offer legitimate alternatives to illegal downloading. I want all these companies to thrive because the competition is going to help consumers. Our bill will protect our copyright-holders. It is going to spur innovation.

Finally, I would like to draw attention to a letter sent by Mr. McGuiness and some others in the consumer electronics industry to the Committee on July 6. It states, quote, "We agree with the need to penalize those who intentionally cause copyright infringement," close quote. Well, that is precisely what 2560 does.

I understand that some have concerns with the specifics of our legislation. Then work with us on these. We are going to have time. No one wants to undermine the iPod or any other piece of technology out there, but we have to understand that some people use peer-to-peer technology in ways that are wrong and illegal. Every single person in this room knows that.

So I appreciate your coming. Mr. Chairman, I appreciate you having this hearing. Give us some ideas. We will work on them. I actually have Internet at my farm house in Vermont. I have mail, but it takes on an average a little over a week to get a letter all the way from Washington to there. I am not sure how it is sent, but I do get e-mail.

Thank you.

Chairman HATCH. Well, thank you, Senator.

Our panels for this hearing are well qualified to assist the Committee in reviewing S. 2560 and any alternative solutions that may be proposed. We are really interested in getting it right, so one great reason for this hearing.

Our first panel consists of one witness, who is more than adequate to take up the role of many witnesses—Marybeth Peters, the Register of Copyrights. She appears today as the Federal Government's leading expert on the interaction of copyright law and technology.

We have always appreciated your appearances before this Committee. You have always been so cooperative and you have really helped us through the years with a lot of these very difficult problems. So we look forward to further help from you today, if we can.

STATEMENT OF MARYBETH PETERS, REGISTER OF COPYRIGHTS, UNITED STATES COPYRIGHT OFFICE, WASHINGTON, D.C.

Ms. PETERS. Mr. Chairman and Senator Leahy, I am pleased to be here. Let me begin by thanking both of you for your leadership and efforts over the past several years in addressing important copyright issues related to our digital environment.

I would like to also congratulate both of you on your exceptional staffs. The Copyright Office is most appreciative of their dedication and hard work.

Today, we are here today to discuss S. 2560, the Intentional Inducement of Copyright Infringements Act, which addresses the most important issue facing our copyright system today—new services that employ peer-to-peer technology create vast global networks of copyright infringement. There should be no question that such services are liable for copyright infringement they encourage and profit from. The Copyright Office supports S. 2560 because it addresses this problem and will hold those services responsible.

The legal controversy here revolves around secondary liability for copyright infringement. For decades, copyright law has recognized that those who encourage and foster infringement can be held liable, just as those who commit infringing acts.

Courts have developed, as you mentioned, two doctrines—contributory infringement and vicarious liability—to address those who help others infringe. These concepts are critical to the effectiveness functioning of copyright because they allow copyright owners to enforce their rights against entities that are involved in the infringement and have the resources and ability to satisfy a judgment or to enter into a license.

In the *Betamax* case, the court analyzed these doctrines in assessing whether the manufacturer of a VCR could be held liable for the infringement committed by its customers. It held that sec-

ondary liability could not be imposed on *Sony* because the VCR is capable of substantial non-infringing uses, namely time-shifting of broadcast television programming, which the court found to be fair use.

Courts have struggled to apply these doctrines and the *Sony* case to peer-to-peer services that have created networks of massive copyright infringement. The early versions of these services, Napster and Aimster, were found liable by the Ninth and Seventh Circuits, but they applied different interpretations of *Sony* and the secondary liability doctrines.

Last year, a California district court found the Morpheus and Grokster services not liable for copyright infringement they encourage, based in large part on the *Sony* decision. I think the Grokster decision is wrong as a matter of copyright law. In my view, the court applied a needlessly cramped and unprecedented interpretation of secondary liability doctrines. As a matter of policy, the decision is flawed.

By letting peer-to-peer services off the hook, the court has left copyright owners with little recourse but to sue individuals for copyright infringement. It would be much more efficient and make much more sense if the companies at the center of these infringements whose businesses depend on infringements were held responsible for it.

S. 2560 would help bring about this result. It makes it clear that when someone intentionally induces another to commit infringement, he will be held liable for that infringement. It recognizes that someone's state of mind often cannot be shown by direct evidence, and therefore it allows a court to look at and examine the conduct of a defendant to determine such intent. The standard is appropriately technology-neutral. It doesn't look at the technology employed. It looks at the action of the defendant in the context of all of the circumstances.

Some have criticized the bill as over-broad. They say it potentially could make someone liable for merely selling a device like a portable music player. In my view, these concerns are unfounded. The bill requires specific intent—a very high standard for state of mind. In my written testimony, I detail facts from peer-to-peer contexts that would constitute evidence of intentional inducement. These go far beyond the mere provision of copying technology.

The current peer-to-peer services make it almost inevitable that users become infringers merely by turning on the software, at which point they immediately become distributors of all they have downloaded, and more. This is essential to their business model. They must attract new users to their networks to increase their advertising revenue. This is clearly evidence of inducement.

Critics of the bill also assert that it would overturn *Sony*. I disagree. By focusing on inducement and the behavior of the defendant, S. 2560 addresses factual circumstances not before the Supreme Court in *Sony* which acknowledge that the defendant did not induce its customers to infringe.

I also reject the comparison between the current peer-to-peer services and a manufacturer of the VCR. If the VCR had been designed so that when a user simply turned it on, all of the programs he had recorded immediately became available to all other VCRs

in the world, I am confident the *Sony* case would have come out the opposite way. While I believe that the bill does not raise the concerns mentioned, if the Committee thinks language clarifying these points would be helpful, the Copyright Office would be pleased to assist you.

Finally, I am concerned that future generations of technology-based pirates may devise a way around this bill. In the future, the Committee may wish to consider additional legislative approaches that will provide guidance to courts in such situations. While the approach taken here is careful and preserves the Supreme Court's decision in *Sony*, to the extent the *Sony* decision is an impediment against enforcement against future companies that enable massive infringements, eventually this Committee may want to look at replacing the *Sony* decision with a more appropriate rule for the digital age, one that better balances effective copyright protection with the development of new technologies. As the Supreme Court noted, copyright protection need not be merely symbolic in the face of new technology.

Thank you.

Chairman HATCH. Well, thank you.

Ms. Peters, as you know, some members of the copyright community are concerned that rights-holders could file abusive or harassing claims for intentional inducement. I want to address those concerns, and given that this type of liability can and should be recognized under existing law, it seems that the legislative process should provide the best means to evaluate and resolve such concerns.

During the August recess, I would like your office, if it can, to assist this Committee in coordinating efforts to identify and resolve potential concerns about potential abuses of domestic and intentional inducement liability.

Could we count on you to help us with that?

Ms. PETERS. Absolutely. I just identified this as the most important question in copyright today. We would be more than happy to assist the Committee in facilitating and bringing about hopefully a result that could work.

Chairman HATCH. I had heard that, so I was just making sure that you would agree to work with us.

Ms. PETERS. We would never say no to you.

Chairman HATCH. Well, that is an interesting comment.

[Laughter.]

Senator LEAHY. It is sort of the attitude of all of the Senators up here.

Chairman HATCH. Don't worry. Your sterling reputation is intact. I just want you to know that.

We will turn to Senator Leahy, if he has any questions.

Senator LEAHY. I am too flustered, Mr. Chairman.

We are delighted, Ms. Peters, that you are here. You have been an enormous help to this Committee. I cannot think of a time that any member of the Committee, either Republican or Democratic, has asked for help from you or your office and hasn't gotten it.

Ms. PETERS. Thank you.

Senator LEAHY. You are the mark of the type of people in our Government that makes our Government work well. I mean that as a compliment. You really are.

Ms. PETERS. Thank you very much.

Senator LEAHY. One of the concerns I have is the failure of the Grokster court to correctly impose secondary liability, as the copyright-holders have had to resort to infringement suits against individuals rather than the companies that encourage and profit from that infringement.

Do you think our Act would be effective in shifting legal attention from the individuals to those companies that are the real cause of infringement?

Ms. PETERS. I certainly would hope so. As I stated, I think that even under existing law today, which doesn't have the intent standard but still has an induce standard, they could get there. But if they don't, yes, this would be an enormous help.

Senator LEAHY. This, I assume, would be a policy that you would prefer to see?

Ms. PETERS. Yes.

Senator LEAHY. You have reminded us that the 1976 Copyright Act included very specific language meant to encourage the free development in the courts of the doctrine of secondary liability for copyright infringement. The 1976 Act makes clear that the holder of a copyright has the exclusive right to authorize anyone else to make use of the rights of a copyright-holder. If technology changes, then the threat posed by the middleman changes, too. In 1976, none of us could have envisioned what is going on.

Does the language of the 1976 Act give the courts the power to address changing situations created by the new technology?

Ms. PETERS. I believe it does, I believe it does.

Senator LEAHY. I have long supported the *Sony* case. It has been a cornerstone of technological growth. I believe because of that, the court wisely created the kind of flexibility that you need for new technology. Obviously, at the time they decided it, they couldn't have seen far enough over the horizon to see what kind of technologies we have.

But your testimony noted that courts have had a hard time applying the *Sony* case to the situation of peer-to-peer networks. The case obviously didn't expressly address the situation we have here where someone intentionally induces another to commit copyright infringement. Some believe we should take this opportunity to codify Betamax.

Should we codify *Sony*, and if we do, are there any dangers to that?

Ms. PETERS. Well, I basically said I thought maybe you might want to look at the future, whether or not the standard that is there was the correct one. Although it worked fine in 1984 when the court decided the case with the VCR, the technology at the time and the use that was made of it, making copies off the air and time-shifting of programming that they otherwise would have gotten, the language "merely capable of substantial non-infringing uses"—and I am underlying the word "capable"—I cannot think of any technology today that doesn't have a "merely capable" aspect of a non-infringing use to it. In fact, it can be specifically designed

to have just one little non-infringing use that is of substance. So I think it would be helpful before codifying it to reexamine it.

Senator LEAHY. Thank you.

I have other questions, Mr. Chairman, but we have a lot of witnesses and I will submit them for the record.

Chairman HATCH. Well, that will be fine.

We want to thank you once again, Ms. Peters, for being here. You have always been so helpful to the Committee and to us personally, and we just really appreciate you.

Ms. PETERS. Okay, thanks very much.

Chairman HATCH. Thanks for taking the time, and we are so glad you agree with us.

Senator LEAHY. He says that to me once every three to 4 years.

Chairman HATCH. Not that often.

[Laughter.]

Chairman HATCH. Thank you again. We really appreciate you coming over.

[The prepared statement of Ms. Peters appears as a submission for the record.]

Chairman HATCH. Our second panel consists of five private sector witnesses who can provide an array of perspectives on solving the file-sharing problem.

Gary Shapiro is the president and CEO of the Consumer Electronics Association, and Chairman of the Home Recording Rights Coalition. Robert Holleyman is the president and CEO of the Business Software Alliance. Andrew Greenberg represents the Institute of Electrical and Electronics Engineers-USA. Kevin McGuiness is the director of NetCoalition, an association of Internet-based companies, including Google and C–NET. Mitch Bainwol is the CEO of the Recording Industry Association of America.

All of them are excellent people who have helped us in the past, and we are really looking forward to getting your advice here today. So if you will take your seats at the table, we would appreciate it.

Mr. Shapiro, we will proceed with you first and then go right across the table.

STATEMENT OF GARY J. SHAPIRO, CHIEF EXECUTIVE OFFICER, CONSUMER ELECTRONIC ASSOCIATION, ARLINGTON, VIRGINIA

Mr. SHAPIRO. Mr. Chairman, Senator Leahy, thank you for holding this hearing. Based on what you said, Chairman Hatch, I guess I represent the law-abiding technology interests. I am president of the Consumer Electronics Association, and I am also Chairman of the Home Recording Rights Coalition. Moreover, my written statement has been endorsed by the Digital Futures Coalition, the Computer and Communications Industry Association, as well as the consumer group Public Knowledge and the Electronic Frontier Foundation. S. 2560 has united the technology industry.

Mr. Chairman, you said that it was developed with the support of leading technology companies. I cannot find one technology company that supports this legislation as it is written. Indeed, companies are extremely concerned about how it could block the introduction of valuable new technology.

This is a very broad bill which targets more than P2P companies. If this bill was the law, Americans would not be able to enjoy many devices, from the VCR to the Tivo, from the iPod to the photocopier. It is even more dangerous because of the age we are entering now. We are entering a growth age in technology. It is an age where consumers can easily create, manipulate and shift content around to different devices they own. Because of this new freedom to create and be your own music and movie producer, we are seeing a renaissance of creativity, of studios at home, of content creation by millions of Americans.

This bill is by far the biggest threat to personal creativity, new technology and innovation in 20 years. I urge you to consider the harm that it will engender. It will certainly unleash litigation over every new development in technology which allows content to be moved from one form to another, from one transmission medium to another.

Twenty years ago, the Supreme Court rejected Hollywood's efforts to have VCRs banned as illegal products. The court sided with innovation. It set forth a clear bright-line standard. A manufacturer is not liable for infringing copyright if the product that they are selling has any commercially significant non-infringing use.

The *Betamax* case is definitely our magna carta. It gave a green light to inventors and venture capitalists, ensuring that they can go forward without the fear of liability. Many of my members did not even exist 20 years ago. We had only 80 members then. Today, we have 1,700 corporations that are in the technology industry thriving today because of the protections offered by the *Betamax* decision.

This bill would reverse and rewind *Betamax*. An intent standard radically shifts the copyright law and voids the Supreme Court's bright-line objective test and replaces it with what is a very subjective test. The concept of inducement under the bill is so broad as to apply not only to innovators who build products, but also to venture capitalists who fund them, and even journalists who write about or review them.

Intel's co-founder, Les Vasquez, pointed this out in an editorial opposing this legislation in yesterday's Wall Street Journal. He said, "The chilling effect that a law like this would have on innovation cannot be underestimated. If this bill is enacted, many new opportunities will migrate outside the United States. Others will never happen." That is why the entire consumer technology industry, Internet portals, financial services companies, telecommunications industry, ISP, venture capitalists and consumer groups, are all concerned about this bill.

We understand and we hear you that you say you did not intend to undermine the *Betamax* holding, but there is no way the Supreme Court objective test and the bill's subjective test can coexist. *Betamax* objectively assesses a product's capabilities. This bill relies on a subjective evaluation going to business and investment records, or on circumstantial evidence on what someone had in mind in bringing a product to market. Unfortunately, there is no way at all that investors can predictably make this determination before they are sued.

The result of this legal uncertainty will be the creation of massive new liability, as innocent products and services are targeted for litigation. Given your leadership on class action reform, we hope you recognize how this subjective standard will invite litigation. Even if a defendant eventually proves that it did not intend to induce infringement, the bill's mandate that intent requires a consideration of all circumstances means that suits will not easily be dismissed on summary judgment. Defendants will be tied up in court and spend massive sums to prove that they did not intend to induce. Consumers will lose as venture capitalists back away, innovation is chilled, and new products never come to market.

Since virtually every American is a copyright-holder, it does not take any imagination at all to see the creative uses the trial bar will put to this broad, new cause of action. Indeed, motion picture studios recently claimed in court that standard features on personal video recorders like Tivo are, quote—and this was in the complaint—"inducements," end of quote, to copyright violation.

Media giants have already challenged lawful technologies such as MP3 players, personal video recorders and the clear play content filtering system. This legislation gives them a deadly new tool to stop any technology at all that they don't like.

Let me give you another example. Recently, a well-funded pornographer sued Visa and Mastercard, accusing them of inducing people to infringe their copyrighted pornographic images by providing online payment systems. This legislation would hand a powerful new statutory weapon for pornographers and others to engage in similar nuisance legislation.

We believe that there is a hard choice. It is called personal responsibility, and it is a better approach than putting product innovation and lawful use in jeopardy. In this Congress, we worked with Congressional staff and the Motion Picture Association to craft legislative history for the ART Act, as provisions in State law that would assure that the use of camcorders in movie theaters could be prosecuted, but not endangering their use or demonstration in homes or retail stores.

Mr. Chairman and Senator Leahy, we share your concerns about commercial piracy and we pledge our cooperation. In return, we hope that you share our conviction that painting a massive liability bull's eye on the technology and venture capital industry is not in our country's interests. Your staff has been very generous with their time and courtesy in soliciting and receiving our views, and we look forward to cooperating with them and with the Committee in the legislative process.

Thank you for giving us this opportunity and listening to our views.

Chairman HATCH. Thank you, Mr. Shapiro. I take it you don't like this bill very much.

[Laughter.]

Mr. SHAPIRO. Well, I held back a little bit. I could keep going if you would like.

Chairman HATCH. I figured you were being your usual laid-back self, I will tell you. But we are very interested in how we can improve the bill and how you can help us to do so. I acknowledge that if your concerns have validity to them, then all of us have to be

concerned about them. So we will look forward to having you help us, but that means positive help because we haven't had much help from the industry people.

Go ahead.

Mr. SHAPIRO. We first saw this bill just a few weeks ago and our responses were very clear and very quick. So here we are.

Chairman HATCH. Well, that is one reason for this hearing.

[The prepared statement of Mr. Shapiro appears as a submission for the record.]

Chairman HATCH. Mr. Holleyman, we will turn to you.

STATEMENT OF ROBERT HOLLEYMAN, PRESIDENT AND CHIEF EXECUTIVE OFFICER, BUSINESS SOFTWARE ALLIANCE, WASHINGTON, D.C.

Mr. HOLLEYMAN. Good afternoon, Mr. Chairman and Senator Leahy. My name is Robert Holleyman. I am president and CEO of the Business Software Alliance. The BSA wishes to commend you, Mr. Chairman and Senator Leahy, for bringing focus to bear on the problem of online piracy of copyrighted materials.

In my testimony this afternoon, I would like to focus on two key points. Number one, piracy is a matter of great concern to BSA member companies, who are themselves often the targets of such illegal activity. BSA believes that many of the best ways to address the problem do not require new laws. Number two, any new law must ensure that it will not encumber the development and distribution of legitimate, innovative technologies.

This Committee has embraced the challenge of crafting a law that deters bad actors without stifling technological advancement. This is not an easy task and we remain committed to working with you to achieve that goal. We believe that new legislation, properly balanced, should be viewed as only one of several elements in finding a solution to the problem of P2P piracy.

First, the BSA believes that the most effective way to address the harm done by operators of illicit P2P networks is through the marketplace by providing consumers with legal alternatives.

Secondly, the Justice Department should prosecute the operators of illicit file-sharing networks under existing laws in appropriate cases. Third, we believe it is also vitally important to educate all Internet users about safe and legal ways to harness the power of this important resource. Finally, technology can play an important role in protecting digital content through secure distribution.

If the Committee determines that legislation is needed, we urge that any new law be properly balanced to avoid unintended consequences for legitimate technology companies. BSA members themselves are the leading developers of computers, software, security and networking technologies. To meet customer needs, these products are designed and intended to be multi-purpose. By their very nature, many of these products are freely programmable and can be modified by the user.

We recognize that you do not mean to impose specific constraints on the design of general purpose technology products or the functions that they include. As noted in your statement, Mr. Chairman, these decisions should be left to the marketplace and engineers.

To make certain this is the case, key elements of existing law and jurisprudence should be spelled out in any legislation. Unfortunately, we realize that certain bad actors intentionally design their services to make piracy almost unavoidable. And to distinguish bad actors from good, we believe that there are five key areas that need to be addressed in specific legislation.

First, it should make clear that technology products used for significant legitimate purposes are not subject to copyright infringement liability. To this end, the bill should state clearly that the Supreme Court's decision in the *Betamax* case is unaffected.

Second, it should be made clear that to meet the required intent standard, an actor must be shown to have engaged in conscious, recurring, persistent and deliberate acts demonstrated to have caused another person to commit infringement.

Third, the language should state explicitly that the mere knowledge by a technology provider of the infringing acts of another person does not demonstrate intent to induce copyright infringement.

Fourth, it should be made clear that the bill does not create liability based on advertising or providing support to users. This language should cover manual or handbooks, as well as providing assistance for using products through a company's online help system or telephone help services. Lastly, a mechanism needs to be included to effectively deter weak, harassing or frivolous lawsuits.

Today's solutions must leave intact the important contributions computing technologies bring to our daily lives and allow these technologies to make even greater contributions in the future.

Mr. Chairman, we commend you, Senator Leahy and the members of this Committee for your substantial long-term commitment to combatting piracy. We fully support your efforts. We look forward to working with you as you continue to address piracy challenges, while preserving an environment in which BSA members and all technology companies can continue to innovate, which is what they do best.

Thank you very much.

[The prepared statement of Mr. Holleyman appears as a submission for the record.]

Chairman HATCH. Well, thank you, Mr. Holleyman.

Mr. Greenberg, we will take your testimony.

STATEMENT OF ANDREW C. GREENBERG, VICE CHAIRMAN, INTELLECTUAL PROPERTY COMMITTEE, INSTITUTE OF ELECTRICAL AND ELECTRONICS ENGINEERS-UNITED STATES OF AMERICA, WASHINGTON, D.C.

Mr. GREENBERG. Mr. Chairman, Senator Leahy, I must say I stand in awe of anyone, to paraphrase *Sony*, who has the mere capacity to make the Register of Copyrights blush.

Chairman HATCH. I do that with regularity, I want to tell you. [Laughter.]

Mr. GREENBERG. IEEE–USA advances the public good and promotes the careers and public policy interests of more than 225,000 technology professionals who are its U.S. members. I should add that I also have a personal interest in this bill. I am not only an intellectual property lawyer, but also a software engineer who created the Wizardry series and other computer games.

We engineers are on the front line of the copyright system. We create copyrighted content, as well as the technology to create and deliver that content. While other witnesses today will give eloquent accounts of their constituents' interests, we are here to stand for the proposition that our intellectual property framework must be about the balancing of those interests.

We have significant concern that neither the status quo nor Senate 2560, as written, adequately balances those interests today. This is why we have proposed a substitute that should achieve the aims of the bill's supporters while maintaining that balance.

We are mindful that new technologies may be misused to infringe a copyrighted work, and some will promote that to their own benefit. At the same time, we are concerned that the Copyright Act must not be changed in ways that would inhibit research and novel technologies before their social value can be fully demonstrated.

IEEE–USA believes that copyright owners must not be permitted to restrict the sale of technology having non-infringing uses unless the seller has independently and actively induced a copyright infringement. In Senate 2560 as introduced, the proposed definition of intentional inducement represents a significant and perhaps unbalanced departure from standard secondary liability principles. It creates a practical uncertainty over the law's scope and application that may well chill innovation.

In any case, using untested standards for determining inducement instead of, for example, the well-tested standards of inducement under the Patent Act could have far-reaching and unintended consequences. Imagine a vendor who is sued by a content company after selling a technology known to have both infringing and non-infringing uses. We find it difficult to imagine how, under Senate 2560 as drafted, the defendant could ever prevail in a motion to dismiss or summary judgment.

It is unclear whether the court would have achieved the same result in the *Sony* case under this rule. For nascent technologies, such uncertainty is the practical equivalent of a rule barring innovation. Copyright inducement applies to all copyrighted works and all technologies, and not just to file-sharing. Our members create and use hardware and software tools that create, tools that adapt, and tools that modify hardware designs, programs and content.

Virtually every general-purpose computer and technology tool has features that manipulate, control and display content, including copyrighted content. Reuse and reverse-engineering are not dirty words to us; they are terms of art for essential engineering paradigms. And after 2560, each could be potential sources of copyright infringement.

Whatever the test for secondary liability is used, those tests should be simple, clear, predictable and objective. Our proposal codifies *Sony* and provides express definitions drawn from existing law, well-tested for contribution, vicarious liability and inducement. It makes clear that ordinary marketing of a technology having non-infringing uses is never in and of itself an actionable inducement.

We offer our substitute proposal to illustrate how a more balanced framework has been achieved in the past and how this might be applied in the case of copyright. Even so, we recognize that this

is a very difficult problem that requires careful and comprehensive deliberation before we step off into the new and untrodden ground.

Mr. Chairman, you are the guardians and the architects of the balance that is built into the Copyright Act. Should you determine it needs rebuilding, we respectfully suggest that you measure twice and cut once.

[The prepared statement of Mr. Greenberg appears as a submission for the record.]

Chairman HATCH. This is a very interesting hearing, is all I can say. It is great.

[Laughter.]

Chairman HATCH. Mr. McGuiness, we are happy to welcome you back to the Committee and to the Senate. We appreciate all the service you have given in the past.

STATEMENT OF KEVIN S. MCGUINESS, EXECUTIVE DIRECTOR, NETCOALITION, WASHINGTON, D.C.

Mr. MCGUINESS. Thank you, Senator, and it is very different, after working for you all those years and having the opportunity to sit behind you for over a decade, to now sit down here. I clearly have a much different perspective of this process.

Chairman HATCH. I can hardly wait to get that.

Mr. MCGUINESS. Off to the traditional role already.

Senator Hatch, Senator Leahy, my name is Kevin McGuiness. I am the executive director of NetCoalition, and on behalf of my organization and other interested parties in the Internet community, thank you for holding today's hearing and providing us the opportunity to testify.

I would like to make four general points, if I could. First, the members of NetCoalition agree with the intent behind the legislation to ensure that copyright owners can seek relief from those who unlawfully download and distribute their creative work. As creative people in our own right, we fully appreciate the emotional anguish and economic consequences when one's work is misappropriated.

Second, it is important to remember when discussing proposals to restrict or ban online copying that the Internet is basically one big copying machine. Consequently, any legislative proposal such as the one before us today which would regulate or prohibit copying hardware devices or software, unless fashioned extremely carefully, can jeopardize the essential architecture of the Internet.

Consider, if you would, the following hypothetical example. Let's assume, Chairman Hatch and Senator Leahy, that you were back in the private sector. Let's assume that the next Bill Gates walks into your office. He has developed a new form of instant messaging that automatically transfers audio and video. He believes most people will use his product lawfully, but realizes some might use it to download copyrighted content, and he asks you whether he will be sued if he goes to market.

Under current law, you could tell him with great confidence to go innovate. Because of the *Betamax* decision, he has nothing to fear, since his product is capable of substantial non-infringing uses. You can also indicate that if he does get sued, in all probability he can quickly have that suit dismissed.

If S. 2560 is enacted, however, you would have to give a much different answer. The bill allows any copyright-holder to sue him, or literally anyone associated with his product, for an intentional inducement. There is no exception for products capable of substantial non-infringing use. There is no requirement that a plaintiff demonstrate that there were active steps beyond the sale or manufacture to encourage direct infringement. There will be no quick dismissal. The case will undoubtedly go to trial and he will be cross-examined about his state of mind when developing his technology.

Instead of financing his invention, he will need to finance his legal defense. In fact, the only way he could accurately determine the extent of his legal vulnerability would probably be to meet in advance with the lawyers at Warner and EMI or Death Row to see how they feel about his product. And if he somehow survives the recording industry, he would then have to meet with the lawyers at Paramount and Universal and Disney, and so on.

Third, the legislation really puts the entertainment industry in a very enviable legal position. Since the bill allows them to sue anyone they assert is aiding, abetting, procuring or inducing, the potential pool of targets could include venture capitalists, credit card companies, common carriers, even entities providing nothing more than editorial reviews of products. If the entertainment industry gains this kind of leverage over domestic technologies, online innovation undoubtedly will travel to more hospitable environments overseas.

Fourth, Mr. Chairman, we suggest that the Committee may want to consider along the lines of the testimony already given the following principles as it considers whether or not new legislation is needed or how it should be fashioned.

First, the legislation must codify the Supreme Court's ruling in *Betamax*, as well as protections afforded under patent law. Second, the legislation should target unlawful behavior, not platforms or technologies. Third, the legislation must provide a bright line between lawful and unlawful conduct which is absolutely critical for the next generation of innovation. Finally, the legislation should ensure that entities that provide product reviews that simply demonstrate how a product can be used are not swept into the scope of possible defendants.

Mr. Chairman, Senator Leahy, throughout your careers you have been extremely sensitive to the needs of both the online world and the entertainment community. Consequently, I hope you will agree with us that this issue will never be resolved satisfactorily if the solution does nothing more than forces one to choose between the creative community and the tech community.

The members of NetCoalition stand ready to work with you and the other members of the Committee to find the right solution, one that prohibits unlawful online copying without putting at risk the promise and potential of the Internet.

Thank you.

[The prepared statement of Mr. McGuiness appears as a submission for the record.]

Chairman HATCH. Well, thank you, Mr. McGuiness.

Mr. Bainwol, we will take your testimony.

STATEMENT OF MITCH BAINWOL, CHAIRMAN AND CHIEF EXECUTIVE OFFICER, RECORDING INDUSTRY ASSOCIATION OF AMERICA, WASHINGTON, D.C.

Mr. BAINWOL. I am Mitch Bainwol, the CEO of the RIAA. Let me start by saying—

Chairman HATCH. You are supposed to hold up your end. This other end has been—

Mr. BAINWOL. I want to say that I appreciate the staff's humor putting Bainwol on the far left and Shapiro on the far right.

[Laughter.]

Mr. BAINWOL. My testimony today reflects the uniform view of the American music community—labels, artists, songwriters and publishers, from pop, country, Latin, gospel, from Hollywood to Motown to Nashville to the Big Apple. We are united, and we are united because the U.S. music family has been decimated by piracy, with online piracy by way of file-sharing on peer-to-peer networks, otherwise known as P2P, the most significant source of our economic decline.

From the advent of the first illegal P2P service in 1999 through last year, our sales plummeted by more than 30 percent. Our concern is not academic. The consequence: thousands of job losses and slashed artist rosters at record labels, both majors and indies. Fewer artists are finding the venture capital necessary to finance their dreams. The richness of their art is lost forever.

The scope of the P2P problem is mind-boggling: about a billion downloads—that is billion with a "b"—every month. Four of the top ten applications on the Internet are P2P programs, popular for sure, but law-breaking nonetheless. Some say P2P has great potential. We don't disagree. That is one of the reasons we were pleased with the IMAX settlement announced earlier this week.

But let's strip out the technological mumbo-jumbo and the rationalizing rhetoric, and instead look at the facts. Ninety-seven percent of the transactions on the P2P networks currently are the taking of property created by artists in this country and developed and financed by our member companies—97 percent.

These P2P services hide behind the veil of technology, but it is easy to pierce that veil and see their scam, and a scam it is. They make money by selling advertising and bundling other software, including spyware, in with their applications. They use our music as a lure to draw eyeballs and to pad their advertising profits. Consumers come to share so-called free music.

The P2P companies don't pay for that music. Instead, they provide a mechanism for high-tech theft. They offload the liability on American kids. They provide nothing remotely close to conspicuous warnings about the law. They make a total mockery of property rights. They thumb their nose at this Congress and they laugh all the way to the bank. In short—and this is important—their business model is predicated on the taking of property. There is nothing legitimate about it at all.

Along the way, in addition to inducing kids to break the law, these P2P companies provide havens for pornographers to inject their filth into homes. They compromise computer security and they facilitate unintended disclosure of personal information—tax, medical and other records. No objective review of these services can

possibly conclude that they have any pretense of legitimacy. These networks don't compensate artists or songwriters or the labels. They don't invest in new art. They are technological parasites.

My industry continued to sue users, many of them kids, to establish deterrence and to educate the public. The lawsuits have had phenomenal education value. But the real villains are not the kids. The villains are these profiteers who are gaming the gap in American law. Wouldn't it be better to put these bad actors in the vise of the law? Isn't it time to stand up for the fundamental American value of property?

That is exactly what your bill does, and we commend you both, Senator Hatch and Senator Leahy, and the leaders of the parties, Senators Frist and Daschle, and Senator Boxer and Senator Graham, for introducing this bill. You have properly focused the spotlight exactly where it needs to be placed on the bad actors that hijacked neutral technology.

Even the critics of the bill, who I believe are more worried than necessary about the reach, note that they concur with the fundamental objective underlying this legislation. They wrote, quote, "We agree with the need to penalize those who intentionally cause copyright infringement." I have got to say that again: "We agree with the need to penalize those who intentionally cause copyright infringement." And so you should.

There is a canyon separating the behavior of good companies like Apple and other legitimate businesses from the behavior of the likes of Kazaa. I love the iPod. I have got one. Mine holds my entire family's CD collection. When I bought it, I ripped off the sticker that says "don't steal music." I ripped all my CDs into the hard drive and downloaded it. It is part of our life. It is great.

But there is a huge difference between my iPod and the P2P services like Kazaa. Apple doesn't intentionally induce people to steal, even though people can put stolen music on the iPod, and it doesn't depend on infringement to thrive or even to survive. Looking at all the evidence, I can't imagine a reasonable person concluding that Apple intentionally induces infringement.

Kazaa, like the other major P2Ps, is a totally different story. If you use the product as designed, you are infringing. The default is rigged so that the user automatically uploads to millions of people. We use their instant messaging function to try to alert users to infringement. They turn the function off. We try to frustrate the system with dummy files; they try to filter them out.

The bottom line: You take away infringement and the business model of Kazaa and these other nefarious actors collapses. There is nothing to it once you take out the infringement. That, Senators, is the critical difference.

Some have suggested that the language of the bill may be too broad. I don't think it is, though you and your staff can make a better assessment of that. But if the bill is deemed to be too broad, let's not let a technical question about definition derail a vitally important and overdue effort to give our community a chance for a robust future.

We are suffering harm. The source of that harm has been pinpointed and now it is time for Congress to give us the tools necessary to defend our property rights. Let's find a way to get to

"yes." We will commit to that process. Let's not find a way and excuses to get to "no."

We thank you for your interest and for holding this hearing.

[The prepared statement of Mr. Bainwol appears as a submission for the record.]

Chairman HATCH. Well, thank you. I think all of you have done a good job in expressing yourselves about your respective opinions here.

Let me start with you, Mr. Shapiro. You are on record as saying you are deeply concerned about copyright piracy. Yet, I really can't recall a single instance when you have been before this Committee that you haven't vigorously opposed legislation to address this problem. I also recall months ago you filed a brief telling the Ninth Circuit Court of Appeals that only Congress and this Committee have the institutional competence to adjust the standards for contributory liability in order to address the problems of file-sharing networks.

Now, I guess my question is what have you done since then to help this Committee identify the best way to address this serious problem. I would like to have that great mind of yours helping us on this problem rather than just criticizing. I don't mind the criticism. I think that is legitimate to be able to criticize, but I would like some substantive suggestions on how we change this bill so that it meets the concerns that you have, if they are truly worthwhile concerns.

Mr. SHAPIRO. I think your very question actually makes the point on the induce bill. When we filed that brief, we didn't intend to induce you into introducing legislation like this, but yet somehow it is read as that.

Chairman HATCH. We didn't read it that way either.

Mr. SHAPIRO. We filed the brief as a neutral party and we were just saying this is the *Sony-Betamax* doctrine and we hope you apply it. Indeed, if you read the actual court order in that case—and I am questioning the need for this legislation, as well, and here is why. There are three cases that are at issue here. Two of them have been decided exactly the way the RIAA wanted them to be. The third one is now on appeal and it hasn't been ruled on.

The district court judge said to the content owners who brought the lawsuit in his order sending it up for emergency appeal that they refused to address the controlling law in the *Betamax* case. I am not sure they litigated that case right, but let's see what the Ninth Circuit says. What is the rush? So far, the *Sony-Betamax* case has served well for at least two out of three, and a third is still on appeal.

In terms of what we have done, as I said in my testimony, we were up here with the MPAA on the ART Act coming to a very reasonable, clear compromise. We worked on the Home Recording Act. We are very reluctant, obviously, to have technology restricted because we don't know the ramifications for the future, but sometimes it is necessary and it should be extremely narrow; it should be clear. The rights and responsibilities must be laid out and it must be a clear and compelling reason that benefits both the content owners and the technology community.

What we have here is a frontal attack on the technology community, and that is how it is being taken. It was surprising to hear the Register of Copyrights and others who don't have to counsel people as to whether to introduce products and don't have to put their money at risk as to whether or not they go forward with something.

We have the most exciting, dynamic technology economy in the world and we are producing a phenomenal array of new products and there is a lot more coming. The uncertainty of going to an induce standard of intent is so chilling and so broad that the ramifications—I have never seen a response to legislation like this in three weeks.

When we had Senator Hollings's legislation a couple of years ago, it took almost 8 months before the technology community responded even half as much. Here, there is a real response and the reason is because when you go to someone's intent, especially a company, it is a long, lengthy, expensive lawsuit which especially the smallest companies will definitely avoid.

So, first, is there a problem? I don't know if there is a problem. I do know that there are at least two studies out there which say that music industry sales benefit from P2P, including one by Harvard, and also one by Forester. I do know I have heard the music industry say they can't compete with free. Well, you know, someone does compete with free, and although I heard that you represent the entire music industry, the fact is that there are literally thousands of artists that want to have their products on P2P sharing and they are doing very well from it, and it drives people to sharing.

The way I look at this time in history is it is the same time as when we were shifting from the horse and buggy to the car. Now, if the horse and buggy industry was as powerful as the content industry, I suspect we would still be behind horses now. We wouldn't have gone to automobiles.

We have shifted dramatically in technology as a country, and every new technology that has come along has been opposed by the content community and they have been wrong every time. So I don't know if the harm has been proven yet. I know there is a lot of downloading. I know that every download is equated to a lost sale, and I think that is mistaken. I think BSA's consultant was quoted in the New York Times this week as saying, well, yes, there is a ten-fold exaggeration there in terms of piracy because not every download and not every copy is a lost sale.

So I think the copyright balance has shifted so much in favor of the copyright community that we are off kilter. As Professor Lessig has pointed out, the penalty for stealing for a CD—when you take a CD from a store and steal it, it is almost nothing compared to the penalty for downloading that CD; it is 10 or 25 times as much. Intellectual property used to be less than real property, and somehow now it is much more than real property. And I think the balance is out of kilter.

But, yes, we oppose commercial piracy, and we have supported every statutory increase in the penalties. But the balance is so out of kilter that we have to put our foot down and say this is not the right approach.

Chairman HATCH. Well, you are pushing me back to blowing up their sets, you know. I had more e-mails on that than any other thing I have ever said, and I was just joking. You should see when I get serious.

Let me just ask you to review this quote.

Senator LEAHY. You mean you are really going to blow them up now?

Chairman HATCH. Sure. He wants the privilege of expanding technology. That may be where we are headed. You never know. Again, I am just being humorous, I hope.

Let me just have you review this quote from Nikki Hemming, the CEO of Sharman Networks, and please assume, as I do, that Kazaa is capable of substantial non-infringing uses and that this quote shows that Kazaa was redesigned to help infringing users avoid spoofed files that the recording industry places to thwart infringing uses of Kazaa.

It basically says, "We have given users better opinions and more tools than ever before," said Sharman Networks CEO Nikki Hemming, "including an option to filter bogus music and video files designed to help users avoid misnamed or incomplete files that may have been uploaded by record labels and copyright owners trying to frustrate file-sharing."

Now, do you believe that *Sony* presently allowed Sharman to avoid liability for redesigning its product to facilitate its infringing use by showing that it is still capable of a substantial non-infringing use?

Mr. SHAPIRO. Well, I certainly applaud the RIAA and the recording industry for going forward and trying an approach like that. It makes perfect sense to me. It is a free marketplace.

Again, there have been three courts that have looked at these issues. Two have come out exactly the way the music industry wanted and one court is still under consideration. I don't think that has gone to court yet. I am not a judge and I am not going to pretend I know all the facts of what else they are used for. I do know that even with that *Sony-Betamax* standard, which the Register of Copyrights wants changed, two of those services have been held to be illegal. It is possible that that one would be held illegal as well.

Chairman HATCH. Well, let me reframe the question as a pure hypothetical. Maybe I can do that. Suppose I were shown that the distributor of a copyrighted device had redesigned that device specifically to facilitate and encourage clearly infringing uses of the device. Now, based on existing law as you interpret it, could that distributor avoid liability by showing that the copying device redesigned to facilitate infringing uses was still capable of substantial non-infringing uses?

Mr. SHAPIRO. It goes to the facts of the case. Again, there have been two courts which have held that those types of similar products are illegal under the *Sony-Betamax* standard. I would imagine in that case, it is possible as well, but that is why the *Sony-Betamax* standard is good. It has worked in at least two out of three instances, and the third one is still under review.

Chairman HATCH. Well, let me go to Mr. Bainwol.

Mr. Bainwol, there are concerns that the recording industry would bring claims under S. 2560, broad claims against any party

that might distribute copying devices that might be used to infringe.

Do you believe that this Act lets you sue distributors of portable MP3 players, CD burners or personal video recorders simply because those devices can be used to infringe?

Mr. BAINWOL. The short answer is no. I am not an attorney. My mom wishes I was, but I am not. As I read the bill, it seems very highly targeted, and I think everybody here that is criticizing the bill ought to go ahead and read the thing. "Nothing in this subsection shall enlarge or diminish the doctrines of vicarious and contributory liability." This is very tight.

"Intent may be shown by acts from which a reasonable person would find intent to induce infringement based upon all relevant information, including whether the activity relies on infringement for its commercial liability." I think that is the anchor of this thing.

When I talked about these P2P services, 97 percent of these transactions are infringement. You know, it is a amazing to me that, as a practical matter, we get lost in kind of legal theories here. Let's forget about the law for a second. Let's just look at the fundamental reality. Ninety-seven percent of these transactions are illegal and we are quibbling about definitions.

I understand definitions are important, but there is a major harm going on here. And for Gary to suggest that P2P helps sales, I think, is ludicrous. Look at this chart, Top Ten Hits. I can filibuster as well as Shapiro.

Chairman HATCH. I am not sure about that.

[Laughter.]

Chairman HATCH. Let's give it a rip here.

Mr. BAINWOL. Well, let me practice some. I am practicing.

Top ten hits in 2000 sold 60 million units. File-sharing kicks in and Top Ten Hits in 2003 sold 33 million. Where P2P really gets us is not on catalog; it is on the new hits. The pattern is as clear as night and day. The Harvard study gives Harvard an awfully bad name.

Look at this, the number of units that the top ten units sold. In 2000, four of the top ten hits sold more than 6 million units; in 2003, 1 million. None of the top ten units sold less than 3 million units in 2000. In 2003, five of the top ten were under 3 million. This has decimated the hits. The hits are the source of the investment capital of this industry. It is destroying the investment base. We are all committed to free markets, we are all committed to innovation, but the notion that we can just eviscerate property rights—we need to deal with that.

Chairman HATCH. Well, let me go to you, Mr. McGuiness. Certainly, I am going to turn to Senator Leahy.

Senator LEAHY. That is all right. Go ahead. I am enjoying this. I think it is worthwhile.

Chairman HATCH. I am going to ask you a question, but go ahead. If you have a comment, go ahead.

Mr. MCGUINESS. First of all, I always think it is a little disconcerting for those of us especially in the Internet community to sit idly by watching legislation go forward based upon the presumption of good intentions forever on behalf of lawyers for the en-

tertainment community. It is a little bit troubling that may never, ever, ever use this statute for economic benefit.

Chairman HATCH. This is a wonderful panel. I really enjoy it, I will tell you.

Mr. MCGUINESS. Two years ago, we were talking about Napster. Last year, we were talking about Aimster. This year, we are talking about Grokster. Next year, we could be up to Earth Station 5, or my personal favorite, e-donkey 2000.

The question we have to ask is if Mr. Bainwol's organization won all of its cases, which it still may well do, would that cure the problem for them? Would that be sufficient? If this law was passed, would that stop illegal fire-sharing and downloading? The answer is no.

We have to at some point give a little consideration to the reality that there is a new medium that is being used for music to share music and to obtain music. And instead of ignoring it or litigating against it, it may be time to embrace it.

When the VCR arrived, Hollywood, in my book, initially focused exclusively on the record button. A couple of years later, they decided to focus on the play button, and as a result they now sell more DVDs, if I understand correctly, than tickets in theaters. At some point, the recording industry is going to need to come to terms with the fact that if they really want to protect their copyrights, they are going to have to focus on education and legal relief. But they also are going to have to step forward and start providing a delivery system comparable to what is going on on the Internet today that they find illegal.

Mr. BAINWOL. If I may, it is not that we find it to be illegal. It is 97-percent per se illegal. And let me say we are doing exactly what you want us to do. The only way the iToons of the world and the Wal-Marts of the world have a chance to prosper, and for the legal system on the Internet to work, is if we establish that the illegal system won't be tolerated. That is what is going on here.

The only way to give a vibrant marketplace a chance to grow and to have our industry have a fighting chance for the future is to separate illegal and illegitimate from legal and legitimate. I don't know why in the world, just because we are in the technological space, we abandon the notion of property. That is an absurd notion. The only way we get the marketplace to work is if we say that theft is unacceptable.

Chairman HATCH. Senator Leahy, we will go to you, and then I have some more questions after. But Senator Leahy may have to leave.

Senator LEAHY. Well, prompted by that last exchange, I will ask this question of everybody on the panel, except Mr. Greenberg. And I will explain why. I don't want you to feel lonely or unloved. I think we have all felt the love in the room this afternoon.

[Laughter.]

Mr. GREENBERG. Virginia is for lovers, yes?

Senator LEAHY. Look at how well the Chairman and I are getting along. If we got along any better, they would think we are heading to Vermont.

[Laughter.]

Senator LEAHY. Or worse yet, Massachusetts. But, anyway, moving right along—

Chairman HATCH. This is a banner day, is all I can say.

[Laughter.]

Senator LEAHY. My mother would be so proud.

Let me say this. The Copyright Office supports S. 2560, as does Mr. Bainwol. Even those who question the language of it support the idea. Mr. McGuiness said, and I think I am quoting him right, "unlawful peer-to-peer file-sharing of copyrighted materials is wrong. Also, users and companies that engage in these activities should not be allowed to operate beyond the reach of the law." But only Mr. Greenberg and the IEEE have provided concrete legislative language laying out their concerns.

So let me ask each one of you, will you provide us with legislative language that you would support? Mr. Shapiro?

Mr. SHAPIRO. Yes. I think there have been actually some good suggestions on the panel. I mean, this is a relatively novel concept that all of a sudden we are liable for a new cause of action called "induce." But, certainly, we would support a codification of the *Sony-Betamax* principles. We clearly support that.

Senator LEAHY. When will you show us that?

Mr. SHAPIRO. The codification of the *Sony-Betamax* principles? We could do that in a few weeks.

Senator LEAHY. Okay. Mr. Holleyman, what about you?

Mr. HOLLEYMAN. I outlined in my testimony five key principles that we feel need to be addressed. We will proceed to work with you and the Committee about possible language that might reflect those and other concerns.

Senator LEAHY. Mr. McGuiness?

Mr. MCGUINESS. Senator Leahy, we would love the opportunity to work with you, and regret that we were not afforded that opportunity when you were drafting the bill.

Senator LEAHY. Well, that is why we are having these hearings.

Mr. MCGUINESS. Great.

Senator LEAHY. So you will supply—

Mr. MCGUINESS. Yes, sir.

Senator LEAHY. When?

Mr. MCGUINESS. The next couple of weeks. Of course, we would have to run it by our members, but clearly in the next couple of weeks.

Senator LEAHY. I understand that. I was just trying to get some general idea.

Mr. BAINWOL. I would simply suggest that we don't believe—we like the bill as it is, but our objective is to go after bad actors and if there is another way to get there, we are happy to sit down with responsible players here in a reasonable way and try to find a solution. Again, we want to get to "yes," and we can't afford paralysis here; we need action.

Senator LEAHY. Mr. Shapiro, you said in your testimony and in answers to questions that you agree that we need legislation that targets bad actors. I assume that some will determine bad actors in different ways.

Mr. Holleyman, you offer support to the Committee in crafting a law that deters bad actors who use technology to intentionally cause others to infringe.

Mr. Greenberg, in your testimony you offer support for the concept of the bill you have offered that has specific suggested changes.

Mr. McGuiness, you state that the law must enable copyright owners to seek relief from those who unlawfully download and distribute their work.

Mr. Bainwol offers support for S. 2560 specifically, but also in general for legislation that targets unlawful behavior rather than technology. Of course, as one of the sponsors of this bill, that is what I see as the purpose of the bill.

Now, have I quoted all of you accurately? Mr. Shapiro says I haven't quoted him accurately. Go ahead, here is your shot.

Mr. SHAPIRO. I don't think we are advocating legislation. I think what we are talking about is personal responsibility. I think technology changes quickly. Although it is a natural Congressional desire often to legislate very quickly and try to stay ahead of technology, I think that is almost impossible. I think you really have to prove some harm and see where technology is going.

As was said earlier, I can't even imagine what legislation you would come up with, even if it was what was proposed today, which would—

Senator LEAHY. So you see no need for legislation?

Mr. SHAPIRO. What I am saying is the legislation today would not do what you want it to do because it wouldn't stop that Internet site in Palestine or anywhere else in the world from doing it. I think the reality is that Congress can't legislate against everything.

I think what you are doing here is you are burning the carpet to kill the spider. The whole concept of "induce" is something which really doesn't fit into the copyright context, and that is what we are concerned about. If you want to come up with a different approach on legislation that says peer-to-peer sites aimed at children and pornography are somehow illegal, you should take that approach. But peer-to-peer doesn't appear in the legislation.

Senator LEAHY. Excuse me. I apologize for interrupting you while you were interrupting my earlier question.

Mr. SHAPIRO. That is all right. I was interrupting you.

Senator LEAHY. I want to make sure I understand. Earlier, I understood you to say that you were going to offer within the next few weeks some legislation. Now, you seem to be saying we don't need legislation. I am just a small-town lawyer. You deal in the big-time world. Do we or don't we need any legislation?

Mr. SHAPIRO. I think it is fair to say that there may be legislation necessary to codify the *Sony-Betamax* case because at least the Register of Copyrights is interpreting it extraordinarily narrowly. But it is good law; it stands. It has served us for 20 years. The copyright industries have survived. It has allowed technology to thrive.

I would say even with those charts that you have shown, the music industry and the motion picture industry and the entire content industry has grown many-fold. Even music industry sales are

up this year. Things have a way of working themselves out. Hits are cyclical. That is just a fact. Again, the are a lot more artists now that there were 20 years ago, and that is because of technology.

So, yes, we are willing to offer legislation to codify the Supreme Court's *Sony-Betamax* case. But I don't think right now legislation is necessary because the harm is so much greater than any benefit that will be derived.

Senator LEAHY. Mr. Holleyman, do you agree with the way I characterized your testimony?

Mr. HOLLEYMAN. Senator, I think you fairly characterized my testimony. The two points I would make are that the problem of piracy is significant and online piracy is growing across all copyright industries. The valuable part of the intent of your legislation was to try to address bad actors and avoid technology mandates, and that is an important principle to maintain.

Senator LEAHY. Mr. Greenberg, am I correct that you are offering support for the concept of the bill, but you also offer specific suggested changes?

Mr. GREENBERG. Indeed, our view is that the status quo is both too much and not enough protection to adequately give clarity to the actors to know what they can and what they cannot do. This is a great opportunity to bring things together and make clear for the entire community to show how secondary liability is to be balanced against the interests of the various constituents.

Senator LEAHY. Mr. McGuiness, am I correct that you say that the law of this country has to enable copyright owners to seek relief from those who unlawfully download their works?

Mr. MCGUINESS. Yes, sir, I said that.

Senator LEAHY. Mr. Bainwol, you have offered support for it, but also in general for legislation that targets unlawful behavior rather than technology?

Mr. BAINWOL. That is correct.

Senator LEAHY. In that regard, I would think in some ways we all agree because none of us could anticipate—I mean, if the Congress gave Senator Hatch and myself—and on these issues we tend to think very much alike—if they gave us the right and ability to write legislation for all time anticipating all technology, of course, we couldn't do that.

I mean, just the way technology changes, I think, extraordinarily, fascinatingly, and the fact that I can e-mail photographs of my grandchildren back and forth and that we can get pictures—I was mentioning to somebody today that during the early part of the current war, the commander of our fleet in the Persian Gulf was from Vermont, Admiral Costello. I was going down to a meeting at the White House and I e-mailed Admiral Costello as I was leaving my office.

As I walked into the meeting with the President, my Blackberry vibrated and there was a response from him. Fortunately, he said all the rights things, so I could show it to the President. But the point is who would have thought of this? I mean, who would have thought even a few years ago that you could be doing this?

I will have other questions and, as the Chairman said, I am going to have to leave. I am going to submit some to you for the

record, whether it is how you import parts of the patent law into the copyright law. But just so you understand, we are trying to protect people who own these copyrights, people who have worked and put their own talent and genius into what it is.

Mr. Bainwol, some artists sell and some don't. If you have got somebody who really does a bad job or they don't have any appeal or, at best, a niche appeal, the market will take care of that. But even those who have the niche appeal ought to be able to get the value from that niche, whatever it might be. And the Internet is a wonderful way to give more exposure to a lot of these artists, some of them being able to step out way beyond the control of individual companies, individual management, to get their own work out there. I think that is wonderful, but they should be protected in what they have.

Now, I don't care if we have 20 different online companies selling movies and music and everything else, provided their copyrights are protected, because the more you have out there, the more the competition is going to be and the better off the people who buy, like myself, are going to be. But we have to find some way to grapple at least with the basic copyright laws in a way that will reflect as this changes.

I will close with this, Mr. Chairman. I mean, we could write a piece of legislation today that would be specific to the mechanics, specific to the state of the art, whether on the Internet or anything else. We could do that, and I guarantee you within a very, very short time, somebody would devise a way around that. In the same way that, whether it is Microsoft or anybody else, put patches in their computers or in their software to stop hackers, within a few weeks somebody else was trying a new way to hack in. So the legislation has got to speak not to the mechanics, but to the intent, and we will figure out a way to do it.

Mr. Chairman, thank you very much. I am encouraged—and I hope you are, too—I am encouraged by at least the expressed willingness of everybody here to continue to work with us to find an answer that we can agree on.

Chairman HATCH. Well, thank you, Senator Leahy.

I just have a couple of more questions to ask and then we will finish this. This has been a very stimulating hearing as far as I am concerned. I have really enjoyed it. I have enjoyed each of you. You are real experts in your fields, and we would appreciate all the help you can give.

Mr. Holleyman, I haven't had a chance to really talk with you about this, but the type of pernicious adware and spyware distributed with file-sharing software is driving demand for the so-called spyware laws both here in Congress and even in my home State of Utah. I know your organization worries that such laws are overbroad, but the threats to privacy and Internet commerce that they seek to address seem to me to be real, and I think most people would say they are real.

I wonder whether you can discuss whether our legitimate technology industries can continue to allow the bad actors that everybody has been talking about here who distribute certain file-sharing software to drive debates ranging from spyware to copyright piracy.

For example, if the Grokster decision is upheld by the Ninth Circuit, there will be a split between the Ninth and the Seventh Circuits that could force the Supreme Court to reconsider the scope and propriety of its ruling in the *Sony-Betamax* case. Do any of us benefit from forcing a Supreme Court reexamination of *Sony* that must focus on the likes of Kazaa and Morpheus, just to mention a few, and the viruses, spyware and mislabeled pornography that are probably just side effects of their attempts to design around the Napster ruling?

Mr. HOLLEYMAN. Mr. Chairman, you correctly point out that the bad actors are driving much of this debate. We think that these are issues that Congress should look at. It should not always have to play out in the courts with differing decisions in different circuits and a lengthy period of time before there may ultimately be a Supreme Court review.

It is correct, as Mr. Bainwol earlier indicated, that many of the P2P systems that are being designed now disguise the infringement. They are, however, premised on infringement, sustained by substantial ad revenues are also the type of spyware that is now calling for legislation not only in your home State, but legislation that has been reported out of the House Energy and Commerce Committee and legislation that Senate Commerce is reviewing.

We would rather deal with this issue by coming directly to Congress, talking about specific, narrow proposals that will address the problem. Hopefully, by dealing with the piracy problem, we are also better able to reduce the level of spyware that is out there. The key in both is to focus on the bad actors and to try to avoid technology-specific mandates.

Chairman HATCH. Mr. Greenberg, I don't want to leave yo without some sort of comment here, but I want to thank IEEE–USA for its thoughtful analysis and its political courage in actually presenting the public with a written proposal intended to address the problems of contributory liability in the online world.

I am sure that you knew that anyone who dared to put pen to paper and tried to resolve this problem was going to suffer from criticism. As this Committee looks at the analysis of S. 2560 and the IEEE proposal and any alternatives proposed by others, I just want to know whether IEEE can agree to continue providing input on all these proposals for us, because I suspect that we are going to try and resolve this over the month of August. That means I am going to ask all of you to participate, but in particular I would like to ask you if you would do that.

Mr. GREENBERG. Senator, it would be our pleasure to assist in any way we can. We are kind of used to sitting in the center and proposing something as an alternative. That was the position we took in the Festow case when the Supreme Court faced another balancing of interests on the question of the doctrine of equivalence.

There, I recall Justice O'Connor's first question to one party was what did you think of the IEEE amicus? And Judge Bork responded, arguing for the plaintiff, it was awful, worse than what the Federal Circuit had done. The same question was asked of the attorney representing the defendant and he said the same thing. We were pretty sure then we had gotten it right.

Chairman HATCH. Well, I would like to just ask this last question of all of the panelists, and we will start with Mr. Shapiro. I would like you to address this final question that I have.

As I indicated in my written statement, I believe that addressing the resolution of the file-sharing problem has been too long delayed by the parties. They tell the courts that we must defer to Congress. I think it is time for us to do that, just as they expect us to defer to them.

This situation now endangers artists, consumers, legitimate Internet commerce, and even the continued vitality of the important *Sony-Betamax* case. At least that is my view. That ruling is an important ruling, as we all know. I really intend to find a solution to it that protects both copyrights and technological innovation. I believe that we can and must find such a solution during this session of Congress, and I would appreciate the sincere efforts of every one of you to help us to get there. I don't have any pride of authorship on these matters. We would like to get it right.

I would just like to ask each of you, can each of you commit to work with this Committee over the next seven weeks, while we will be out because of the recess and also the conventions, to identify the approach that best protects both copyrights and technology?

Mr. Shapiro?

Mr. SHAPIRO. Mr. Chairman, first of all, thank you very much for your sincerity and your willingness to hold the hearing and hear our views. You obviously do want to take an approach which won't hurt technology companies, as well as support the copyright industry. We would be happy to do everything we can to help move this process along. We obviously want to see something which works for everybody.

Chairman HATCH. And I think you really should put some real time in it because we are going to do this. We are going to get this done, and it would be nice if it was something that at least tended to please the technology side of this industry, as well, because I agree with Mr. Bainwol that it is a dog-gone catastrophe to these artists and creative people what is happening.

There is no question in my mind that that business has been cut about in half and it has been because of illegal file-sharing. I am sure there are illustrations that can be made that would show that it is not all illegal file-sharing, but I know that the vast majority of it is. Whether it is 97 percent or not, I believe it probably is that high, but the fact of the matter is it is a catastrophe and it has got the potential of really hurting our innovative people and our artists and our creative writers, and so forth, and those who have to invest and promulgate their materials, and I think in the end will really hurt technology as well. So this is something that is worthwhile doing.

Mr. Holleyman.

Mr. SHAPIRO. Could I just add something?

Chairman HATCH. Sure.

Mr. SHAPIRO. I don't represent Kazaa and I have like thousands of hours of frustration of how they screwed up my computer. So I have no problem doing something which would shut down some of those services.

Chairman HATCH. This is your chance to get even.

Mr. SHAPIRO. Not that I have ever downloaded anything.

Chairman HATCH. I am glad to have that confession.

Mr. HOLLEYMAN. Mr. Chairman, I can reaffirm our commitment to continue to work with you to find the proper balance.

Chairman HATCH. You have really been a major source of help to us over the years. As I work in this area—and I like this area; this is one of my favorite areas in all of the Congress because what you folks do is really remarkable and wonderful, and it has kept our country at the technological and software cusp of leadership throughout the whole world and it is really important to us. So it is important that we get it right. I have to admit we never quite get it right, but if we can substantially get it right, I hope that you will all cooperate in helping us to do that.

Mr. Greenberg.

Mr. GREENBERG. Senator Hatch, I think the key observation is there is no silver bullet. This is a balancing of competing interests that are in some senses inherently irreconcilable. This is not to say that we do not act or that we act precipitously, but it is to say that we must act with care.

Absolutely, the content people need to have adequate capacity to enforce their rights, but it must be understood that secondary liability by its definition is asserting intellectual property rights against somebody who has not infringed those rights. Therefore, when we define this, we must be mindful particularly when the defendant is a technology company selling a technology, that we do not give to the copyright owners who have written this song the effective patent-like protection over an unpatented product for something that the songwriter did not invent.

There is where we feel a line clearly needs to be drawn between the scope of their capacity as a plaintiff to demand technology mandates either de facto or in the language of the statute itself. And we would be pleased to work with you to the extent we can to help that along.

Chairman HATCH. We have appreciated your willingness to work.

Mr. McGuiness.

Mr. MCGUINESS. Chairman Hatch, we appreciate the opportunity to work with you. We also greatly appreciate your interest in finding the right balance. I hope you will give some thought, though, to the observation I made earlier that the ultimate solution to this problem may be broader than just new legislation.

Chairman HATCH. We will be interested in listening to you. You have represented your group very well here today.

Mr. Bainwol.

Mr. BAINWOL. I have made the observation a few times that 97 percent of the transactions on these P2P services are illegal, and I am going to give Gary the benefit of the doubt that he is in the 3 percent.

Chairman HATCH. That was very gracious of you.

[Laughter.]

Mr. BAINWOL. I am a nice guy.

That said, the objective that I think your staff and the staff of Senator Leahy began this exercise with was to target bad actors and not to get good actors into the net. That is what we support. That is our objective, as well, and we are fully committed to work-

ing with you and your team and the staff of this Committee to get that job done.

There is a sense of urgency for us. I know Gary does not see the harm, but I can tell you there are songwriters on the streets of Nashville who are not writing songs and there are a lot of folks who are just out of the creative business. That is a disaster for the country economically and artistically, so we have got to solve this problem.

Thank you, sir.

Chairman HATCH. There are some of us writing songs that aren't getting cut, too, because of this terrible dilemma that we are all facing here.

[Laughter.]

Chairman HATCH. I have really appreciated this panel. It has been a wide-ranging panel. You all have contributed greatly. In the end, I am just going to do what Marybeth Peters tells me to do anyway. You all know that.

[Laughter.]

Chairman HATCH. Shapiro almost passed out right there on the spot.

Let me just say this. This is a very brilliant panel. You folks can help us here, and you know what I am saying. If you will help us, we just might get it right. But if you don't, we are going to do it because something has to be done here. So I would suggest you really pitch in and do it.

Frankly, these are tough issues. They are not easy to explain and they are not easy to understand for many of us here in Congress. So we can use your help. But in the end, I hope that there will also be some element of cooperation and compromise because there is no way you can solve these problems so that everybody is totally pleased.

I do share your view—and I thought it was a dirty dig to bring up the class action bill at the beginning of this. That was supposed to be humorous, but it apparently didn't go over very well.

[Laughter.]

Chairman HATCH. You are right. I think we have far too much litigation and I think we have far too much stifling of our economy because of, I think, intemperate litigation, and we have to find some way around that. I don't want this to result in improper litigation that would stifle creativity in the technological world. On the other hand, sometimes having the law so that everybody understands what it is and that it really means business helps everybody to pay attention to the law and pay attention to doing what is right.

I will tell you one thing. I do want to solve this problem for the recording industry and the movie industry and the book industry. You name any copyright industry there is and they are getting very badly treated because of the technological innovations of some who don't give a damn about copyright. Well, we have to give a damn about copyright because copyright has been one of the most important principles that has made this country the greatest country in the world. A lot of people don't realize that, but it has.

So I just want to thank all of you for being here. It has been a stimulating meeting to me. I usually hate hearings, but I have enjoyed this one very much. Thank you so much.

We will recess until further notice.

[Whereupon, at 3:47 p.m., the Committee was adjourned.]

[Questions and answers and submissions for the record follow.]

QUESTIONS AND ANSWERS

Mr. Mitch Bainwol
Answers to Questions from Senator Leahy

1. *I was glad to read that the RIAA has reached a settlement with the peer-to-peer music sharing company iMesh, and I hope that this is the beginning of a less-contentious time for Internet music. The report I read mentioned that the settlement includes an agreement to use technology to "affirmatively monitor and patrol for" unlicensed songs. Please describe this technology and how it will be used.*

The record company plaintiffs have reached a settlement agreement with iMesh and iMesh has agreed to become a legitimate service. This is real progress and reveals that it is indeed possible for P2P business models to seek legitimate content and sources of revenue. The agreement does not require iMesh to use any particular technology. The company, however, acknowledges that there are many technologies currently available to actively filter unlicensed songs on their network (such as Audible Magic's CopySense), and they will determine themselves what technology works best for them.

2. *In your testimony you address at length the economic impact of piracy on the recording industry. And while this is an important issue to address in order to ensure the U.S. continues to be a leader in intellectual property, I would like your thoughts on another important aspect of illegal file-sharing. Copyright protection is designed to spark innovation and foster creativity. Can you share your thoughts with us on the long-term impact of file-sharing on innovation and creativity within the music industry?*

The two interests you state above are not mutually exclusive. In fact, as the framers of the Constitution understood in granting to creators the "exclusive right" to their works, economic reward is a major factor in sparking innovation and fostering creativity.

Producing and distributing creative content can be an expensive and time-consuming proposition. There are many who undertake such initiatives only upon the prospect of receiving compensation or, more hopefully, a positive return on their investment.

The recording industry plays a major role in this creative incentive plan. Few individuals have the financial means to write, record, produce, distribute, and promote their own music to reach the larger public necessary to build a career. By funding and supporting such artists, record companies are able to discover, introduce, and sustain those who would otherwise remain unknown to the world. In addition to enabling those individuals to remain innovative and creative, the success of these artists serves to inspire and motivate others. In this way, the recording industry—and the thousands who compose it—directly fund the future of creative work in this country.

As stated, file sharing has had a devastating impact on the music industry. The mass piracy and blatant disregard for copyright law has unsettled the fine balance of investment and reward that serves to ensure the continuation of innovation and creativity in the music industry, as well as in other creative communities. Artist rosters of many

labels have been slashed, and the diminishing prospect of even breaking even has resulted in fewer investors taking a chance on new and diverse artists. In sum, file sharing has had a ripple effect. The economic impact of piracy on the recording industry is ultimately felt by every aspiring young singer and songwriter, as well as by every potential consumer of his or her work.

3. *You noted in your testimony that peer-to-peer file sharing has had its greatest impact on the sales of "top ten hits." Please explain why this particular harm is so devastating to your industry, and how it affects the development of new artists.*

In addition to the points made in question #2 above, we would like to note the following:

While the public is generally exposed to the successful artists in the music industry, these are exceptions to the rule. In fact, only one in ten artists make back the money invested in them. These are the artists who become most popular; these are the artists who create the "top ten hits." And, on any given day, on any given file sharing network, these are the artists whose works are being offered to millions without authority *for free*. These artists (and the industry), while gaining the exposure they've worked so hard to achieve, become victims of their own success.

The reason this is so devastating to the music industry is that it is the financial return on these "top ten" artists that largely covers the losses on the remaining investments. These artists, in essence, support the industry and fund the ongoing efforts to discover and nurture new talent. File sharing is quickly destroying the industry's ability to bring this talent to the world and robbing the public of a more prolific and creative future.

4. *What steps has your industry taken to utilize the Internet for distribution of music, and how successful has this effort been?*

The music industry has embraced the Internet and the new opportunities it presents. Major and independent labels have licensed their content to many different legitimate online services, including the following:

Amazon.com	iTunes	RealOne MusicPass
Artist Direct	LiquidAudio's BurnItFirst.com	Rhapsody
BestBuy	MP3.com	RioPort
Buy.com	MusicMatch	SamGoody
CenterSpan's Scour	MusicNet	Spinner
Click Radio	MusicNOW	Streamwaves
Emusic	Napster 2.0	TowerRecords
Instavid	NetScape Music	

These services offer huge catalogues of music, accessible in a wide range of formats (such as streaming audio, tethered and permanent downloaded files) at different price

points. Consumers can choose the service and price that works best for them. Also, statutory license provisions grant Internet radio stations and broadcast simulcasters the right to transmit copyrighted sound recordings. These outlets provide a plethora of options for listening to music.

In addition to the guarantee of legitimate content, users of these services are provided with files and connections untainted by viruses, spyware, and corrupted data.

5. In your testimony you repeatedly offered to work with interested members of the technology community to craft a bill that protects property rights, but still encourages new technology. What steps could be taken to protect new technology from the fear of unintended liability, and unwarranted litigation, while still protecting property rights?

By focusing on the *actions* of certain parties rather than on the technology itself, the Induce Act seeks to safeguard the development and support of new products. Creators and owners of intellectual property are not interested in eliminating the multitude of valuable products and services that have been presented to benefit consumers. Rather, we are interested in holding accountable those who have hijacked these offerings for their own corrupt and self-serving interests to the detriment of all others.

Again, it is the actions—a clear course of conduct—engaged in by a limited set of bad actors that remains the focus, rather than the technology itself. Such a distinction is intended to address the "fear of unintended liability and unwarranted litigation." We remain engaged in discussions to find new language which conveys this point, but which may be more acceptable to all interested parties.

6. Many opponents of this bill are concerned about its impact on the Betamax case. I do not wish to see the important holding of Betamax undermined – that technologies with substantial non-infringing uses are not liable under a theory of contributory infringement. If Betamax were codified as part of this bill, would you still be in favor of it? Would that diminish efforts to punish unlawful behavior?

Citing any case, including *Betamax*, by name in a statute would be inappropriate, as the doctrine of secondary liability is continuously evolving. It would be a mistake to codify a fluid policy based on the specific facts of any particular case.

Nonetheless, the Act expressly preserves the legal standards set forth in *Betamax* by targeting only those who *intentionally* cause copyright infringement. As with *Betamax*, the Act finds no responsibility from merely providing technology that *may be* used to infringe. Rather, it is the actions of specific parties in connection with those technologies that is the focus.

It should again be pointed out that the Induce Act deals with activity clearly and specifically not addressed in *Betamax*. After pointing out that a manufacturer or

distributor *could* be liable for infringement if he "intentionally induced,"[1] the Court found that Sony did not do so merely by putting into the stream of commerce a machine that *may* be used to infringe. The Induce Act deals with actions set aside by *Betamax* after the Court found they didn't apply—namely that the defendant "intentionally induce[s] its customers to make infringing uses of [another's] copyrights."[2]

[1] *Sony Corp v. Universal City Studios*, 464 U.S. 417, 439 n. 19 (1984).
[2] *Id.* (internal quotations and brackets omitted)

Answers to Questions from Senator Cornyn

1. Do you foresee a claim under S. 2560 as being used in unintended ways, such as to attempt to punish funding or other entrepreneurial activity in aid of a party who intends to induce infringement?

No. S. 2560 addresses actors who intentionally induce infringing activity. The Act is *not* concerned with those who merely bring a technology to market with knowledge that others may use it to infringe. Intent is an extremely high standard and a built-in safeguard against abuse of the Act.

2. Do you agree with the claim of proponents of S. 2560 that the Act covers only a narrow class of cases not at issue in Sony Betamax – those in which a distributor of copying devices intends to induce infringement? Do you see any problems with possible broad application of the definition of "intentional inducement?" Does the language in S. 2560 adequately maintain the defense of "substantial noninfringing uses" as promulgated by the Sony Betamax *decision?*

S. 2560 does indeed cover cases not at issue in *Sony Betamax*. As stated in our answers to Senator Leahy, the Induce Act deals with activity clearly and specifically not addressed in *Betamax*. After pointing out that a manufacturer or distributor *could* be liable for infringement if he "intentionally induced,"[1] the Court found that Sony did not do so merely by putting into the stream of commerce a machine that *may* be used to infringe. The Induce Act deals with actions set aside by *Betamax* after the Court found they didn't apply—namely that the defendant "intentionally induce[s] its customers to make infringing uses of [another's] copyrights."[2]

3. Is S. 2560 intended to apply to any conduct occurring prior to the effective date of enactment of S. 2560? If so, is it intended to apply to any such conduct other than that by Grokster or other P2P systems?

We appreciatively note the recognition that it is the *conduct* of the offending party, rather than the technology that is the focus of S. 2560. It is this corrupt behavior of *Grokster* and similar illicit P2P businesses which became the driving force behind the bill. These services have escaped responsibility for their wrongful actions through a misapplication of law. S. 2560 seeks to correct that.

The legislation does not contain a clause applying its provisions to conduct occurring before the effective date. In the absence of such a clause, the legislation is presumed to apply prospectively.

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[1] *Sony Corp v. Universal City Studios*, 464 U.S. 417, 439 n. 19 (1984).
[2] *Id.* (internal quotations and brackets omitted)

4. If the Ninth Circuit reverses the district court in the Grokster case, do you believe that S. 2560 would still be needed? In your opinion, what, if anything is the bill intended to capture beyond Grokster, Kazaa and other P2P file-sharing devices?

N/A. The fact that the Ninth Circuit affirmed an extraordinarily narrow reading of current legal guidelines reaffirms the importance of the Induce Act.

The Ninth Circuit nowhere dispelled the District Court's notion that "Defendants may have intentionally structured their businesses to avoid secondary liability for copyright infringement, while benefiting financially from the illicit draw of their wares."[3] Clearly, legislative guidance, suggested by the District Court itself, is needed to restore the overlooked and misapplied doctrine of inducement—a doctrine conspicuously missing since the Supreme Court set it aside in a factually distinguished case.

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

Written Responses to Questions From Committee Members

Further Testimony of
Andrew Greenberg

Intellectual Property Committee

to the

Senate Committee on the Judiciary

On

"Protecting Innovation and Art While Preventing Piracy"

An Examination of S. 2560,
The Inducing Infringement of Copyrights Act of 2004

September 3, 2004

Mr. Chairman and Distinguished Members of the Committee:

In response to correspondence from Senator Hatch, dated, August 6, 2004, I am honored to submit IEEE-USA's written responses to questions from Committee Members:

QUESTION BY SENATOR LEAHY:

1. I know from your testimony that you are concerned that liability for inducement can occur whether or not there is actual infringement. But the Inducing Infringement of Copyrights Act specifically states that the legislation does not enlarge or diminish the existing doctrines of vicarious, contributory, and secondary liability, which are all predicated on actual infringement. In light of this, do you still maintain that there is a possibility that inducement liability might attach in the absence of an actual infringement?

Response:

Yes. IEEE-USA is concerned that S.2560 permits an action for inducement to lie without allegations of direct infringement, giving rise to the possibility of liability for mere solicitation of an infringement.

I should note that in my earlier testimony, IEEE-USA asked the Committee to carefully measure when "it is appropriate to extend copyright infringement liability to someone who has not infringed a copyrighted work." By this remark, IEEE-USA was not addressing the traditional requirement that secondary liability requires a threshold proof that a third party had committed a direct infringement. Rather it was simply noting that where a copyright owner seeks to expand its limited monopoly to shut down a technology that does not itself infringe to avoid the cost and risk of suing a direct infringer, it is important to assure that such expansion does not work to deprive society of the benefits lawful use of that technology can provide. More important, it is essential to assure that the expansion does not chill development of other pioneering inventions or technological improvements.

Of course, IEEE-USA does not challenge the legitimate interest of copyright owners to deter infringement. At the same time, IEEE-USA recognizes that the interest of the copyright owner is not the only relevant interest to maintain the necessary balance of Federal intellectual property policy. Because society benefits both from pioneering work as well as incremental improvement of that work, the scope of the limited monopolies under Copyright and Patent Law

must carefully balance all of these competing interests, and remain cabined by the overarching policy to promote progress.

Although my IEEE-USA testimony was, in fact, along different lines than the issues set forth in Senator Leahy's question, we have undertaken to study the Senator's question, and respond in the affirmative. The reasoning follows:

Consider a hypothetical complaint alleging secondary liability for inducement without alleging that a direct infringement actually occurred. While Senator Leahy correctly observed that Sec. 2 does create new Section 501(g)(3) of the Copyright Act, IEEE-USA does not agree that the provision would assure the dismissal of the hypothetical complaint. In particular, new 501(g)(3) only provides that:

> Nothing in this subsection shall [(i)] enlarge or diminish the doctrines of vicarious liability for copyright infringement or [(ii)] require any court to unjustly withhold or impose any secondary liability for copyright infringement.

There are two clauses, annotated above as "i" and "ii" respectively. In the following, I shall refer to the first section as the "non-enlargement clause," and the second section as the "justice clause."

The non-enlargement clause is expressly limited to the "doctrines of vicarious and contributory liability." In the hypothetical, a plaintiff would likely argue that the assertion of inducement under new Section 501(g)(2) is a new cause of action that does not fall under either doctrine, and is not implicated by the non-enlargement clause. IEEE-USA is concerned that a court would find this argument persuasive.

The justice clause is broader in scope, applying to "any secondary liability for copyright infringement," and clearly would apply to the demurrer. Here, however, the plaintiff would argue that, for purposes of a Motion to Dismiss, that the naked notice pleading allegation that "It

would be unjust to withhold secondary liability," must be presumed true, particularly if taken together with additional allegations concerning the justice and policy issues. Indeed, it may well be the case that the justice question may not even be amenable to Summary Judgment. This procedural argument would likely be available regardless of the merits, as "justice" issues may flow merely from the fact that the plaintiff owns a copyright, combined with any nasty statements made by the defendant allegedly attempting to induce an infringement.

QUESTION BY SENATOR LEAHY:

2. The controversy about this bill centers on possible unintended consequences. I want to ask you about the intended consequences. Modern digital technology has made it possible for a company to avoid direct infringement itself, while intentionally facilitating and profiting from massive infringement by others. This bill would make such companies liable. Do you agree with this intended consequence?

Response:

Yes and no. We may well agree in certain cases, but the hypothetical given was too broadly defined for IEEE-USA to provide a more definitive response. IEEE-USA believes that copyright owners must not be permitted to restrict the sale of technology having non-infringing uses unless the seller has independently and actively induced a copyright infringement. The devil lies in the details of the specific conduct proscribed and the state of mind giving rise to liability. In particular, IEEE-USA believes that mere marketing of a technology having infringing and noninfringing uses, without more, should not constitute an actionable inducement.

IEEE-USA does not sanction willful creation of an "infringement machine," combined with a concerted marketing effort to induce its use for widespread infringement. IEEE-USA is likewise concerned that vested interests in an existing commercial infrastructure can always spin development of new distribution or duplication technology as the willful creation of an

"infringement machine" and marketing of that technology as an "effort to induce its use for widespread infringement." This has historically been the case.

> From the advent of the player piano, every new means of reproducing sound has struck a dissonant chord with musical copyright owners, often resulting in federal litigation. . . . The introduction of new technology is always disruptive to old markets, and particularly to those copyright owners whose works are sold through well-established distribution mechanisms.

Metro-Goldwyn-Mayer Studios, Inc. v. Grokster, Ltd, 2004 WL 1853717 (9th Cir. 2004). IEEE-USA suggests that a highly conservative, rather than proactive legislative posture, is generally indicated in such circumstances, because "time and market forces often provide equilibrium in balancing interests, whether the new technology be a player piano, a copier, a tape recorder, a video recorder, a personal computer, a karaoke machine or an MP3 player." Id. at *9. Today's decentralized file-sharing technologies hold great promise and opportunity for artists and the consuming public, by "significantly reducing the distribution costs of public domain and permissively shared art and speech." Id. at *7. As just one example, my family and other interested parties are now able to download and view a video capture of my testimony only because of a Bittorrent feed, which was graciously provided by an individual citizen who could not otherwise have justified the expense of building internet servers for that purpose.

Courts have wrestled for some time with hard copyright cases involving neutral technologies and egregious conduct, and the resulting law has become a mire. Existing forms of secondary liability have expanded beyond recognition, in part, because of a desire to punish what was perceived as bad conduct. This, in turn, has led to considerable uncertainty in many areas of internet law, an uncertainty that serves no salutary purpose.

For this reason, IEEE-USA testified that today's vast expansion of secondary liability predicated on "mere capacity to control" is at once too much and not enough copyright

protection. The status quo combines the unhealthy mixture of undue trade regulation of essential technology with the inability to reach bad actors who actively and knowingly induce infringement by others with the specific and actual intent that the infringing acts occur.

Because secondary liability in intellectual property law is routinely used by plaintiffs as a litigation tactic, care must be taken to assure that liability is meted out where appropriate without placing undue litigation expense and risks of liability upon actually innocent defendants. IEEE would agree with liability in appropriate cases, but not otherwise: IEEE-USA believes that copyright owners must not be permitted to restrict the sale of technology having non-infringing uses unless the seller has independently and actively induced a copyright infringement.

QUESTION BY SENATOR LEAHY:

3. You state that "copyright owners must not be permitted to restrict the sale of technology having non-infringing uses unless the seller has independently and actively induced a copyright infringement." I agree. What steps could be taken to protect against inducement, without threatening the development of technology with substantial non-infringing uses?

Response:

IEEE-USA is gratified by Senator Leahy's endorsement of this position.

The IEEE-USA proposal to protect against inducement without threatening the development of dual-use technologies has been set forth in a proposed substitute in an appendix that accompanied my written testimony. The substitute provides five essential provisions that interoperate to maintain this essential balance. These provisions comprise codification of secondary liability standards for contribution, vicarious liability and inducement; careful codification of the dual-use exclusions for each theory; and damage provisions tailored to more fairly balance the equities in inducement cases.

QUESTION BY SENATOR LEAHY:

4. There has been a lot of talk, and a lot of concern, about the effect of our bill on the Supreme Court's decision in the Sony-Betamax case. In fact you said of the inducement doctrine that "[i]t is unclear whether the Court would have achieved the same result in the Sony case under this rule." You do recognize that the Court in Sony said explicitly in that case that Sony was not inducing infringement of copyright with its VCRs, do you not?

RESPONSE:

Senator Leahy correctly notes that the Supreme Court majority opinion discussed, in a footnote, whether Sony might have satisfied the "narrow standard" used to determine secondary liability under trademark law. This may inform, but does not resolve, how a court today would apply the different and expansively broader sui generis standard in S. 2560. Particularly in view of how the Betamax facts were treated by the Supreme Court dissent, Circuit Court and District Court opinions, IEEE-USA continues to believe it is uncertain what result would obtain in Sony under the proposed legislation.

It is apparent that mere incantation of the word "inducement," without more, does not define a clear and particularized standard or require a particular result. Sony illustrates this in four different opinions, each of which applied different standards relating to "inducement" to reach differing results. Each Judge and Justice reviewed the same facts:

(i) **Technology Facilitates Infringement.** The Betamax enabled home users to reproduce and distribute copyrighted content.

(ii) **Actual Infringement.** There was direct and survey evidence of significant conduct alleged to be infringing.

(iii) **Advertising Inviting Acts Alleged to Infringe.** The defendants in Sony published national Betamax advertisements for magazines, newspapers and television. These national advertisements were introduced into evidence, exhorting the public to "record your favorite show" and "classic movies" to "build a library."

(iv) **No Notices or Warnings.** There were no notices or warnings in the advertisements that such conduct might be infringing.

(v) **Knowledge of Infringements.** There were also allegations of knowledge on the part of the defendants that the allegedly infringing acts occurred.

480 F. Supp. 429, 435-36 (C.D. Cal. 1979) (Ferguson, J.). Under those facts, each opinion applied differing standards to reach differing results on the question of inducement.

District Court: No Liability for Lack of Direct Evidence of Inducement; Different Result Likely Under S. 2560. Writing for the District Court, Judge Ferguson required not only proof of an attempt to induce, but also proof that the infringements were actually "influenced or encouraged by the advertisements." Id. at 480. He did not find inducement under that standard. It is unclear whether Judge Ferguson would have come to the same result under S. 2560, since Section g(1) expressly permits intentional inducement to be shown indirectly through acts from which a "reasonable person" would find intent to induce infringement based upon the totality of the circumstances.

Circuit Court: Liability because "No Doubt" Facts Support Claim of Inducement; Liability Also Likely Under S. 2560. Judge Kilkenny, writing for a unanimous panel of the Ninth Circuit, applied a different standard to conclude that "there is no doubt that appellees have met the other requirements . . . inducing . . . the infringing conduct of another." Sony, 659 F. 2d 963, 975-76 (9th Cir. 1981). They would have found inducement under that standard, and it appears likely they would also have done so under S. 2560.

Blackmun Dissent (4 Justices): Liability Because Inducement May Be Shown by Indirect Evidence; Liability Also Likely Under S. 2560. Justice Blackmun would have reversed the District Court, opining that the fact of inducement "can be shown indirectly," as mandated in the language of S. 2560, and concluded on the record that the evidence sufficiently indicates that "Sony has induced . . . infringing conduct of Betamax owners." Sony, 464 U.S.

440, 489-91 (Blackmun, J., dissenting). He would have found inducement under that standard, and it appears he would likely have found inducement under S. 2560.

Majority Opinion (5 Justices): No Inducement under "Narrow" Trademark Standard; Uncertain Result under S. 2560. The Supreme Court majority, after rejecting the suitability of tests for secondary liability in trademark law in a footnote, nevertheless applied the "narrow standard" from a trademark case, Inwood Laboratories, as dicta. There, the Court concluded that "Sony certainly does not 'intentionally induce' its customers to make infringing uses" under the trademark standard. Sony, Id. at 439-440 n. 19. It is unclear how this would inform the application of those facts under the S. 2560 standard.

It is safe to say that nobody can know for sure how Courts will treat the much broader sui generis S. 2560 inducement standard. In the absence of clear standards and safe harbor exclusions for the definition of "inducement," a prospective inventor, manufacturer and investor in potentially ground breaking technologies will necessarily face significant uncertainty and the risks of potentially ruinous liability. As IEEE-USA has testified, such uncertainty of claims coming from every copyright holder anywhere is the practical equivalent of a rule barring innovation.

In closing, the IEEE-USA is grateful to the Chairman, Senator Leahy and other distinguished members of the Committee for this opportunity to comment on these important questions.

Questions submitted by Senator Patrick Leahy
Hearing before the Committee on the Judiciary
"Protecting Innovation and Art while Preventing Privacy"

Questions for Mr. Robert Holleyman

1. You note correctly that a proper solution to the current crisis in copyright infringement must ensure that new technologies with multiple uses are not hindered. I share that view. Many opponents of this bill are concerned about its impact on the Betamax case. If Betamax were codified as part of this bill, would you be in favor of it?

   Answer:

   As I stated in my testimony, we believe the goal of any legislation in this area should be to thwart piracy while ensuring that the drive to innovate and bring new technologies to market is not dampened. The Supreme Court's Betamax decision has provided technology companies with a clear test to determine whether a new product or service will have copyright law implications. That test has served our industry well: the remarkable wave of technology innovation we have enjoyed over the past 20 years bears this out. Thus, the key goal from our perspective is ensuring this test remains viable. Codification is one way to reach that goal, but we are certainly open to other ideas as well.

2. In the Grokster case, a popular peer-to-peer network had taken affirmative steps to encourage and facilitate copyright infringement. It also took affirmative steps to help its users get away with infringement, and in fact the company designed its entire business model around the infringing use of technology. If someone takes such dramatic steps to encourage and assist its users to infringe copyright, do you believe that it would be a meaningful defense for that person to be able to say that its product might also be used for a noninfringing purpose although its efforts were directed at inducing others to use it illegally?

   Answer:

   As I noted in my testimony, it's our view that the intent of the party to facilitate infringing activity should be a key consideration. Behavior and intent should be a focal point for establishing liability. Objective acts such as specifically encouraging persons to engage in infringement, and taking deliberate steps in the design of business models which rely on infringement for their success should be weighed by the courts.

3. You noted in your testimony that one part of a broader solution would be for the government to engage in an advertising campaign to raise awareness about the dangers of illicit file-sharing. I agree. I was very happy to appear with Chairman

Hatch in Billboard magazine, as part of that magazine's legal downloading advertising campaign. You refer to three specific ad campaigns that the government has undertaken, concerning the environment, smoking and drugs. Each of those three issues is important to all Americans. That is why each has been the target of a government ad campaign. It is also why each of those three very important issues represents a highly regulated industry. I do not want to see high technology go the way of those three subjects. I know you share that view. Do you believe that legislation is possible that protects copyright holders, but does not send us down the path toward regulation?

Answer:

We believe that legislation should focus on the intent and behavior of actors, rather than the capabilities or functions of technology products. The reality is that good technology in the hands of bad persons can be used for illicit purposes. The culprit in these situations is the bad actor, not the technology they have hijacked to their own ends. We believe legislation can be crafted which regulates bad behavior while avoiding regulation of technology.

4. You note in your testimony that important issues like the one at hand should always have to play out in the courts, with differing decisions in different circuits and a lengthy period of time before there may ultimately be a Supreme Court review. In your view, what are some of the dangers posed by the scenario you describe, in which courts can reach contrasting decisions?

Answer:

I do not recall stating that the courts should be left without further guidance to determine how current law applies to on-line piracy. The courts certainly have played and need to play a key role in this regard. But it is our sense that the Congress needs to take a hard look at these issues, as your Committee is now doing, and develop, through legislation as needed, additional guidance for the courts.

5. Mr. Holleyman, during our hearing Mr. Shapiro questioned the loss figures in your latest report on software piracy. As I understand it, your study estimates worldwide retail losses of nearly $30 billion for the software industry. How was that figure arrived at, and does is overstate lost sales to your industry, as Mr. Shapiro stated?

Answer:

BSA has been releasing estimates of unauthorized use of software for over ten years. Because the market for software has changed over that time, this year BSA contracted with IDC, the leading firm doing economic research and analysis for the technology industry, to update and revise our study. After more than six

months of research, IDC's results present what we believe to be an accurate landscape of software theft in the global marketplace. It is based on market data and in-the-field interviews with 5,600 industry professionals in 15 countries. With ongoing coverage of hardware and software markets in more than 65 countries, IDC had a broad and deep information base from which to develop piracy rates. They undertook a straightforward market measurement.

Last year, the world spent more than $50 billion for commercial packaged software that runs on personal computers. Yet, IDC concluded that software worth almost $80 billion was actually installed. For every two dollars' worth of software purchased legitimately, one dollar's worth was obtained illegally. As a result, IDC estimated a global piracy rate of 36 percent in 2003, with a U.S. rate of 22 percent.

IDC estimated that $29 billion in software was installed and used without permission from the software developer during 2003. Stated differently, this is the value of the software IDC estimates is now used illegally. This is not to say that if these users were compelled to stop using this illegal software they would go out and buy a legitimate copy. We understand that certain people would not be willing to pay for the same software they were using for free. As the chief research officer at IDC has stated, "conversion isn't the issue . . . what matters is the software market activity related to lower piracy." A separate IDC study on the economic impact of software piracy released in 2003, concluded that reducing piracy by a dollar raises legitimate industry revenues by a dollar. These results draw a significant and clear correlation between piracy and industry losses. Reducing piracy has a big impact on industry revenue, jobs, tax receipts and contribution to GDP.

This year's estimate of the value of illegal software use is substantially higher than previous estimates. In part, this is the result of a more complete accounting of software sales and use based on IDC's analysis. In part, it is a result of the fact that past estimates focused only on a more limited set of business productivity applications, and did not include a range of important software products such as operating systems and consumer applications.

The bottom line is that an astounding amount of software is now used illegally and that fact causes substantial harm to innovative software developers. The complete results of the IDC study and an explanation of the methodology used can be found at www.bsa.org/globalstudy.

NetCoalition.com

September 3, 2004

VIA Hand Delivery and Electronic Delivery

Mr. Barr Huefner
Senate Committee on the Judiciary
224 Dirksen Senate Building
Washington, DC 20510

Re: Responses to Questions from Committee Members Regarding the Hearing on "Protecting Innovation and Art While Preventing Piracy."

Dear Mr. Huefner:

Attached please find NetCoalition's responses to questions from Senate Judiciary Committee members regarding the hearing on "Protecting Innovation and Art While Preventing Piracy."

Please let me know if you have any questions.

Sincerely,

Markham C. Erickson
General Counsel

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NetCoalition Responses to Questions from Committee Members.

Questions from Senator Leahy

1. The controversy about this bill centers on possible unintended consequences. I want to ask you about the unintended consequences. Modern digital technology has made it possible for a company to avoid direct infringement themselves, while intentionally facilitating and profiting from massive infringement by others. This bill would make such companies liable. Do you agree with this intended consequence?

> It is important to recognize that in this context we are debating the parameters surrounding *secondary* liability for copyright infringement. The direct infringers are those that are illegally downloading and sharing copyrighted works. We do not condone such activity and believe that these individuals can and should be held accountable for their actions.
>
> Our concern with the bill is its inevitable impact on the scope of secondary liability. By undermining the protections afforded Internet and technology companies as a result of the Supreme Court's decision in Sony Betamax as well as related judicial decisions, the legislation would expose myriad entities, whose current operations are considered legal, to massive and protracted litigation. In addition, new technological development would be discouraged, since it would be impossible to predict with any legal certainty what would and would not be subjected to a lawsuit by the content community.
>
> Moreover, there is also some doubt whether the legislation would in fact reach its intended targets. It is unclear from reading the District Court and Ninth Circuit opinions in the *Grokster* case whether S. 2560 would indeed allow the recording industry to prevail against Grokster, especially given the factual stipulations agreed to by the plaintiffs. Moreover, the legislation provides no real relief against illegal file sharing operations based overseas.

2. In your testimony you note that this legislation should be focused more on behavior, in this case encouraging copyright infringement, and focus less on particular technologies. I could not agree more. That is why this bill does not single out any technology. Rather, a reading of this bill quickly reveals that it addresses only those who, regardless of the

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technology at issue, intentionally induce others to engage in copyright infringement. Given the fact that this bill is already technology neutral, what else could this Committee do to focus on behavior as opposed to technology?

> Because of the subjective nature of the cause of action, S. 2560 would increase the likelihood of protracted litigation over technologies about which the entertainment industry has concerns. Consequently, the act could be used by plaintiffs to target certain technologies that this industry finds threatening to its existing business models and marketing strategies. The entertainment industry has a long history of resisting new technologies and suing manufacturers of those technologies. We propose that the bill be more narrowly focused on specific, objective behaviors that rise to the level of illegal activity so that plaintiffs cannot use the law to merely hold hostage companies that produce technologies that are capable of being misused.

3. There has been a lot of talk, and a lot of concern, about the effect of our bill on the Supreme Court's decision in the Sony Betamax case. You do recognize that the Court held explicitly in that case that Sony was not inducing infringement of copyright with its VCRs, do you not?

> Our concern with S. 2560 is that it is creating a new "induce" right of action under secondary copyright liability law to which the Sony Betamax standard would not be a defense. If S. 2560 were the law during the dispute between the motion picture industry and Sony, it is unclear whether Sony would have prevailed in its court case.

4. In your testimony you state that the provision of software by ISPs is protected by the Betamax standard, but that "under S. 2560, an ISP could be sued for inducing infringement by distributing software that enables infringement, such as software enabling broadband service." Would you still have this concern if the Inducing Infringement of Copyrights Act were to codify or otherwise affirm Betamax?

> Clearly, affirming the *Betamax* standard would be a step in the right direction. S. 2560 creates a new "induce" right of action and specifically does not incorporate the Betamax safe harbor. Consequently, a court could be compelled to conclude that the omission was intentional, that Congress did not intend to prohibit the use of this new right of action, even in instances where it could be proven that the technology was capable of substantial noninfringing uses. We have drafted an alternative approach, which we have shared with your staff. A copy is attached.

5. In the Grokster case, a popular peer-to-peer network had taken affirmative steps to encourage and facilitate copyright infringement. It also took affirmative steps to help its users get away with infringement, and in fact the company designed its entire business

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model around the infringing use of its technology. If someone takes such drastic steps to encourage and assist its users to infringe copyright, do you believe it would be a meaningful defense for that person to be able to say that their product might also be used for a noninfringing purpose although their efforts were directed at inducing stores to use it illegally?

> As you know, the 9th Circuit recently affirmed the trial court in the *Grokster* case. The Court concluded that Grokster was not liable for contributory or vicarious liability for copyright infringement. Based on the court's discussion of the case, it does not appear that Grokster did take the kind of affirmative steps referenced in your question. The draft legislation we have attached would make clear an entity that undertakes conscious, recurring, persistent and deliberate acts that cause another person to commit such infringement can be secondarily liable.

6. You note in your testimony that the Internet itself "is being used for music to share music and to obtain music. And instead of ignoring it or litigating against it, it may be time to embrace it." I note tha the music industry has licensed its content to a number of lawful services such as iTunes. Do you agree that in order for these services to flourish, measures must be taken against the services that encourage their users to steal copyrighted materials?

> Naturally, measures must be taken against entities that are breaking the law. This not only reflects current law but also makes business sense. Some of NetCoalition's members offer lawful music services for which they charge fees in the expectation of a profit. Obviously, it is in the interest of our members who offer these kinds of lawful services not to be forced to compete against illegal file sharing.
>
> The point I was trying to make is somewhat different. What was not mentioned at the hearing is that the legislation, even if enacted in its current form, will not solve the real problem the Internet poses for the recording industry. As noted above, there are real questions whether the legislation would reach Grokster. It certainly would have no impact on file sharing operations based overseas. The unspoken reality is that the only effective, comprehensive solution to the problem of music privacy, short of disconneting America from the Internet, will require not only taking measures against those who break the law but also the creation of new distribution systems so that consumers have the opportunity to access music through convenient and affordable online platforms.

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Questions from U.S. Senator John Cornyn:

1. As one who is very supportive of reforming our civil justice system, I am concerned that the lack of clarity in the definition of inducing infringement could create an inducement to litigation. Do you see that as a likely outcome if this bill were passed?

Yes. Although the "intentional inducement" standard in the bill sounds like a difficult standard to meet, it does not require proof that the defendant actually intended to induce infringement. Consequently, plaintiffs would be allowed to engage in extensive and intrusive discovery, demanding email, market research data and depositions of anyone affiliated with the development, marketing, or management of a product. The new standard could be used not as a tool of justice but as an economic weapon against potential new businesses.

At the Committee's request, we have drafted an alternative proposal that would address these litigation concerns by replacing the subjective intent standard with an objective one that would hold an entity secondarily liable for copyright infringment if the entity undertakes conscious, recurring, persistent and deliberate acts that cause another person to commit infringement. This standard would help eliminate frivolous lawsuits filed by copyright holders who attempt to use litigation as an economic weapon against technologies they do not support. In addition, to further prevent frivolous litigation, we have included a provision that requires plaintiffs to plead the facts supporting allegations of infringement with particularity. And, we would require that the court reimburse the prevailing party in a lawsuit with court costs and attorneys fees.

2. Some people say that there is really no panacea to the problem of piracy and that to try to carve-out legislation that will punish a handful of wrong-doers can have adverse consequences to the economy, technological advancement and innovation. Do you share this view, and, if so, can you expand upon these thoughts?

NetCoalition strongly opposes the illegal peer-to-peer file sharing of copyrighted works. Some of our members offer lawful online music services for which they would like to compete fairly in the marketplace and not have to compete against services that encourage illegal file-sharing.

Unfortunately, new laws will not fully solve the problem of music piracy. Even a complete ban on file sharing in the United States will not prevent consumers from accessing overseas sites to download music. Any comprehensive solution must involve a combination of effective legal relief, consumer education, and a reasonably priced, convenient, and portable distribution system that makes it as possible to download music legally as can be done today illegally.

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September 3, 2004

Mr. Barr Huefner
Office of the Honorable Orrin G. Hatch
Senate Judiciary Committee
224 Dirksen Senate Office Building
Washington, D.C., 20510

Dear Mr. Huefner:

In response to the August 6 letter from Chairman Hatch, enclosed please find written responses to the questions submitted by Senate Judiciary Committee members regarding the hearing on "Protecting Innovation and Art While Preventing Piracy," held on July 22, 2004.

Sincerely,

Marybeth Peters

Marybeth Peters
Register of Copyrights

Enclosure

U.S. Copyright Office
Responses to Questions Submitted by Senator Patrick Leahy
Hearing before the Committee on the Judiciary
"Protecting Innovation and Art while Preventing Piracy"

Question 1

One of the more unfortunate aspects of the failure of the Grokster court to correctly impose secondary liability is that copyright holders have had to resort to infringement suits against individuals, rather than against the companies that encourage and profit from that infringement. You state that imposing liability on those who induce copyright infringement is "critical to the effectiveness" of our copyright laws. Can you explain why such liability is so critical?

Copyright has always faced the problem that in many cases infringement is conducted by individuals whose conduct is difficult to detect and costly, if not impossible, to enforce against. For example, individual musicians or bands would perform works to the public without permission, but it was impractical for the copyright owners in those works to find and sue those direct infringers, and even if they could, it was likely that the defendants were judgment-proof. Secondary liability doctrines, however, place infringement liability on proprietors of the venues (the concert halls and dance halls) that hire such direct infringers, so that the copyright owners can enforce (and ultimately license) their copyright for these uses. As has happened in the "dance hall" context, copyright owners developed licensing mechanisms for the use of music in those venues, but first the liability of such venues must be established. We believe imposing liability on peer-to-peer services under the new inducement provision would work a similar result.

There is another good reason why secondary liability is critical, especially in the peer-to-peer context. In those circumstances, the peer-to-peer services are the ones building a business around and profiting from the infringement of copyrighted works, and appropriately they should be the parties held accountable for those actions. They are the parties primarily responsible for creating a massive network of infringement, and rightly should be charged with liability for those actions.

Question 2

You stated in your testimony that fears that copying devices like portable music players might be liable under the Inducing Infringement of Copyrights Act are "unfounded." You go on to refer to the differences between portable music players and the types of networks at issue in the Grokster case. How would you distinguish those networks from other information networks designed to share technology, but not intended to induce copyright infringement? Does the current language of the Inducing Infringements of Copyrights Act make clear this distinction?

As my written testimony indicated, there are several acts that the infringing P2P services take to induce their users to infringe copyright. For example, they make distribution of the users' files automatic upon turning the software on, and make it hard for the user to "turn off" the distribution of those files. One service also encourages users to distribute "large and interesting" files (knowing that those files will most likely be popular, copyrighted music and movies) by offering improved download performance to those who have distributed the most material. We also understand that some services have interfered with copyright owners' efforts to communicate with users of these networks and inform them of the copyright violations occurring on them. These are not the actions of companies that merely provide technology to users to allow them to share information. The companies that are targeted by this bill are consciously exploiting a market for infringement tools; they are not simply providing a technological service such as e-mail or instant messaging the uses of which are overwhelmingly (if not exclusively) noninfringing. Nevertheless, we understand the concerns that have been expressed that the language of the bill might unnecessarily cover otherwise legitimate use and dissemination of network technology. As you have requested, we are working with staff and the interested parties to propose revisions to the bill to avoid these unintended consequences.

Question 3

The courts have slowly been clarifying the doctrine of secondary copyright liability ever since the 1976 Copyright Act was passed, but it has become a much more urgent matter in the context of modern digital technology. As you note, clever software and the Internet make it possible for companies to avoid direct copyright infringement while encouraging and profiting from massive copyright infringement by others. You also note that in response to this new technology, courts have created conflicting legal precedent. In your view, does the current state of the law adequately protect the rights of copyright holders and give the technology industry stable guidance with respect to their potential liability?

As I said in my testimony, I believe the law should strike a balance between effective copyright protection, on the one hand, and not interfering with innovation in technology, on the other hand. At present, the law of secondary liability is not striking the right balance, particularly in the context of peer-to-peer services, where the Ninth Circuit's recent decision in the *Grokster* case leaves copyright owners with only "merely symbolic" protection against the rampant infringement occurring on peer-to-peer networks. For this reason I support S. 2560 as an important step towards recalibrating that balance back towards effective copyright protection, without unduly burdening technological innovation.

Question 4

You stated in your testimony that the Copyright Act of 1976 gives the courts the power to address changing circumstances created by new technologies. In your view, is it preferable for the courts to address new technologies first? At what point should Congress step in and address a failure in the development of secondary liability law?

In the peer-to-peer context, we have now had several courts consider the application of copyright to this new technology, and they have come to conflicting results. It is my view that Congressional guidance in such circumstances is both warranted and appropriate, noting, however, that this is also an area in which the Supreme Court could also resolve the problems faced here. I think the approach in S. 2560 is the right one, because it recognizes the reality that courts need some flexibility to find or deny liability in future circumstances that we cannot predict. However, guidance from Congress appears necessary so that courts are able to consider all of the circumstances of a case and come up with the result that best reflects Congress' intent behind the copyright laws.

Question 5

I fear that the concerns expressed by some about the Inducing Infringement of Copyrights Act stem from an incomplete understanding of common law principles relating to secondary copyright liability. In particular, I fear that there is a misunderstanding about the importance of intent under current common law. In your view, how should a manufacturer's intent come into play in determining secondary liability?

It is my view that a manufacturer's intent is relevant to the ultimate determination of whether it should be liable for its users' copyright infringement. If a manufacturer of technology intends for its users to use that technology to infringe copyright, a court should be able to consider that fact in assessing liability. The existing secondary liability doctrines, however, do not explicitly guide courts on how the intent of the defendant should be considered. For example, in its typical formulation, contributory infringement looks only to defendant's knowledge of and material contribution to the infringement, not explicitly the defendant's intent. Although the determination of defendant's knowledge might have some aspects that are similar to analyzing intent, it is not always the same. For example, the Seventh Circuit recently clarified that a defendant's "willful blindness" to infringement it is enabling equates to knowledge of that infringement -- in other words, defendant's intent to avoid being liable by remaining ignorant can and should be used against it in those circumstances. With vicarious liability, neither the element of financial benefit nor right and ability to supervise appear to encompass an analysis of the defendant's intent.

As I noted in my testimony, the typical formulation of contributory infringement includes a reference to the defendant "inducing" the direct infringer to commit infringement. This

concept of "inducement" is a dormant one in copyright law, with no court yet considering it fully. The concept of "inducement" seems to involve implicitly a notion of intent on the part of the defendant, but it is unclear how it is to be applied because of the lack of court cases. In my view, S. 2560 is an appropriate effort to create an explicit form of this dormant species of secondary liability.

Question 6

Some have claimed that the Inducing Infringement of Copyrights Act would undermine fair use. You and I have long worked together to protect this important doctrine. Would the Inducing Infringement of Copyrights Act undermine fair use?

No. S. 2560 does not and should not have any effect on fair use. It is a bill addressing secondary liability for copyright infringement, which requires that the underlying activity on which it is based is in fact infringement. A determination of infringement necessarily involves a finding that an exemption like fair use does not apply to the activity.

I believe some have asserted that a new form of liability might eliminate technology that someone might use to make a fair use of copyrighted works. The whole point of S. 2560, and our effort to work with your staff and interested parties over clarifying language, is to ensure that the bill does not target general purpose technology like that which might be used by someone engaging in fair use. That is why I support the behavior-based approach taken in this bill, which does not target technology, but how technology is used by the services seeking to profit from the clear infringement of others they induce.

U.S. Copyright Office
Responses to Questions Submitted by Senator John Cornyn
Hearing before the Committee on the Judiciary
"Protecting Innovation and Art while Preventing Piracy"

1. *Elements from S. 2560 are drawn from the patent law. Specifically, the heart of the bill is based on "intentional inducement" of copyright infringement. However, the Patent Act uses he terminology "active" inducement. Where in the language of S. 2560 is the requirement of an "active" inducement. Can you explain the pros and cons of using the language of intentional inducement as opposed to active inducement?*

S. 2560 draws from the patent law to the extent that it explicitly recognizes a form of secondary liability for copyright infringement for intentionally inducing others to infringe, in the manner that Section 271(b) of the Patent Act creates liability for actively inducing others to infringe. As I understand the goal of S. 2560, it is not to replicate the patent law standards into copyright law, but to recognize a cause of actions against those parties that enlist others to commit infringement and profit from that infringement. It is my view that we should develop liability tailored to the needs of an effective copyright system first and foremost.

As to a comparison between the standards of "active" inducement and "intentionally induces," it should be noted that neither I nor my staff are patent experts. In my view, however, "intentionally induces" is an appropriate standard for this form of copyright liability, as it provides a relatively high level of *mens rea* that should limit its applicability to only those "bad actors" the bill targets. Indeed, the standard of proof laid out in the definition of "intentionally induces" provides that intent may be shown by "**acts** from which a reasonable person would find intent to induce ...," which places the focus on examining what the defendant has done to determine his or her intent. We understand the concerns raised by some that this standard may be too indefinite to provide guidance to actors in the marketplace, and are working with those parties and committee staff to develop changes to the bill that address those concerns.

2. *I recognize that the law is far from clear on this point – but the Patent Act has been interpreted – at least in some case law – as requiring a specific intent to induce infringement. Specific intent is necessarily a subjective intent. How do you reconcile that with the text of S. 2560 which seems to indicate that the required intent will be based on an "objective, reasonable person standard"?*

Because we are not patent law experts, we cannot make a detailed comparison of the specific intent standard in the patent context and the intent standard in S. 2560. It is my view that an intent standard is needed in S. 2560 to make clear that passive activity, such as the mere dissemination of a product that might be used to infringe, would not be liable under this bill. However, the required intent cannot be entirely subjective, because that would permit any defendant to escape liability by simply testifying that he or she did not have the intent to induce another to infringe. It might also permit a defendant to escape

liability when he or she honestly believed that the conduct he or she is inducing (e.g. by so-called "file-sharing" without authorization of the copyright owner) is not infringing. Courts must be able to look to evidence of how that person acted in the circumstances to determine whether the intent requirement is satisfied. We are working with staff and interested parties to provide more clarity to the nature of the evidence of intent that would be considered by the court.

3. *Proponents of S. 2560 claim that the bill covers only a narrow class of cases not at issue in Sony Betamax – those in which a distributor of copying devices intends to induce infringement? Is this an accurate statement? Does the language in S. 2560 adequately maintain the defense of "substantial noninfringing uses" as promulgated by the Sony Betamax decision?*

I agree that S. 2560 is intended to cover circumstances not at issue in the Betamax decision – those in which the provider of a service or technology intentionally induces others to infringe. The bill would recognize a separate form of liability for inducement, and leave untouched the existing doctrines of contributory infringement and vicarious liability, and the defenses to those doctrines, including the Betamax case. It is my view that manufacturing or selling a device capable of substantial noninfringing uses will not itself be sufficient to constitute inducement under S. 2560, absent other acts showing an intent to induce infringement. As I noted in our testimony, we are open to making this conclusion more explicit in the bill itself, and are working with staff and interested parties on potential changes to the bill that would more explicitly address this issue.

4. *It is my understanding that under that Patent Law, the manufacturer or seller of a device capable of noninfringing uses can be held liable for inducing patent infringement only if he takes active steps beyond the sale or manufacture to encourage direct infringement. Is that a fair statement? If so, how would this concept of inducement transfer to the concept advanced by S. 2560?*

Again, we are not experts in the patent law, so we cannot offer a definitive answer to your characterization of when manufacturers of devices are liable under the Section 271(b). That said, we understand that that principle appears to be fairly well established under the patent case law. *See* 5-17 *Chisum on Patents* sec. 17.04[3] and notes 9-11. It is my understanding that the inducement liability contained in S. 2560, with its "intentionally induces" standard, is meant to incorporate that principle. As I noted above, we understand that some have concerns that the bill could be more explicit on this point, and we are working to develop language that would clarify this issue.

Questions By Senator Leahy for Gary Shapiro

1. Do you agree that unauthorized distribution of copyrighted materials is illegal?

Section 106(3) of the Copyright Act gives copyright owners an exclusive right "to distribute copies or phonorecords of the copyrighted work ***to the public***...."[1] The mere act of "distribution" does not constitute infringement. An unauthorized distribution to the public of an entire copyrighted work is widely regarded as illegal. However, there are many circumstances in which an unauthorized "distribution" may not be "to the public," or if to the public may be regarded as fair use or be otherwise within the rights of the person performing such a distribution:

- A portion of the copyrighted material may be publicly distributed for purposes of news reportage, criticism, scholarship, satire, parody, essential functionality, or other fair use purposes.
- The entire work might be transmitted for private, noncommercial purposes among individuals in a manner that falls short of a distribution to the public. Such a "distribution" does not, alone, intrude on a right reserved to a copyright owner, and in particular circumstances may also qualify as a fair use.
- Fixations of copyrighted materials may also be physically redistributed, on a commercial or noncommercial basis, after an initial authorized distribution by the copyright owner. The right to such distribution is protected by the "first sale" doctrine, codified at 17 U.S.C. § 109.

2. Do you agree that under current common law principles, inducing others to commit copyright infringement is illegal?

Under the Copyright Act, which incorporates common law principles, "inducement" may be an element of the doctrine of contributory infringement. Facts supporting a finding of "inducement" do not and should not, however, automatically lead to a finding of secondary liability. All participants in the hearing, with the possible exception of the Register of Copyrights, seemed to agree that the following circumstances – which arguably involve "inducement" -- ought *not* to lead to a finding of secondary liability:

- A device such as an "iPod" facilitates and arguably "induces" the unauthorized identification, capture, storage, organization, and repeated playback of copyrighted songs.
- A computer program imbuing a device with "TiVo" – type functionality provides a program "guide" and operational software for the unauthorized identification, search, recording, indexing, and "librarying" of copyrighted works.

[1] 17 U.S.C. § 106(3) (emphasis supplied).

- An email program provides for the unauthorized transmission of copyrighted works over the Internet. The same device may contain a program that enables and simplifies the "posting" of such a work on an Internet web site.

3. *Modern digital technology has made it possible for a company to avoid direct infringement themselves while intentionally facilitating and profiting from massive infringement by others. This bill would clarify that such companies are liable for their conduct. Do you agree with this intended consequence?*

The fact that favorable consequences may flow from legislation does not make passage advisable if unfavorable and / or unintended consequences may flow as well. In such a circumstance, I would not agree with pursuing achievement of the intended consequences. However, CEA and HRRC have joined several other private sector organizations in suggesting discussion of an alternative approach that is targeted more directly at precisely the type of "massive infringement" that motivated S 2560.

4. *You claim that this legislation represents a "radical and unfortunate change" to the principles laid down in the Betamax decision. I support the Supreme Court's decision in Betamax, but perhaps you have a different understanding of the decision than I do. Do you believe that decision can reasonably be read to address the situation in which companies build their businesses by intentionally inducing others to infringe copyright?*

Yes. The case law following *Betamax* contains examples of such secondary liability under existing doctrines. It is the addition of a separate, independent, and necessarily imprecise cause of action for "intentional inducement" that we have identified as a radical departure from *"Betamax"* principles.

5. *You stated in your testimony that the Inducing Infringement of Copyrights Act "targets more than P2P companies." To the extent that you were referring to the fact that the Act targets no particular technology, but rather the behavior of inducing others to infringe copyrights, your statement appears to be correct. You go on to say, however, that under the Inducing Infringement of Copyright Act Americans would not be able to enjoy the VCR. However, in the Betamax case, the Supreme Court stated explicitly that VCRs do not induce copyright infringement. Do you disagree with the Supreme Court's express statement regarding VCRs, and the historically narrow scope of the inducement doctrine in copyright law?*

Specifically, in my written testimony I said:

- "For example, actual or constructive knowledge of infringement, coupled with providing a technology or service that facilitates that infringement (e.g., selling a VCR or CD-R or DVD recorder) could provide proof of intent.

- Is the relevant intent the specific intent to cause copyright infringement, or is it enough that the alleged inducer intends to cause another to do an act (when the inducer does not know the act is infringing)?"

I also quoted from the complaint in a lawsuit,[2] filed only a few years ago by several major motion picture studios, in which the following independent cause of action was set forth:

"The Seeking, Recording, Sorting and Storage Features"

"Defendants cause, accomplish, facilitate and ***induce*** the unauthorized reproduction of Plaintiffs' copyrighted works in violation of law. *** The ReplayTV 4000 device provides expanded storage, up to (currently) a massive *320 hour* hard drive, which allows the unlawful copying and storage of a vast library of material. *** ReplayTV 4000's expanded storage and sorting features organize disparate recordings into coherent collections, and ***cause, facilitate, induce and encourage*** the storage or "librarying" of digital copies of the copyrighted material, which harms the sale of DVDs, videocassettes and other copies, usurps Plaintiffs' right to determine the degree of 'air time' a particular program receives in various cycles of the program's distribution ...."[3]

In fact, the standard of "inducement" that would be established by S 2560 and by a success in the "Replay" case seems virtually the same as the standard advocated by Justice Blackmun and his colleagues in their ***dissent*** in the *Betamax* case.[4] That dissenting opinion would have sent the case back for a trial in which infringing conduct would have been more readily presumed, and knowledge of the likelihood of such conduct would have played a major role in the case's determination. I cited the inevitable result in my testimony:

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[2] *Metro-Goldwyn-Mayer Studios, Inc. et al v. ReplayTV, Inc.*, U.S. District Court, Central District of California, Case No. 01-09801, Complaint of MGM, Orion Pictures, Twentieth Century Fox, Universal City Studios, and Fox Broadcasting, ¶¶ 24-25, November 14, 2001 (only bolded emphasis is supplied).

[3] *Id.* These allegations were grouped and made *separately* from those concerning the "distribution" (¶¶ 19-23) and "autoskip" (¶¶ 28-29) features that received more press attention. The pleadings in this case can be found at http://www.eff.org/IP/Video/Paramount_v_ReplayTV/.

[4] "The District Court also concluded that Sony had not caused, induced, or contributed materially to any infringing activities of Betamax owners. Id., at 460. In a case of this kind, however, causation can be shown indirectly; it does not depend on evidence that particular Betamax owners relied on particular advertisements. In an analogous case decided just two Terms ago, this Court approved a lower court's conclusion that liability for contributory trademark infringement could be imposed on a manufacturer who 'suggested, even by implication' that a retailer use the manufacturer's goods to infringe the trademark of another. Inwood Laboratories, Inc. v. Ives Laboratories, Inc., 456 U.S. 844, 851 (1982); see id., at 860 (opinion concurring in result). ***I think this standard is equally appropriate in the copyright context***." 417 U.S. 417, 489 (dissenting opinion of Justice Blackmun, emphasis supplied).

- "S. 2560 would effectively force anyone hoping to come to market with a product that transmits or stores copyrighted works to **negotiate *in advance***, to quiet *any* of the concerns of *any* copyright proprietor that has the resources to sue."

6. *You praised the Betamax case as giving a "green light" to inventors and venture capitalists. I have long supported the outcome in that case, and I agree that that case gives important protections to those who bring us new technologies. However, your statement that the Inducing Infringement of Copyrights Act would reverse Sony appears unfounded, as that case itself acknowledged the doctrine of inducement, even as it applied the objective "substantial non-infringing use" test. In your view, did the Sony case intend to undermine the common law doctrine of inducement of copyright infringement?*

The *Betamax* majority opinion did not address *copyright* "inducement" as such, although it did reject the dissent's suggestion that secondary infringement should be analyzed under an inducement standard borrowed from *trademark* jurisprudence.[5] Since "inducement" was recognized then, as it is recognized now, as part of the doctrine law of contributory infringement,[6] the Court in *Betamax* implicitly rejected the applicability of a separate common-law theory of inducement liability to the particular facts in the record. As such, the *Betamax* case would not support or pre-endorse the dramatically expanded version of inducement set forth in S. 2560, which – as I testified – goes far beyond anything recognized in traditional copyright.

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[5] "We have consistently rejected the proposition that a similar kinship exists between copyright law and trademark law, and in the process of doing so have recognized the basic similarities between copyrights and patents. The Trade-Mark Cases, 100 U.S. 82, 91-92 (1879); see also United Drug Co. v. Theodore Rectanus Co., 248 U.S. 90, 97 (1918) (trademark right "has little or no analogy" to copyright or patent); McLean v. Fleming, 96 U.S. 245, 254 (1878); Canal Co. v. Clark, 13 Wall. 311, 322 (1872). ***Given the fundamental differences between copyright law and trademark law, in this copyright case we do not look to the standard for contributory infringement set forth in Inwood Laboratories, Inc. v. Ives Laboratories, Inc., 456 U.S. 844, 854-855 (1982), which was crafted for application in trademark cases.*** There we observed that a manufacturer or distributor could be held liable to the owner of a trademark if it intentionally induced a merchant down the chain of distribution to pass off its product as that of the trademark owner's or if it continued to supply a product which could readily be passed off to a particular merchant whom it knew was mislabeling the product with the trademark owner's mark." 464 U.S. 417, 439 (n. 19, emphasis supplied). In *dictum*, the Court also commented that even if it the trademark standard were applied, it would not support a finding of liability on the facts found by the district court in *Betamax*.

[6] The *Gershwin* case included an inducement allegation. As noted by the Supreme Court: "In Gershwin Publishing Corp. v. Columbia Artists Management, Inc., 443 F.2d 1159 (CA2 1971), the direct infringers retained the contributory infringer to manage their performances. *** The Court of Appeals emphasized that the contributory infringer had actual knowledge that the artists it was managing were performing copyrighted works, was in a position to police the infringing conduct of the artists, and derived substantial benefit from the actions of the primary infringers. Id., at 1163." 464 U.S. 417, 438.

7. *Evidence strongly suggests that certain peer-to-peer networks take affirmative steps to encourage copyright infringement, to protect infringing users from getting caught, and attempt to thwart the effort of copyright holders to enforce their rights. In your view, can any distinction be drawn between these types of networks that clearly attempt to induce their users to infringe copyrights, and those who create and maintain useful new technologies that might also be put to some infringing use?*

CEA, HRRC, and our private sector colleagues, at your invitation and Senator Hatch's, have labored to do so in the alternative draft that we have submitted to the Judiciary Committee staff. Like all possible amendments to the Copyright Act, this draft should be rigorously scrutinized and reviewed to assure that it *does* address deliberate and specific facilitation of the mass, indiscriminate infringement of copyrighted works *without* damaging, or providing a disincentive for the creation of, new and useful technologies that might also be used for infringing purposes. A copy of this discussion draft is attached.

8. *You state that there is no way that " the Supreme Court objective test and the bill's subjective test can coexist." Why is this area of the law different from the many areas of the law that provide both objective and subjective tests for liability?*

With respect to the marketing of a device or software, a test that is essentially subjective generally can be pursued in court only via massive discovery aimed at gleaning the intention behind the product's conception, design, development, testing, manufacture, and marketing. Even in cases in which summary adjudication (which seems highly unlikely as S 2560 is written) may be available, the potential cost of such discovery, as undertaken by a well-funded claimant, may be such as to discourage the innovation, or its funding, in the first place. And, if the innovation is undertaken, the prospect of such a claim, and its attendant discovery, may chill and distort creative and financial processes.

9. *You appear to deride the Register of Copyrights, as, you say, she does not "have to counsel people as to whether or not to introduce products and don't have to put their money at risk[.]" I have worked with the Register and with many in the copyright and technology communities toward useful solutions for many significant problems. Is it your position that the Register of Copyright's view that the Inducing Infringement of Copyrights Act adequately clarifies existing common law is unfounded?*

While we have great respect for the Register personally, and for her office, we view with alarm her suggestion – which ran counter to the your views, those of Senator Hatch, and of all other participants in the hearing – that the *Betamax* doctrine, in the long run, may not be useful or worthy of preservation. We feel that this view infused the conclusions, and the concluding portion of, the Register's testimony. We believe that the Register's view of S. 2560 is more consistent with her long-term view of the *Betamax* doctrine than it is with the preservation of that

doctrine. We appreciate the Register's candor about her lack of support for the *Betamax* holding, but disagree with any such outcome.

10. You state that the Inducing Infringement of Copyrights Act is ill-conceived because "technology change quickly," and you have to "see where technology is going." I agree that solutions to online file-sharing should not focus on technology, which is why this bill deals explicitly – an only – with conduct, and does not target any specific technology. In what way do you feel that legislation targeting certain unlawful behavior might be undermined by the fact that technology is ever-changing?

We opposed Senator Hollings' bill in the last Congress, as well, on the basis that it would chill technological development by requiring a negotiation with content owners before even fairly generic new products could come to market. As I indicate above, we think that an intent-based inducement approach would chill the conceptual, developmental, and marketing stages of product development, causing technology to change *less* quickly than either our competitiveness or our markets would otherwise demand. The legislation would not necessarily be undermined by the changes in technology; *it would be the changes in technology that would be undermined by the legislation.*

Questions By Senator Cornyn for Gary Shapiro.

1. Would you agree that the actions of some peer-to-peer technology providers such as KazAa are wrong? That the behavior in which they engage – be it allegedly blocking the spoof efforts of the copyright holders, or opting users into opening their hard drives and other key actions does have the effect of encouraging the infringement of copyright?

We don't have first-hand knowledge of the technical measures employed by technology providers and the counter-measures that content providers may use. More generally, we think that to the extent self-help counter-measures are available to content providers in reaction to public redistribution practices, they should be considered as alternatives to any legislatively mandated scheme. Similarly, we think consumers deciding to use network services or software should maintain control of, and responsibility for, the use of their own hard drives. To the extent any service provider denies to consumers the right and ability to control access to their own hard drives, this may be an issue for scrutiny. "Inducement" legislation, such as S 2560, however, is not the appropriate vehicle for such scrutiny.

2. *Follow-up: Should that behavior be stopped – be it through the courts, legislation or other action?*

We think some elaboration on context would be necessary to answer this question. Our proposal, made jointly with several other private sector groups, for the discussion of an alternative approach addressing services or products specifically aimed at the "mass, indiscriminate infringing" distribution of works may indeed address the practices framed in this question. As we have indicated, we think our own draft ought to be thoroughly reviewed and discussed as to its effects and implications.

3. *I recognize you are opposed to this specific legislation. Do you have any ideas or even your own solution for Congress to consider in our effort to stop companies engaging in behavior that arguably is aiding, abetting, inducing – or whatever words you wish to choose – the infringement of copyrighted works?*

Yes. The alternative draft, referred to above, has been provided to Committee staff. It is also enclosed with these answers for reference. We believe this approach provides a more appropriate basis for further discussion – though we stress that careful consideration and review should be given to *any* legislation that would amend the copyright laws.

SUBMISSIONS FOR THE RECORD

Statement of Mitch Bainwol
Chairman and CEO
Recording Industry Association of America
Before the
Committee on the Judiciary
United States Senate
On
S. 2560, the "Inducing Infringement of Copyrights Act of 2004"

July 22, 2004

Mr. Chairman and Ranking Democratic Senator Leahy, thank you for holding this important hearing today to examine S. 2560, the "Inducing Infringement of Copyrights Act of 2004".

The beginning of the 21st century has been a trying time for intellectual property. The promise of new opportunities in production and distribution has been hijacked by some who would rather use emerging technology to plunder entire creative content industries. We cannot afford to remain complacent as these parties further erode the value of our nation's intellectual property assets.

S. 2560 is designed to provide a remedy against companies whose business models are premised on the wholesale theft of the creative work of others. Technology is *not* the focus of this bill. Rather, S. 2560 targets behavior, namely specific actions taken by those who have hijacked technology to perpetrate and promote theft on a massive scale of this country's leading export. It's a moral behavioral test that targets the bad guys, not legitimate commercial actors.

As you know, the music industry has been devastated by worldwide piracy. In 2000, the top ten hits sold 60 million units in the U.S. Seven of the ten sold more than 5

million units each; every one of them sold at least 3 million units. But last year, in 2003, the top ten hits were cut almost in half, to 33 million units. Just two of the ten sold more than 5 million units; five of those top ten hits sold less than 3 million units. This slide has been caused predominantly by illicit P2P (peer-to-peer) services, where these top ten hits and other valuable content are offered to users—unauthorized and for free. Some have suggested that these services in fact help us by driving sales. This defies logic and common sense. If one can get something for free, without consequence, buying it becomes less attractive. In any case, given the unfortunate sales figures just stated, we respectfully ask that these illegitimate services do us no more favors.

Record labels are particularly vulnerable because they are dependent upon a single source of revenue – sales of recorded music. Record labels do not have a full performance right and therefore earn no royalties from radio play. They do not make money from artist tours or merchandise. They do not make money from endorsements of other products. Unauthorized file-sharing—especially that of the biggest hits—destroys a label's sole revenue stream.

While the free-for-all nature of illicit P2P services is alluring to users in the short term, it will ultimately drain the well dry—and faster than anyone thinks. Jobs in the music industry are down by about a third over the last several years. Families have suffered. And so has the music. Artist rosters have had to be slashed as cost cuts continue. Fewer dreams are being funded and this creative product is lost forever. Illicit P2P services, the inspiration for S. 2560, are precisely the ones stealing these dreams.

An independent study conducted last summer noted that over 97% of the files "shared" using these P2P networks are illegal. The infringement is remarkably pervasive.

A recent academic study estimated that almost a billion illegal downloads take place each and every month. Four of the top ten downloaded applications on the Internet are P2P programs operated by companies who purposefully profit from illegal conduct.

To make their money from advertising and bundled spyware in their applications, these rogue P2P companies must first generate as many eyeballs as they possibly can. They do that by inducing American kids – and others – to break the law by stealing the work of creators. These companies are far from the benign services they claim to be. They are havens for pornographers. They compromise computer security. They facilitate the unintended disclosure of personal documentation – resumes, tax and credit card data, medical returns and more. And their warnings – about privacy abuse, security, pornography and copyright - are anything but conspicuous. No objective review of these services can possibly conclude that they have any pretense of legitimacy.

It is important to note that P2P technology itself is not to blame. Rather, the problem is caused by profiteers who have taken a promising new technology and corrupted it for self-serving interests. Common sense dictates that these operators should be held responsible for their actions, but usage of existing law has veered off course. While the law has not changed, evolution of P2P technology has confused some courts in its application.

Using previous court decisions as a roadmap, new P2P services created a "de-centralized" system intended to avoid the liability imposed upon the original services that were operated by a central server. Claiming a lack of "control" over their users' activities, these services have managed to shift the focus of liability to those users. But regardless of the "centralized" or "de-centralized" structure of these services, their

actions are what should dictate their liability. It is their intentional inducement of infringement on their networks that should be the proper focus.

Unfortunately, a District Court in California misinterpreted existing law, ruling that these new services were not liable despite their obvious profit-by-infringement business model. Yet even this court recognized the injustice of its own decision and called for "additional legislative guidance."

That additional legislative guidance is available in S. 2560. Setting the concept of secondary liability back on track, it focuses on behavior, *not* technology. This bill merely targets bad actors—those who have hijacked technology for their own illegitimate purposes—and not on the technology itself. It applies an extremely high standard: *intentional* inducement. Specifically, intentional inducement to *infringe*, not simply to *use* technology which may infringe. This standard is consistent with the 1984 *Sony Betamax* case, and recognizes that technology can be used for both legitimate and illegitimate purposes. Those who simply produce devices that can be used for either purpose are not covered by this legislation. Providing such technology, regardless of how it is ultimately used, is not enough to find inducement. S. 2560 requires purposeful action, deliberate and intentional conduct to induce others to break the law. It's the premise behind aiding and abetting under the criminal laws. There are people who make illegal archival copies of videos and others who illegally download unauthorized songs onto their iPods. But the companies who offer the technology that makes these activities possible have not intentionally induced such infringement. Sony, Apple, and other legitimate participants in the marketplace, remain untouched under this bill.

Even opponents of S. 2560 have conceded that those who intentionally cause copyright infringement should be punished. We realize that many of these opponents are concerned that the bill's current language may be misinterpreted to apply to legitimate products, and we stand ready to work together to address valid concerns. We therefore encourage those expressing opposition to work cooperatively and productively so that the principle underlying the bill – that those who intentionally cause copyright infringement should be punished – is fulfilled.

But inaction is simply not acceptable. Legitimate businesses, consumers, and the many people engaged in the creative and technology communities deserve legislation that will ensure a fairer, safer, and more productive future. The music industry has already embraced the Internet and the incredible opportunities for new products and services that benefit consumers. The delivery of digital music online from licensed services, for example, has ushered in an exciting new way for consumers to listen to the music they love. But these new offerings cannot survive in competition with illicit businesses. It is imperative that Congress insist on the rule of law and not accept a business model based on thievery.

Committee on the Judiciary

Statement of Ed Black
Computer & Communications Industry Association

Concerning Unintended Consequences of
S. 2560, the Inducing Infringement of
Copyrights Act of 2004

July 22, 2004

I appreciate the opportunity to present the views of CCIA on this very important subject. CCIA members come from across the industry, and include computer hardware and software makers, Internet service providers, telecom equipment manufacturers, system integrators among others. Together our members have annual sales of more than $200 billion annually and employ more than 500,000 people worldwide.

Summary

Our member companies produce and depend on intellectual property for almost all facets of their business and we continue to support strong copyright protection. Thus, we greatly appreciate the concern and effort necessary to develop new legislation in this vitally important and complex area.

Unfortunately, the Induce Act is an overly broad and vague bill that significantly increases the litigation exposure of many companies whose products or services might be used to make both legal and illegal copies. This will impair innovation, and new products and services related to the handling of third party media will be greatly curtailed, if not eliminated. The foreseeable reduction in companies' freedom to innovate will cause innovating firms to move offshore to more friendly technology environments or be held hostage by content developers. Technology companies will be forced to

negotiate the design of their products with content companies that have shown a complete unwillingness to adapt to new technologies unless forced to by external forces. The history of new communications technology over the last century, be they piano rolls, radio, the VCR or MP3 files, has been one of incumbents seeking to block or cripple the innovator. We fully expect the future will be no different, and to empower the incumbents with more legal tools is unwise and unnecessary.

S. 2560 creates a murky legal climate by the adopting a standard of inducement that tries to hold developers of new technology liable for encouraging others to make illegal copies of copyrighted works. Unfortunately, the bill's attempts to transplant a similar doctrine from patent law and apply it to the entirely different world of copyright law upsets the delicate balance that has been molded out of decades of consistent case law.

The Chilling Effects of the IICA

The dominant players in the content industry have a long history of attempting to stop innovation whenever it seems to threaten their contemporary business models. Most famously, the MPAA tried – and failed – to litigate the VCR into extinction, and we have all benefited from that decision. The recording industry, however, succeeded in hobbling the digital tape recorder into effective irrelevancy by insisting on copy control technologies that consumers did not accept.

CCIA agrees that creators need protections from illegal copying, but not through the punishment of an entire industry or the destruction of consumers' rights for the actions of a few. The Supreme Court seems to agree. Indeed, the court ruled in *Betamax* that new technologies evolve in ways that cannot be easily foreseen. Such evolution changes the marketplace for the better.

We see no such spur to the marketplace from S. 2560. Rather than encouraging innovators to invent, S. 2560 places a roadblock in their way. This measure signals to our industry that we must abandon all hope of innovation in new media unless it carries the approval of entrenched entertainment interests.

Given the language before us, we feel confident that many companies will find little to like in the entertainment sector. Venture capitalists, likewise, will be wary of funding new media for fear that their already risky ventures will die slow deaths in court before they have a chance to reap the profits of their work.

Worse still, we believe that, if passed, S. 2560 will serve as leverage for content companies to demand the redesign of existing devices that might be used to infringe their copyrights. The end result will be a world of more consumer frustration, less choice, and less creativity.

Since we have little expectation that all other countries will follow our lead on this bill, we come to this simple conclusion: Others will innovate where we refuse to. Faced with an effective ban on media technologies not approved by all major content companies, other countries will be well positioned to take our place in the global marketplace.

The IICA Is Vague

S. 2560 is said to "fix" the *Grokster* ruling, which found that developers of peer to peer software cannot be held liable for illegal copying unless they have specific knowledge of, and control over, such infringement. Since such knowledge and control is absent in many peer to peer applications today, a new standard of inducement would presumably hold liable at least some peer-to-peer developers who have not been liable to date.

S. 2560 goes well beyond the borders of current doctrines relating to inducement, however. For while individuals who actively lure others into infringement would be liable under this bill, so, too, would untold numbers of innovators who want simply to improve the ways in which we enjoy creative works of all kinds. S. 2560 applies to anyone who intentionally "aids, abets, induces or procures" infringement, with the intent inferred in accordance with a "reasonable person" standard. Courts are invited to make this determination independent of the *Betamax* standard, which applies to manufacture of devices, but not the state of mind of the producer of those devices.

We worry about the consequences of such language. *Betamax*, it has been said, is the Magna Carta of the technology industry. Under the *Betamax* standard, innovators who can show that there are substantial, non-infringing uses of their technologies are generally immune from claims that they themselves are infringing. This standard is objective, and thus allows for dismissal of frivolous lawsuits. S. 2650, by contrast, does not ask anything at all about non-infringing uses. Rather, it requires only that plaintiffs convince a finder of act that an inventor somehow planned to make it easy for others to infringe, and did so with his device. This finding is based on a subjective evaluation of a defendant's state of mind, and not the merits of his invention. Given the nature of the inquiry, it is hard to imagine that any such suit could be resolved before trial. Because S. 2560 ignores the device in question entirely, it leaves *Betamax* standing by circumventing it entirely.

IICA Imports a Criminal Law Standard Into Civil Law

Supporters have made frequent references to the criminal law of aiding and abetting in explaining why this concept should be imported into copyright law. The criminal law contains several types of secondary liability. They include convincing an innocent person to commit a crime, engaging in a conspiracy to commit crime, and so on. Similarly, the IICA creates civil penalties for anyone who "intentionally aids, abets, induces, or procures" a copyright violation.

Many procedural safeguards, such as the presumption of innocence, protect those accused of crimes. Because of these safeguards, criminal cases must be comprehensive and detailed, and require prosecutors to prove their cases "beyond a reasonable doubt." Civil proceedings such as those anticipated under S. 2560 lack such protections. If the evidence tips even slightly in the plaintiff's favor, then the defendant is guilty. The broad, comprehensive concept of criminal inducement, which was developed to work within the

safeguards of a criminal case, would become a blunt and undiscriminating weapon in a civil copyright suit between private parties, ultimately favoring the strong, incumbent firm over the comparatively weak startup.

Copyright Law Already Prohibits Intentional Inducement

The "secondary liability" that is inducement is generally not defined by Congress, but instead created by case law. This allows for an important flexibility: it lets judges protect legitimate, beneficial activities that Congress may not have anticipated against the threat of lawsuits that arise from the actions of others.

Copyright law, like many areas of the law, already contains a ban against knowingly helping someone to violate a copyright. Over the past twenty years, the courts have refined this ban into a consistent but flexible doctrine that protects technology innovators, particularly consumer electronics and software makers, while punishing those whose only purpose is to assist copyright violations. A company can be found liable for "contributory infringement" if it assists a user in violating a copyright. The assistance must be substantial and meaningful: merely renting space to a copyright violator, or providing the violator with a general-purpose tool, is not enough to make the company liable. By analogy, a hardware store owner who sells a crowbar to a burglar is not guilty of assisting the burglary, because a crowbar can be used for many things. If the crowbar came with instructions on how to use it to break into buildings, the hardware seller may be liable.

More specifically, the Supreme Court articulated a shield for technology companies that create popular, multi-use products. Under the existing law of contributory copyright infringement, if a product is sometimes used for illegal copying, but has other possible uses as well, the makers of the product will not be liable without other evidence that they encouraged the copyright violation. Until now, Congress has wisely refrained from disturbing this balanced approach that has worked so well.

For more than 100 years, Congress and the Courts have allowed inventors to invent, and creators to create. Litigious as our society is, most inventors have known that if they built something better than what came before, they would likely be rewarded for it.

S. 2560, unfortunately, seems ready to tip the balance strongly in favor of entrenched interests and away from innovators. Whatever difficulties we may have with abused of intellectual property today, we believe S. 2560 will engender problems whose consequences will be far worse.

STATEMENT OF

THE DIRECTORS GUILD OF AMERICA

Submitted to

THE SENATE JUDICIARY COMMITTEE

HEARING ON THE INDUCING INFRINGEMENT OF COPYRIGHTS ACT OF 2004

July 22, 2004
Washington, DC

The Directors Guild of America (DGA) submits this statement in support of the "Inducing Infringement of Copyrights Act of 2004." We commend Senator Hatch and Senators Leahy for the introduction of this groundbreaking legislation. This Guild places great importance on the prevention of wide spread pirating of U.S. made movies, television programs and other creative works. It is our members who create these works and those who illegally and with full knowledge induce others to "steal" them are knowingly destroying the fundamental protections—both economic and creative—that copyright law exists to preserve.

The Directors Guild represents over 12,600 directors and members of the directorial team who work in feature film, television, commercials, documentaries, and news. The DGA protects and advances these directors' economic and creative rights--working for their artistic freedom and fair compensation for our work.

Film and television are indigenous American art forms, which filmmakers have raised to their level of creativity and popularity. Motion Pictures have documented, reflected upon and portrayed the American experience for almost 100 years. Our goal is to ensure that this craft continues unabated for the benefit of millions of film and televisions viewers' worldwide, and that our members continue to earn their living giving their talents to a craft they love.

We are now in the digital age that has begun to fundamentally change the relationship between creators and the public. American consumers—consumers around the world—have gained instant access to all kinds of content, including the motion pictures our directors make. The question of how this access is used and abused, has major implications for not only for copyright holders and consumers, but also for filmmakers and other creative artists in our industry.

This is why we applaud the introduction of S 2560. For the first time it addresses the real problem of Internet piracy by putting the criminal intent where it rightly lies, not on the consumer, the very people for whom our members' create films and television productions—but on the companies that create illegal P2P networks and then knowingly entice the public (most often teenagers) to infringe the copyright. We recognize that P2P technology has many benefits, but it also permits companies to go into business with the full intent of enabling widespread and unauthorized uploading and downloading of movies, television programming, music and software files. And it is those companies who have opened the floodgates to blatant piracy of copyrighted works.

When you hear the arguments that those who want unfettered access brought forth, it appears that most of them believe—or want others to believe—that once a film or a television program is completed, its value to those who create it is gone. Nothing could be further from the truth. Directors –and other creative talent—are very real stakeholders in the outcome of efforts to stem illegal P2P file sharing networks. There are very real economic and creative consequences to the creator if unauthorized P2P networks are allowed to effectively "steal" our members' work.

Illegal—and thus often criminal—infringement of copyrights' protections not only adversely affects the value of the copyrighted work to the producers/copyright holder; it also diminishes the economic value flow to the creators. That is why directors' livelihoods are dependent on the premise that their work will be protected from copyright infringement that is made possible by a number of P2P networks. Our members depend not only on the full compensation for their works when they are released but also on the residual payments for those works when they are "reused" on free and pay television, DVDs and videocassette, both domestic and international.

Our industry's residual system--which in the DGA's case has existed for 40 years--is designed to provide appropriate compensation to our members whose contributions to a motion picture or television program are so fundamental that without them it cannot be produced. In 2003, DGA collected and distributed in excess of $200 million in residual payments. These dollars represent bread and butter income to our members—a reality made even more necessary because our industry operates on the concept of freelance employment, meaning that our members are hired by a variety of employers on a production-by-production basis. Our members cannot count on a regular paycheck. What they can count on is ongoing income in the form of residual payments—that support their families and go into their pension and health plans.

In other words, businesses that encourage others to engage in P2P piracy—by allowing our copyrighted works to be downloaded without our authorization or compensation---take income directly out of directors pockets and their retirement plans. In addition, directors work--when distributed in an unprotected digital format—again through illegal infringement made possible by P2P networks, is easily altered and exploited, so that it no longer resembles what they have created even though their name may remain on it.

We submit this statement today to because the DGA wants to make clear that we cannot afford to have our members' livelihoods weakened by institutions or companies, who enable others to download and share our copyrighted work. All the while this companies pretend it is their "right" to do so without regard to the economic consequence of their actions on the original creators. Ironically, they admire our members' work so much that they feel justified in telling others to take it illegally.

P2P networks, if properly regulated, legally created and legitimately operated, can represent a market that may greatly benefit our members. However, if our members' works are not protected and pirated copies are openly available through these networks around the world without payment to our members, it is very likely that in the end neither the creator nor the copyright holder will find it easy to continue to make those works.

Enacting public policy that enables the creative artist and the copyright holder to sue the very companies that profit from encouraging copyright infringement, as proposed in the "Inducing Infringement of Copyrights Act of 2004," will go a long way to providing meaningful copyright protection. It is not only in the interests of our industry that the DGA supports this legislation, but also of the very public whose love of this most American of art forms began so many decades ago.

Testimony of

Andrew C. Greenberg

Intellectual Property Committee

to the

Senate Committee on the Judiciary

on

An Examination of S.2560,
The Inducing Infringement of Copyrights Act of 2004

22 July 2004

Mr. Chairman and Distinguished Members of the Committee:

I am honored to submit information on behalf of the Institute of Electrical and Electronics Engineers – United States of America concerning the implications of S. 2560 with respect to technological innovation and American Competitiveness.

IEEE-USA advances the public good and promotes the careers and public policy interests of the more than 225,000 technology professionals who are U.S. members of the IEEE. To that end, IEEE-USA supports our nation's prosperity and competitiveness by fostering technological innovation and promoting U.S. industry for the benefit of all. IEEE-USA is dedicated to promoting sound technology and public policy.

U.S. IEEE members serve on the "front line" of the U.S. Copyright and Patent System. Our members include inventors and software authors who create and use cutting-edge technology, who research and publish professional articles and journals, and who develop published standards that are the basis for widely adopted and critical technologies. They are the entrepreneurs and employees of firms that acquire, license and market the copyrighted product of those activities. For these reasons, IEEE-USA is deeply concerned that sufficient incentive be given to inventors and authors to innovate and write without unduly chilling the creation and development of non-infringing technology and improvements.

IEEE-USA has a compelling interest to ensure that copyright law comports with the principles set forth by the Founders in the U.S. Constitution, to promote the progress of sciences and the useful arts. Copyright law intimately affects the practices and advice that engineers give, and IEEE-USA respectfully suggests that the law enacted by Congress should not only promote progress, but should be comprehensible and practical for the professionals who provide that progress.

U.S. IEEE members are content owners and technologists alike, as well as members of the public. And so, IEEE-USA does not so much stand for any of these interests alone, as it does for all of them. Because promotion of progress requires a delicate balancing between those interests, IEEE-USA speaks, rather, for the balance itself, in the interest of our content makers, technologists and society as a whole.

As Abraham Lincoln noted, intellectual property laws serve to "add the fuel of interest to the fire of genius." However, that interest must not be so great, either in fact or because of uncertainty in its scope, as to grant authors control over any technology that may incidentally be used to infringe upon a work. Such technology regulation will unnecessarily stifle innovation and progress, and with it, the jobs and prosperity it would bring. For these reasons, IEEE-USA believes that it should *not* be indirect infringement of a copyright to manufacture, distribute or provide a hardware or software product or process that is capable of enabling substantial non-infringing use of a copyrighted work, unless the manufacturer, distributor or maker actively induces the infringement of a copyrighted work by another. By doing so, the well-established balance between proper incentives for copyright owners and protecting technological innovations from undue regulation can be maintained.

IEEE-USA believes that Senators Hatch and Leahy and their honorable cosponsors have spotlighted a valuable approach to a knotty problem in current copyright law with S. 2560. Nevertheless, IEEE has significant concerns about whether the language of S. 2560, as introduced, both reaches the goals and achieves the balance of interests that we believe bill's drafters were aiming for; with these reservations in mind, our testimony offers a substitute proposal that we think comes closer to achieving the aims of the bill's authors and sponsors, and we respectfully offer that alternative in an appendix.

Promoting Progress Of Science and Useful Arts Requires a Delicate Balance Between Interests of Copyright Owners and Technologist

Charged by the Copyright Clause, Congress crafted a Copyright system to promote the progress of science by granting authors exclusive and limited rights to their writings, together with powerful remedies under law to enforce those rights. Congress has also been mindful that granting rights to an individual has societal costs as well.

Accordingly, Congress carefully circumscribed the scope and nature of those rights. To protect only the expression of an idea, principle or discovery, but not the ideas themselves. 17 U.S.C. § 102(b). To allow the next generation of authors to freely use those ideas, and even to make fair comment and use of their expression. 17 U.S.C. § 107. To permit secondary markets for copies of a work after the author has been compensated by the first authorized sale of the copy. 17 U.S.C. § 109. Aspects of those ideas, principles and discoveries unprotected by copyright are governed by the Patent system, which in turn is circumscribed with its own system of checks and balances.

These limitations are as important to promoting progress as the grant of rights themselves. This is because, to paraphrase Ecclesiastes, nothing is entirely new under the sun. All invention and literature is ultimately created by those who have stood on "ye shoulders of Giants." This permit the next generation to borrow from the public domain that which Congress carefully reserved for all of us, and to satisfy that debt, with interest, in the form of new and even greater works and inventions made therefrom.

These protected and unprotected aspects of our works and inventions form an ecosystem for even further creativity and economic growth. The result has been a body of knowledge and culture with breadth and scope unparalleled in the American Experiment, together with tools and devices of unprecedented scope and power with which we may study, distribute and synthesize from those works

yet more works, inventions and tools. From this we all benefit with new jobs, forms of entertainment and access to knowledge and information in a way not previously known to the human endeavor.

And as with all ecosystems, the community of creators and inventors will flourish only when the balance is properly struck. Protections must not be too strong or uncertain in their application, lest overprotection of works today crush the development of technology tomorrow. Nor can protections be allowed to become so weak and toothless that inventors and writers abandon their craft for more individually profitable endeavors.

There is no silver bullet. While the principles are eternal, their application must be carefully observed and calibrated to a constantly changing world. Changes are in no small part a consequence of the thriving progress of a creative ecosystem, and should often be embraced, not only as a natural event, but as an important engine to drive further progress and prosperity. In rare cases, change may be so disruptive as to require action to preserve the balance.

Congress serves as the guardian of that balance in a changing world. You are the architects of that balance – the ones who measure and cut the chords of intellectual property policy; and the ones who determine whether our best and brightest will choose to write the Great American Novel, or go to law school. But Congress must also be mindful of how it measures and cuts the limits to those rights, to assure that our next generation of writers may use the works that have come before, and stand on the shoulders of giants.

As Congress is charged to deliberate whether and how to change our creative ecosystem to adapt to a changing world, it is essential that these cuts be made carefully: measured twice, and cut once. The balance cut between the interests of content owners and the public will determine whether we are promoting progress of Sciences by improving revenues for owners of existing works, or introducing an undue and dangerous form of technology regulation that may stunt innovation entirely.

Secondary Liability in Copyright: A Précis

Today, the Senate is once again asked to measure and cut, this time to consider when it is appropriate to extend copyright infringement liability to someone who has not infringed a copyrighted work.

Classical Vicarious Infringement. Although the question seems an odd one at first blush, it would be equally odd --and unjust-- not to hold an employer liable when its IT director tries to save money by installing unauthorized copies of a computer program pursuant to instructions. Although the employer did not directly infringe by making copies, we hold it vicariously liable for the directly infringing conduct of its employees who made the copies. Hardly a new idea, this judge-made notion of vicarious infringement is derived from the classical notion of *respondeat superior*, holding a principal liable for the tortious conduct of agents acting within the scope of their agency.

Classical Contribution to an Infringement. Likewise, it would be unjust not to hold liable a person lending a lawfully acquired print of a motion picture to a friend who is not an employee, but knowing that the friend intends to use the copy for an unauthorized public performance. While only the friend directly infringes, and the distribution of the legitimate copy was not itself an infringement, this example presents the classic case where liability occurs under the judge-made doctrine of contribution to the infringement of another.

Expansion of Classical Secondary Liability Principles. As we know, hard cases make bad law, and judges will from time to time, undertake to explain and extend existing secondary liability law to reach analogous and unjust circumstances. And so it was as courts wrestled to fit various forms of bad acting into the rubric of vicarious and contributory liability.

Dance Halls and Record Stores – the Expansion of Liability By Relationship. Vicarious Liability, traditionally, was liability from the relationship between defendant and the infringer. It has

been more than seventy years since the first of the Dance Hall cases, where vicarious liability was extended from the confines of principal-and-agent relationships to find the owners of dance halls responsible for the infringement of independently contracting orchestras, even where the owners may not have known or determined the songs that were played. Herbert v. Shanley Co., 242 U.S. 591 (1917); Dreamland Ball Room v. Shapiro, Bernstein & Co., 36 F.2d 354 (7th Cir. 1929). Inspired by the Dance Hall cases, the Second Circuit stated the modern rule to reach a chain of record stores for bootleg record sales by contracting retailers. Shapiro, Berstein & Co. v. H.L. Green Co., 316 F.2d 304 (2d Cir. 1963). There, the court found liability because the chain had "the right and ability to supervise" and "a direct financial interest" from the infringing activity. Unfortunately, as is all too common, the expansive language of this otherwise reasonable rule, when unmoored from the facts, has led to risk of judicial mischief.

Traditionally, a principal has an intimate relationship with and presumptive responsibility for the relevant conduct of its agents. This is likewise true for an employer and employee. However, the "right and ability" and "direct financial interest" words, in their broadest sense have been applied far more widely, to create liability arising from the ownership relationship of a shareholder or parent to a corporation. See, e.g., UMG Recordings, Inc. v. Bertelsmann AG, ___ F.R.D. ___, 2004 WL 1588137 (N.D. Cal. July 14, 2004). Some courts have constrained these tests by narrowly construing the word "direct" in "direct financial interest," or requiring not only the capacity to control, but the affirmative exercise of that control as preconditions for liability. On the other hand, we have also seen this modern test has become something of a chameleon through which courts have suggested expansive liability to resolve hard cases.

Limitations to Contribution: the Sony Test. At times, the courts have sought to stretch the notion of contribution to reach noninfringing conduct of others who have materially provided means

used to infringe other than copies of the infringing work. Technology, such as copying machines, scanners and audio and video recording equipment, both analog and digital, have given individuals significantly greater control over the means by which they can create, capture, use and replay copyrighted content. And the convergence of these technologies with communication and computing technologies, including the Internet, have led to remarkable new ways to distribute, share and view that content.

However beneficial these technologies may have been to our nation, both personally and professionally, these technologies have also been disruptive of content owners' ability to control the distribution of copies of their works, and placed into the hands of the public new means to commit individual copyright infringement.

Understandably, content owners have sought, from time to time, to quash that infringement at the source, claiming that the sale of these technologies was itself conduct that should be actionable. Something had to be done to address the widespread infringement that the technology enabled. On the other hand, grave risks likewise arise when content owners are given control over industries and technology with which they have no particular expertise and, for the time being, at least an arguable conflict of interest. So it was with the much-heralded Betamax case, Sony Corp. v. Universal Studios, 464 U.S. 417 (1984).

The Supreme Court refused to accept so broad an interpretation of the copyright as to grant "all copyright owners collectively . . . the exclusive right to distribute [products] simply because they may be used to infringe copyrights." As paean to the balance Congress has built into the Copyright Act, the Court noted the importance of not allowing copyright owners to leverage their statutory monopoly into technology markets, and articulated the landmark rule that liability for contribution to an infringement

for the sale of a noninfringing product, however disruptive, will not lie when the product is "merely [] capable of [a] substantial noninfringing use[]." Id. at 442.

On this point, the IEEE-USA concurs with the wisdom of the Court. While the Constitution grants Congress the power to promote the progress of science and the useful arts, to expand the power of copyright owners over technologies capable of substantial noninfringing uses would have precisely the opposite effect. Content owners are not, either individually or collectively, competent to be entrusted with the robust and competitive development of technology. This is more properly the work of technologists, the free market and the American public.

The Sony test worked well and has withstood the test of time for nearly twenty years. Far from destroying the market for content, successors to the Betamax were plentiful and cheap, and spawned entire new markets for distribution of content, creating a significant, and in some cases principal, new source of revenue for content owners savvy enough to capitalize.

Point-to-Point File Sharing and the Ascendance of Control. The close of the twentieth century saw a new convergence between digital recording and network communications technologies, culminating in the point-to-point file sharing technology that was Napster. Faced with what these courts felt to be hard fact, and given only the two rubrics of vicarious and contribution to infringement to work with, the Courts devised a means to find liability arising from the apparent failure to exercise an arguable capacity to police infringement customers of a service.

Faced with these facts, the courts first extended liability for vicarious infringement farther from its principal-and-agent roots, finding liability in a customer-and-vendor relationship from a "right and ability to supervise" the infringement, and a "direct financial benefit" arising therefrom. As to contribution, the courts also found liability, despite existence of a capacity for noninfringing use. They distinguished Sony, because of the provision of an ongoing and centralized search engine service

having, at least in theory, a capacity to control and police against infringement. Ultimately, in Napster and Aimster, both vicarious and contributory liability hinged upon the perceived capacity to control that a centralized p2p network provider had over users to facilitate and stop the infringing activities.

Secondary Liability Grounded in Control Is Both Too Much and Not Enough

IEEE-USA believes that the mere capacity to control, of the type comprehended in Napster and Aimster, is both too much and not enough to serve as a basis for secondary liability. At the same time, it unduly chills and regulates valuable new potential technologies, while failing to adequately protect content owners against organized and intentional efforts to induce, exploit and profit from widespread individual infringement.

Mere Capacity to Control Is Too Much. It is too much because a capacity to control can be inferred from almost any networked distribution technology involving a centralized server. Even software that is not networked, but regularly and routinely updated by users with new versions can have an imputed degree of control from the failure to add limiting features between such new versions.

The difficulty with permitting mere capacity to control to be the predicate for liability is that it potentially exposes vendors of virtually every new technology converging with a network to the claim that it has failed to satisfy the desire of each and every owner of copyrighted content to exercise a capacity to control from each and every owner of content who was unsatisfied with an owner's failure to modify the technology to his satisfaction. Where exposure can be measured by multiplying the corpus of registered copyrighted works by the minimum statutory damages of $750, plus ruinous attorney fees, the potential chilling impact of this test on innovation is significant.

While it is difficult to estimate the impact of such a test, its impact can be understood with an example. After Sony, but prior to Napster, a technologist could readily obtain clear and unqualified legal advice concerning the exposure of releasing products using that technology. After first

determining whether the technology itself directly infringed applicable patents and copyrights, the lawyer would investigate the extent and nature of noninfringing uses for the technology. In most cases, a reasonable and reasonably unqualified legal opinion could issue. After Napster and Aimster, it is all but impossible to give an unqualified opinion for any technology connected to a network.

Mere Capacity To Control Is Not Enough. The standard has also been demonstrably insufficient to protect the interests of content owners. Despite allegations that defendants were "capable of controlling the activities of their users," and what Senator Hatch has characterized as clear evidence of intent to promote and encourage infringement, a group of more than twenty studios suffered summary judgment of noninfringement in the Grokster case.

What happened here is not unlike that which happens when skilled engineers engineer around a patent. The Court stated that infringement will lie when there is a capacity to control, and so they designed a system that delegated any capacity to control to a decentralized network, while retaining to themselves the benefits of centralized advertising for the use of the service. In this way, they supported a business model without actually falling within the Napster and Aimster standard. Faced with these facts, the Grokster court could not be blamed for the result. Any other alternative would improperly have read Sony out of the law.

Where We Are. The state of the law is a standard that simultaneously chills ongoing and novel technologies that might provide entirely new forms of media and distribution of media, while permitting individuals to exploit and induce copyright infringement on a massive scale. The natural flow of common-law jurisprudence has landed us in a place that imposes potentially ruinous liability to inventors and their investors, while leaving content owners without recourse against those who would actively, knowingly and intentionally induce infringements of another. And this frames the problem

that S.2560 has addressed: How, then, can we reach such blatant wrongdoing without unduly limiting important and useful innovation?

Revisiting the Patent Act

Reasoned common-law jurisprudence regarding secondary liability led to significant lack of clarity once before, in the realm of patent infringement, just prior to the enactment of the 1952 Patent Act. There, as here, secondary liability was largely the result of judge-made law. There, as here, a spate of alternatively pro-plaintiff and pro-defendant decisions rendered the law to a state of confusion whether or when there would be secondary liability. And the Congress responded with a codification, so far as possible, of the corpus of law at that time, making such changes as were necessary to give clarity to the law that had stood the test of time.

The result was Section 271 of Title 35, which set forth in straightforward language the texture of direct and secondary liability for patent infringement. The elegance of the language benefited from the richness of the jurisprudence that preceded it, and the language provided a simple, clear, predictable and objective framework for analysis. To be sure, it was no panacea. But it has worked. Technology flourished under the Act. Businesses are readily able to innovate with reasonable comfort, lawyers are reasonably able to advise their clients and, for the most part, the Patent Act successfully promotes the progress of the useful Arts.

The Congress adopted three forms of liability: (i) direct infringement for violation of the exclusive rights of the patent grant; (ii) liability for the active, knowing and intentional inducement of the infringement of another; and (iii) liability for knowing and material contribution to the infringement of another, other than by sale of a staple product having capacity for substantial noninfringing use. In the fifty years since that codification, no meaningful parade of horribles has occurred. To the contrary, our technological and information economy has flourished.

Patent Contribution: the Genesis of the Sony Test. It was this language from the Patent Act and supporting public policy from which the Supreme Court drew its inspiration in reaching the Sony "substantial noninfringing use" test. To that end, it is perhaps worthwhile to consider whether the other prong of secondary liability of the patent act could inform the very question we are asking today.

Patent Inducement: Conduct Instead of Control. Except for strict principal and agent relationships, the patent law looks to the conduct of a defendant, rather than its relationship with the direct infringer, as the basis for finding secondary liability. Under Section 271(b) of the Patent Act, the Federal Circuit has found liability appropriate in patent cases where a party engages in an affirmative undertaking to induce conduct known to be an infringement, with the specific intent that the particular acts known to constitute infringement will occur. Hewlett-Packard Co. v. Bausch &Lomb, Inc., 909 F.2d 1461, 1469 (Fed. Cir. 1990) (Rich, J).

Each of the limitations has been found significant, and operate to avoid uncertainty as to the scope of secondary liability and to ensure that the patent grant is not unduly extended to reach noninfringing technologies. For example, the failure to act or to do something cannot constitute an active inducement. Nor can someone induce a patent infringer with a sound and good faith basis for believing that the acts so induced would not constitute an infringement. Further, courts have held that the seller of a product with a substantial noninfringing use can be liable for inducing infringement if the seller takes active steps beyond the mere sale of the product that encourages direct infringement by another. On the other hand, control is no prerequisite to liability. Even if every measure has been taken to avoid control over the direct infringer, active and knowing inducement with specific intent to induce are grounds for liability. Rather than inquiring into the nature of relationships on an ad hoc basis, a court must instead inquire as to the actual degree of culpability in determining whether a defendant should be liable for the infringement of another.

In wide contrast to continuing controversy over judge-made developments in secondary liability under the Copyright Act, the development of secondary liability under the Patent Act has been relatively uneventful. In no small part, this difference may rest with the carefully delineated and neutral statements of policy embodied in the patent standards. Courts are neither invited nor inclined to broaden or narrow those standards, as courts have done in the Copyright Realm.

There Should Be No Secondary Liability When Another Infringes Using a Product or Process Having Capacity for a Substantial Noninfringing Use, Unless the Vendor Actively Induced the Infringement

The effectiveness of these rules under the Patent Act has led IEEE-USA to conclude that it should not be indirect infringement of a copyright to manufacture, distribute or provide a hardware or software product or process capable of substantial noninfringing use, unless the manufacturer, distributor or maker actively induces the infringement of a copyrighted work by another. In this way, the well-established balance between proper incentives for copyright owners and protecting technological innovations from undue regulation can be maintained. Changing the focus from the extent and nature of relationships and control to whether inducement is being actively induced provides a better way to deal with technologies having both infringing and non-infringing use. If this could be established with rules that are simple, clear, predictable and objective, IEEE-USA would support such legislation.

IEEE-USA Concerns With S. 2560

While IEEE-USA understands the appeal of inducement as a measure for secondary liability, it has significant concerns with the particular definition of "intentional infringement" set forth in the bill.

S. 2560 Does Not Adequately Clarify Existing Law. As a threshold, the bill does not appear to introduce inducement as a mechanism to clarify, replace or constrain control as a test for vicarious or contributory copyright infringement. Indeed, to the contrary, it contains the language that appears to

adopt existing case law without change. If so, S. 2560 could do nothing to resolve the confusion and ambiguity faced by technologists under present case law.

S. 2560 Intentional Inducement Is a Significant Departure from Existing Secondary Liability Principles. Rather than adapting the well-developed standard of inducement used in patent law, the definition of "intentional inducement" departs from and thereby teaches against the adoption of decades of balanced and accepted jurisprudence. For example, the standard of "intentional inducement" does not appear to require actions independent of lawful marketing of features of a technology capable of both infringing and noninfringing uses; does not appear to require knowledge that the acts to be induced would require an infringement; and does not appear to require a subjective specific intent to induce the infringing acts.

Practical Uncertainty over Scope and Application of the New Standard Will Chill Innovation. This definition is not simple, clear or predictable. IEEE-USA is concerned that a too-broad definition of inducement may impose a dangerous burden to development of and investment in useful and beneficial technologies to the detriment of U.S. competitiveness. IEEE-USA is further concerned that this definition would effectively provide patent-like protection to non-technologists for an indefinite term, and for a product that the *defendant*, not the non-technologist plaintiffs, had actually conceived and invented.

It is difficult for IEEE-USA to conceive of a fact pattern consistent with a defendant's sale of a technology known to have infringing and noninfringing uses, in which the defendant could prevail in a motion to dismiss or for summary judgment. Consider, for example, the facts of the Sony Betamax case, in which the District Court found advertising promoting the downloading of broadcast signals to create and exchange private libraries of movies. Under the standard in S. 2560, the relevant question would be whether a reasonable person would consider Sony to have intended to induce infringement.

IEEE-USA believes that under S. 2560, it would be unclear whether District Court would have reached the same result.

This bill could have far-reaching economic impact on the development of new technologies. Should the bill be enacted, a company producing a disruptive technology must resign itself to a jury trial on the issue of "intentional inducement" in nearly every case. Since the class of potential plaintiffs includes every content owner with a registered copyright, the potential statutory damages of $750.00 times the number of works, together with an award of attorney fees, could easily result in ruinous damages even for a large corporation. In turn, it would be foolhardy for capital markets to consider investing in a company proposing to deliver a technology in such an environment.

Copyright Inducement Would Apply to All Copyrighted Works and All Technologies. S. 2560 reaches more broadly than file sharing. Because Copyright inducement applies to all copyrighted works and is technology-neutral as to the secondary technology it regulates, IEEE-USA members may be directly affected in their professional capacity. We create and use hardware and software development tools; tools that create, tools that adapt and tools that modify hardware designs, programs and content alike. Virtually every general-purpose computer and technology tool has features that manipulate, control and display content, including copyrighted content. Reuse and reverse engineering are not dirty words to us, even to our members who are content owners, but are terms-of-art for essential engineering paradigms. These tools and practices are routinely used by engineers to make the products that define the modern age. IEEE-USA is concerned that the tools and practices so essential to our profession, as well as the ongoing innovation in the development of these tools, may be negatively impacted by this proposed legislation.

Patent Inducement Provides the Superior and Less Risky Test. In contrast, it is settled under the Patent Act, that mere marketing of a technology having infringing and noninfringing uses,

without more, cannot constitute the inducement of a patent. Dynacore Holdings Corp. v. Phillips, 363 F.3d 1263 (Fed. Cir. 2004) (Gajarsa, J) (discussing patent inducement in the context of Sony and providing that the sale of lawful products by lawful means is noninfringing). Moreover, the subjective and good-faith belief that conduct would be noninfringing, as Sony asserted was private copying, is sufficient to preclude a finding of inducement.

Using untested standards is a significant departure from established copyright law and significantly different from the analogous aspects of the Patent Act. Using untested standards for determining inducement instead of, for example, the well-tested standards of inducement under the Patent Act, appropriately adapted to the Copyright Act, could have far reaching and unintended consequences.

An IEEE-USA Proposal to Balance Secondary Liability Concerns of Content Owners and Technologists

At the request of Senate Judiciary Committee Staffers, IEEE-USA has proposed a draft substitute, which attempts to do for secondary liability under the Copyright Act what the drafters of the Patent Act did for patent law: to codify so much of existing law as possible, while rationalizing difficulties in the status quo. IEEE-USA recognizes that there is no silver bullet, and that much further development of the proposed framework may be necessary before a workable and satisfactory solution is found. To that end, the IEEE-USA draft substitute is attached in the hope it may inform to that debate.

Like the language in S. 2560, the IEEE-USA substitute adds a new subsection (g) to Section 501 to address secondary liability. Section (1) provides a definition of a new form of secondary copyright liability for inducement, closely modeled after the language and Federal Circuit gloss on 35 U.S.C. § 271(b). Section (2) codifies a rule for contribution patterned after Section 271(c). Section (3) provides a codification of the modern rule for vicarious infringement. Section (4) defines

limitations on these three doctrines in the context of marketing technologies capable of infringing and noninfringing use. Subsection (A) restates Judge Gajarsa's rule in Dynacore for inducement. Subsection (B) restates the test in Sony, for contribution and vicarious liability. Section (5) raises attempts to balance the expanded scope of liability for inducement and exposure to unknown infringing conduct by limiting damages in secondary cases to actual damages actually known to the defendant, to permit the Court to focus on the most relevant remedy in such cases: an injunction against further inducing of an infringement.

As drafted in the IEEE-USA substitute, inducement is intended to require actions, and not omissions, that are independent from the ordinary manufacturing, sale and marketing of non-infringing devices having both infringing and noninfringing uses. It is intended that no secondary liability of any kind would arise, without more, from lawful steps to develop or sell lawful products having infringing and noninfringing uses.

Under Federal Circuit gloss, intent and knowledge may be proved, as usual, by circumstantial evidence of inducement. Water Technologies Corp. v. Calco, Ltd., 840 F.2d 660 (Fed. Cir. 1988) (Nies, J.). However, summary judgment for defendant would always be appropriate where all material evidence of inducement merely evidences otherwise lawful steps to sell lawful products having non-infringing uses. Finally, a reasonable and actual good-faith belief that the induced acts are noninfringing, uncontradicted by controlling case law, should be a defense to a claim for damages, but not an injunction.

Conclusion

The IEEE-USA is concerned that the Copyright Act should not be changed in ways that would inhibit research and novel technologies before their worth can be demonstrated, through application that may not be apparent at the time the technology is first developed. However, IEEE-USA is

mindful that technologies may be misused to infringe a copyrighted work, and some will promote that fact to their own benefit. Existing tests grounded in control have proved to be both too much and not enough to balance the competing interests of content owners and technologists.

Whatever test for secondary liability is used, the test must be simple, clear, predictable and objective. S. 2560 does not accomplish this. It is a significant departure from existing law, and unmoored from any well-understood economic and legislative basis for intellectual property liability. In contrast, decades of experience under the active inducement provisions of the Patent Act confirm that indirect liability for noninfringing conduct amounting to active inducement has protected inventors without an undue burden to technological innovation. Tracking those principles is essential to maintaining the balance.

IEEE-USA stands for the careful balancing of interests between technologists and content owners who make up its membership, and recognizes that every change to that balance can have unanticipated and far reaching consequences to U.S. competitiveness and economy. The 108th Congress stands as the architects and guardians of this balance. Once changed, it may be impossible to undo the impact of these changes. For this reason, IEEE-USA respectfully suggests that, as you measure and cut the chords of intellectual property policy to address these issues, be mindful of the balance, and take note of the wisdom of the most fundamental rule of carpentry:

Measure Twice, Cut Once.

Submitted by:

JOHN STEADMAN, IEEE-USA President
GLENN S. TENNEY, Chair, IEEE-USA Intellectual Property Committee
ANDREW C. GREENBERG, Vice Chair, IEEE-USA Intellectual Property Committee

APPENDIX

Proposed Substitute to S. 2560

Section 501 of title 17, United States Code, is amended by adding at the end the following:

(g)(1) Inducement of Infringement. Whoever actively and knowingly induces infringement of a copyrighted work by another with the specific and actual intent to cause the infringing acts shall be liable as an infringer.

(2) Contribution to an Infringement. Whoever knowingly and materially contributes to the infringement of a copyrighted work by another shall be liable as an infringer.

(3) Vicarious Infringement. Whoever has the right and ability to supervise an activity resulting in a direct infringement and has a direct financial interest in such activity and infringement shall be liable as an infringer.

(4) Limitations on Secondary Liability.

(A) manufacture, distribution, marketing, operation, sale, servicing, or other use of embodiments of an otherwise lawful technology by lawful means, with or without the knowledge that an unaffiliated third party will infringe, cannot constitute inducement of infringement under Subsection g(1) in the absence of any additional active steps taken to encourage direct infringement.

(B) manufacture, distribution, marketing, operation, sale, servicing or other use of embodiments of an otherwise lawful technology capable of a substantial noninfringing use cannot constitute contribution to an infringement under Subsection (g)(2) or vicarious infringement under Subsection (g)(3).

(5) Damages for violations of section (g)(1) of this section shall be limited to an injunction against inducement, and actual damages for infringement of a work for which the defendant had specific and actual knowledge the work would be infringed.

Statement of Sen. Orrin Hatch
Before the United States Senate Committee on the Judiciary
Hearing on

"PROTECTING INNOVATION AND ART WHILE PREVENTING PIRACY"

At this hearing, leading experts on the intersection of copyright law and technology will share their views on how this Committee can best restore the ability of copyright holders to challenge the large, for-profit global piracy rings that threaten the future of today's cinema and recording industries. Research now suggests that these piracy rings – which call themselves filesharing networks – will create between 12 and 24 billion infringing copies this year alone. This unprecedented level of piracy fundamentally threatens America's world-leading music, movie and software industries and the future of legitimate Internet commerce.

The architects of this filesharing piracy make millions of dollars while attempting to avoid any personal risk of the severe civil and criminal penalties for copyright infringement. I think all here today would agree that these pernicious schemes to encourage others – and unfortunately these are mostly kids – to break federal law allows these pirates to collect huge revenues while subjecting users to the risk of prison or crippling damage awards.

To implement their schemes, the architects of filesharing piracy must encourage users to infringe copyrights in two different ways. First, they must encourage users to infringe copyrights by downloading infringing copies of works. This is an easy task because downloading users get for free valuable works that they would otherwise have to purchase. Unsurprisingly, the user-interfaces of most filesharing software provide no warnings about the prevalence of infringing files or the severity of the civil and criminal penalties for succumbing to the pervasive temptation to download them.

But infringing downloads cannot occur unless infringing files are available for download. The architects of filesharing piracy must thus encourage users to infringe copyrights again by uploading files for distribution to millions of strangers. This is a difficult task: A user infringing by uploading gets nothing in return for his or her illegal act except a risk of prosecution.

Free-riding downloaders are unlikely to become altruistic uploaders, so most filesharing software automates the decision to upload: When used as intended, this software automatically redistributes every file downloaded. This makes uploading and redistribution automatic and invisible to the average user. This design ensures that while an infringing download requires a conscious choice, the separate and more dangerous infringing act of uploading usually does not.

Automatic uploading ensures that many free-riding downloaders will unwittingly turn their home computers into global piracy distribution centers. Harvard's Berkman

Center for the Internet and Society warns that it can be extremely difficult for a non-expert computer user to shut down this automatic redistribution. The Center further warns that the complexity of Kazaa's installation and disabling functions can leave users unaware that they are distributing infringing files to potentially millions of strangers.

Filesharing software also automates infringing redistribution in other ways. For example, some distributors, like Bearshare, use installation wizards that – by default – cause users to redistribute every media file on their computer. This automatically turns people who have copied music CDs onto their computers for personal use into global redistributors of entire music collections. Such wizards can automatically create high-volume infringers and enforcement targets.

There can be no doubt that automating redistribution induces mass infringement that would otherwise never occur. For example, here is the sworn testimony of one user of filesharing software who lost her life savings in an uploading-related settlement:

> I never willingly shared files with other users.... As far as I was concerned, the music I downloaded was for home, personal use.... I downloaded songs I already owned on CD because I didn't want to mix them manually.... I don't know how to "upload" songs on the computer either. As far as I was concerned copyright infringement was what the people in Chinatown hawking bootlegged and fake CDs on the street corner were doing.

This testimony captures the problem: Unwitting consumers can break the law, subjecting themselves to significant liability and lawsuits that no one wants to be forced to bring.

The design of some filesharing software thus enables its distributors to automate, induce, and profit from copyright piracy. We must stop these for-profit commercial piracy operations. They threaten the future of artists, legal commerce, and all but their most cautious and expert users. Indeed, I suspect that this piracy continues today only because its proponents have become adept at playing one branch of the federal government against another.

For example, Sharman Networks, the distributors of Kazaa, recently told the Ninth Circuit that courts must await legislative action on filesharing piracy: Here, legislative action, not judicial law making, is particularly needed because political issues of comity are implicated in the legal subject matter. Yesterday, Sharman told Congress that legislative action on filesharing piracy must await the courts: [I]t has been Congress' long-established practice to prudently refrain from intervening in active litigation. Passage of S. 2560, without awaiting final adjudication of [Grokster], would set the precedent for powerful interests to seek Congressional action challenging the outcomes of civil trials.

In short, Sharman is telling the courts that they must do nothing until Congress acts and then telling Congress that it must not act until the courts finish doing nothing.

This tactic of delay and obfuscation is not isolated: In the appeal of Grokster, over 42 parties and amici argued that judges must perpetuate any absurd results flowing from judge-made secondary-liability rules because only Congress has the competence to adjust these judge-made rules.

This exercise in self-contradiction may produce paralysis, but at a high price. Congress has always given courts flexibility to adapt secondary liability rules. Courts exercised that power most famously in the Sony-Betamax case. In Sony, a 5-to-4 majority of the Supreme Court altered the balance between copyrights and copying technologies by narrowing the prevailing secondary-liability rule. Sony narrowed that rule as to a small class of defendants by importing the substantial-noninfringing-use rule that Congress had codified only in the Patent Act. Consequently, anyone who argues that judges lack the competence to adjust secondary liability rules to balance the interests of copyrights and technology argues that Sony-Betamax is illegitimate and wrongly decided. I do not agree with that argument – and I doubt that its apparent proponents do either.

To address this problem, Senator Leahy and I introduced S. 2560, the Inducing Infringement of Copyrights Act. The Act provides that the courts can impose secondary liability upon those who intend to induce copyright infringement. We developed this approach with the help and support of leading technology companies. We want to continue to work with interested parties to make refinements that will help us achieve the bill's intent.

The approach taken in S. 2560 is intended to have three key attributes.

First, S. 2560 is technology neutral: It does not single out peer-to-peer networking technology for punitive regulation just because a few bad actors have misused it. This technology has intriguing, legitimate uses: Pioneering companies like Wurld Media, Snowcap, and UniConnect Software in Utah are developing innovative and legitimate new peer-to-peer services for consumers. S. 2560 thus targets only bad behavior – and only intentional behavior that is bad enough to trigger criminal liability under existing law. This type of behavior-based, technology-neutral approach has been long advocated by technology interests.

Second, S. 2560 uses a proven model for structuring secondary liability. The substantial-noninfringing-use rule that Sony imported from the Patent Act coexists there alongside liability for intent to induce infringement – a concept that the Patent Act calls active inducement. This proven model can address cases of intent to induce infringement that were explicitly not covered or addressed by the Supreme Court in Sony.

And third, it is our intent that S. 2560 change the law of contributory liability only for a very narrow class of defendants. It is our expectation that most defendants will never be affected by S. 2560 because they already face broader liability for inducing copyright infringement. In 1976, Congress codified its intent to continue imposing liability upon contributory infringers. Both then and now, the prevailing rule for contributory infringement imposes liability upon anyone who knows or has reason to

know of infringing activity and induces, causes or materially contributes to the infringing conduct of another. For the overwhelming majority of defendants governed by this rule of liability for knowing inducement, no additional liability results from liability for intentional inducement.

Nor do we intend to affect defendants for whom Congress or courts have narrowed the general rule of secondary liability for knowing inducement. In the Digital Millennium Copyright Act, Congress created safe harbors for certain internet service providers. Their requirements substitute for other forms of secondary liability, so ISPs operating within a safe harbor are not subject to liability under S. 2560.

It is also not our intent to affect distributors of copying devices who merely know that their devices can be or are being used by others to make infringing copies. In Sony, the Supreme Court narrowed the scope of secondary liability as to these defendants. Sony also held that evidence showing that a distributor of copying devices knew that its devices could be used to infringe provides no evidence of intent to induce infringement. This ruling checks potential abuse of an intentional-inducement claim, and S. 2560 preserves it.

By preserving the general rule of liability for knowing inducement and its DMCA and Sony limitations, S. 2560 thus affects only of distributors of copying devices who intend to induce infringing uses of their devices. In the Napster and Grokster cases, such distributors distracted courts by raising issues of non-infringing uses that should have been as irrelevant as they were to the defendants' business plans. S. 2560 will end the confusion caused by these flawed analyses.

As our hearing today will show, some technology companies have expressed concerns that claims for intentional inducement might be misused against companies that merely sell copying devices. We do not believe this to be the case, but are willing to enter into a constructive dialogue to ensure that the language is drawn as tightly as possible.

This bill is intended to preserve intact the protections that Sony provides to distributors of copying devices whose businesses are substantially unrelated to copyright infringement. It is my hope that an objective study of Sony and the rest of the inducement caselaw upon which S. 2560 operates will help further our study.

For example, there is a mock complaint circulating that alleges that the Apple iPod violates S. 2560 because mp3 players would never have been commercially viable but for the preceding, massive wave of for-profit filesharing piracy that was defended by groups like the Electronic Frontier Foundation.

A real court would respond to that mock complaint in two words: Complaint dismissed. The caselaw states that no one can "induce" unlawful acts that have already occurred. Neither Apple nor the iPod violate S.2560 – even if portable mp3 players became commercially viable only because filesharing piracy created mp3 collections too large to be explained by legal purchase.

I want to continue working with our technology industries to resolve any concerns about possible abuse of liability for intentional inducement. If there are alternative ideas, let us discuss them.

Just as the Sony Court never intended to allow the substantial-noninfringing-use rule to be misused as a license to enter the copyright piracy business, I do not intend to allow S. 2560 to be misused against legitimate distributors of copying devices. On its face, the Sony decision precludes claims that S. 2560 would have imposed liability on distributors of Betamax VCRs, and it should not impose liability upon distributors of computers, software media players, Tivos, iPods, instant messaging systems, or email systems.

Testimony of Robert Holleyman
President and CEO
Business Software Alliance
before the
Senate Committee on the Judiciary
July 22, 2004

Good afternoon. My name is Robert Holleyman. I am the President and CEO of the Business Software Alliance[1]. BSA is an association of the world's leading software and hardware companies. BSA's members create approximately 90% of the office productivity software in use in the U.S. and around the world.

The BSA commends you, Mr. Chairman, and Senator Leahy, for bringing a focus to bear on the problem of online piracy of copyrighted material. This is a matter of great concern for BSA member companies that are the targets such illegal activity. BSA believes that ways need to be found to address piracy generally, and online piracy specifically, which do not encumber the development and distribution of innovative technologies.

The Committee has embraced the challenge of crafting a law that deters bad actors who use technology to intentionally cause others to infringe while preserving unfettered the ability of legitimate companies to develop and

[1] The Business Software Alliance (www.bsa.org) is the foremost organization dedicated to promoting a safe and legal digital world. BSA is the voice of the world's commercial software industry and its hardware partners before governments and in the international marketplace. Its members represent one of the fastest growing industries in the world. BSA programs foster technology innovation through education and policy initiatives that promote copyright protection, cyber security, trade and e-commerce. BSA members include Adobe, Apple, Autodesk, Avid, Bentley Systems, Borland, Cisco Systems, CNC Software/Mastercam, Entrust, HP, IBM, Intel, Internet Security Systems, Intuit, Macromedia, Microsoft, Network Associates, RSA Security, SolidWorks, Sybase, Symantec, UGS and VERITAS Software.

invent new technologies and services unencumbered by the threat of frivolous litigation. We commend you for doing so. We recognize this is not an easy task and we remain committed to working with this Committee to achieve that goal.

We believe that new legislation, properly focused and balanced, should be viewed as only one of several elements of finding a solution to the problem of P2P piracy. In a statement of joint policy principles endorsed by BSA, the Recording Industry Association, and the Computer Systems Policy Project, we recognized that meeting the challenge of piracy requires a multifaceted approach that includes creating legitimate and content rich on-line alternatives to illicit P2P file sharing systems as well as consumer education, enforcement of existing civil and criminal statutes, the use of technological protection measures and strengthening international sanctions for piracy.

Consistent with these agreed principles, BSA believes that the most effective way to address the harm done by operators of illicit file sharing networks is through the marketplace. Consumers will embrace appealing legal alternatives that offer a rich and varied array of content. A number of these alternatives are already available for music, including iTunes and a now legal Napster, and their commercial success speaks volumes.

A second approach to the challenge is to prosecute the operators of these illicit file-sharing networks under existing laws. For example, the Justice Department has recently created a task force to address piracy specifically. We think this is a very timely and positive development and we encourage the Justice Department to pursue such cases as appropriate.

Third, we believe it is vitally important to educate all users of the Internet about safe and legal ways to harness the power of this important resource.

BSA sponsors an active education campaign, as do a number of other groups. But this is not enough. We believe the government should also play a role: specifically we recommend an ad campaign similar to past public awareness campaigns on the environment, smoking and drugs: it is timely and much needed with respect to the Internet.

Finally, technology can play an important role in protecting digital content. Just as banking and other commercial transactions can be performed securely over computer networks, digital content can be distributed securely through the use of existing technology tools. The marketplace is working to provide the tools necessary to secure distribution of digital assets, including content and we fully support continued industry-led efforts to wards this end.

If the Committee determines that an additional cause of action, such as S. 2560, is necessary to address the problem of online piracy, we urge that any such bill be carefully crafted and properly balanced to curtail irresponsible and harmful practices while avoiding adverse unintended consequences for legitimate technology companies.

Finding this balance will not be easy. We think that by focusing on regulating conduct the sponsors have identified a key element of any viable solution. As you move forward, we urge you to ensure that beneficial technologies are not put at risk by the need to stop bad actors and to avoid overbroad or ambiguous standards that could chill innovation, deprive consumers of access to beneficial new technologies, and encourage costly litigation.

Any new law should be crafted against the backdrop of the existing law that ensures legitimate technologies can be developed and made available to

consumers. To make certain this is the case and to ensure that the language of a new law is interpreted consistent with your intent, key elements of existing law and jurisprudence should be specifically spelled out in the bill. BSA stands ready to work with this Committee to structure sound legislation, that does not burden those who, in good faith, develop, manufacture, or consume general or multi-purpose technology products such as software and computers.

BSA's member companies are the leading developers of computers, software, security and networking technologies. To meet customer needs, these products are designed and intended to be multipurpose products. By their very nature, many of these products are freely programmable and can be modified by the user. How customers use these products changes over time and such uses are limited only by the customer's needs and imagination.

The functions built into these products are also by design multipurpose. These functions enable copying, modifying and transmitting a broad variety of digital content. For example, they permit users to copy documents they create on storage media such as optical disks for safekeeping, to edit, cut and paste text data and graphics to enable graphics designers to do their jobs more efficiently, and to edit family photos or home video recordings to share with other family members. These functions are at the heart of the information technology revolution.

We know that it is not your intent Mr. Chairman nor that of Senator Leahy to put at risk any of these functions or the legitimate companies that make products incorporating these functions. It is also our understanding that you do not mean to impose specific constraints on the design of general-purpose technology products or the functions they include. As you noted in your

floor statement, Mr. Chairman, these decisions should be left to the marketplace and engineers.

It is a fact that unscrupulous persons have harnessed technology to provoke others into engaging in illegal acts such as infringement of copyright. Today's piracy threat is posed by such unscrupulous persons using fundamentally sound P2P technologies for illicit purposes by encouraging infringement for their own ends from the sale of advertising and spyware.

These unscrupulous persons, in many cases, are not themselves the direct infringers. The direct infringers are the persons who are drawn to these services by the opportunity to get software and other works for free through unauthorized acts of uploading and downloading.

To ensure their ends, these bad actors intentionally design their services to make piracy almost unavoidable. Most often file-sharing functions are enabled by default, are very hard to disable, and often continue running in the background, even after the user has closed the application. These practices are well known and well documented.

To distinguish bad actors from good, we believe that five key areas need to be addressed through specific language.

- To effectuate your intent that legitimate products and technologies not be threatened, it should be made clear that technology products that can be used for significant legitimate purposes – in the copyright vernacular, substantial non-infringing uses – are not subject to copyright infringement liability. To this end the bill should state clearly that the Supreme Court's decision in the *Betamax* case is unaffected. That decision has stood for 20 years, and technology companies and the marketplace have come to rely on it.

- To ensure that only bad actors are found liable, it should be made clear that to meet the intent standard of the bill an actor must be shown to have engaged in conscious, recurring, persistent and deliberate acts demonstrated to have caused another person to commit infringement.
- The bill should state explicitly that mere knowledge by a developer of a technology or a provider of a service of the actual or potential infringing acts of another person using that technology or service does not demonstrate intent to induce copyright infringement.
- It should also be made clear that the bill does not create liability based on advertising or providing support to users, including instructions for using the technology or service provided through manuals or handbooks, nor by providing assistance for using a product through a company's on-line help system or telephone help services.
- Finally, a mechanism needs to be included to effectively deter weak, harassing or frivolous law suits. The legislation should establish a procedure to ensure that frivolous cases do not go forward and that discovery is appropriately limited and not unnecessarily intrusive.

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Persons with bad motives have repeatedly used developments in the marketplace and technology to their own ends. Today is no different. In the past such bad actors have used the postal system, telephones, automobiles, and other avenues of commerce for their own illicit ends. Now, they are also using computers, software and the Internet. Just as past solutions focused on these bad actors, and did not outlaw overnight delivery, cars, or telephones, today's solutions must leave intact the

important contributions computing technologies make to our daily lives, and allow these technologies to make even greater contributions in the future.

As I noted at the outset Mr. Chairman we commend you and Senator Leahy for your long-term commitment to combating intellectual property piracy. We fully support your efforts. We look forward to working with you as you continue to address piracy challenges while preserving an environment in which BSA members and other technology companies can continue to innovate, which is what they do best.

Thank you.

Statement of Senator Patrick Leahy
Ranking Member, Senate Judiciary Committee
"Protecting Innovation and Art while Preventing Piracy"
July 22, 2004

I would like to thank Chairman Hatch for holding this hearing today and to also thank our witnesses for being here. I am glad we can discuss the "Inducing Infringement of Copyrights Act" with an eye towards moving this legislation in the fall. The issues facing the copyright and technology communities in the digital age are daunting, and the role of Congress must be to bring those communities together in consensus. The Chairman and I recognize that the process of legislating in such an area will be both tense and intense. But we are committed to building that consensus that is the hallmark of successful and useful legislation, and we will make sure that our commitment results in law.

I am always glad to hear from the Register of Copyrights, Marybeth Peters, who will testify about the need for this bill and about how it clarifies longstanding principles of contributory copyright liability without targeting technology. I agree with her, and I encourage our other witnesses to study her statement. Mr. Bainwol says that while technology is not to blame, we need to target those who have hijacked technology and undermined the rights of copyright holders. I agree. Mr. Holleyman declares that mere knowledge of a given technology's potential to be used to infringe another's copyright should not by itself constitute inducement. I agree, and I wish to offer the Business Software Association my sincere thanks for bringing its open-minded cooperation and considerable expertise to the earlier drafting stages of this bill.

I am heartened even by the testimony of those skeptical of the bill. Mr. Shapiro says that the Sony-Betamax ruling is good law. I agree. Mr. Greenberg and Mr. McGuiness urge Congress to craft our intellectual property laws so that they promote technological growth. I agree, and I believe we have done this with our bill.

As Senator Hatch and I have worked to promote the great possibilities of the Internet and the technologies that capitalize on its potential, one problem consistently appears: the copyright holders often fear these very same new and exciting technologies. Their reticence is not without merit. Our copyright industries lose billions of dollars each year to copyright piracy, and just as importantly, our artists lose the rights to their own works.

By clarifying a longstanding principle of secondary copyright liability, S.2560 will give copyright holders reason to embrace new technologies. And while the legal principle is an old one, the problems of inducement for copyright are a relatively new product of the digital age – an age in which it is easy (and often profitable) to induce others to violate copyrights through illegal downloading from the Internet. The 1976 Copyright Act codified the principle that copyright holders not only have exclusive rights inhering in their copyrights, but that only they can authorize others to exercise those rights – such as the right to distribute and the right to make copies of their work. Since the advent of the Internet, some have harnessed peer-to-peer technology to run roughshod over these

rights, and the courts have grappled with how to apply existing common law principles to the resulting legal cases, all the while calling for congressional guidance. The "Inducing Infringement of Copyrights Act" does this by reaffirming Congress's intent in the 1976 Act.

The patent code already provides liability for inducing infringement. And our experience there shows us that such provisions work: over the years, the number of patents has steadily grown and patent-related industries continue to thrive. But while, it has long been relatively simple, and economically worthwhile, to induce patent infringement, only recently has the ability to illegally download music, books, software, and films made it necessary for Congress to clarify that this principle also applies to copyrights.

Of course, there are significant differences between patents and copyrights, and we are not transplanting one liability regime to another part of the code. But we have learned useful lessons in the patent realm, and we should not ignore that utility when it can benefit the appropriate enforcement of copyrights.

In making this clarification, our bill does not undermine the Sony-Betamax decision, it does not undermine the "fair use" doctrine, and it does not target or penalize any technology. In fact, our bill will help companies like Apple who, through their iTunes service and iPod devices, offer legitimate alternatives to illegal downloading. This bill will protect our copyright holders and spur innovation.

Finally, I would like to draw attention to a letter sent by Mr. McGuiness and some others in the consumer electronics industry to the Committee on July 6. It states: "...We agree with the need to penalize those who intentionally cause copyright infringement..." That is precisely what S.2560 does. While I understand that some have concerns with the specifics our legislation, I say to you this: work with us. No one wants to undermine the iPod, but we must recognize that some people use peer-to-peer technology in ways that are wrong and illegal

Thank you again to all of our witnesses for being here today and for your testimony. I look forward to working with you during the next month to produce a version of this legislation that can pass the Senate this fall.

# # # #

NetCoalition.com

BEFORE THE UNITED STATES SENATE
COMMITTEE ON THE JUDICIARY
STATEMENT OF KEVIN S. MCGUINESS
EXECUTIVE DIRECTOR
NETCOALITION
JULY 22, 2004

Good afternoon, Chairman Hatch, Senator Leahy, and Members of the Committee. My name is Kevin McGuiness, and I am the Executive Director of NetCoalition. On behalf of the members of my organization, thank you for the opportunity to testify on S. 2560, the "Inducing Infringement of Copyrights Act of 2004" ("Induce Act" or "IICA"). NetCoalition serves as the public policy voice for some of the world's most innovative Internet companies on the key legislative and administrative proposals affecting the online world.

The members of NetCoalition appreciate the interests of the sponsors of S. 2560 in protecting children by addressing certain types of activities that infringe copyrights. Moreover, we agree that the law must enable copyright owners to seek relief from those who unlawfully download and distribute their work.

As currently drafted, however, S. 2560 is much broader in its scope than described by its proponents and open to multiple interpretations. As a result, it would have severe repercussions on Internet companies, products, and services; jeopardize the introduction of new technologies; and trigger a flood of litigation. This result is not beyond the realm of possibility. If the past is any indication, the entertainment industry has proven its willingness to litigate no matter the cost or consequences.

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Therefore, we commend Chairman Hatch and Senator Leahy for convening a hearing to more fully explore the legislation and its consequences. Given the concerns raised by such divergent interests—the Internet community, hardware and software manufacturers, telecommunication services, network providers, chip makers, publishers, consumer electronic manufacturers, wholesalers, retailers, and consumers, libraries and universities, financial service companies, and venture capitalists to name a few—it is imperative that the Committee ensure that the legislation successfully targets the conduct it intends to prohibit without jeopardizing the promise and potential of the Internet.

INTRODUCTION

Today, it is hard to imagine the world without the Internet. This dynamic, relatively new medium provides an open, democratic and international means of communication. Any user can surf or engage in a transaction with literally millions of different web sites that represent everything from large corporations, governments, and public interest sites to individuals, social organizations and families. The Internet connects people all over the world in a manner, scope, and ease that would be impossible anywhere but online. It provides a voice for even the most modest members of society to disseminate ideas on a scale traditionally reserved only for the most powerful.

Today, any of the Internet's more than 500 million users worldwide can become a publisher, set up an online business, create a web log (or "blog"), organize a chat room, and communicate his or her ideas anywhere in the world instantaneously. Search engines and web portals provide a tremendous opportunity to discover new content. Leading search engines in the United States perform over 625 million searches every day and can link users to literally tens of billions of web pages. Amazingly, this represents only a fraction of what can be found on the Web.

Simply put, there is no other communications medium that permits such diverse activities. And yet, we know that the very qualities that make the Internet an indispensable tool for worldwide commerce and communication also attract those

seeking to exploit new technologies to engage in unlawful behavior. So it is not surprising that the Internet, which is used by most people for lawful and constructive activities, is also used improperly.

It is also true that concerns are raised whenever new technologies are developed that empower consumers to generate, share and distribute information in new and more efficient ways. It was true five hundred years ago, when Gutenberg developed the moveable type press. It was true with the advent of radio and television. And it was true two decades ago, when Hollywood called for legislative relief to address copying technologies it condemned with terminology normally associated with serial killers. Fortunately, those demands were ignored, and today, the movie studios have come to embrace digital versatile disks ("DVDs") and videocassette tapes. In fact, profits from the sale of pre-recorded media now exceed those derived from in-theater viewing.[1]

Today, the recording industry, among others, is calling for legislative relief to address illegal file sharing over Internet peer-to-peer networks, or P2P networks. While the members of NetCoalition strongly oppose the unlawful downloading and distributing of copyrighted works over P2P networks, we also caution against the summary adoption of what purports to be a simple legislative fix to complex online problems. The Internet is essentially a peer-to-peer network, a tool that allows users to connect with other users. Technologies such as email, instant messaging, search engines, web browsers, and broadband, to name just a few, are basically peer-to-peer platforms. Any proposal designed to eliminate one kind of a P2P platform has the potential of barring comparable communications platforms that are considered by most users to be not only lawful but essential.

In addition, almost everything on the Internet involves, allows, or perhaps more accurately, requires the copying of information or data. Emails and web site content are

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[1] "Hollywood Sees the Big Picture with DVDS," Frank Ahrens, Washington Post, October 7, 2002, Page A01 ("In today's Hollywood, box office revenue makes up less than a quarter of a film's total take. The largest piece of a movie's money pie comes from sales and rentals of its DVDs.").

routinely copied and stored, at least temporarily, as content moves through the infrastructure of the Internet to reach its ultimate destination. Online communications systems are intentionally designed to permit "copying and pasting" of content which can then be shared with intended recipients. Therefore, any legislative proposal to regulate or prohibit copying hardware, devices, or software can jeopardize the essential architecture of the Internet.

As the Committee considers S. 2560, or whether additional legislation is even necessary, we respectfully suggest that it embrace the following five key principles which are critical to a balanced and effective solution:

- Legislation must be premised on the Supreme Court's ruling in *Betamax*[2] that a provider of a technology that is capable of substantial legal uses cannot held liable for copyright infringement simply because the technology can be used by third parties for unlawful purposes.

- Legislation should target unlawful behavior and uses of technology rather than the technology itself.

- Legislation must provide a bright line between lawful and unlawful conduct so that litigation cannot be used as an economic weapon against innovators and entrepreneurs.

- Legislation that attempts to codify concepts of secondary liability for copyright infringement should incorporate current case law relating to contributory infringement, vicarious liability, and the *Betamax* standard.

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[2] *Sony Corp. v. Universal City Studios*, 464 U.S. 417 (1984).

- Legislation should ensure that entities that advertise and provide product reviews that simply demonstrate how a product can be used are not swept into the scope of possible defendants under any new cause of action.

This Committee has repeatedly worked with NetCoalition and other interested parties to fashion solutions to complex intellectual property issues and the myriad problems associated with legislating in both the online and off-line worlds. This collective approach has proven effective as Congress considered the Digital Millennium Copyright Act, the USA Patriot Act, the Electronic Communications Privacy Act, the Computer Fraud and Abuse Act, as well as legislation relating to privacy, spam, and identity theft.

We stand ready to join other interested stakeholders to work with the Committee to make sure there are adequate online protections against copyright infringement. Chairman Hatch, as you observed a few years ago in a similar context:

> We need policies that foster innovation and creativity, and that the users of the technology can enjoy. In the field of entertainment, for example, artists can potentially connect more directly with their audience using new digital delivery systems like the Internet. Music fans can more easily enjoy music on wireless devices, taking all of their music with them wherever they go without having to lug cases of CDs with them.... With creative thinking there is substantial synergy to brighten the lives of all of us in the more interconnected future.[3]

S. 2560 UNDERMINES THE SUPREME COURT'S *BETAMAX* DECISION

As currently drafted, S. 2560 would undermine the Supreme Court's 1984 decision in *Sony Corp. of America v. Universal City Studios, Inc.*, 464 U.S. 417 (1984)(the "*Betamax*" decision). There, the court ruled that a manufacturer of a product could not be held secondarily liable for infringing uses of the product by others so long as the product was "capable of substantial noninfringing uses." In other words, the

[3] *Utah's Digital Economy and the Future: Peer-to-peer and other emerging technologies, before the Senate Comm. on the Judiciary,* 106th Congress (2000)(Statement of Senator Orrin G. Hatch, Senate Judiciary Committee).

production and distribution of technology by itself could rarely be considered unlawful in the copyright context.

This clear standard has been one of the cornerstones of the growth of the Internet, because it strikes a reasonable balance between the interest of copyright holders and the technical realities of the online world. Indeed, the *Betamax* decision has widely been described as the Magna Carta of the technology industry. As noted before, almost everything on the Internet involves, allows, or perhaps more accurately, requires copying of information or data. As a result, in almost every instance, the investors and manufacturers of a new online technology have realized, at some point prior to marketing, their product may be used by some consumers to infringe certain types of copyrights.

Moreover, once the products have been on the market, they undoubtedly know that their products are being used to infringe copyrights. Because of the *Betamax* standard, however, they also know they are safe from liability if their product is capable of substantial noninfringing uses. As a result, new technologies such as email, instant messaging, web browsing, and search engines have been developed even though in each instance there is the potential that they could facilitate copyright infringement.

Unfortunately, S. 2560 undermines the bright line in the *Betamax* decision. The legislation would create a new cause of action for "intentional inducement." It would allow a copyright holder to sue any entity it believed was intentionally inducing infringement of someone's copyrights. The bill also contains additional language that purports to leave intact current doctrines of vicarious and contributory liability for copyright infringement, yet nothing in the legislation applies the protections in case law surrounding these theories of liability to the new cause of action. Consequently, if S. 2560 is enacted, the manufacturer of a new online technology would have no assurance that it would be free from litigation even if it could prove conclusively that its product was capable of substantial noninfringing uses.

Moreover, it is unclear whether the entertainment industry is willing to acknowledge that the Supreme Court's ruling applies to anything other than Sony Betamaxes. In fact, in briefs submitted in the *Grokster* case, the entertainment industry asked the appellate court to replace the bright line of the *Betamax* case with a cost-benefit analysis. They referenced the following non-binding dicta by Judge Posner:

> Even when there are noninfringing uses of an Internet file-sharing service...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. [4]

This cost-benefit analysis, if adopted nationwide, would cripple the Internet industry. In order to avoid copyright liability, a company that marketed a product would have to constantly assess: (1) whether the infringing uses were substantial; and (2) if they were substantial, whether the infringements could be reduced or eliminated in a manner that would not be disproportionately costly. Since virtually all Internet technology products have some infringing uses, manufacturers and service providers would operate in a perpetual state of uncertainty and confront unending litigation as copyright owners and courts second-guessed every engineering decision the manufacturers made.

S. 2560 WOULD TRIGGER A FLOOD OF LITIGATION

As currently drafted, S. 2560 would increase the likelihood of extended litigation and the potential that lawsuits could be used as an economic weapon against technologies the entertainment industry finds threatening. For example, although "intentional inducement" standard in the bill might sound like a difficult standard to meet, it does not require proof that the defendant actually intended to induce infringement. Rather, the defendant's intent can be inferred, culled from literally any document within the defendant's possession.

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[4] *In re Aimster Copyright Litigation*, 334 F.3d at 653 (7th Cir. 2003).

Plaintiffs would be allowed to engage in extensive and intrusive discovery, demanding email, market research data, and depositions of anyone affiliated with the development, marketing, or management of a product. Such tactics would prove burdensome for a large corporation. They would be fatal for a start-up company, the very kind of entrepreneurs that have been the pioneers of the Internet.

In addition, unlike current law, where a defendant can move to dismiss a case based on the simple fact that its product is capable of substantial noninfringing uses, it is doubtful that any court would grant a motion to dismiss or summary judgment in cases alleging intentional inducement, even if it appears clear that a plaintiff is engaged in little more than a fishing expedition. Many courts would feel compelled to allow a plaintiff the opportunity to discover evidence that could convince a jury that the defendant intended to induce infringement, as well as cross-examine a company's chief executive officer at trial to demonstrate that he or she intended to induce infringement when bringing a new technology to market.

Inevitably, copyright owners will be in a very enviable position. They can sue any developer of a new technology they find threatening. Or, they can use this new cause of action to force online companies to incorporate digital rights management ("DRM") technologies promoted by the copyright owner. Making matters worse, there is no guarantee that different copyright owners will seek inclusion of the same DRM technology. It is not inconceivable that within a short period of time, the entertainment industry will control domestic technologies, and online innovation, until now dominated by American entrepreneurs, will be shipped overseas.

Moreover, the cause of action under the proposed legislation is not limited to manufacturers of technology. Under the bill, anyone who can be considered to be aiding, abetting, procuring, or inducing someone to engage in copyright infringement is subject to liability. Consequently, venture capitalists, credit card companies, common carriers,

and even entities providing editorial reviews of products, could find themselves the target of litigation.

S. 2560 COULD UNDERMINE THE SAFE HARBORS CONTAINED IN THE DIGITAL MILLENNIUM COPYRIGHT ACT.

The Digital Millennium Copyright Act ("DMCA") contains safe harbors that limit the remedies available against Internet service providers ("ISPs") for infringements that occur on their systems. These safe harbors ensure that ISPs will not be held liable for copyright infringement by third parties when the ISPs provide basic Internet functions such as routing, hosting, and linking.

While these limits would continue to apply with respect to the *services* offered by ISPs (*i.e.,* routing, hosting, and linking), they would not apply to *software* provided by the ISPs to consumers to enable these services (*e.g.*, instant messaging or Internet access software). Currently, the provision of the software is protected by the *Betamax* standard. But, under S. 2560, an ISP could be sued for inducing infringement by distributing software that enables infringement, such as software enabling broadband services.

S. 2560 DOES NOT FULLY INCORPORATE THE STATUTORY FRAMEWORK IN THE PATENT ACT.

The proponents of S. 2560 assert that the inducement standard is taken from the Patent Act. Unfortunately, S. 2560 borrows from the Patent Act in an incomplete and inaccurate manner.

Section 271(b) of the Patent Act provides that "[w]hoever actively induces infringement of a patent shall be liable as an infringer." Section 271(c) of the Patent Act states that any person who sells a component of a patented machine, knowing that the component is especially made for use in infringement of the patent, and "not a staple article or commodity of commerce suitable for substantial noninfringing use, shall be liable as a contributory infringer."

The Patent Act does not explain the relationship between 271(b) and 271(c), but the Federal Circuit in *Dynacore v. Philips*, 363 F.3d 1263, 1276 n.6 (Fed. Cir. 2004), stated that "although a seller of a device that is capable of substantial noninfringing use will not be liable for contributory infringement, liability may still be established under § 271(b) if, in addition to the sale of that product, active steps are taken to encourage direct infringement." (Citations omitted.)

In other words, the manufacturer or seller of a device capable of noninfringing uses can be liable for inducing patent infringement only if he takes **active steps beyond the sale or manufacture to encourage direct infringement**.

S. 2560 paraphrases Section 271(b) by providing that "whoever intentionally induces" a copyright infringement "shall be liable as an infringer." But it does not codify 271(c), nor the relationship between 271(b) and 271(c) developed by the case law. The sponsors of S. 2560 assert that codification of 271(c) is unnecessary. They argue that the Supreme Court in *Betamax* transposed Section 271(c) to the copyright context when it ruled that the manufacturer of a device capable of a substantial noninfringing use was not a contributory infringer, and the *Betamax* rule is preserved in S. 2560's savings clause.

But as discussed above, S. 2560 creates a new form of secondary liability to which *Betamax* is not a defense. If Congress concludes that the Patent Act is an appropriate model for secondary copyright liability, then it should import the entire Patent Act framework: Section 271(b), Section 271(c), and the case law defining the relationship between Sections 271(b) and 271(c).

Additionally, S. 2560's definition of "intentionally induces" is far broader than the courts' interpretation of "actively induces" under Section 271(b). If Congress decides to proceed in the direction of the Patent Act, it should look to the definition of "actively induces" in the patent case law.

S. 2560 MAY NOT PROVIDE A REMEDY FOR *GROKSTER*

The proponents of the legislation assert that S. 2560 was introduced in response to the District Court's decision in *MGM v. Grokster, Ltd.*, 259 F. Supp. 2d 1029 (C.D. Cal. 2003). Based on our review of the District Court's decision, however, we believe there is a significant question whether the entertainment industry would prevail in an inducement action under S. 2560 against Grokster and the other P2P defendants.

In *Grokster*, the court stated that the defendant P2P software providers "are not significantly different from companies that sell home video recorders or copy machines, both of which can and are used to infringe copyrights." The court did not find that "Grokster or StreamCast do anything, aside from distributing software, to actively facilitate ... their users' infringing activity." Consequently, the court found that "[a]bsent evidence of active and substantial contribution to the infringement itself, Defendants cannot be liable."

In briefs to the Ninth Circuit, in the press, and in communications to Senators, the entertainment industry contends that Grokster and other P2P companies not only induce infringement, but actually "seduce" children into engaging in infringing acts. However, the *Grokster* court found no evidence of such seduction. It did not find a single advertisement encouraging users to engage in the unauthorized trading of copyrighted works. It did not find a single email instructing users how to break the copyright laws. Accordingly, if the entertainment industry were to bring an inducement action under S. 2560 against Grokster, the suit would probably survive motions to dismiss and for summary judgment, because the industry could argue that Grokster intended to induce infringement; but the suit would probably fail at trial unless the industry could produce more solid evidence of intent to induce infringement.

Unfortunately, balanced against this serious question of whether S. 2560 would provide plaintiffs with an ability to take down Grokster, we know that S. 2560 would impose tremendous collateral damages on large sectors of the U.S. economy for reasons

articulated in this testimony. Any legislation should narrowly target bad behavior while not imposing these kinds of collateral damages on "good actors."

Ultimately, we believe that the Ninth Circuit employed the proper analysis in the *Napster* case by making a distinction between behavior and technology. It stated in that case, "We are compelled to make a clear distinction between the architecture of the Napster system and Napster's conduct in relation to the operational capacity of the system." *Napster*, 239 F.3d at 1020. This distinction between architecture and conduct is the key to *Napster* and to contributory copyright infringement analysis in the digital era.

Unfortunately, the entertainment industry is urging this Committee and has urged the courts to blur the bright line between behavior and technology. This Committee should not be lured into penalizing technologies that can be used for unlawful purposes, but rather should focus on illegal behavior. Recently, Howard Beales, the Director of the Bureau of Competition at the Federal Trade Commission provided testimony before a Senate committee, which underscored the importance separating behavior from platforms and technologies that allow unlawful behavior to occur. He stated:

> [C]onsumers can use e-mail to send or receive copyrighted materials, pornography, viruses, and spyware. Similarly, search engine technology may expose consumers inadvertently to child pornography, viruses, and spyware. Videotape recorders and compact disk recorders may be used in violation of copyright laws by individuals who are unaware that they are doing so. Many risks associated with P2P file-sharing seem to result largely from the actions of individual users, rather than from the operation of the P2P file-sharing software itself.[5]

CONCLUSION

Unlawful peer-to-peer file sharing of copyrighted materials is wrong. Users and companies who engage in these activities should not be allowed to operate beyond the reach of the law. The Committee should recognize, however, that bad actors—and not

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[5] *The Future of Peer-to-Peer (P2P) Technology, before the Senate Comm. On Commerce, Science and Transportation,* 108th Cong. (2004)(Statement of Mr. Howard Beales, Director, Bureau of Consumer Protection, Federal Trade Commission).

technology—are responsible for the illegal activities. If the Committee determines that a legislative response is appropriate, we urge Members to ensure that legislation be narrowly focused to target behavior and not put at risk the companies and innovators that allow most consumers to lawfully enjoy new and exciting technologies.

In addition, the recording industry must recognize that the real solution to the problem of unlawful file sharing cannot be achieved exclusively through legislation. Even a complete ban on file sharing in the United States will not prevent consumers from accessing overseas sites to download music. Any comprehensive solution must involve a combination of effective legal relief, consumer education, and a reasonably priced, convenient, and portable distribution system that makes it as possible to download music legally as can be done today illegally. In the long run, the recording industry will be no more able to prevent online file sharing than Hollywood could stop the VCR or the DVD.

Thank you for the opportunity to testify, and I would be happy to answer any questions from the Committee.

July 7, 2004

By Hand

Hon. Orrin G. Hatch, Chairman
United States Senate
Judiciary Committee
226 Dirksen Senate Office Building
Washington, DC 20510

Re: Opposition to, and Call for Multiple Hearings on, S. 2560, the "Inducing Infringement of Copyright Act" of 2004

Dear Senator Hatch:

P2P United is the non-profit trade association of the peer-to-peer file search and sharing software industry. Formed just under one year ago, the organization currently represents the developers and distributors of five globally popular peer-to-peer software programs: BearShare, Blubster, eDonkey, Grokster and Morpheus. We do not represent KaZaA and are otherwise unaffiliated with it and associated ventures.

We write today, Mr. Chairman, to associate ourselves generally with the scores of other technology industry associations, individual companies and public interest organizations that have criticized the "Inducing Infringement of Copyrights Act," S. 2560, as a dangerous and unnecessary technology mandate with the potential to chill all forms of further innovation in information technology. P2P United and its member companies look forward to multiple hearings on the substance and effects S. 2560 in all Committees of competent jurisdiction.

With respect, we believe that the dramatic and far-reaching shift in current law -- and the radical chilling effect upon technological innovation -- that S. 2560 would produce demands nothing less than an extremely thorough and open process of hearings and debate. We are particularly eager to participate in such proceedings as the Senate Judiciary Committee may find it desirable and convenient to schedule in both this and the next Congress, and we stand ready to assist the Committee as it may request.

We also write today specifically on behalf of the peer-to-peer software industry to correct the most egregious of the factual errors, exaggerations and distortions regarding peer-to-peer technology (and those who make it available to the public) contained in your statement of June 22, 2004 upon introduction of this dangerous and unnecessary legislation. To that end, Mr. Chairman, please permit us here to correct the record in the following three, but particularly important, respects:

1) The astonishing claim that the kind of wholly decentralized peer-to-peer software developed by the members of P2P United "functions like Earth Station 5's 'piracy machine'" is utterly inaccurate and indefensible.

P2P United has chosen the preceding words advisedly, Mr. Chairman. Earth Station 5 is not a member of P2P United and, given its clear disdain for the principles set forth in our industry Code of Conduct adopted last September (please see attached) would be denied that status even if requested. "ES5" is a rogue software developer based in Jenin in Palestinian territory. It deliberately flauts American and international copyright law by expressly disclaiming the jurisdiction of all such laws and, most egregiously, proudly supplying downloads of first run motion pictures ***from its centralized computer servers***. We were, therefore, particularly dismayed to note your statement's repeated use of this transparently inapt, misleading and false comparison.

In truth, Mr. Chairman, the "business models" and actual technologies of the members of P2P United bears absolutely *no resemblance whatsoever* the illicit infrastructure and practices of ES5. Specifically, in stark contrast to ES5, the members' of P2P United:

a) fully and freely subject themselves to American jurisprudence (indeed, the Federal Court ruling that S. 2560 is intended to legislatively reverse in the midst of an ongoing appeal concerned two P2P United member's programs directly: Grokster and Morpheus);

b) continue to refine and make available what the GAO repeatedly has confirmed to be content-agnostic software that permits *users* to establish wholly decentralized connections among individuals who elect to use such software in various ways – infringing and non-infringing alike – over which P2P United's members have no control; and

c) to state what should be the obvious, the members of P2P United make *software* – not a machine of any kind – available to the public. We understand, Mr. Chairman, why the proponents of your legislation might seek to conjur images of "black boxes" like those used for cable TV theft, for example. Such physical "machines," the sole purpose and capability of which is theft, properly subject their makers and users to serious copyright infringement liability because these devices – manifestly *unlike* decentralized peer-to-peer software – are not capable of and have no "substantial noninfringing uses," as the Supreme Court so aptly put it in the *Betamax* decision. By contrast, decentralized peer-to-peer software was found – as a matter of uncontested fact in the *Grokster* case – to be routinely and increasingly used for the lawful distribution of copyrighted material, public domain information, scientific data, and to facilitate significant forms of e-commerce.

2) Allegations that peer-to-peer technology and the software made available to the public by the members of P2P United are dangerous to the public in general, to children in particular, and that our members adequately fail to warn the public of risks associated with P2P software have been rejected both by the General Accounting Office and the Federal Trade Commission.

Despite the repeated framing of inquiries to these bodies by Congressional investigators in ways seemingly intended to produce the most myopic and statistically skewed forms of data, both arms of the government noted above recently have returned findings making clear that, "Many risks associated with P2P file-sharing seem to result largely from the actions of individual

users, rather than from the operation of the P2P file-sharing software itself." (*See* June 23, 2004 Testimony of Howard Beales, Director of the FTC's Bureau of Consumer Protection before the Competition Subcommittee of the Senate Commerce Committee.) For these reasons, Mr. Beales noted for the record, "we are not aware of *any* basis under the FTC Act for distinguishing P2P from other neutral consumer technologies [e.g., "e-mail," "search engine technology," "video-tape recorders and compact disc recorders" cited elsewhere in Director Beales' prepared statement].

Significantly, Mr. Beales also testified that: "The FTC staff's review revealed that distributors of P2P file-sharing programs use a variety of means to convey risk information to consumers. Distributors disclose risk information on their own Web sites or in their licensing agreements with consumers. Some distributors also provide consumers with a hyperlink to risk information at www.P2PUnited.org, one of the P2P file-sharing software industry's trade associations. In addition, one of the main portals for downloading such programs, www.Download.com, discloses some risk information on its site. FTC staff reviewed and analyzed the representations made by these distributors about the risks associated with downloading and using their programs. None of these representations appear on their face to be false or misleading." (Emphasis added.)

Accordingly, said Mr. Beales, the agency concluded that there is neither a basis in law nor the need for unusual or extraordinary warning and disclosure requirements to be imposed upon the members of P2P United and similarly responsible companies. He did recommend, however, that some existing warnings be "more accessible" to users and stated that the agency would follow through with appropriate companies and organizations on these matters. P2P United and its member companies remain committed to appropriate risk disclosures, Mr. Chairman, and met voluntarily and cooperatively last week with FTC senior staff to that end.

The General Accounting Office was equally balanced and forthright in its two reports to Congress in the past six months on child pornography exposure. Asked solely whether juveniles inadvertently may be exposed to pornographic materials by using peer-to-peer software and actively downloading files, the honest answer – not surprisingly – came back in the affirmative. Fortunately for the public policy process, though not asked specifically to do so, the GAO also responsibly presented data to Congress placing that risk in context and in proportion to those faced by children from other prominent Internet-delivered sources of such material. In doing so, it quoted data from the federal Center for Missing and Exploited Children for calendar years 2002 and 2003 documenting that unwanted exposure to such material was a vastly *greater* risk through websites and e-mail.

Indeed, based on CMEC hotline tips (the best data available to the GAO) websites were *50 times* more likely – and e-mail almost *15 times* more likely -- to be a source of offensive exposure to children than P2P files actively downloaded by children. That same data also showed that the risks to children from websites and e-mails had increased between 2002 and 2003 by almost 70% and nearly 100%, respectively, while exposure in the same period from P2P sources rose just 11% despite a significant increase in P2P software usage in that timeframe.

Finally, Mr. Chairman, regarding warnings of potential liability for copyright infringement and warnings to parents about the need to be vigilant in protecting their children from child pornography and pornographers, P2P United respectfully reminds you of its voluntarily constructed "Parent to Parent Resource Center" launched last fall www.p2punited.org /PostNuke-0.726/ html/parents.php), its extremely strong warnings against copyright

infringement *and the particular danger of prosecution associated with downloading music* (www.p2punited.org/ PostNuke-0.726/html/parents.php) and its recent outreach to the FBI (reported upon in May 13th's Washington Post) to help the Bureau apprehend suspected predators.

As we have said many times in multiple submissions to Congress and to you, Mr. Chairman, the peer-to-peer industry is already doing more than its fair share – and will continue to do so – to fight this scourge, but the limits of our decentralized technology (also documented by the GAO and others) define the limits of our abilities. *We ask for no exemption from actionable responsibility, only respite from the ceaseless and factually baseless demonization of our industry and of our software of which S. 2560 appears to be the latest and most draconian example to date.*

3) Seemingly "immortal" allegations that the developers of decentralized peer-to-peer software have it within their power – but simply refuse – to "filter" out substantively offensive, dangerous, or copyrighted material are simply false and should play no further role in the legislative and policy processes. ***Any lingering doubt on such technical matters should be resolved promptly by an independent investigation of neutrally framed questions by the National Academy of Sciences.***

With respect, Mr. Chairman, the wholly mistaken suggestions in your June 22 statement to the effect that the decentralized architecture of modern P2P software is inefficient, "makes little sense," and was deliberately chosen by P2P software developers to escape copyright liability are so inaccurate as to argue for an immediate moratorium upon any and all legislation that would have the practical effect of modifying the Supreme Court's ruling in the *Betamax* case. While we hope to discuss these matters with you and members of the full Committee in greater detail, both privately and in public, we urge you to briefly consider the following:

a) no matter what measure is adopted – total bandwidth use, file transfer time, system stability and robustness, or security – the decentralized nature of modern peer-to-peer software programs renders such programs vastly *more* efficient than the "hub and spoke" design that characterized early file-sharing architecture. Indeed, such decentralized design precisely parallels computer and military scientists' vision of the original DARPAnet, and the subsequently developed public internet, for all of the reasons stated above;

b) the argument that P2P software companies have deliberately designed their software to evade copyright law (advanced before the Ninth Circuit Court of Appeals by music industry counsel in oral argument in the pending *Grokster* case) was expressly rejected from the bench. Indeed, counsel was admonished from the bench that the programs seemed to have been designed to *comport* with all applicable copyright laws and the courts' rulings in Napster;

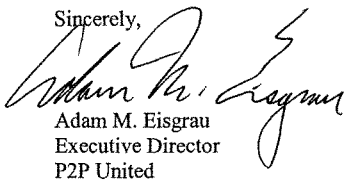
c) requiring the defining feature of currently decentralized peer-to-peer software to be changed to permit presently impossible forms of centralized content controls would constitute a massive "technology mandate" of precisely the kind that, it is claimed, S. 2056 seeks to avoid. As we have noted many times before, Mr. Chairman, residual distrust of peer-to-peer developer claims that their products cannot centrally filter should be evaluated, once and for all, by a neutral and highly competent scientific body such as the National Academy of Science. It is time to bring the endless rounds of "he said/she said" fulmination and speculation on this account to a responsible end with responsible science.

Conclusion

P2P United does not question the sincerity of your commitment to protecting copyright or children, Mr. Chairman. We do take serious issue, however, with the factual inaccuracy and inflammatory rhetoric that informs both S. 2560 and your statement on its behalf.

As a mutually productive means of going forward, we make a simple proposal. Let us in the coming months replace rhetoric with fact, propaganda with policy, and – perhaps most importantly – doomsaying with deliberation before legislating against the most useful and transformative general purpose communication technology ever to have been developed. In that spirit, P2P United looks forward to a dispassionate and balanced *series* of hearings on S. 2560 and related matters before the Committee, and to appearing before you in those proceedings.

Sincerely,



Adam M. Eisgrau
Executive Director
P2P United

Attachment

cc: Hon Patrick J. Leahy, Ranking Member
Members of the Senate Judiciary Committee

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Committee on the Judiciary

United States Senate

July 22, 2004

Hearing on S. 2560, the Intentional Inducement of Copyright Infringements Act of 2004

Statement of the Honorable Marybeth Peters,

Register of Copyrights

Mr. Chairman, Senator Leahy, Members of the Committee, good afternoon. Thank you for giving me the opportunity to testify about S. 2560, the Intentional Inducement of Copyright Infringements Act. I believe this bill addresses the most important issue facing our copyright system today: new services that employ peer-to-peer technology to create vast, global networks of copyright infringement. There should be no question that such services should be liable for the copyright infringement they encourage and from which they profit.

The Copyright Office supports S. 2560 because it improves the existing law of secondary liability for copyright infringement. This area of the law is essential for effective copyright protection, but it has become confused as courts have struggled to apply the existing common-law doctrines to the new peer-to-peer services, with conflicting results. This bill recognizes liability for the "intentional inducement" of copyright, which will allow courts to examine fully the circumstances behind infringing activity to find those truly responsible, such as the operators of the current peer-to-peer networks who depend upon infringement for their commercial viability.

I. Background

A. Contributory Infringement and Vicarious Liability

S. 2560 and the controversy surrounding peer-to-peer services revolve around the central legal issue of secondary liability for copyright infringement. For decades, courts have recognized that those who assist and facilitate copyright infringement are liable just as those who actually commit the acts of infringement. For example, in 1929 the Seventh Circuit Court of Appeals in *Dreamland Ballroom, Inc. v. Shapiro, Bernstein & Co.*,[1] held that a dance hall that hired an orchestra to provide music to its patrons was liable for the unauthorized public performance of musical works committed by that orchestra. That case is an example of "vicarious liability," which the landmark case of *Shapiro, Bernstein & Co. v. H.L. Green Co.*[2] explained this way :

> When the right and ability to supervise coalesce with an obvious and direct financial interest in the exploitation of copyrighted materials ... the purposes of copyright law may be best effectuated by the imposition of liability upon the beneficiary of that exploitation.

Thus, vicarious liability requires two elements: (1) the right and ability to supervise or control the infringing activity; and (2) a direct financial benefit from that activity. It is closely related to the doctrines of enterprise liability and respondeat superior in tort law.

There is another form of secondary liability in copyright law, "contributory infringement," which stretches back to 1911.[3] As the Second Circuit Court of Appeals has explained, contributory infringement occurs where "[o]ne who, with knowledge of the infringing activity, induces, causes, or materially contributes to the infringing conduct

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[1] 36 F.2d 354 (7th Cir. 1929)
[2] 316 F.2d 304, 307 (2d Cir. 1963)
[3] *See Kalem v. Harper Brothers*, 222 U.S. 55 (1911).

of another."[4] In general, the two elements of contributory infringement are (1) knowledge of the infringing activity; and (2) material contribution to the activity.

Note that the common formulation of contributory infringement includes a reference to those who "induce" another to commit infringement, which is similar to the language of the proposed bill. In theory, the existing contributory infringement doctrine may be flexible enough to cover situations where a defendant induces another to commit infringement. When actually applying this standard, however, courts have not focused on the inducement aspect of contributory infringement, and thus, as I will explain, legislation is needed to address these circumstances directly to remove any doubt about liability for inducement.

These doctrines were developed by case law under the 1909 Copyright Act, which did not contain any express provision on secondary liability. In the 1976 Act, Congress recognized secondary liability in the grant of rights under copyright, providing authors and copyright owners with the "exclusive right to do *and to authorize*" the enumerated rights.[5] As the legislative history to the Act explains, "[u]se of the phrase 'to authorize' is intended to avoid any questions as to the liability of contributory infringers."[6] The statute, however, left the details of the secondary liability doctrines to the courts to apply in specific cases.

From a policy perspective, the secondary liability doctrines are critical to the effective functioning of our copyright system, and even more so in the new digital environment. They allow copyright owners to focus their enforcement (and licensing) efforts on those entities that foster infringing activity and have the resources and

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[4] *Gershwin Publishing Corp. v. Columbia Artists Management, Inc.*, 443 F.2d 1159, 1162 (2d Cir. 1971).
[5] 17 U.S.C. § 106 (emphasis added).
[6] H.R. Rep. 94-1476, at 61.

wherewithal to either pay licensing fees or satisfy an infringement judgment, without bringing costly, time-consuming and usually futile actions against multiple, mostly judgment-proof individual defendants. As one court has explained,

> Recognizing the impracticability or futility of a copyright owner's suing a multitude of individual infringers ... the law allows a copyright holder to sue a contributor to the infringement instead, in effect as an aider and abettor.[7]

Thus, enforcement against the "middlemen" who encourage, facilitate and benefit from infringement has long served an important role in providing meaningful and efficient copyright protection. As another court explained, in finding a supplier of "time-loaded" cassettes liable for infringement facilitated by those cassettes:

> Regrettably, in copyright litigation, enforcement efforts seem ineffective. Misappropriation may often needlessly succeed. Thus, liability for contributory infringement is particularly appropriate here. Given the apparent division of labor in the counterfeit recording industry, the actions of contributory infringers make possible the wide dissemination of the infringing works.[8]

As I will explain, a similar phenomenon is occurring in the digital environment, as proprietors of services that use peer-to-peer technology rely on a "division of labor" strategy that enlists millions of consumer to become distributors of infringing copies, thereby attracting more users and advertisers who generate revenue for these companies, but which is designed to leave the proprietor without legal liability. Secondary liability is appropriate in these situations, but there is confusion in the courts as to whether current law reaches that result. I will next describe the state of the law and how it has been applied to these new services.

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[7] *In re Aimster*, 334 F.3d 643, 646 (7th Cir. 2003) (Posner, J.).
[8] *A&M Records, Inc. v. General Audio Video Cassettes, Inc.*, 948 F. Supp. 1449, 1455 n.4 (C.D. Cal. 1996).

B. The *Sony* Betamax Case

Perhaps the most significant development in secondary liability was the Supreme Court's first attempt to interpret the 1976 Copyright Act, *Sony Corp. of Am. v. Universal City Studios, Inc.*[9] Often referred to as the Betamax case, *Sony* involved the question of whether a manufacturer of a VCR could be held liable under the doctrines of secondary liability for the infringing actions of the customers who buy the VCR. The Court recognized that secondary liability was established in copyright law:

> [V]icarious liability is imposed in virtually all areas of the law, and the concept of contributory infringement is merely a species of the broader problem of identifying the circumstances in which it is just to hold one individual accountable for the actions of another.[10]

But the Court concluded that these doctrines had not been applied to a situation presented by the VCR, where the manufacturer did not have actual knowledge of the infringing activity for which customers used the device, only "constructive knowledge of the fact that its customers may use that equipment to make unauthorized copies of copyrighted material."[11]

To resolve this situation, the Court looked to patent law, specifically the "staple article of commerce" doctrine embodied in Section 271(c) of the Patent Act, which provides that sale of a "staple article or commodity of commerce suitable for substantial noninfringing use" is not contributory infringement, on the grounds that patent rights should not extend the patentee's control to allow it to control the sale of staple articles or commodities. Applying this concept to the copyright context, the Court explained that:

> [t]he staple article of commerce doctrine must strike a balance between a copyright holder's legitimate demand for effective – not merely symbolic

[9] 464 U.S. 417 (1984).
[10] 464 U.S. at 435.
[11] *Id.* at 439.

> – protection of the statutory monopoly, and the rights of others freely to engage in substantially unrelated areas of commerce.[12]

Based on this reasoning, the Court adopted the following approach to address the question of whether Sony could be held liable for copyright infringement:

> 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. The question is thus whether the Betamax is capable of commercially significant noninfringing uses.[13]

It found that the Betamax met this test, based largely on its separate conclusion that the customers' "time-shifting" of broadcast television programs was a fair use. The Court noted, however, that judgments in this area were primarily the responsibility of Congress rather than the Courts, and that it might be appropriate for Congress to take a "fresh look" at these issues in new copyright legislation.

C. Secondary Liability and Peer-to-Peer Services

The *Sony* decision has played a substantial role in the legal dispute over "peer-to-peer" services like Napster and its progeny, such as Aimster, Grokster, Morpheus and Kazaa. As I explained in my testimony before this committee last Fall, the courts have struggled to apply *Sony* to resolve the question of whether companies who operate peer-to-peer networks are liable for the massive amounts of infringement that take place on them. In the case of Napster and Aimster, the courts have held the operators of those services liable under theories of secondary liability. In the case of Grokster and Morpheus, a district court found that secondary liability did not apply to those peer-to-peer services, in large part because of the *Sony* decision. To understand how secondary

[12] 35 U.S.C. § 271(c).
[13] 464 U.S. at 442.

liability and *Sony* have operated in this context, I will go into these cases in some more detail.

1. *A&M Records v. Napster*

The first peer-to-peer service to prompt copyright infringement litigation was Napster.[14] A user would download Napster's "Music Share" software and install it on his computer. When he started the software, it would send information to the Napster servers about the MP3 files the user had stored in the "shared folder" of his hard drive. The file names that were sent to the Napster servers were included in an index of all of the files being made available by users of the Napster network. When the user searched for an artist or title of a song, the Music Share software used the index on the Napster server to locate another user with that MP3 file. If he chose to download the file, the software then connected the two users together and a transmission proceeded directly between them, rather than go through any Napster server.[15]

Because the user's equipment, and not Napster's, actually reproduced and distributed the MP3 file copies of the copyrighted works, Napster could only be liable for secondary liability, rather than direct copyright infringement. The major record companies and musical work copyright owners brought suit against Napster in 2000 for contributory infringement and vicarious liability. The district court issued a preliminary injunction against Napster in July 2000, and the Ninth Circuit affirmed that decision in part in February 2001, finding that the plaintiff copyright owners had shown a likelihood of success on the merits to support a preliminary injunction.

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[14] *A&M Records, Inc. v Napster, Inc.*, 239 F.3d 1004 (9th Cir. 2001).
[15] *Id.* at 1012-13.

The panel found that Napster met the requirements for both contributory infringement and vicarious liability. As to contributory infringement, the Ninth Circuit found that Napster had actual knowledge of infringing activity being made possible by its software, and that the software and services Napster provided were its "material contribution" to the infringement.[16] On the issue of vicarious liability, the panel found that Napster enjoyed a financial benefit from the infringement, and has the right and ability to supervise the infringing conduct by blocking users' access to the Napster service.[17]

The Ninth Circuit discussed the *Sony* case and its effect on the issue of contributory infringement, as it interpreted *Sony* as providing a defense only to that form of secondary liability. It held that *Sony* was "of limited assistance to Napster" because Napster had "actual, specific knowledge of direct infringement" occurring on its network.[18] It viewed the *Sony* test of whether the technology is "capable of substantial noninfringing uses" as a means for imputing knowledge of infringement to the technology provider. Where such knowledge was actually present, the Ninth Circuit held the *Sony* test does not apply. In this way, the court felt "compelled to make a clear distinction between the architecture of the Napster system and Napster's conduct in relation to the operational capacity of the system."

The *Sony* case also played a role in the panel's review of the district court's preliminary injunction, where it narrowed the scope of the injunction to apply only where Napster had reasonable knowledge of infringing files on its service and failed to take action to prevent the distribution of those files. It noted that the mere existence of the

[16] *Napster*, 239 F.3d at 1019-22.
[17] *Id.* at 1022-23.
[18] *Id.* at 1020.

network on which files could be distributed was not enough to render Napster liable, citing *Sony*. This reflects the Supreme Court's concern over inhibiting non-infringing uses of technology through an overly-broad application of secondary liability under copyright.

As a result of the Ninth Circuit's opinion, Napster was forced to filter out infringing files from its network. Unable to find a way to continue operating in light of the injunction, it shut down in 2002.

2. *In re Aimster*

The Seventh Circuit was the next appellate court to consider the liability of a peer-to-peer service in the case of *In re Aimster*.[19] Aimster operated in conjunction with an instant-messaging ("IM") service, such as AOL's Instant Messenger, hence the AIM in Aimster. When users were online using an IM program to chat, they could also trade music files through the Aimster P2P software. The transmissions between users were encrypted such that the proprietor of the Aimster service argued that he could not know whether the files being transmitted were copyrighted or not. The district court issued a preliminary injunction against Aimster, and the Seventh Circuit affirmed that decision in an opinion written by Judge Richard Posner.

Judge Posner's opinion addresses Aimster's liability only in terms of contributory infringement, not vicarious liability.[20] It concludes that Aimster did have sufficient knowledge of infringing activity, based on evidence from the software's tutorial that showed examples of how it is to be used that only included copyrighted music files.[21]

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[19] 334 F.3d 643 (7th Cir. 2003).
[20] *Id.* at 654-55 (noting that existence of vicarious liability was "academic" in light of contributory infringement finding).
[21] *Id.* at 649. In so doing, the Seventh Circuit departed from the Ninth Circuit's holding that where a

Also, the service offered a "Club Aimster" option for a monthly fee that lists the 40 most popular songs being made available on the service, which the court found were "invariably under copyright."[22] The panel rejected Aimster's argument that the encrypted nature of the transmissions prevented it from having knowledge of the infringing activity, concluding that this feature was an attempt by Aimster to avoid liability by remaining purposefully ignorant of the infringement, and noting that "willful blindess is knowledge, in copyright law … as it is in the law generally."[23]

Judge Posner also extensively analyzed the *Sony* defense raised by Aimster, ultimately rejecting it on the grounds that Aimster had offered no evidence that its software could be used for noninfringing purposes.[24] He noted that it is not enough for a defendant to show that a "product or service be physically capable … of a nonfringing use."[25] Even if Aimster could show such substantial noninfringing uses, the panel held that the defendant would have to "show that it would have been disproportionately costly for [it] to eliminate or at least reduce substantially the noninfringing uses,"[26] which Aimster also failed to do.

3. *MGM Studios v. Grokster*

In contrast to the *Napster* and *Aimster* decisions, in the case of *Metro-Goldwyn-Mayer Studios, Inc. v. Grokster*, the District Court for the Central District of California ruled that the peer-to-peer services Morpheus (operated by Streamcast) and Grokster

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provider of technology has actual knowledge of specific infringing uses the *Sony* defense becomes inapplicable.

[22] *Id.* at 651-52.

[23] *Id.* at 650.

[24] *Id.* at 653 ("Aimster has failed to produce any evidence that its service has ever been used for a noninfringing use, let alone evidence concerning the frequency of such uses.")

[25] *Id.*

[26] *Id*

were not liable for the copyright infringement of their users.[27] The court focused on the central technological difference between these new services and Napster – rather than maintain a centralized index of files being distributed on their servers like Napster, the defendants' software either creates *ad hoc* indices on the computers of users on the network, known as supernodes, or it uses no centralized index at all. In essence, the court accepted defendants' characterization that all they did was sell a piece of software to users, and had no further interaction after that, just as Sony merely sold a VCR to consumers. Based on this fact, the court concluded that Grokster and Streamcast could not limit the infringement occurring on their networks, because there was no centralized index through which they could control infringing uses of their software.[28]

Thus, when applying the tests for contributory infringement and vicarious liability, the court's characterization of defendants as mere providers of software became essential to its analysis. Although it recognized that the defendants had actual knowledge of infringement thanks to plaintiffs' numerous notices sent to defendants, it held that contributory infringement requires knowledge of specific infringement at the precise moment when defendants could limit such infringement.[29] In this case, the court, relying heavily on the *Sony* decision, found that once the software had been downloaded, then the defendants could not longer control the use of the software, and thus their knowledge of infringement occurring after the download was irrelevant.

With respect to the material contribution element of contributory infringement, the court relied again on *Sony* to find that defendants did not materially contribute to the infringement, comparing their software to the VCR or a photocopying machine – devices

[27] 259 F. Supp. 2d 1029 (C.D. Cal. 2003).
[28] *Id.* at 1041-42.
[29] *Id.* at 1037.

that enable both infringing and non-infringing uses. On these grounds the court denied contributory infringement.

On vicarious liability, the court found that defendants gained a direct financial benefit from the infringement that takes place on their service. As the court explained:

> Here, it is clear that Defendants derive a financial benefit from the infringing conduct. The ability to trade copyrighted songs and other copyrighted works certainly is a "draw" for many users of Defendants' software. As a result, Defendants have a user base in the tens of millions.
>
> * * *
>
> [I]ndividuals are attracted to Defendants' software because of the ability to acquire copyrighted material free of charge. While those who use Defendants' software do not pay for the product, Defendants derive substantial revenue from advertising. For example, StreamCast had $ 1.8 million in revenue in 2001 from advertising. ... And as of July of 2002, StreamCast had $ 2 million in revenue and projects $ 5.7 million by the end of the year. ... Grokster also derives substantial revenue from advertising. ... The more individuals who download the software, the more advertising revenue Defendants collect. And because a substantial number of users download the software to acquire copyrighted material, a significant proportion of Defendants' advertising revenue depends upon the infringement. Defendants thus derive a financial benefit from the infringement.[30]

Yet, on whether they had the right and ability to control the infringement, the court again relied on the lack of a centralized index to find that defendants could not control the infringement taking place on the network created by their software.

In the end, the court acknowledged that its result might not be the right one from a policy standpoint. It noted the "possibility that Defendants may have intentionally structured their businesses to avoid secondary liability for copyright infringement, while benefiting financially from the illicit draw of their wares."[31] It also noted that "additional legislative guidance may be well-counseled" in this circumstance. The case is currently

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[30] *Id.* at 1044.
[31] *Id.* at 1046.

on appeal to the Ninth Circuit, where oral argument was held this past February, but no decision has been issued to date.

In my view, the *Grokster* decision was wrongly decided, and I hope the Ninth Circuit corrects the errors in the district court's decision. The court employed an unnecessarily cramped view of existing secondary liability doctrines, creating a much narrower test of "knowledge", "material contribution" and "right and ability control" than any case before it, including the Ninth Circuit's decision in *Napster*. It also misapplied the *Sony* decision to an inaccurate characterization of the defendants as mere providers of software, comparing them to maker of a VCR, when their services were functionally the equivalent of Napster and Aimster. Most importantly, the *Grokster* decision fails to see the forest for the trees; it essentially ignores defendants' intent to establish and create a network of massive infringement – by enlisting ordinary consumers to engage in piracy – upon which they have built their business.

* * *

As can be seen from the discussion of these cases, application of the secondary liability doctrines in the peer-to-peer context has produced conflicting results. On the one hand, the Napster and Aimster services were found to be liable by the Ninth Circuit and Seventh Circuit, while, on the other hand, Grokster and Streamcast were not found liable by the Central District of California. Each of the cases involved different interpretations of the Supreme Court's decision in *Sony* and its effect on the secondary liability doctrines.

But there is one constant in all of these cases. All of the services at issue facilitate massive copyright infringement involving literally billions of copies of copyrighted

works. There is also no dispute that the use of these services constitutes copyright infringement – unlike the *Sony* case which held that the principal use of the VCR was a fair use. It is also undisputed that the defendants who operate these services rely on the copyright infringement as a draw to attract users, thereby attracting advertisers. These facts make the comparison to *Sony* remarkably inapt. In my view, if the VCR had been designed in such a way that when a consumer merely turned it on, copies of all of the programs he recorded with it were immediately made available to every other VCR in the world, there is no doubt the *Sony* decision would have gone the opposite way.

It would seem, in these circumstances, that sensible application of secondary liability doctrines would result in liability against these companies, even accounting for the concerns expressed by the Supreme Court in the *Sony* decision. As I noted above, the doctrine of contributory infringement, which includes notions of inducement, is likely broad enough to find liability in these circumstances. Yet, as the *Grokster* case shows, it appears that defendants are able to evade copyright liability successfully while still profiting from massive copyright infringement which they enable and encourage.

As I testified last year, I believe that legislative action in this area is warranted if courts interpret current law to exonerate proprietors of P2P services like Grokster, Morpheus and Kazaa. In my view, S. 2560 would help correct the problems created by the Grokster court's misapplication of *Sony* and secondary liability doctrines in the peer-to-peer context. I will now turn to the provisions of the bill.

II. The Inducing Infringements Act

The Inducing Infringements Act would add a new subsection (g) to Section 501 of the Copyright Act. The existing Section 501 defines copyright infringement – in

subsection (a) – and provides a civil cause of action for the legal or beneficial owner of copyright to bring against infringement.[32] The new subsection would create a new species of copyright liability by making clear that anyone who "intentionally induces any violation of subsection (a) shall be liable as an infringer." In other words, a person who "intentionally induces" infringement would be liable as if he or she committed the infringement. The bill defines "intentionally induces" as meaning:

> [i]ntentionally aids, abets, induces, or procures, and intent may be shown by acts from which a reasonable person would find intent to induce infringement based upon all relevant information about such acts then reasonably available to the actor, including whether the activity relies on infringement for its commercial viability.

Paragraph (3) of the new subsection makes clear that the new form of inducement liability is in addition to existing common-law secondary liability doctrines, and does not modify them in any way. It also provides that nothing in the bill "require[s] any court to unjustly withhold or impose any secondary liability for copyright infringement."

As you explained in your floor statement, Mr. Chairman, this provision draws from patent law and federal criminal law. Section 271(b) of the Patent Act provides that "[w]hoever actively induces infringement of a patent shall be liable as an infringer."[33] Similarly, the Section 2 of the Federal Criminal Code provides that "[w]hoever commits an offense against the United States or aids, abets, counsels, commands, induces or procures its commission, is punishable as a principal."[34] You have noted that the concept of liability for "inducement" was not at issue in *Sony*, as the Court made clear that no evidence existed that the defendant in that case "intentionally induce[d] its customers to make infringing uses of respondents' copyrights, nor does it supply its products to

[32] 17 U.S.C. § 501(a) & (b).
[33] 35 U.S.C. § 271(b).
[34] 18 U.S.C. § 2.

identified individuals known by it to be engaging in continuing infringement of respondent's copyrights."[35]

In my view this change would be a positive addition to the copyright law. As I described above, secondary liability for copyright infringement is an important feature of copyright – it helps ensure real, effective enforcement of copyright against those who are truly responsible in both legal and financial terms. This is especially true in the context of peer-to-peer services, which have created vast networks of copyright infringement by relying on clever technology and inducing others to join the network and infringe copyright. As I testified last year, we are seeing the natural consequences of what happens when secondary liability doctrines are not applied in this context: enforcement against infringement is left to suits against individual users, rather than the businesses that are profiting from the infringement. As you pointed out in your floor statement, Mr. Chairman, this result makes no sense, and is a departure from traditions of copyright, which has regulated the relationship between copyright owners and intermediaries (like dance halls and swap meets) for the ultimate benefit of consumers. Decisions like *Grokster* scramble this venerable structure, forcing copyright law to administer the relationship between copyright owners and consumers, to the undeserved benefit of intermediaries like Kazaa and Grokster.

The bill is appropriately tailored to the defendant's intentions and behavior, rather than the technology it chooses to employ, making the bill technology neutral. It would allow courts to examine all of the circumstances of a particular case to determine whether the defendant had intentionally constructed its business to profit from infringement of others that it induced. Recognizing that an actor's state of mind can often only be shown

[35] *Sony*, 464 U.S. at 439 n. 19.

by indirect evidence, the definition of "intentionally induce" allows a court to apply an objective, reasonable person standard to the conduct of defendant to determine whether that evidences the requisite intent. The central definition, however, requires that the defendant "intentionally aids, abets, induces or procures" infringement, which is a high level of *mens rea* that should limit application of this bill only to the most egregious actors.

For example, the provisions of this bill would appropriately place liability on the operators of the current peer-to-peer services such as Grokster, Kazaa and Morpheus/Streamcast. There is a wide array of evidence that the proprietors of those services induce users to infringe copyright:

1. Their business is based on advertising revenue, which is based on the number of users participating on the network, which, as the *Grokster* court recognized is based on the free availability of copyrighted works on that network.

2. The availability of copyrighted material on the network is assured by the software, which automatically and invisibly to the user immediately begins making their copies of works available to the millions of others on the network. As the Harvard Law School's Berkman Center for Internet and Society explains: "With Kazaa, it is easy to begin file sharing, but much more difficult to turn it off."[36] The Berkman Center explains the several different steps Kazaa has programmed into is software to make sure the user is "sharing" as many files as possible:

- "[B]y default, Kazaa starts itself immediately when the user turns on his computer. The program runs in the background, pre-set with the file-sharing feature turned 'on' and configured to allow an unlimited number

[36] Brief of Amicus Curiae Berkman Center for Internet & Society at Harvard Law School, filed in *Capitol Records, Inc. v. Alaujan*, No. 1:03-CV-11661-NG at 9-12 (D. Mass. filed May 24, 2004).

of uploads at a time. Many users may not be aware that the program is running continuously in this fashion."

- "When a user downloads a file from another Kazaa user, by default that copy is stored in the publicly shared folder, which means that it becomes immediately available for copying by others on the Kazaa network. Kazaa defaults to creating a shortcut to open this folder on the user's desktop; however the user may not be aware where exactly the folder itself is located on his computer."

- "Unlike most computer applications, clicking on the 'x' button on the top right-hand corner of the Kazaa program does not shut down Kazaa. This action merely hides the Kazaa program from the screen while the program continues to run the program in the background. To actually shut down the program, the user must then right-click the Kazaa icon located in Windows taskbar and choose the 'close' option."

- "Disabling the default file-sharing features in Kazaa is a complicated process due to an intricate series of steps within the software itself. In addition, the available resources that detail how to disable file sharing are often inconsistent or provide incomplete instructions."

As the Berkman Center concludes, "it can be extremely difficult for a non-expert computer user to shut down their file-sharing capability." That difficulty is not an accident – it is the intentional design of the proprietors of these services.

3. The defendants also affirmatively encourage people to distribute as many files as possible, knowing that most people will share infringing files. Kazaa implements what it calls "Participation Levels", which increase a user's download performance based on the amount uploaded from that user.[37] In other words, the more attractive the files you are sharing with other, the easier it will be for you to download copies from others. Indeed, Kazaa suggests that the user "share large and interesting files." This feature encourages users to make available popular copyrighted works, which will likely be the most frequently downloaded by others.

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[37] *See* Kazaa User Guide Glossary, "Participation Level" at http://www.kazaa.com/us/help/glossary/participation_ratio.htm.

4. The proprietors of these services employ strategies of "plausible deniability" and "disaggregat[ing] functions" to avoid legal liability but allow copyright infringement on their networks to continue. As one attorney for these services explained:

> Can you plausibly deny what your users are up to? ...
>
> Have you built a level of 'plausible deniability' into your product architecture? If you promote, endorse, or facilitate the use of your product for infringing activity, you're asking for trouble. ... Software that sends back user reports may lead to more knowledge than you want. Customer support channels can also create bad "knowledge" evidence. Instead, talk up your great legitimate capabilities, sell it (or give it away), and then leave the users alone.
>
> Disaggregate functions ... In order to be successful, peer-to-peer networks will require products to address numerous functional needs—search, namespace management, security, dynamic file redistribution, to take a few examples. There's no reason why one entity should try to do all of these things. ...
>
> This approach may also have legal advantages. If Sony had not only manufactured VCRs, but also sold all the blank video tape, distributed all the TV Guides, and sponsored clubs and swap meets for VCR users, the Betamax case might have turned out differently. ...
>
> A disaggregated model, moreover, may limit what a court can order you to do to stop infringing activity by your users.[38]

As I noted above, secondary liability, like the form proposed in this bill, can and should be used to impose liability where the defendant organizes its business structure to permit illegal activity to continue unabated but keep itself insulated from liability.

In short, the way Kazaa and other peer-to-peer technologies have structured their businesses and designed their software, they make a user's infringement almost inevitable. Indeed, many users probably don't know they are engaged in the distribution of works, and continue to do so even after they think they've turned the program off.

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[38] Fred von Lohmann, Electronic Frontier Foundation, "IAAL [I am a Lawyer]: What Peer-to-Peer Developers Need to Know about Copyright Law", § V.7 (December 2003) (http://www.eff.org/IP/P2P/p2p_copyright_wp.php).

When all of these circumstances are considered, they meet the test of "intentionally induce," and courts should be able to find liability based on them under the new provision.

These circumstances also help to show why the concerns about the breadth of the bill are misplaced. As Senator Leahy's floor statement makes clear, those who merely provide copying technology should not be liable under this bill, because they would lack indicators of "intentional inducement" like those found in the peer-to-peer context. For example, the seller of a portable MP3 player does not make it nearly inevitable that the user will commit copyright infringement just by turning the device on. Rather, several additional steps must be taken by the user before any potential infringement takes place. Also, the seller of the portable device is very likely not reliant on building a network like the peer-to-peer service that is trying to sell advertising, and therefore it typically has no need to and does not encourage users to become distributors of copyrighted works.

While I believe the bill as drafted does not present the concerns raised by some, to the extent you wish to confirm this interpretation of the scope of the bill with additional clarifying language, the Copyright Office would be pleased to assist you with suggestions that would help achieve this result.

In addition, concerns that this bill would affect liability of Internet Service Providers ("ISPs") are unfounded. Normal activity of an ISP like that defined in the Section 512 safe harbors could not reasonably be considered intentional inducement. Even if such actions could be considered within this new species of liability, nothing in this bill affects operation of Section 512, so that the same limitations of liability would apply to qualifying ISPs for this new form of liability.

While I think this bill would provide courts with a useful and effective means of assessing the liability of the current generation of infringing services, I am concerned that the next generation of technology-based pirates will be able to devise a way around this new species of liability. They may be able to limit evidence of their "inducement," yet still be able to reap substantial financial benefit from enabling and encouraging massive copyright infringement, just as Grokster, Kazaa and Morpheus appear to have devised a way around the *Napster* decision. To achieve a more comprehensive solution, this Committee may want to consider other legislative approaches in addition to this bill that would provide guidance to courts so that liability can be found in appropriate circumstances. While you have carefully crafted this bill to preserve the 20-year-old decision in the *Sony* case, it may become necessary to consider whether that decision is overly protective of manufacturers and marketers of infringement tools, especially in today's digital environment. If the *Sony* precedent continues to be an impediment to obtaining effective relief against those who profit by providing the means to engage in mass infringement, it should be replaced by a more flexible rule that is more meaningful in the technological age, but that still vindicates the Court's goal to balance effective "and not merely symbolic" protection of copyright with the rights of others to engage in substantially unrelated areas of commerce.[39] The Copyright Office offers whatever assistance this Committee would need with respect to such efforts.

Let me be clear, however, that our concern about its future application should not hold up this bill. It is an important improvement over existing law that will help avoid results like the district court opinion in *Grokster*. It also has a sufficiently high standard of intent that will not subject legitimate businesses to any new liability. I support enactment of the Inducing Infringement Acts of 2004.

[39] *Sony*, 464 U.S. at 440.

Testimony of Neil Portnow
President of the National Academy of Recording Arts & Sciences
For
Senate Committee on the Judiciary
"An Examination of S. 2560, the Inducing Infringement of Copyrights Act of 2004."
Thursday, July 22, 2004 at 2 p.m.

Chairman Hatch, Senator Leahy and member of the Committee, good afternoon. My name is Neil Portnow, and I am President of the National Academy of Recording Arts and Sciences, an organization comprised of thousands of individual music makers from across the country. We are primarily known for producing the GRAMMY Awards. However, the Recording Academy is also at the forefront of advocacy on behalf of musicians, singers, songwriters, producers and engineers.

I thank you for the opportunity to submit testimony regarding the Inducing Infringement of Copyrights Act of 2004, a bill supported by the Academy. As the members of this Committee know quite well, the illegal sharing of music files has had a devastating effect on those who create music. I have been in this business for more than 30 years—as a musician, a label executive, and now as President of the Academy. I can tell you there has never been a more perilous time for the music community than today. As I travel the country speaking with our members in our twelve Chapter cities, the future of online music distribution is the one topic of most interest—and most concern. And without a legislative solution to illegal file sharing, the problem will only get worse

We continue to do our part to educate the public about legal vs. illegal online music acquisition. Our website, www.whatsthedownload.com, gives music fans a place to go to get accurate information on the legal music marketplace and information regarding the impact of downloading on the creative artist community.

The major labels' trade association has also taken action. Lawsuits against individual file sharers have resulted in a noticeable reduction of file sharing. While the Recording Academy understands the reasons for this approach by the industry, I believe we would concur that suing music fans is not a preferred method of stopping piracy. However, because the law allows P2P companies to hide behind the individuals they induce to participate in this theft, it was the only legal option open to pursue.

Today, there is another option on the table. Thanks to the foresight of the Chairman and Ranking Member of this Committee, we have the Inducing Infringement of Copyrights Act. The Academy is grateful to the Senators who have already joined in support of this bill, and we hope this bi-partisan momentum will build. Through passage of this bill, those companies that induce others, many of them minors, to steal music would at last be held accountable for their actions. This bill would certainly help the music community by turning the tide of music theft. But it is also ultimately a pro-consumer act, as it will hopefully lessen the need to target consumers in legal action, and help the legitimate music marketplace thrive on a level playing field.

In closing, I'd like to echo something I said during my remarks on this year's GRAMMY telecast. In asking our worldwide audience to be thoughtful when considering how they get music online, I stated, "we ask you to help us keep music strong and alive for this and for generations to come. You can be sure that we will continue to do our part; we're counting on you to please do yours." Mr. Chairman, this plea is equally appropriate for the members of this Committee and the Senate as a whole. We in the recording community want to continue to provide the music that brings joy and satisfaction to our citizens, but we rely on the Congress to ensure that those who write, perform and produce the music that we all love receive fair compensation for their efforts. Passage of the Inducement Act will help the music community survive, perhaps even thrive, during these times of transition. With your support, we will emerge from this perfect storm and continue to provide the world with the finest music, delivered conveniently by legal online services that fairly compensate creators.

Thank you very much.

Before the United States Senate
Committee on the Judiciary
Testimony of Gary J. Shapiro
On behalf of the
Consumer Electronics Association
and the
Home Recording Rights Coalition

"An Examination of S. 2560, the
Inducing Infringement of Copyrights Act of 2004"
July 22, 2004

As the Chief Executive Officer of the principal trade association of the consumer electronics industry, the Consumer Electronics Association,[1] I appreciate the opportunity to appear and to express our very grave concerns over S. 2560. Although I believe this bill to be a novel and sincere approach to dealing with an issue that merits much discussion, I also believe it would make a radical and unfortunate change to legal principles on which my industry and many others have relied in order to bring new technology to American consumers.

I am also here today as the Chairman of the Home Recording Rights Coalition. The HRRC was formed in October, 1981, the day after the U.S. Court of Appeals for the Ninth Circuit effectively found the home VCR to be a contraband article of commerce, whose sale to consumers could be enjoined by judicial decree. The Supreme Court reversed the Ninth Circuit's judgment twenty years ago. But for these twenty years, we have faced a series of legal, regulatory, and legislative proposals aimed at trimming, obliterating, or conditioning the rights that the Supreme Court affirmed. In our view, S. 2560 is the most fundamental threat that consumers and technology industries have faced since the Ninth Circuit's decision in 1981.

The *Betamax* Doctrine Is Necessary To Technological Innovation And Investment

Earlier this year, the consumer electronics and information technology industries celebrated the 20th anniversary of the Supreme Court's historic ruling in the *Betamax* case, in which the Court turned back efforts by two motion picture studios to obtain a court injunction against the sale of consumer VCRs. We have long referred to this holding as the *Magna Carta* for our industry. The firm principle that the court established – that the sale of staple articles of commerce (such as home recorders and cameras, photocopiers, etc.) with significant noninfringing uses could not be enjoined on copyright grounds – established and ensured technology innovation that has continued into today's digital age.

[1] CEA is the principal trade association of the consumer electronics and information technology industries and the sponsor of the International Consumer Electronics Show. CEA represents more than 1,500 corporate members involved in the design, development, manufacturing, distribution, and integration of audio, video, mobile electronics, wireless and landline communications, information technology, home networking, multimedia and accessory products, as well as related services that are sold through consumer channels. Combined, CEA's members account for more than $90 billion in annual sales.

The Supreme Court in *Betamax* gave technology companies the confidence and incentives to invest in new technology because it set an *objective* legal standard: a safe harbor for manufacturers and distributors of hardware and software products. Unfortunately, the *subjective* legal standard proposed in S. 2560 would fill this harbor with unchartable mines. The Supreme Court said:

> "The staple article of commerce doctrine must strike a 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. Accordingly, 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."[2]

This holding is in stark, and in our judgment, irresolvable contrast with the language of S. 2560:

> "Whoever intentionally induces any [copyright violation] shall be liable as an infringer. *** 'Intentionally induces' means intentionally aids, abets, induces, or procures, and intent may be shown by acts from which a reasonable person would find intent to induce infringement based upon all relevant information about such acts then reasonably available to the actor ...."

Mr. Chairman, we understand that there was no intent to undermine the Supreme Court's holding. But we do not see how these two tests could be viewed as nearly the same, or even remotely similar. One is based on an objective assessment of a product's capabilities, as may readily be established by documentary evidence and precedent. The other is entirely based on an *ad hoc,* completely subjective evaluation that can *only* be based on either reading the mind of an entrepreneur and his investors, or on completely circumstantial evidence of what someone *must* have had in mind in bringing an item of commerce to market.

<u>The Test Set Forth In S. 2560 Is Hopelessly Subjective</u>

Either of the ways of measuring "inducement" under S. 2560 would be potentially ruinous to innovation and investment. Almost all technology-based associations of which I am aware have expressed strong concern and objection to this legislation; frankly I cannot understand how any group concerned with technological progress could support legislation, built around this concept, that applies to articles of commerce.

Let me cite an example of how such a test might be misapplied. Proponents of the legislation have suggested that when several organizations, including my own, filed *amicus curiae* briefs in a case currently on appeal to the Ninth Circuit, we "asked" the Congress, and more specifically, the Senate Judiciary Committee, to legislate. I signed off on the brief filed by

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[2] *Sony Corp. of America v. Universal City Studios, Inc.,* 464 U.S. 417, 442 (1984).

CEA and HRRC.[3] Neither I nor any of our member companies thought we were inviting the Congress in general or this Committee in particular to step in and write a law that would decide the case or change the rules of copyright liability.[4]

Under the standard proposed in S. 2560, the only way to resolve the question of my mental attitude -- whether I "intentionally" meant to induce the introduction of S. 2560 when I signed off -- would be through a full jury trial, examining "all relevant information" that was then available to me, so that the jury can form its own opinion of my business motives. How could anyone run a business, or attract investors, if this is the standard by which their product decisions will be assessed *after the fact*? ***How could any business avoid a jury trial over any product in which any copyrighted work is recorded or transmitted?***

The Real-World Result Would Threaten Innovation At Least As Much As The "Technology Mandate" Bill In The Last Congress

Unfortunately I -- and most of my colleagues in technology associations and companies -- have come to the conclusion that S. 2560 would have the same net effect as the "technology mandate" legislation introduced in the last Congress by Senator Hollings, which was universally opposed by technology-based associations:

- S. 2560 would effectively force anyone hoping to come to market with a product that transmits or stores copyrighted works to **negotiate *in advance,*** to quiet *any* of the concerns of *any* copyright proprietor that has the resources to sue.
- The only difference is, rather than directly requiring such a negotiation, as the mandate bill did, S. 2560 subjects the entrepreneur to incalculable risk unless such negotiations occur. This makes attracting investment even *more* difficult than under a "tech mandate" regime.

This result is directly contrary to the logic and analysis of the Supreme Court in *Betamax.* S. 2560 creates the very result that the Court explicitly sought to avoid:

> "[A] sale of an article which though adapted to an infringing use is also adapted to other and lawful uses, is not enough to make the seller a contributory infringer. ***Such a rule would block the wheels of commerce.***"[5]

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[3] *Metro-Goldwyn-Mayer Studios Inc. v. Grokster Ltd,* Nos. 03-55894 & 03-56236, *Jerry Lieber v. Grokster Ltd.*, Nos. 03-55901, U.S. Court of Appeals for the Ninth Circuit, Brief of Consumer Electronics Association and Home Recording Rights Coalition As *Amici Curiae* Supporting None of The Parties And Urging Neither Affirmance Nor Reversal, September 26, 2003.

[4] What we said was: "For the foregoing reasons, CEA and HRRC respectfully urge this Court not to weaken the *Betamax* doctrine or expand the doctrine of vicarious liability in the manner proposed by Plaintiffs-Appellants and their *amici* but instead leave any alteration in the rule of copyright liability in the hands of Congress, where it properly belongs." *Id.* at 25-26.

[5] 464 U.S. at 441 (emphasis supplied).

The "Savings Provisions" Do Not Offer Protection For Innovators, Investors, Or Merchants

The so-called "savings" provisions of S. 2560 do nothing to ameliorate this harsh result, or to make the Supreme Court's warning against "blocking the wheels of commerce" any less valid. These provisions are:

> "Nothing in this subsection shall enlarge or diminish the doctrines of vicarious and contributory liability for copyright infringement ...
>
> ... or require any court to unjustly withhold or impose any secondary liability for copyright infringement."

The problem with these provisions is that they do little or nothing to address the actual dangers to innovation presented by the rest of S. 2560:

- The bill, clearly on its face, establishes a distinct cause of action for *inducing* copyright infringement. Thus, the fact that it does not "enlarge or diminish" the *existing* causes of action for infringement provides no protection. *If this bill could not change the outcome of cases in which the contributory and vicarious doctrines produce no liability, there would be no point in passing it.*

- We understand and appreciate the notion that liability would be "unjust" in cases of first impression, where a device manufacturer might not know how a jury would relate his device to the conduct of others. Once there is a single District Court decision or jury verdict, however, this rationale would no longer apply. *The manufacturer, if he kept his product on the market, would no longer be able to take advantage of this provision – and his investment in the product, and those of this distributors, and their risk, would have grown throughout the first trial.* Could such a product remain on the shelves?

There Is No Way To Be Properly Selective According To Intent

The real problem with this entirely subjective approach in copyright legislation is that *any* approach based primarily on discovering original intent, before the fact, or on circumstantially divining intent, after the fact, can not filter out the "approved" actors from the "bad" actors when applied to the world of markets, and staple and generic products. There is simply no "**Maxwell's Demon**" available to investors before the fact, or to courts after the fact, that can do this. Despite all the "intelligence" that has been built into modern consumer electronics and information technology products, they still cannot *think* – hence, judging these products by an "intent" standard must involve determining why *people* went to market when and how they did. An after-the-fact determination by trial lawyers and juries cannot do anything but chill innovation, investment, and commerce.

Mr. Chairman, in your floor statement explaining how such selective decision making could in fact be beneficial in weeding out bad actors from good, you gave the example of the literary character Fagin:

> "In *Oliver Twist*, Fagin and Bill Sikes profited by inducing children to steal. In the film *Chitty-Chitty Bang-Bang*, the leering 'Child-Catcher' lured children into danger with false promises of 'free lollipops.'"

But is a very broad *inducement* cause of action really the best way to pursue a modern-day Fagin while not crushing the marketplace for ideas?

In the case of Fagin, modern law would offer many more targeted and satisfactory ways to bring such a character to justice. He would be apprehended for more specific offenses of contributing to the delinquency of a minor; conspiracy; vicariously engaging in the thefts involved; and for violations of local child health and welfare laws. These all seem more logical and likely to discourage abhorrent behavior by others than subjecting Fagin to a civil suit, brought by those who believe he influenced someone to pick their pocket.

Conversely, a new cause of action for *inducement* verges perilously on punishing speech. I am aware that even product reviewers have voiced concern over whether they might be sued for "inducement" based on what they *say* about, *e.g.*, undocumented capabilities they may find in a product, or their own observations about the uses to which it might be put.

In fact, the Supreme Court *did* consider, in the *Betamax* case, applying an "inducement" standard derived from the trademark law. The Court specifically decided *not* to do so:

> "Given the fundamental differences between copyright law and trademark law, in this copyright case we do not look to the standard for contributory infringement ... crafted for application in trademark cases. There we observed that a manufacturer or distributor could be held liable to the owner of a trademark if it **intentionally induced** a merchant down the chain of distribution to pass off its product as that of the trademark owner's or if it continued to supply a product which could readily be passed off to a particular merchant whom it knew was mislabeling the product with the trademark owner's mark."[6]

S. 2560 Provides Movie And Recording Interests With The Head-On Attack On *Betamax* That They Have Long Sought

This brings me back to my fundamental point: Because it is so doctrinally different, and relies on a fundamentally different test -- intention vs. capability of product -- there is no way that S. 2560, if it is applicable to staple hardware and software products, can or will be read by potential plaintiffs, and by courts, as anything other than a frontal attack on the holding of the Supreme Court in the *Betamax* case. Any statements of private sector proponents to the contrary

[6] 464 U.S. at 439, n. 19, emphasis added. The Court observed in a footnote that Sony probably would have passed such a test on the facts before it, but clearly rejected it as a basis for judgment where possible restraints on commerce were involved, as it would involve questions of knowledge of subsequent product users, rather than of product capability at the time of manufacture.

would not be legislative history, and even if they were, would not necessarily be persuasive to a court.[7] But these statements do not, in fact, offer any reassurance.

The Motion Picture Association of America (MPAA) – which supported the studios' suit for an ***injunction*** against the *Betamax* – said in a recent lobbying piece in support of S. 2560:

> "Nothing in the Induce Act will abrogate or affect [the *Betamax*] holding that liability does not attach merely because the maker of a copying device has constructive knowledge that its product could be used to infringe, and so the substantial-noninfringing-use rule will continue to govern for such multi-purpose devices."

But this MPAA statement does not affirm that the "substantial noninfringing-use rule" will continue to apply so as to avoid liability for consumer product manufacturers. In fact, the MPAA and its members do *not* believe that modern personal video recorders, with their present storage capacities, should receive protection under their own narrow and tortured reading of the *Betamax* case. Just a few years ago, Replay, a company marketing personal video recorder products, was driven into bankruptcy by copyright litigation brought by MPAA members. An entire chapter of the complaint brought by MGM, Orion Pictures, Fox Film Corporation, Universal City Studios Productions, and Fox Broadcasting specifically attacks *standard features, found on any PVR product,* as "inducements" to copyright violation:

> "The Seeking, Recording, Sorting and Storage Features"[8]
>
> "Defendants cause, accomplish, facilitate and ***induce*** the unauthorized reproduction of Plaintiffs' copyrighted works in violation of law. *** The ReplayTV 4000 device provides expanded storage, up to (currently) a massive *320 hour* hard drive, which allows the unlawful copying and storage of a vast library of material. *** ReplayTV 4000's expanded storage and sorting features organize disparate recordings into coherent collections, and ***cause, facilitate, induce and encourage*** the storage or "librarying" of digital copies of the copyrighted material, which harms the sale of DVDs, videocassettes and other copies, usurps Plaintiffs' right to determine the degree of 'air time' a particular program receives in various cycles of the program's distribution ...."[9]

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[7] *See, e.g., RIAA v. Diamond Multimedia Systems, Inc.*, 180 F. 3d 1072, 1078 (9th Cir. 1999), in which the court rejected the legislative history cited by one of the private sector drafters of the Audio Home Recording Act: "RIAA's assertion that computer hard drives do not fall within the exemption is irrelevant because, regardless of that portion of the legislative history which addresses the exemption from the definition of digital music recording ... the Rio does not reproduce files from something that falls within the plain language of the basic definition of a digital music recording ...."

[8] *Metro-Goldwyn-Mayer Studios, Inc. et al v. ReplayTV, Inc.*, U.S. District Court, Central District of California, Case No. 01-09801, Complaint of MGM, Orion Pictures, Twentieth Century Fox, Universal City Studios, and Fox Broadcasting, ¶¶ 24-25, November 14, 2001 (only bolded emphasis is supplied).

[9] *Id.* These allegations were grouped and made *separately* from those concerning the "distribution" (¶¶ 19-23) and "autoskip" (¶¶ 28-29) features that received more press attention. The pleadings in this case can be found at http://www.eff.org/IP/Video/Paramount_v_ReplayTV/.

With respect, Mr. Chairman, citing the MPAA and the RIAA as the guides and protectors of the *Betamax* doctrine would be akin to appointing Fagin as Oliver Twist's personal protector. In fact it would be worse: Fagin sought to exploit Oliver, not to kill him. Neither the MPAA nor the RIAA has ever agreed that the *Betamax* case was correctly decided, or that private, noncommercial home recording by consumers is and ought to be legal. Each is on record as wanting to limit the principles underlying the *Betamax* holding strictly to its narrowest possible set of facts. So of course they see no "threat" posed by S. 2560.

Early Attacks On Products And Methods Are Not Likely To be Well Focused

Even if it *were* possible magically to sort out the good from the bad, is it really *wise* for Congress to legislate based on reactions to products and techniques that are still evolving and being studied? History suggests that it is not:

- As has so often been noted, the head of the MPAA initially compared the consumer VCR to the "Boston Strangler," and supported his members in seeking a court injunction against its sale. Within a few years, VCR-based home video surpassed the box office as Hollywood's biggest revenue producer.

- Only a few years ago, in the *Replay* case, movie studios pleaded in court that standard storage capacity and indexing features, as might be found on other "PVRs" (such as a *TiVo* or a PC-based PVR) induce copyright infringement.

- In 1999, the RIAA was still seeking judicial relief against the *Rio,* the first MP3 player.[10] If RIAA had succeeded, it seems unlikely that an *iPOD* could have come to market.

The case against "Peer To Peer" technology is also one that involves more exploration than conclusion. Last week, the Business Software Alliance released a study that attached a dollar figure to losses from "piracy." This week, the research director of the company that conducted the study admitted that the figure announced to the press assumed that every unauthorized copy was a lost sale, whereas in reality perhaps one in ten actually represented such a loss.[11] Nor, of course, is every use of "P2P" an instance of unauthorized copying, nor have all authorities concluded that such copying is damaging on a net basis.[12] Nor does every use of P2P software necessarily involve or invoke a service.[13] Indeed, any effort to shut down P2P technology also threatens individuals and organizations that are finding creative uses for sharing

[10] *RIAA v. Diamond Multimedia Systems, Inc.,* 180 F. 3d 1072 (9th Cir. 1999).
[11] Steve Lohr, "Software Group Enters Fray Over Proposed Piracy Law," *New York Times,* July 19, 2004.
[12] *See, e.g.,* Felix Oberholzer, Koleman Strumpf, *The Effect of File Sharing on Record Sales An Empirical Analysis* (Mar. 2004), http://www.unc.edu/~cigar/papers/FileSharing_March2004.pdf
[13] It is just such issues that are presently before the Ninth Circuit, awaiting decision in the *Grokster* case. In their *amici* brief, CEA and HRRC did not express an opinion as to how the facts of that case should be resolved.

content using P2P technologies, and existing P2P services, that do not involve the uploading of copyrighted materials.[14]

A problem with an "inducement" approach, based on intent, is that *there is no going back.* Once a product has been labeled by a fact finder as signifying an *inducement* there is no way to make it safe to market the product again – even though the initial *Boston Strangler* impression *would have been* disproved in the marketplace, and a new market would have been created. This is in stark contrast to the Supreme Court's *Betamax* standard, which measures *capability,* and which considers potential uses in the context of defenses, rather than as bases – often proved by events to have been misguided – for banning a product from the marketplace in advance.

S. 2560 Is Basically Inconsistent With *Betamax* In Many Particulars

Although proponents have sought verbally to close the gap between *Betamax* and S. 2560, one can count the ways in which S. 2560 is fundamentally inconsistent with the doctrine as established by the Supreme Court. S. 2560 would add a new, additional, and separate doctrine of "induced" liability, to make one entity responsible for the actions of another. In our first several hundred years of copyright law, we have had two ways in which such responsibility can be found:

- *Contributory infringement* – a finding that you knowingly materially contributed to conduct, which may include the supply of tools used for infringement, that had no substantial purpose other than to infringe, and

- *Vicarious infringement* – a finding that through conduct of your own, which may include supplying a product, you directed or participated in the infringement of another.

S. 2560 purports to leave these two doctrines undisturbed, but adds another:

- *Induced infringement* – a finding from a "reasonable" evaluation of all "information," that whatever you did – whether advocacy, persuasion, advertising, or just having a particular state of mind when providing a tool -- had the effect of "inducing" someone else to engage in infringing conduct.

The notion of launching a third vehicle for finding indirect liability arises out of frustration with the results from the existing two:

- In *Betamax*, the Supreme Court held that a party marketing a staple article of commerce cannot be found liable for *contributory* infringement if the product has any commercially significant non-infringing use. (Thus, the court allowed the consumer VCR to reach the American market.)

[14] Kim Zetter, "Downloading for Democracy," Wired News (July 19, 2004), http://www.wired.com/news/politics/0,1283,64237,00.html. *See also,* "FileSharing HOWTO," Project Gutenberg, http://www.gutenberg.net/howto/p2p-howto.

- A finding of *vicarious* infringement must rest on active involvement in specific conduct by another. This is difficult to demonstrate in a marketplace where each actor is deemed to take personal responsibility for his own conduct.

The separate doctrine of *induced infringement* represents an attempt to filter the marketplace, to screen out "bad" purveyors of goods and services (Fagin), and to leave "good ones" standing, through some "reasonable man" standard of after-the-fact evaluation. There are only two ways to do this:

-- *circumstantially* – looked at later, did the goods or services seem to have some inducing effect?

-- *by determining state of mind* – could a reasonable jury conclude, after the fact, that in placing product Y on the market, the manufacturer or retailer had some *intent* to "induce" action X by somebody else?

Basing a civil cause of action on either of these tests inevitably would injure commerce and new technology in the United States. There is simply no way to apply any objective measure to either test. Nor is there any way to make a determination without a full jury trial. Hence, there is no way for an inventor, an entrepreneur, a venture capitalist, a manufacturer, a distributor, a retailer, or even a journalist or product reviewer to determine which inventions, products, or actions will incur copyright liability, and which will not. So, even though a new doctrine of ***civil copyright inducement*** would nominally leave in place, and undisturbed, the existing doctrines of contributory and vicarious infringement, it would wash away their bright line distinctions that have supported a viable market in the digital age.

In the *Betamax* case, the Supreme Court understood this. It found possible precedent in cases arising under patent and trademark statutes for applying the doctrine of "contributory infringement" to a copyright case. The Court considered and discussed which was more closely analogous – a patent doctrine based on *use,* or trademark doctrine based on *inducement.* It specifically rejected the inducement model. Instead, the Court chose to go in an entirely different direction, and to focus on objective *use*, rather than on the subjective *state of mind* of an "inducer" or the amount of influence that such a state of mind might later be found to have exerted on some unknown third party. The Court said that any *other* test would threaten to dampen commerce, by giving the owner of a copyright grant the power to limit the scope and utility, or even the availability, of a patent grant.

To try to carve out an "inducement" exception to this doctrine is simply to destroy it. The existing doctrine of contributory infringement already includes inducement as a basis for creating liability.[15] There is no need to create an entirely new doctrine. At minimum, it is essential to understand the relationship between the two doctrines.

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[15] *Gershwin Pub. Corp. v. Columbia Artists Management, Inc.*,443 F. 2d 1159 (2d Cir. 1971) ("one who with knowledge of the infringing activity, induces, causes, or materially contributes to the infringing conduct of another" is liable as a contributory infringer.)

Virtually any copyright owner of even a single work could be a potential plaintiff under this bill. The remedies for copyright infringement are extreme, and include attorneys' fees and statutory damages of up to $150,000 per infringed *work*.

- The factual nature of the intent inquiry virtually precludes summary judgment. Knowing this, any copyright owner can go after anyone selling a product they do not like, simply "because they can."

- Every case will pose an enterprise-threatening risk that could force defendants to settle for large sums, even where they have a legitimate defense. Such results will attract more litigation.

- The subjective intent test assures that litigation will include a lengthy and expensive discovery process, including document production and depositions intruding into all product design and marketing considerations. This prospect will induce many entrepreneurs, large and small, to forego investing in innovative multi-use products and networks, even when they are confident of their legality.

- The bill does not explain how a court is to determine the number of works that were subject to induced infringement, further increasing the risk of huge statutory damage awards.

Proponents note that intentional inducement of criminal copyright infringement is, itself, currently a crime.[16] But this bill goes beyond that doctrine in key respects, and creates a much greater risk of liability against legitimate activity.

- First, the infringement that is induced need not be criminal—that is, inducing even non-willful and non-commercial infringement will violate the proposed 512(g).

- Second, the criminal law requires proof of intent to induce *beyond a reasonable doubt*. S. 2560 relies upon the much lower civil preponderance of the evidence standard.

- Third, the criminal law requires a U.S. Attorney to decide a case is worth prosecuting. S. 2560 would permit every copyright owner (read, any citizen, including any citizen with a grudge or business agenda his own) to bring or threaten an action.

In this context of ruinous civil litigation and "private attorneys general," "intent" remains wholly undefined, subjective, and potentially arbitrary in its application.

- For example, actual or constructive knowledge of infringement, coupled with providing a technology or service that facilitates that infringement (e.g., selling a VCR or CD-R or DVD recorder) could provide proof of intent.

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[16] *See* 18 U.S.C. § 2.

- Is the relevant intent the specific intent to cause copyright infringement, or is it enough that the alleged inducer intends to cause another to do an act (when the inducer does not know the act is infringing)?

S. 2560 Does Not Successfully Borrow Any Patent Law Concept

It has been suggested that S. 2560 represents a simple "borrowing" of a doctrine from patent law, just as the Supreme Court made reference to patent law defenses to the doctrine of contributory infringement. However, in copyright guise, a new "inducement" doctrine would have *none* of the barriers to suit, limitations, or defenses to contributory liability that are built into its use (and, indeed, that the Supreme Court relied on in *Betamax*) under patent law.

Under the Patent Act, "Whoever ***actively induces*** infringement of a patent shall be liable as an infringer."[17] But, as applied in patent law, there can be no finding of inducement unless the patent owner proves that the defendant actively encouraged another to infringe the patent and that the defendant specifically intended to cause a direct infringement of a ***particular patent.*** Indeed, if taken straight from patent law rather than being recast as in S. 2560, this doctrine would not brook a single deviation from results under the *Betamax* holding:

- If there are substantial non-infringing uses for a product there can simply be no finding of inducement, even if there is knowledge of patent infringement.[18]
- "The principles of inducing infringement [under the Patent Act] are analogous to aiding and abetting in a criminal context."[19]
- "A person induces infringement under 271(b) by actively and knowingly aiding and abetting another's direct infringement [of the patent]."[20]
- Inducement requires a "specific intent to encourage another's infringement and not merely that the defendant had knowledge of the acts alleged to constitute inducement."[21]

If a person owns a valid patent that claims a method of treating a headache by ingesting an aspirin, he could successfully pursue a cause of action against a manufacturer of aspirin *only* if ***all*** of the following conditions are satisfied:

- the manufacturer makes and sells the aspirin for the sole purpose of causing consumers to take the aspirin for a headache;
- the manufacturer specifically intends that consumers will infringe the patent by ingesting the aspirin; ***and***

[17] 35 U.S.C. § 271(b).
[18] *Warner-Lambert Co. v. Apotex Corp.*, 316 F.3d 1348, 1364 (Fed. Cir. 2003).
[19] *Alcon Labs., Inc. v. Allergan, Inc.*, 256 F.Supp.2d 1080, 1087 (C.D. Cal. 2003).
[20] *C.R. Bard Inc. v. Advanced Cardiovascular Sys., Inc.*, 911 F.2d 670, 675 (Fed. Cir. 1990).
[21] *Manville Sales Corp. v. Paramount Sys., Inc.*, 917 F.2d 544, 553 (Fed. Cir. 1990).

- the manufacturer specifically and affirmatively promotes or encourages doctors, pharmacists, or other health-care providers to prescribe the aspirin for headaches.

However, if the court were to find that there are ***substantial noninfringing uses*** of aspirin, such as its ability to treat leg pains or prevent heart attacks, that are not covered by the patent, a manufacturer who makes and sells aspirin for those purposes (as well as for a headache) will not be liable for inducement.[22]

S. 2560 sweeps far more broadly than the Patent Act's concept of inducement, eliminating these requirements and limitations, so as to create liability for conduct far outside the bounds of what would be covered by the Patent Act:

- The Patent Act applies only if one "***actively*** induces infringement of a patent."[23]
  - S. 2560 does not require "active" inducement; it applies to anyone who "intentionally" induces where "intent" is defined expansively to capture even passive conduct where a "reasonable person would find intent."
- Under the Patent Act, summary judgment dismissing the claim must be entered if the plaintiff fails to present evidence that the defendant has actively promoted infringement with specific intent to cause infringement.[24]
  - S. 2560, in contrast, incorporates such a broad definition of intent based on a reasonable person standard that plaintiffs will easily and perhaps universally avoid summary judgment and force unwarranted claims to trial.
- The Patent Act requires "specific intent to encourage another's infringement."[25]
  - S. 2560, in contrast, contains no requirement of specific intent and instead could cover nearly any type of activity arguably connected to an infringement, no matter how remote.
- Under the Patent Act, "merely that the defendant had knowledge of the acts alleged to constitute inducement" cannot make the defendant liable for inducement.[26]
  - S. 2560, in contrast, could cover inducement based on no more than the defendant's knowledge of the acts alleged to constitute inducement if a "reasonable person" would find intent.

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[22] *See Warner-Lambert*, 316 F.3d 1348 (Fed. Cir. 2003).
[23] 35 U.S.C. § 271(b).
[24] *Id.*
[25] *See Manville Sales*, 917 F.2d at 553.
[26] *Id.*

- Under the Patent Act, "where a product has substantial noninfringing uses, intent to induce infringement cannot be inferred even when the defendant has actual knowledge that some users of its product may be infringing the patent."[27]
    - S. 2560, in contrast, contains no such protections, so the protections currently in place under *Betamax* are unlikely to be available in cases involving this new cause of action.
- The Patent Act requires a direct infringement before there can be liability for inducement.[28]
    - S. 2560 is ambiguous at best on this point; it will invite litigation and potentially capture conduct even where there is not a direct infringement.

S. 2560 Does Not Contain Provisions To Protect Consumer Rights And Their Reasonable And Customary Expectations

Mr. Chairman, as I noted at the outset, I am also here today as the Chairman of the Home Recording Rights Coalition. S. 2560, despite its laudable intention to target bad actors, would limit the freedom of consumers to purchase and then use technology that would enrich their lives. In all fairness, they should not be limited in what they can do with technology simply because "bad actors" can't be trusted to use technology responsibly.

As content owners can attest, both HRRC and CEA have worked constructively for many years to achieve balanced outcomes. HRRC representatives and members were among the founders of the Copy Protection Technical Working Group (CPTWG) and have attended all meetings and Work Groups for more than eight years. Most of the commercial proponents of the "DRM" technologies that are used to protect works in the digital age are members of CEA, and indeed, several are corporate members of the HRRC.

The HRRC "filter" for considering whether copyright or technology legislation may be worthwhile and is fair to consumers is based on three determinations:

(1) Do consumers receive the benefit of technological advances, or are they employed only to constrain reasonable and customary consumer conduct?

(2) Would technology, innovation, and investment be chilled or encouraged?

(3) Would the legal certainty and predictability necessary for free markets be increased or degraded?

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[27] *Warner-Lambert*, 316 F.3d at 1364.
[28] *C.R. Bard Inc. v. Advanced Cardiovascular Sys., Inc.*, 911 F.2d 670, 673 (Fed. Cir. 1990).

HRRC believes that, where there is a hard choice, *personal responsibility* is a better approach than putting product innovation and lawful use in jeopardy. In this Congress, the HRRC worked with congressional staff and the MPAA to craft legislative history for the ART Act, and provisions in state law, that would assure that the use of camcorders in movie theaters could be prosecuted, but that this would not endanger the use or demonstration of such products in homes or retail stores.

In previous Congresses, HRRC has supported measures, in the House and the Senate, that would impose personal responsibility on individuals. CEA and HRRC members tend to be intellectual property proprietors, and they suffer in myriad ways from commercial piracy, along with everyone else. We have been open to a number of legislative approaches that are consistent with the principles I have described. Every day our members work on technologies that are consistent with them.

Applying these principles to S. 2560, however, leaves us very uncomfortable. The number of open questions and the degree of open-ended liability for innovators, investors, manufacturers, retailers, consumers, product reviewers, product installers, and consumers – all part of the HRRC constituency – is daunting. Nevertheless, we realize that this is a legislative process that is barely a month old.

Changes to the Copyright Act do, and for sound policy reasons should, take far, far longer – in some cases, more than one Congress. We recognize your desire, Mr. Chairman, to get on with this process in the present Congress, and we pledge our cooperation. Your staff, and Senator Leahy's staff, have been generous with their time and courteous in soliciting and receiving our views. We look forward to cooperating with them, and with the Committee, in the legislative process.

Thank you for having given me the opportunity to appear today.

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